CASE 6431: HNG OIL COMPANY FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO

CASE NO.

6431

APPLICATION,
TRANSCRIPTS,
SMALL EXHIBITS,
ETC.

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION

JERRY APODACA
GOVERNOR

NICK FRANKLIN
SECRETARY

POST OFFICE BOX 2088
STATE LAND OFFICE BUILDING
SANTA FE, NEW MEXICO 87501
(505) 827-2434

May 2, 1979

Mr. Tom Kellahin
Kellahin & Kellahin
Attorneys at Law
Post Office Box 1769
Santa Fe, New Mexico

Re: CASE NO. 6431
ORDER NO. R-5994

Applicant:

HNG Oil Company

Dear Sir:

Enclosed herewith are two copies of the above-referenced Division order recently entered in the subject case.

Yours very truly,

JOE D. RAMEY
Director

JDR/fd

Copy of order also sent to:

Hobbs OCC x
Artesia OCC x
Aztec OCC

Other

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION

IN THE MATTER OF THE HEARING
CALLED BY THE OIL CONSERVATION
DIVISION FOR THE PURPOSE OF
CONSIDERING:

CASE NO. 6431
Order No. R-5994

APPLICATION OF HNG OIL COMPANY
FOR COMPULSORY POOLING, EDDY
COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 9 a.m. on January 31, 1979, at Santa Fe, New Mexico, before Examiner Richard L. Stamets.

NOW, on this 2nd day of May, 1979, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS:

(1) That due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) That the applicant, HNG Oil Company, seeks an order pooling all mineral interests in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East, NMPM, Eddy County, New Mexico.

(3) That the applicant has the right to drill and proposes to drill a well at a standard location thereon.

(4) That there are interest owners in the proposed proration unit who have not agreed to pool their interests.

(5) That to avoid the drilling of unnecessary wells, to protect correlative rights, and to afford to the owner of each interest in said unit the opportinity to recover or receive without unnecessary expense his just and fair share of the gas in said pool, the subject application should be approved by pooling all mineral interests, whatever they may be, within said unit.

(6) That the applicant should be designated the operator of the subject well and unit.

(7) That any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(8) That any non-consenting working interest owner that does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(9) That any non-consenting interest owner should be afforded the opportunity to object to the actual well costs but that actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(10) That following determination of reasonable well costs, any non-consenting working interest owner that has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(11) That $2398.00 per month should be fixed as a reasonable charge for supervision (combined fixed rates) while drilling and that $318.00 per month should be fixed as a reasonable charge for supervision while producing; that this charge should be adjusted annually based upon the percentage increase or decrease in the average weekly earnings of crude petroleum and gas production workers; that the operator should be authorized to withhold from production the proportionate share of such supervision charge attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(12) That all proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(13) That upon the failure of the operator of said pooled unit to commence drilling of the well to which said unit is

dedicated on or before August 1, 1979, the order pooling said unit should become null and void and of no effect whatsoever.

IT IS THEREFORE ORDERED:

(1) That all mineral interests, whatever they may be, in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East, NMPM, Eddy County, New Mexico, are hereby pooled to form a standard 320-acre gas spacing and proration unit to be dedicated to a well to be drilled at a standard location thereon.

PROVIDED HOWEVER, that the operator of said unit shall commence the drilling of said well on or before the 1st day of August, 1979, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Pennsylvanian formation;

PROVIDED FURTHER, that in the event said operator does not commence the drilling of said well on or before the 1st day of August, 1979, Order (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division for good cause shown.

PROVIDED FURTHER, that should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Order (1) of this order should not be rescinded.

(2) That HNG Oil Company is hereby designated the operator of the subject well and unit.

(3) That after the effective date of this order and within 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject unit an itemized schedule of estimated well costs.

(4) That within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and that any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(5) That the operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the well; that if

no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, that if there is an objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(6) That within 60 days following determination of reasonable well costs, any non-consenting working interest owner that has paid his share of estimated costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

(7) That the operator is hereby authorized to withhold the following costs and charges from production:

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(8) That the operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(9) That $2398.00 per month is hereby fixed as a reasonable charge for supervision (combined fixed rates) while drilling, and that $318.00 per month is hereby fixed as a reasonable charge for supervision while producing, provided that this rate shall be adjusted on the first day of April of each year following the effective date of this order; that the adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the preceding calendar year as shown

by "The Index of Average Weekly Earnings of Crude Petroleum and Gas Production Workers" as published by the United States Department of Labor, Bureau of Labor Statistics, and the adjusted rate shall be the rates currently in use, plus or minus the computed adjustment; that the operator is hereby authorized to withhold from production the proportionate share of such supervision charge attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(10) That any unsevered mineral interest shall be considered a seven-eights (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(11) That any well costs or charges which are to be paid out of production shall be withheld only from the working interests share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(12) That all proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Eddy County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; that the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

(13) That jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

JOE D. RAMEY
Director

S

fd/

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION
State Land Office Building
Santa Fe, New Mexico
31 January 1979

EXAMINER HEARING

IN THE MATTER OF:

Application of HNG Oil Company for compulsory pooling, Eddy County, New Mexico.

CASE 6431

BEFORE: Richard L. Stamets

TRANSCRIPT OF HEARING

A P P E A R A N C E S

For the Oil Conservation Division: Lynn Teschendorf, Esq.
Legal Counsel for the Division
State Land Office Bldg.
Santa Fe, New Mexico 87503

For the Applicant: W. Thomas Kellahin, Esq.
KELLAHIN & KELLAHIN
500 Don Gaspar
Santa Fe, New Mexico 87501

I N D E X

E X H I B I T S

MR. STAMETS: We'll call now Case Number 6431.

MS. TESCHENDORF: Case 6431. Application of HNG Oil Company for compulsory pooling, Eddy County, New Mexico.

MR. KELLAHIN: I'm Tom Kellahin of Kellahin and Kellahin, Santa Fe, New Mexico, appearing on behalf of the Applicant, and I have two witnesses to be sworn.

MR. STAMETS: Any other appearances? Have the witnesses stand and be sworn, please.

(Witnesses sworn.)

RAYMOND PARKER

being called as a witness and having been duly sworn upon his oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. KELLAHIN:

Q Would you please state your name and occupation?

A My name's Raymond Parker. I'm a consultant for HNG Oil Company in land matters.

Q Mr. Parker, have you previously testified before the Oil Conservation Division in your capacity as a land man in other cases?

A. Yes, sir.

MR. KELLAHIN: We tender Mr. Parker as an expert.

MR. STAMETS: The witness is considered qualified.

Q. (Mr. Kellahin continuing.) Mr. Parker, have you made a study of and are you familiar with the land situation concerned in this application?

A. Yes, sir, I have.

Q. Would you refer to what I've marked as Exhibit Number One and identify that?

A. This is a plat of the north half of Section 35, Township 23 South, Range 28 East, Eddy County, New Mexico.

The acreage colored in yellow represents leasehold interests owned by HNG Oil Company. The orange, leasehold interest owned by Phillips Petroleum; the blue leasehold by Jack E. Russell and Associates; the green and the pink are owners of minerals that we have been unable to locate.

Q. Do you have an approximation as to how many acres are uncommitted to the unit?

A. There's a total of 6.875 mineral acres that are uncommitted to what we propose to poolin the north half.

Q. That's indicated on Exhibit Number Two?

A. That's true.

Q. Would you describe the information contained on Exhibit Two for us?

A. The first item shows a mineral interest of 1.875 acres out of a 5-acre tract, which shows on the plat, Exhibit One, as Tract 664. 15/24ths of that particular tract are owned as a leasehold by Phillips Petroleum. The remaining interest is owned by the heirs of Albert Larson and Olaf Inrude, last known address Caldwell, Kansas.

Q. With regard to that interest, Mr. Parker, what if anything have you done or directed to be done in contacting those people?

A. We've engaged a man named Tom Burton in Wichita, Kansas, to attempt to locate these lost people. He has contacted several people. Attached as our exhibits are the two affidavits.

Q. As of this date, that acreage is still uncommitted to you?

A. That's true.

Q. All right. Now, you have a 5-acre tract that is in the name of the heirs of Bert Schurr, S-C-H-U-R-R.

A. That's right.

Q. Let me show you what we've marked as Exhibit Number Three and will you describe your efforts to contact those heirs?

A. This is the letter, my letter -- or HNG's letter, my signature, addressed to Mr. Robert E. Coleman of Midland, Texas. Mr. Coleman visited me in my office about ten days ago, advised me that he has located certain heirs of Bert Schurr, using the process of acquiring oil and gas leases covering this outstanding interest.

I have not seen the oil and gas lease; he does not have it in hand. I wrote this letter for the express purpose of inviting him if he has a valid oil and gas lease to join us in the drilling of our well or to farmout on the basis outlined in this letter.

Q. That letter does indicate a paragraph advising the Bert Schurr heirs, through Mr. Coleman, of this particular case here?

A. Yes.

Q. Would you refer to Exhibit Number Four and identify it?

A. Exhibit Number Four is an affidavit of Tom Burton of Wichita, Kansas, as to his attempts to locate Mr. Alfred Larson.

Q. In summary he's not been able to do so.

A. In summary he's contacted a lawyer that at one time represented the Larson people but he is very aged in a nursing home and is unable to correspond.

Q. I have separately as Exhibit Five what ap-

pears to be the same affidavit. Are those two affidavits the same?

A. The affidavit is by the same affiant, and one covering the Inrude people and one the Larson people.

Q. Okay.

MR. KELLAHIN: I have no further questions of Mr. Parker.

MR. STAMETS: Are there any other questions of the witness? He may be excused.

J. STEWART MARTIN

being called as a witness and having been duly sworn upon his oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. KELLAHIN:

Q. Would you please state your name and occupation?

A. J. Stewart Martin. I'm Vice President of Exploration for HNG Oil Company, Midland, Texas.

Q. Mr. Martin, have you previously testified before the Oil Conservation Division?

A. Yes, sir.

Q. In what capacity?

A. As a geologist.

Q. Have you made a study of and are you familiar with the geological facts surrounding this particular application?

A. Yes, sir.

MR. KELLAHIN: We tender Mr. Martin as an expert.

MR. STAMETS: The witness is considered qualified.

Q. (Mr. Kellahin continuing.) Would you refer to what we've marked as Exhibit Number Six and identify that?

A. Yes, sir. This is a plat of the area showing all current drilling wells and completed wells.

Currently we are drilling a well and I believe the location is 2310 from the west line and 660 from the north line of Section 35, Township 23 South, Range 28 East, Eddy County, New Mexico, called our Williams Com 35 No. 1.

Q. The Williams Com 35 No. 1 is the well that will be dedicated to this north half proration unit?

A. Yes, sir.

Q. Would you please refer to Exhibit Number Seven and identify it?

A. This is an AFE of HNG Oil Company on the subject well. The completed well cost is $1,329,746; dry hole, $1,019,051.

Q. What is the total depth of the well, Mr. --

A. 13,400 feet Morrow test.

Q. In your opinion are the anticipated well costs for this particular well consistent with other Morrow wells drilled in Eddy County?

A. This, in this local area, are a little higher, about 20 percent higher than the wells that we have drilled down in Malaga about 3 miles to the south, because of the high pressure zones that have been encountered in the wells immediately to the north.

Q. Do you have a recommendation to the Examiner with regards to a penalty to be assessed against the non-participating owners?

A. Yes, sir, 200 percent.

Q. On what do you base that recommendation?

A. Well, primarily because of the erratic nature of the Morrow. The well to the south in Section 2 on the previous plat is a sub-commercial well, the Phillips Malaga No. 1-A. It's producing about a million feet of gas per month and a cumulative production of 340-million feet of gas. And a well to the north, there's a well in Section 23 in the east half has an Atoka sand, and the only other well that has that sand is the Maddox well in the west half of Section 26.

There are two Morrow completions within this

area, one in Section 22 in the southwest quarter, the Amoco No. 1 Brantley, and the Maddox 1-27 Pardue Farms in the east half of Section 27. These other wells encountered Morrow Sands but have not run any production tests on them.

Q. Would you refer to Exhibit Number Eight and identify it?

A. It's part of our operating agreement that the land department has prepared for the north half of Section 35.

Q. As part of that operating agreement what has been agreed to by the working interest owners for overhead charges or cost for supervision while drilling and after completion of the well?

A. The drilling well rate is $2398 and a producing well rate, $319.

Q. In your opinion would that be a fair sum to charge against the nonconsenting owners in this case?

A. Yes, sir, it's essentially the same as several operating agreements we have in the township to the south.

Q. Who are the operators that will sign this agreement, Mr. Martin?

A. It's HNG Oil Company, Phillips Petroleum, Jack Russell, et al, are the three that have signed the operating agreement.

Q. And HNG desires to be designated the operator?

A. Yes, sir.

Q. What percentage of the unit do they control?

A. At this point 60.935, .935 percent.

Q. I note that your operating agreement also has a method by which the fixed rates are adjusted on an annual basis, on the 1st of April of each year.

A. Yes, sir.

Q. In your opinion would that be an appropriate additional paragraph to add to this particular order to be applied against the nonconsenting parties?

A. Yes, sir.

Q. And were Exhibits Six, Seven, and Eight prepared by you or compiled under your direction and supervision?

A. They were compiled under my supervision.

Q. In your opinion, Mr. Martin, will approval of this application prevent waste and protect correlative rights?

A. Yes, sir.

MR. KELLAHIN: We move the introduction of Exhibits One through Eight.

MR. STAMETS: These exhibits will be admitted.

CROSS EXAMINATION

BY MR. STAMETS:

Q. Mr. Martin, let me confirm that you said that some of the operators, or the operating interests, have already signed the agreement that provides for these well costs of $2398 and $319, is that correct?

A. Yes, sir.

Q. And you anticipate that all will sign that with the possible exception of the people you can't locate?

A. Yes, sir, for the uncommitted interest of 2.148440 percent.

MR. STAMETS: Any other questions f or the witness? He may be excused.

Anything further in this case?

MR. KELLAHIN: No, sir.

MR. STAMETS: We'll take the case under advisement.

MR. KELLAHIN: Thank you.

(Hearing concluded.)

REPORTER'S CERTIFICATE

I, STEPHANIE XANTHULL, A Court Reporter, DO HEREBY CERTIFY that the foregoing and attached Transcript of Hearing before the Oil Conservation Division was reported by me; that the said transcript is a full, true, and correct record of the hearing, prepared by me to the best of my skill, ability, and knowledge, from my notes taken at the time of the hearing.

Stephanie Xanthull, C.S.R.

I do hereby certify that the foregoing is a complete record of the proceedings in the Examiner hearing of Case No. 6436 heard by me on 1-31 1979.

Richard R. Stamets, Examiner
Oil Conservation Division

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION
State Land Office Building
Santa Fe, New Mexico
31 January 1979

EXAMINER HEARING

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CASE 6431

BEFORE: Richard L. Stamets

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Anything further in this case?

MR. KELLAHIN: No, sir.

MR. STAMETS: We'll take the case under advisement.

MR. KELLAHIN: Thank you.

(Hearing concluded.)

REPORTER'S CERTIFICATE

I, STEPHANIE XANTHULL, A Court Reporter, DO HEREBY CERTIFY that the foregoing and attached Transcript of Hearing before the Oil Conservation Division was reported by me; that the said transcript is a full, true, and correct record of the hearing, prepared by me to the best of my skill, ability, and knowledge, from my notes taken at the time of the hearing.

Stephanie Xanthull, C.S.R.

I do hereby certify that the foregoing is a complete record of the proceedings in the Examiner hearing of Case 6431 heard by me on 1-31-79

Richard L. Stamets, Examiner
Oil Conservation Division

JASON W. KELLAHIN
W. THOMAS KELLAHIN
KAREN AUBREY

KELLAHIN and KELLAHIN
ATTORNEYS AT LAW
500 DON GASPAR AVENUE
P. O. BOX 1769
SANTA FE, NEW MEXICO 87501

TELEPHONE 982-4285
AREA CODE 505

April 5, 1979

Mr. Richard Stamets
Oil Conservation Division
P. O. Box 2088
Santa Fe, New Mexico 87501

Re: HNG Oil Company
Division Case No. 6431
Heard January 31, 1979

Dear Mr. Stamets:

In accordance with your request for additional information concerning the requested overhead charges for drilling and after producting, please find enclosed copies of other agreements in the area showing a higher rate charged than those requested in this case.

Very truly yours,

W. Thomas Kellahin

WTK:eps

Enclosure

cc: M. Raymond Parker

hng Oil Company
P. O. BOX 2267, MIDLAND, TEXAS 79702 (915) 683-4871

April 3, 1979

Kellahin & Kellahin
P. O. Box 1769
Santa Fe, New Mexico 87501

Attn: Mr. W. Thomas Kellahin

RE: Compulsory Pooling
N/2 Sec. 35, T-23-S, R-28-E
Eddy County, New Mexico

Gentlemen:

In compliance with your request, we enclose herewith a copy of the fully executed Operating Agreement covering the N/2 of Section 35, T-23-S, R-28-E, Eddy County, New Mexico. Well charges appear on page 3 of the Accounting Procedure.

Also enclosed is a copy of the Assignment and Agreement between HNG Oil Company and Phillips Petroleum Company covering lands in the same area. You will note that the drilling well rate is somewhat higher than the drilling well rate appearing in the Operating Agreement covering the N/2 of Section 35.

Yours very truly,

HNG OIL COMPANY

Raymond Parker

Raymond Parker
Manager of Lands

RP/jw
encls.

A.A.P.L. FORM 610

MODEL FORM OPERATING AGREEMENT—1956

Non-Federal Lands

OPERATING AGREEMENT

DATED

December 1, 19 78,

FOR UNIT AREA IN TOWNSHIP 23 South, RANGE 28 East,

EDDY COUNTY, STATE OF NEW MEXICO.

AMERICAN ASSOCIATION OF PETROLEUM LANDMEN
APPROVED FORM. A.A.P.L. NO. 610
MAY BE ORDERED DIRECTLY FROM THE PUBLISHER
KRAFTBILT PRODUCTS, BOX 600, TULSA 74101

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A.A.P.L. FORM 610

OPERATING AGREEMENT

THIS AGREEMENT, entered into this 1st day of December, 19 78, between HNG OIL COMPANY, hereafter designated as "Operator", and the signatory parties other than Operator.

WITNESSETH, THAT:

WHEREAS, the parties to this agreement are owners of oil and gas leases covering and, if so indicated, unleased mineral interests in the tracts of land described in Exhibit "A", and all parties have reached an agreement to explore and develop these leases and interests for oil and gas to the extent and as hereinafter provided;

NOW, THEREFORE, it is agreed as follows:

1. DEFINITIONS

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

(1) The words "party" and "parties" shall always mean a party, or parties, to this agreement.

(2) The parties to this agreement shall always be referred to as "it" or "they", whether the parties be corporate bodies, partnerships, associations, or persons real.

(3) The term "oil and gas" shall include oil, gas, casinghead gas, gas condensate, and all other liquid or gaseous hydrocarbons, unless an intent to limit the inclusiveness of this term is specifically stated.

(4) The term "oil and gas interests" shall mean unleased fee and mineral interests in tracts of land lying within the Unit Area which are owned by parties to this agreement.

(5) The term "Unit Area" shall refer to and include all of the lands, oil and gas leasehold interests and oil and gas interests intended to be developed and operated for oil and gas purposes under this agreement. Such lands, oil and gas leasehold interests and oil and gas interests are described in Exhibit "A".

(6) 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 Unit Area or as fixed by express agreement of the parties.

(7) All exhibits attached to this agreement are made a part of the contract as fully as though copied in full in the contract.

(8) The words "equipment" and "materials" as used here are synonymous and shall mean and include all oil field supplies and personal property acquired for use in the Unit Area.

2. TITLE EXAMINATION, LOSS OF LEASES AND OIL AND GAS INTERESTS

A. Title Examination:

There shall be no examination of title to leases, or to oil and gas interests, except that title to the lease covering the land upon which the exploratory well is to be drilled in accordance with Section 7, shall be examined on a complete abstract record by Operator's attorney, and the title to both the oil and gas lease and to the fee title of the lessors must be approved by the examining attorney, and accepted by all parties. A copy of the examining attorney's opinion shall be sent to each party immediately after the opinion is written, and, also, each party shall be given, as they are written, a copy of all subsequent supplemental attorney's reports. A good faith effort to satisfy the examining attorney's requirements shall be made by the party owning the lease covering the drillsite.

If title to the proposed drillsite is not approved by the examining attorney or the lease is not acceptable for a material reason, and all the parties do not accept the title, the parties shall select a new drillsite for the first exploratory well; provided, if the parties are unable to agree upon another drillsite, this agreement shall, in that case, come to an end and all parties shall then forfeit their rights and be relieved of obligations hereunder. If a new drillsite is selected, title to the oil and gas lease covering it and to the fee title of the lessor shall be examined, and title shall be approved or accepted or rejected in like manner as provided above concerning the drillsite first selected. If title to the oil and gas lease covering the second choice drillsite is not approved or accepted, other drillsites shall be successively selected and title examined, until a drillsite is chosen

to which title is approved or accepted, or until the parties fail to select another drillsite. As in the case of the drillsite first selected, so also with successive choices if the time comes that the parties have not approved title and are unable to agree upon an alternate drillsite, the contract shall, in that case and at that time, come to an end and all parties shall forfeit their rights and be relieved of obligations under this contract.

No well other than the first test shall be drilled in the Unit Area until after (1) the title to the lease covering the lands upon which such well is to be located has been examined by Operator's attorney, and (2) the title has been approved by the examining attorney and the title has been accepted by all of the parties who are to participate in the drilling of the well.

B. Failure of Title:

Should any oil and gas lease, or interest therein, be lost through failure of title, this agreement shall, nevertheless, continue in force as to all remaining leases and interests, and

(1) The party whose lease or interest is affected by the title failure shall bear alone the entire loss and it shall not be entitled to recover from Operator or the other parties any development or operating costs which it may have theretofore paid, but there shall be no monetary liability on its part to the other parties hereto by reason of such title failure; and

(2) There shall be no retroactive adjustment of expenses incurred or revenues received from the operation of the interest which has been lost, but the interests of the parties shall be revised on an acreage basis, as of the time it is determined finally that title failure has occurred, so that the interest of the party whose lease or interest is affected by the title failure will thereafter be reduced in the Unit Area by the amount of the interest lost; and

(3) If the proportionate interests of the other parties hereto in any producing well theretofore drilled on the Unit Area is increased by reason of the title failure, the party whose title has failed shall receive the proceeds attributable to the increase in such interests (less operating costs attributable thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well; and

(4) Should any person not a party to this agreement, who is determined to be the owner of any interest in the title which has failed, pay in any manner any part of the cost of operation, development, or equipment, or equipment previously paid under this agreement, such amount shall be proportionately paid to the party or parties hereto who in the first instance paid the costs which are so refunded; and

(5) Any liability to account to a third party for prior production of oil and gas which arises by reason of title failure shall be borne by the party or parties whose title failed in the same proportions in which they shared in such prior production.

C. Loss of Leases for Causes Other Than Title Failure:

If any lease or interest subject to this agreement be lost through failure to develop or because express or implied covenants have not been performed, or if any lease be permitted to expire at the end of its primary term and not be renewed or extended, or if any lease or interest therein is lost due to the fact that the production therefrom is shut in by reason of lack of market, the loss shall not be considered a failure of title and all such losses shall be joint losses and shall be borne by all parties in proportion to their interests and there shall be no readjustment of interests in the Unit Area.

3. UNLEASED OIL AND GAS INTERESTS

If any party owns an unleased oil and gas interest in the Unit Area, that interest shall be treated for the purpose of this agreement as if it were a leased interest under the form of oil and gas lease attached as "Exhibit "B" and for the primary term therein stated. As to such interests, the owner shall receive royalty on production as prescribed in the form of oil and gas lease attached hereto as Exhibit "B". Such party shall, however, be subject to all of the provisions of this agreement relating to lessees, to the extent that it owns the lessee interest.

4. INTERESTS OF PARTIES

Exhibit "A" lists all of the parties, and their respective percentage or fractional interests under this agreement. Unless changed by other provisions, all costs and liabilities incurred in operations under this contract shall be borne and paid, and all equipment and material acquired in operations on the Unit Area shall be owned, by the parties as their interests are given in Exhibit "A". All production of oil and gas from the Unit Area, subject to the payment of lessor's royalties, shall also be owned by the parties in the same manner.

If the interest of any party in any oil and gas lease covered by this agreement is subject to an overriding royalty, production payment, or other charge over and above the usual one-eighth (⅛) royalty, such party shall assume and alone bear all such excess obligations and shall account for them to the owners thereof out of its share of the working interest production of the Unit Area.

5. OPERATOR OF UNIT

HNG OIL COMPANY shall be the Operator of the Unit Area, and shall conduct and direct and have full control of all operations on the Unit Area as permitted and required by, and within the limits of, this agreement. It shall conduct all such operations in a good and workmanlike manner, but it shall have no liability as Operator to the other parties for losses sustained, or liabilities incurred, except such as may result from gross negligence or from breach of the provisions of this agreement.

6. EMPLOYEES

The number of employees and their selection, and the hours of labor and the compensation for services performed, shall be determined by Operator. All employees shall be the employees of Operator.

7. TEST WELL

On or before the 10th day of December, 19 78, Operator shall commence the drilling of a well for oil and gas in the following location:

660' FNL and 2310' FWL of Section 35, T-23-S, R-28-E,
Eddy County, New Mexico

and shall thereafter continue the drilling of the well with due diligence to the Morrow formation at a total depth of approximately 13,400 feet,

unless granite or other practically impenetrable substance is encountered at a lesser depth or unless all parties agree to complete the well at a lesser depth.

Operator shall make reasonable tests of all formations encountered during drilling which give indication of containing oil and gas in quantities sufficient to test, unless this agreement shall be limited in its application to a specific formation or formations, in which event Operator shall be required to test only the formation or formations to which this agreement may apply.

If in Operator's judgment the well will not produce oil or gas in paying quantities, and it wishes to plug and abandon the test as a dry hole, it shall first secure the consent of all parties to the plugging, and the well shall then be plugged and abandoned as promptly as possible.

8. COSTS AND EXPENSES

Except as herein otherwise specifically provided, Operator shall promptly pay and discharge all costs and expenses incurred in the development and operation of the Unit Area pursuant to this agreement and shall charge each of the parties hereto with their respective proportionate shares upon the cost and expense basis provided in the Accounting Procedure attached hereto and marked Exhibit "C". If any provision of Exhibit "C" should be inconsistent with any provision contained in the body of this agreement, the provisions in the body of this agreement shall prevail.

Operator, at its election, shall have the right from time to time to demand and receive from the other parties payment in advance of their respective shares of the estimated amount of the costs to be incurred in operations hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an itemized statement of such estimated costs, together with an invoice for its share thereof. Each such statement and invoice for the payment in advance of estimated costs shall be submitted on or before the 20th day of the next preceding month. Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest at the rate of ~~six percent (6%)~~ twelve percent (12%) per annum until paid. Proper adjustment shall be made monthly between advances and actual cost, to the end that each party shall bear and pay its proportionate share of actual costs incurred, and no more.

9. OPERATOR'S LIEN

Operator is given a first and preferred lien on the interest of each party covered by this contract, and in each party's interest in oil and gas produced and the proceeds thereof, and upon each party's interest in material and equipment, to secure the payment of all sums due from each such party to Operator.

In the event any party fails to pay any amount owing by it to Operator as its share of such costs and expense or such advance estimate within the time limited for payment thereof, Operator, without prejudice to other existing remedies, is authorized, at its election, to collect from the purchaser or purchasers of oil or gas, the proceeds accruing to the working interest or interests in the Unit Area of the delinquent party up to the amount owing by such party, and each purchaser of oil or gas is authorized to rely upon Operator's statement as to the amount owing by such party.

In the event of the neglect or failure of any non-operating party to promptly pay its proportionate part of the cost and expense of development and operation when due, the other non-operating parties and Operator, within thirty (30) days after the rendition of statements therefor by Operator, shall proportionately contribute to the payment of such delinquent indebtedness and the non-operating parties so contributing shall be entitled to the same lien rights as are granted to Operator in this section. Upon the payment by such delinquent or defaulting party to Operator of any amount or amounts on such delinquent indebtedness, or upon any recovery on behalf of the non-operating parties under the lien conferred above, the amount or amounts so paid or recovered shall be distributed and paid by Operator to the other non-operating parties and Operator proportionately in accordance with the contributions theretofore made by them.

10. TERM OF AGREEMENT

This agreement shall remain in full force and effect for as long as any of the oil and gas leases subjected to this agreement remain or are continued in force as to any part of the Unit Area, whether by production, extension, renewal or otherwise; provided, however, that in the event the first well drilled hereunder results in a dry hole and no other well is producing oil or gas in paying quantities from the Unit Area, then at the end of ninety (90) days after abandonment of the first test well, this agreement shall terminate unless one or more of the parties are then engaged in drilling a well or wells pursuant to Section 12 hereof, or all parties have agreed to drill an additional well or wells under this agreement, in which event this agreement shall continue in force until such well or wells shall have been drilled and completed. If production results therefrom this agreement shall continue in force thereafter as if said first test well had been productive in paying quantities, but if production in paying quantities does not result therefrom this agreement shall terminate at the end of ninety (90) days after abandonment of such well or wells. It is agreed, however, that the termination of this agreement shall not relieve any party hereto from any liability which has accrued or attached prior to the date of such termination.

11. LIMITATION ON EXPENDITURES

Without the consent of all parties: (a) No well shall be drilled on the Unit Area except any well expressly provided for in this agreement and except any well drilled pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the drilling of a well shall include consent to all necessary expenditures in the drilling, testing, completing, and equipping of the well, including necessary tankage; (b) No well shall be reworked, plugged back or deepened except a well reworked, plugged back or deepened pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the reworking, plugging back or deepening of a well shall include consent to all necessary expenditures in conducting such operations and completing and equipping of said well to produce, including necessary tankage; (c) Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of Fifteen Thousand and No/100---------- Dollars ($15,000.00) except in connection with a well the drilling, reworking, deepening, or plugging back of which has been previously authorized by or pursuant to this agreement; provided, however, that in case of explosion, fire, flood, or other sudden emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion are required to deal with the emergency and to safeguard life and property, but Operator shall, as promptly as possible, report the emergency to the other parties. Operator shall, upon request, furnish copies of its "Authority for Expenditures" for any single project costing in excess of $ 5,000.00 .

12. OPERATIONS BY LESS THAN ALL PARTIES

If all the parties cannot mutually agree upon the drilling of any well on the Unit Area other than the test well provided for in Section 7, or upon the reworking, deepening or plugging back of a dry hole drilled at the joint expense of all parties or a well jointly owned by all the parties and not then producing in paying quantities on the Unit Area, any party or parties wishing to drill, rework, deepen or plug back such a well may give the other parties written notice of the proposed operation, specifying the work to be performed, the location, proposed depth, objective formation and the estimated cost of the operation. The parties receiving such a notice shall have thirty (30) days (except as to reworking, plugging back or drilling deeper, where a drilling rig is on location, the period shall be limited to forty-eight (48) hours exclusive of Saturday or Sunday) after receipt of the notice within which to notify the parties wishing to do the work whether they elect to participate in the cost of the proposed operation. Failure of a party receiving such a notice to so reply to it within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.

If any party receiving such a notice elects not to participate in the proposed operation (such party or parties being hereafter referred to as "Non-Consenting Party"), then in order to be entitled to the benefits of this section, the party or parties giving the notice and such other parties as shall elect to participate in the operation (all such parties being hereafter referred to as the "Consenting Parties") shall, within thirty (30) days after the expiration of the notice period of thirty (30) days (or as promptly as possible after the expiration of the 48-hour period where the drilling rig is on location, as the case may be) actually commence work on the proposed operation and complete it with due diligence.

The entire cost and risk of conducting such operations shall be borne by the Consenting Parties in the proportions that their respective interests as shown in Exhibit "A" bear to the total interests of all Consenting Parties. Consenting Parties shall keep the leasehold estates involved in such operations free and clear of all liens and encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such an operation results in a dry hole, the Consenting Parties shall plug and abandon the well at their sole cost, risk and expense. If any well drilled, reworked, deepened or plugged back under the provisions of this section results in a producer of oil and/or gas in paying quantities, the Consenting Parties shall complete and equip the well to produce at their sole cost and risk, and the well shall then be turned over to Operator and shall be operated by it at the expense and for the account of the Consenting Parties. Upon commencement of operations for the drilling, reworking, deepening or plugging back of any such well by Consenting Parties in accordance with the provisions of this section, each Non-Consenting Party shall be deemed to have relinquished to Consenting Parties, and the Consenting Parties shall own and be entitled to receive, in proportion to their respective interests, all of such Non-Consenting Party's interest in the well, its leasehold operating rights, and share of production therefrom until the proceeds or market value thereof (after deducting production taxes, royalty, overriding royalty and other interests payable out of or measured by the production from such well accruing with respect to such interest until it reverts) shall equal the total of the following:

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

(B) 300% of that portion of the costs and expenses of drilling, reworking, deepening or plugging back, testing and completing, after deducting any cash contributions received under Section 25, and 200% of that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections), which would have been chargeable to such Non-Consenting Party if it had participated therein.

In the case of any reworking, plugging back or deeper drilling operation, the Consenting Parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all such equipment shall remain unchanged; and upon abandonment of a well after such reworking, plugging back or deeper drilling, the Consenting Parties shall account for all such equipment to the owners thereof, with each party receiving its proportionate part in kind or in value.

Within sixty (60) days after the completion of any operation under this section, the party conducting the operations for the Consenting Parties shall furnish each Non-Consenting Party with an inventory of the equipment in and connected to the well, and an itemized statement of the cost of drilling, deepening, plugging back, testing, completing, and equipping the well for production; or, at its option, the operating party, in lieu of an itemized statement of such costs of operation, may submit a detailed statement of monthly billings. Each month thereafter, during the time the Consenting Parties are being reimbursed as provided above, the Consenting Parties shall furnish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the operation of the well, together with a statement of the quantity of oil and gas produced from it and the amount of proceeds realized from the sale of the well's working interest production during the preceding month. Any amount realized from the sale or other disposition of equipment newly acquired in connection with any such operation which would have been owned by a Non-Consenting Party had it participated therein shall be credited against the total unreturned costs of the work done and of the equipment purchased, in determining when the interest of such Non-Consenting Party shall revert to it as above provided; if there is a credit balance it shall be paid to such Non-Consenting Party.

If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest the amounts provided for above, the relinquished interests of such Non-Consenting Party shall automatically revert to it and from and after such reversion such Non-Consenting Party shall own the same interest in such well, the operating rights and working interest therein, the material and equipment in or pertaining thereto, and the production therefrom as such Non-Consenting Party would have owned had it participated in the drilling, reworking, deepening or plugging back of said well. Thereafter, such Non-Consenting Party shall be charged with and shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this agreement and the accounting procedure schedule, Exhibit "C", attached hereto.

Notwithstanding the provisions of this Section 12, it is agreed that without the mutual consent of all parties, no wells shall be completed in or produced from a source of supply from which a well located elsewhere on the Unit Area is producing, unless such well conforms to the then-existing well spacing pattern for such source of supply.

The provisions of this section shall have no application whatsoever to the drilling of the initial test well on the Unit Area, but shall apply to the reworking, deepening, or plugging back of the initial test well after it has been drilled to the depth specified in Section 7, if it is, or thereafter shall prove to be, a dry hole or non-commercial well, and to all other wells drilled, reworked, deepened, or plugged back, or proposed to be drilled, reworked, deepened, or plugged back, upon the Unit Area subsequent to the drilling of the initial test well.

13. RIGHT TO TAKE PRODUCTION IN KIND

Each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the Unit Area, exclusive of production which may be used in development and producing operations and in preparing and treating oil for marketing purposes and production unavoidably lost. Each party shall pay or deliver, or cause to be paid or delivered, all royalties, overriding royalties, or other payments due on its share of such production, and shall hold the other parties free from any liability therefor. Any extra expenditure incurred in the taking in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party.

Each party shall execute all division orders and contracts of sale pertaining to its interest in production from the Unit Area, and shall be entitled to receive payment direct from the purchaser or purchasers thereof for its share of all production.

In the event any party shall fail to make the arrangements necessary to take in kind or separately dispose of its proportionate share of the oil and gas produced from the Unit Area, Operator shall have the right, subject to revocation at will by the party owning it, but not the obligation, to purchase such oil and gas or sell it to others for the time being, at not less than the market price prevailing in the area, which shall in no event be less than the price which Operator receives for its portion of the oil and gas produced from the Unit Area. Any such purchase or sale by Operator shall be subject always to the right of the owner of the production to exercise at any time its right to take in kind, or separately dispose of, its share of all oil and gas not previously delivered to a purchaser. Notwithstanding the foregoing, Operator shall not make a sale into interstate commerce of any other party's share of gas production without first giving such other party sixty (60) days notice of such intended sale.

14. ACCESS TO UNIT AREA

Each party shall have access to the Unit Area at all reasonable times, at its sole risk, to inspect or observe operations, and shall have access at reasonable times to information pertaining to the development or operation thereof, including Operator's books and records relating thereto. Operator shall, upon request, furnish each of the other parties with copies of all drilling reports, well logs, tank tables, daily gauge and run tickets and reports of stock on hand at the first of each month, and shall make available samples of any cores or cuttings taken from any well drilled on the Unit Area.

15. DRILLING CONTRACTS

All wells drilled on the Unit Area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. Operator, if it so desires, may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the field, 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 shall be customary and usual in the field in contracts of independent contractors who are doing work of a similar nature.

16. ABANDONMENT OF WELLS

No well, other than any well which has been drilled or reworked pursuant to Section 12 hereof for which the Consenting Parties have not been fully reimbursed as therein provided, which has been completed as a producer shall be plugged and abandoned without the consent of all parties; provided, however, if all parties do not agree to the abandonment of any well, those wishing to continue its operation shall tender to each of the other parties its proportionate share of the value of the well's salvable material and equipment, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. Each abandoning party shall then assign to the non-abandoning parties, without warranty, express or implied, as to title or as to quantity, quality, or fitness for use of the equipment and material, all of its interest in the well and its equipment, together with its interest in the leasehold estate as to, but only as to, the interval or intervals of the formation or formations then open to production. The assignments so limited shall encompass the "drilling unit" upon which the well is located. The payments by, and the assignments to, the assignees shall be in a ratio based upon the relationship of their respective percentages of participation in the Unit Area to the aggregate of the percentages of participation in the Unit Area of all assignees. There shall be no readjustment of interest in the remaining portion of the Unit Area.

After the assignment, the assignors shall have no further responsibility, liability, or interest in the operation of or production from the well in the interval or intervals then open. Upon request of the assignees, Operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and charges contemplated by this agreement, plus any additional cost and charges which may arise as the result of the separate ownership of the assigned well.

17. DELAY RENTALS AND SHUT-IN WELL PAYMENTS

Delay rentals and shut-in well payments which may be required under the terms of any lease shall be paid by the party who has subjected such lease to this agreement, at its own expense. Proof of each payment shall be given to Operator at least ten (10) days prior to the rental or shut-in well payment date. Operator shall furnish similar proof to all other parties concerning payments it makes in connection with its leases. Any party may request, and shall be entitled to receive, proper evidence of all such payments. If, through mistake or oversight, any delay rental or shut-in well payment is not paid or is erroneously paid, and as a result a lease or interest therein terminates, there shall be no monetary liability against the party who failed to make such payment. Unless the party who failed to pay a rental or shut-in well payment secures a new lease covering the same interest within ninety (90) days from the discovery of the failure to make proper payment, the interests of the parties shall be revised on an acreage basis effective as of the date of termination of the lease involved, and the party who failed to make proper payment will no longer be credited with an interest in the Unit Area on account of the ownership of the lease which has terminated. In the event the party who failed to pay the rental or the shut-in well payment shall not have been fully reimbursed, at the time of the loss, from the proceeds of the sale of oil and gas attributable to the lost interest, calculated on an acreage basis, for the development and operating costs theretofore paid on account of such interest, it shall be reimbursed for unrecovered actual costs theretofore paid by it (but not for its share of the cost of any dry hole previously drilled or wells previously abandoned) from so much of the following as is necessary to effect reimbursement:

(1) Proceeds of oil and gas, less operating expenses, theretofore accrued to the credit of the lost interest, on an acreage basis, up to the amount of unrecovered costs;

(2) proceeds, less operating expenses thereafter incurred attributable to the lost interest on an acreage basis, of that portion of oil and gas thereafter produced and marketed (excluding production from any wells thereafter drilled) which would, in the absence of such lease termination, be attributable to the lost interest on an acreage basis, up to the amount of unrecovered costs, the proceeds of said portion of the oil and gas to be contributed by the other parties in proportion to their respective interests; and

(3) any moneys, up to the amount of unrecovered costs, that may be paid by any party who is, or becomes, the owner of the interest lost, for the privilege of participating in the Unit Area or becoming a party to this contract.

Operator shall attempt to notify all parties when a gas well is shut-in or returned to production, but assumes no liability whatsoever for failure to do so.

~~18. PREFERENTIAL RIGHT TO PURCHASE~~

~~Should any party desire to sell all or any part of its interests under this contract, or its rights and in~~terests in the Unit Area, it shall promptly give written notice to the other parties, with full information concerning its proposed sale, which shall include the name and address of the prospective purchaser (who must be ready, willing and able to purchase), the purchase price, and all other terms of the offer. The other parties shall then have an optional prior right, for a period of ten (10) days after receipt of the notice, to purchase on the same terms and conditions the interest which the other party proposes to sell; and, if this optional right is exercised, the purchasing parties shall share the purchased interest in the proportions that the interest of each bears to the total interest of all purchasing parties. However, there shall be no preferential right to purchase in those cases where any party wishes to mortgage its interests, or to dispose of its interests by merger, reorganization, consolidation, or sale of all of its assets, or a sale or transfer of its interests to a subsidiary or parent company, or subsidiary of a parent company, or to any company in which any one party owns a ma~~jority of the stock~~.

19. SELECTION OF NEW OPERATOR

Should a sale be made by Operator of its rights and interests, the other parties shall have the right within sixty (60) days after the date of such sale, by majority vote in interest, to select a new Operator. If a new Operator is not so selected, the transferee of the present Operator shall assume the duties of and act as Operator. In either case, the retiring Operator shall continue to serve as Operator, and discharge its duties in that capacity under this agreement, until its successor Operator is selected and begins to function, but the present Operator shall not be obligated to continue the performance of its duties for more than 120 days after the sale of its rights and interests has been completed.

20. MAINTENANCE OF UNIT OWNERSHIP

For the purpose of maintaining uniformity of ownership in the oil and gas leasehold interests covered by this contract, and notwithstanding any other provisions to the contrary, no party shall sell, encumber, transfer or make other disposition of its interest in the leases embraced within the Unit Area and in wells, equipment and production unless such disposition covers either:

(1) the entire interest of the party in all leases and equipment and production; or

(2) an equal undivided interest in all leases and equipment and production in the Unit Area.

Every such sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement, and shall be made without prejudice to the rights of the other parties.

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

21. RESIGNATION OF OPERATOR

Operator may resign from its duties and obligations as Operator at any time upon written notice of not less than ninety (90) days given to all other parties. In this case, all parties to this contract shall select by majority vote in interest, not in numbers, a new Operator who shall assume the responsibilities and duties, and have the rights, prescribed for Operator by this agreement. The retiring Operator shall deliver to its successor all records and information necessary to the discharge by the new Operator of its duties and obligations.

22. LIABILITY OF PARTIES

The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the Unit Area. Accordingly, the lien granted by each party to Operator in Section 9 is given to secure only the debts of each severally. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership or association, or to render them liable as partners.

23. RENEWAL OR EXTENSION OF LEASES

If any party secures a renewal of any oil and gas lease subject to this contract, each and all of the other parties shall be notified promptly, and shall have the right to participate in the ownership of the renewal lease by paying to the party who acquired it their several proper proportionate shares of the acquisition cost, which shall be in proportion to the interests held at that time by the parties in the Unit Area.

If some, but less than all, of the parties elect to participate in the purchase of a renewal lease, it shall be owned by the parties who elect to participate therein, in a ratio based upon the relationship of their respective percentage of participation in the unit area to the aggregate of the percentages of participation in the unit area of all parties participating in the purchase of such renewal lease. Any renewal lease in which less than all the parties elect to participate shall not be subject to this agreement.

Each party who participates in the purchase of a renewal lease shall be given an assignment of its proportionate interest therein by the acquiring party.

The provisions of this section shall apply to renewal leases whether they are for the entire interest covered by the expiring lease or cover only a portion of its area or an interest therein. Any renewal lease taken before the expiration of its predecessor lease, or taken or contracted for within six (6) months after the expiration of the existing lease shall be subject to this provision; but any lease taken or contracted for more than six (6) months after the expiration of an existing lease shall not be deemed a renewal lease and shall not be subject to the provisions of this section.

The provisions in this section shall apply also and in like manner to extensions of oil and gas leases.

24. SURRENDER OF LEASES

The leases covered by this agreement, in so far as they embrace acreage in the Unit Area, shall not be surrendered in whole or in part unless all parties consent.

However, should any party desire to surrender its interest in any lease or in any portion thereof, and other parties not agree or consent, the party desiring to surrender shall assign, without express or implied warranty of title, all of its interest in such lease, or portion thereof, and any well, material and equipment which may be located thereon and any rights in production thereafter secured, to the parties not desiring to surrender it. Upon such assignment, the assigning party shall be relieved from all obligations thereafter accruing, but not theretofore accrued, with respect to the acreage assigned and the operation of any well thereon, and the assigning party shall have no further interest in the lease assigned and its equipment and production. The parties assignee shall pay to the party assignor the reasonable salvage value of the latter's interest in any wells and equipment on the assigned acreage, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. If the assignment is in favor of more than one party, the assigned interest shall be shared by the parties assignee in the proportions that the interest of each bears to the interest of all parties assignee.

Any assignment or surrender made under this provision shall not reduce or change the assignors' or surrendering parties' interest, as it was immediately before the assignment, in the balance of the Unit Area; and the acreage assigned or surrendered, and subsequent operations thereon, shall not thereafter be subject to the terms and provisions of this agreement.

25. ACREAGE OR CASH CONTRIBUTIONS

If any party receives while this agreement is in force a contribution of cash toward the drilling of a well or any other operation on the Unit Area, such contribution shall be paid to the party who conducted the drilling or other operation and shall 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 the contribution is made shall promptly execute an assignment of the acreage, without warranty of title, to all parties to this agreement in proportion to their interests in the Unit Area at that time, and such acreage shall become a part of the Unit Area and be governed by all the provisions of this contract. Each party shall promptly notify all other parties of all acreage or money contributions it may obtain in support of any well or any other operation on the Unit Area.

26. PROVISION CONCERNING TAXATION

Each of the parties hereto elects, under the authority of Section 761(a) of the Internal Revenue Code of 1954, to be excluded from the application of all of the provisions of Subchapter K of Chapter 1 of Subtitle A of the Internal Revenue Code of 1954. If the income tax laws of the state or states in which the property covered hereby is located contain, or may hereafter contain, provisions similar to those contained in the Subchapter of the Internal Revenue Code of 1954 above referred to under which a similar election is permitted, each of the parties agrees that such election shall be exercised. Each party authorizes and directs the Operator to execute such an election or elections on its behalf and to file the election with the proper governmental office or agency. If requested by the Operator so to do, each party agrees to execute and join in such an election.

Operator shall render for ad valorem taxation all property subject to this agreement which by law should be rendered for such taxes, and it shall pay all such taxes lawfully assessed thereon. ~~[illegible]~~ Operator shall bill all other parties for their proportionate share of all tax payments in the manner provided in Exhibit "C".

If any tax assessment is considered unreasonable by Operator, it may at its discretion protest such valuation within the time and manner prescribed by law, and prosecute the protest to a final determination, unless all parties agree to abandon the protest prior to final determination. When any such protested valuation shall have been finally determined, Operator shall pay the assessment for the joint account, together with interest and penalty accrued, and the total cost shall then be assessed against the parties, and be paid by them, as provided in Exhibit "C".

27. INSURANCE

At all times while operations are conducted hereunder, Operator shall comply with the Workmen's Compensation Law of the State where the operations are being conducted. Operator shall also carry or provide insurance for the benefit of the joint account of the parties as may be outlined in Exhibit "D" attached to and made a part hereof. Operator shall require all contractors engaged in work on or for the Unit Area to comply with the Workmen's Compensation Law of the State where the operations are being conducted and to maintain such other insurance as Operator may require.

In the event Automobile Public Liability Insurance is specified in said Exhibit "D", or subsequently receives the approval of the parties, no direct charge shall be made by Operator for premiums paid for such insurance for operator's fully owned automotive equipment.

28. CLAIMS AND LAWSUITS

If any party to this contract is sued on an alleged cause of action arising out of operations on the Unit Area, or on an alleged cause of action involving title to any lease or oil and gas interest subjected to this contract, it shall give prompt written notice of the suit to the Operator and all other parties.

The defense of lawsuits shall be under the general direction of a committee of lawyers representing the parties, with Operator's attorney as Chairman. Suits may be settled during litigation only with the joint consent of all parties. No charge shall be made for services performed by the staff attorneys for any of the parties, but otherwise all expenses incurred in the defense of suits, together with the amount paid to discharge any final judgment, shall be considered costs of operation and shall be charged to and paid by all parties in proportion to their then interests in the Unit Area. Attorneys, other than staff attorneys for the parties, shall be employed in lawsuits involving Unit Area operations only with the consent of all parties; if outside counsel is employed, their fees and expenses shall be considered Unit Area expense and shall be paid by Operator and charged to all of the parties in proportion to their then interests in the Unit Area. The provisions of this paragraph shall not be applied in any instance where the loss which may result from the suit is treated as an individual loss rather than a joint loss under prior provisions of this agreement, and all such suits shall be handled by and be the sole responsibility of the party or parties concerned.

Damage claims caused by and arising out of operations on the Unit Area, conducted for the joint account of all parties, shall be handled by Operator and its attorneys, the settlement of claims of this kind shall be within the discretion of Operator so long as the amount paid in settlement of any one claim does not exceed one thousand ($1000.00) dollars and, if settled, the sums paid in settlement shall be charged as expense to and be paid by all parties in proportion to their then interests in the Unit Area.

29. 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 make money payments, 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 affected party shall use all possible diligence to remove the force majeure as quickly as possible.

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.

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, explosion, governmental restraint, 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.

30. NOTICES

All notices authorized or required between the parties, and required by any of the provisions of this agreement, shall, unless otherwise specifically provided, be given in writing by United States mail or Western Union Telegram, postage or charges prepaid, and addressed to the party to whom the notice is given at the

addresses listed on Exhibit "A". The originating notice to be given under any provision hereof shall be deemed given only when received by the party to whom such notice is directed and the time for such party to give any notice in response thereto shall run from the date the originating notice is received. The second or any responsive notice shall be deemed given when deposited in the United States mail or with the Western Union Telegraph Company, with postage or charges prepaid. 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.

31. OTHER CONDITIONS, IF ANY, ARE:

31-A. TAXES ON PRODUCTION

At and during such time or times as Non-Operator is exercising the right to take in kind or separately dispose of its proportionate part of the production as set forth in Section 13 hereof, Non-Operator shall pay or arrange for the payment of all production, severance, gathering, sales or similar taxes imposed upon such part.

At and during such time or times as Operator or any other party is purchasing or selling another Non-Operator's proportionate part of production, as set forth in said Section 13, Operator or the party or parties receiving or selling said production, shall pay or arrange for the payment of all production, severance, gathering, sales or similar taxes imposed upon such party and shall deduct the amount of tax so paid from any proceeds due the owner of such production.

31-B. BURDENS CREATED SUBSEQUENT TO THIS AGREEMENT

Notwithstanding anything herein to the contrary, if any working interest owner shall, subsequent to the execution of this agreement, create an overriding royalty, production payment, net proceeds interest, carried interest, or any other interest out of its working interest (hereinafter called "subsequently created interest"), such subsequently created interest shall be specifically made subject to all the terms and provisions of this agreement. If the working interest owner from which such subsequently created interest is created (a) fails to pay when due its share of costs and expenses chargeable hereunder, and its share of production accruing hereunder is insufficient to cover such costs and expenses, or (b) elects to go nonconsent under Section 12, or (c) elects to abandon a well under Section 16 hereof, elects to surrender a lease under Section 24 hereof, or otherwise withdraws from this agreement, the subsequently created interest shall be chargeable with a pro-rata portion of all costs and expenses hereunder in the same manner as if such subsequently created interest were a working interest, and Operator shall have the right to enforce against such subsequently created interest the lien and all other rights granted in Section 9 hereof for the purpose of collecting costs and expenses chargeable to the subsequently created interest.

31-C. FAIR EMPLOYMENT PRACTICES

In connection with the performance of work under this Operating Agreement, Operator agrees to comply fully with all provisions of Executive Order 11246 of September 24, 1965. A copy of the Equal Employment Opportunity Provision as set out in said order is attached hereto as Exhibit "E".

31-D. COMPLIANCE WITH ALL LAWS, RULES AND REGULATIONS

Operator agrees to comply fully with all applicable laws, rules and regulations pertaining to operations conducted pursuant to this agreement.

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

_____

~~XXXXXX~~

_____
JACK L. RUSSELL

_____
RICHARD S. GADDY

_____
ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

By: _____

_____

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: Cliff Ohr
Cliff Ohr, Attorney-in-Fact

~~XXXXXX~~

JACK L. RUSSELL

RICHARD S. GADDY

ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

By:

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O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~ASSISTANT~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

~~ASSISTANT~~

_____

Jack L. Russell
JACK L. RUSSELL

_____

RICHARD S. GADDY

_____

ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

By: _____

_____

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

_____

~~XXXXXX~~

_____

JACK L. RUSSELL

_____

RICHARD S. GADDY

_____

ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

_____

By: _____

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

_____

~~XXXXXX~~

_____
JACK L. RUSSELL

_____
RICHARD S. GADDY

_____
ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

_____

By: _____

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

~~XXXXXX~~

_____
JACK L. RUSSELL

_____
RICHARD S. GADDY

_____
ROBERT J. JOHNSTON

ATTEST:

Ann Frazier
Ann Frazier, Assistant Secretary

D.D.D.F. COMPANY, INC.

By: E. H. Mills, Jr.
E. H. Mills, Jr., President

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

O P E R A T O R

HNG OIL COMPANY

ATTEST:

~~XXXXXX~~

Judy Walters
Assistant Secretary

By: J. Stewart Martin
J. Stewart Martin, Vice President

N O N-O P E R A T O R

PHILLIPS PETROLEUM COMPANY

ATTEST:

By: _____

_____

~~XXXXXX~~

_____ JACK L. RUSSELL

_____ RICHARD S. GADDY

_____ ROBERT J. JOHNSTON

ATTEST:

D.D.D.F. COMPANY, INC.

_____ By: _____

Robert B. Coleman
ROBERT B. COLEMAN

EXHIBIT "A"

Attached to and made a part of Operating Agreement dated December 1, 1978 between HNG Oil Company, Operator, and Phillips Petroleum Company, et al, Non-Operators

1. (A) LANDS SUBJECT TO CONTRACT

The North Half (N/2) of Section 35, T-23-S, R-28-E, Eddy County, New Mexico

(B) RESTRICTIONS AS TO DEPTH

The base of the Morrow formation at an approximate depth of 13,400 feet

2. INTEREST OF THE PARTIES

	Working Interest Percentage
HNG Oil Company	61.521875%
Phillips Petroleum Company	35.353125%
Jack L. Russell	.390625%
Richard S. Gaddy	.390625%
Robert J. Johnston	.390625%
DDDF Company, Inc.	.390625%
Robert B. Coleman	1.562500%
	100.000000%

3. ADDRESSES OF THE PARTIES

HNG Oil Company
P. O. Box 2267
Midland, Texas 79702

Phillips Petroleum Company
4001 Tenbrook
Odessa, Texas 79762

Jack L. Russell
P. O. Box 1604
Midland, Texas 79702

Richard S. Gaddy
P. O. Box 2572
Midland, Texas 79702

Robert J. Johnston
P. O. Box 1535
Kerrville, Texas 78028

DDDF Company, Inc.
P. O. Box 465
Midland, Texas 79702

Robert B. Coleman
P. O. Box 501
Midland, Texas 79702

EXHIBIT "B"

Attached to and made a part of Operating Agreement
dated December 1, 1978 between HNG Oil Company, Operator,
and Phillips Petroleum Company, et al, Non-Operators

NONE

COPAS — 1974
Recommended by the Council of Petroleum Accountants Societies of North America
COPAS

EXHIBIT "C"

Attached to and made a part of Operating Agreement dated December 1, 1978 between HNG Oil Company, Operator, and Phillips Petroleum Company, et al, 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 of North America.

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

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. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.

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 rate of twelve percent (12%) per annum 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.

5. Audits

A. Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit Operator's accounts and records relating to the Joint Account for any calendar year within the twenty-four (24) month period following the end of such calendar year; provided, however, the making of an audit shall not extend the time for the taking of written exception to and the adjustments of accounts as provided for in Paragraph 4 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make every reasonable effort to conduct joint or simultaneous audits in a manner which will result in a minimum of inconvenience to the Operator. Operator shall bear no portion of the Non-Operators' audit cost incurred under this paragraph unless agreed to by the Operator.

6. Approval by Non-Operators

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

II. DIRECT CHARGES

Operator shall charge the Joint Account with the following items:

1. Rentals and Royalties

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

2. Labor

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

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

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

B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II. Such costs under this Paragraph 2B may be charged on a "when and as paid basis" or by "percentage assessment" on the amount of salaries and wages chargeable to the Joint Account under Paragraph 2A of this Section II. If percentage assessment is used, the rate shall be based on the Operator's cost experience.

C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are applicable to Operator's costs chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II.

D. Personal Expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II.

3. Employee Benefits

Operator's current costs of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II shall be Operator's actual cost not to exceed twenty per cent (20%).

4. Material

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

5. Transportation

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

A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be made to the Joint Account for a distance greater than the distance from the nearest reliable supply store, recognized barge terminal, or railway receiving point where like material is normally available, unless agreed to by the Parties.

B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint Account for a distance greater than the distance to the nearest reliable supply store, recognized barge terminal, or railway receiving point unless agreed to by the Parties. No charge shall be made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by the Parties.

C. In the application of Subparagraphs A and B above, there shall be no equalization of actual gross trucking cost of $200 or less excluding accessorial charges.

6. Services

The cost of contract services, equipment and utilities provided by outside sources, except services excluded by Paragraph 9 of Section II and Paragraph 1. ii of Section III. The cost of professional consultant services and contract services of technical personnel directly engaged on the Joint Property if such charges are excluded from the Overhead rates. The cost of professional consultant services or contract services of technical personnel not directly engaged on the Joint Property shall not be charged to the Joint Account unless previously agreed to by the Parties.

7. Equipment and Facilities Furnished by Operator

A. Operator shall charge the Joint Account for use of Operator owned equipment and facilities at rates commensurate with costs of ownership and operation. Such rates shall include costs of maintenance, repairs, other operating expense, insurance, taxes, depreciation, and interest on investment not to exceed eight per cent (8%) per annum. Such rates shall not exceed average commercial rates currently prevailing in the immediate area of the Joint Property.

B.. In lieu of charges in Paragraph 7A above, Operator may elect to use average commercial rates prevailing in the immediate area of the Joint Property less 20%. For automotive equipment, Operator may elect to use rates published by the Petroleum Motor Transport Association.

8. Damages and Losses to Joint Property

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

9. Legal Expense

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

10. Taxes

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

11. Insurance

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

12. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator in the necessary and proper conduct of the Joint Operations.

III. OVERHEAD

1. Overhead - Drilling and Producing Operations

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

(X) Fixed Rate Basis, Paragraph 1A, or

( ) Percentage Basis, Paragraph 1B.

Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under Paragraph 2A, Section II. The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the Overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by the Parties as a direct charge to the Joint Account.

ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant services and contract services of technical personnel directly employed on the Joint Property shall ( ) shall not (X) be covered by the Overhead rates.

A. Overhead - Fixed Rate Basis

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

Drilling Well Rate $ 2398.00

Producing Well Rate $ 318.00

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

(a) Drilling Well Rate

[1] Charges for onshore drilling wells shall begin on the date the well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days.

[2] Charges for offshore drilling wells shall begin on the date when drilling or completion equipment arrives on location and terminate on the date the drilling or completion equipment moves off location or rig is released, whichever occurs first, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days

[3] Charges for wells undergoing any type of workover or recompletion for a period of five (5) consecutive days or more shall be made at the drilling well rate. Such charges shall be applied for the period from date workover operations, with rig, commence through date of rig release, except that no charge shall be made during suspension of operations for fifteen (15) or more consecutive days.

(b) Producing Well Rates

[1] An active well either produced or injected into for any portion of the month shall be considered as a one-well charge for the entire month.

[2] Each active completion in a multi-completed well in which production is not commingled down hole shall be considered as a one-well charge providing each completion is considered a separate well by the governing regulatory authority.

[3] An inactive gas well shut in because of overproduction or failure of purchaser to take the production shall be considered as a one-well charge providing the gas well is directly connected to a permanent sales outlet.

[4] A one-well charge may be made for the month in which plugging and abandonment operations are completed on any well.

[5] All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease allowable, transferred allowable, etc.) shall not qualify for an overhead charge.

(3) The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the calendar year preceding as shown by the index of average weekly earnings of Crude Petroleum and Gas Fields Production Workers as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian index as published by Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

B. Overhead - Percentage Basis

(1) Operator shall charge the Joint Account at the following rates:

(a) Development

_____ Percent (%) of the cost of Development of the Joint Property exclusive of costs provided under Paragraph 9 of Section II and all salvage credits.

(b) Operating

_____ Percent (%) of the cost of Operating the Joint Property exclusive of costs provided under Paragraphs 1 and 9 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

(2) Application of Overhead - Percentage Basis shall be as follows:
For the purpose of determining charges on a percentage basis under Paragraph 1B of this Section III, development shall include all costs in connection with drilling, redrilling, deepening or any remedial operations on any or all wells involving the use of drilling crew and equipment; also, preliminary expenditures necessary in preparation for drilling and expenditures incurred in abandoning when the well is not completed as a producer, and original cost of construction or installation of fixed assets, the expansion of fixed assets and any other project clearly discernible as a fixed asset, except Major Construction as defined in Paragraph 2 of this Section III. All other costs shall be considered as Operating.

2. Overhead - Major Construction

To compensate Operator for overhead costs incurred in the construction and installation of fixed assets, the expansion of fixed assets, and any other project clearly discernible as a fixed asset required for the development and operation of the 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 $ * :

A. * % of total costs if such costs are more than $ * but less than $ * ; plus

B. * % of total costs in excess of $ * but less than $1,000,000; plus

C. * % of total costs in excess of $1,000,000. *TO BE NEGOTIATED

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 shall be excluded.

3. 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 reason, 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 bases exclusive of cash discounts:

A. New Material (Condition A)

(1) Tubular goods, except line pipe, shall be priced at the current new price in effect on date of movement on a maximum carload or barge load weight basis, regardless of quantity transferred, equalized to the lowest published price f.o.b. railway receiving point or recognized barge terminal nearest the Joint Property where such Material is normally available.

(2) Line Pipe

(a) Movement of less than 30,000 pounds shall be priced at the current new price, in effect at date of movement, as listed by a reliable supply store nearest the Joint Property where such Material is normally available.

(b) Movement of 30,000 pounds or more shall be priced under provisions of tubular goods pricing in Paragraph 2A (1) of this Section IV.

(3) Other Material shall be priced at the current new price, in effect at date of movement, as listed by a reliable supply store or f.o.b. railway receiving point nearest the Joint Property where such Material is normally available.

B. Good Used Material (Condition B)

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

(1) Material moved to the Joint Property

(a) At seventy-five percent (75%) of current new price, as determined by Paragraph 2A of this Section IV.

(2) Material moved from the Joint Property

(a) At seventy-five percent (75%) of current new price, as determined by Paragraph 2A of this Section IV, if Material was originally charged to the Joint Account as new Material, or

EXHIBIT "E"

Attached to and made a part of Operating Agreement
dated December 1, 1978 between HNG Oil Company, Operator,
and Phillips Petroleum Company, et al, Non-Operators

Equal Employment Opportunity Provision

During the performance of this contract, Operator (HNG OIL COMPANY) agrees as follows:

1. The Operator will not discriminate against any employees or applicant for employment because of race, color, religion, sex, or national origin. The Operator will take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex, or national origin. Such action shall include, but not be limited to, the following: employment, upgrading, demotion, or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The Operator agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided by the contracting officer setting forth the provisions of this nondiscrimination clause.

2. The Operator will, in all solicitations or advertisements for employees placed by or on behalf of the Operator, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex, or national origin.

3. The Operator will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice to be provided by the agency contracting officer, advising the labor union or workers' representative of the Operator's commitments under Section 202 of Executive Order 11246 of September 24, 1965, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

4. The Operator will comply with all provisions of Executive Order 11246 of September 24, 1965, and of the rules, regulations, and relevant orders of the Secretary of Labor.

5. The Operator will furnish all information and reports required by Executive Order 11246 of September 24, 1965, and by the rules, regulations, and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records, and accounts by the contracting agency and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations, and orders.

6. In the event of the Operator's noncompliance with the nondiscrimination clauses of this contract or with any of such rules, regulations, or orders, this contract may be cancelled, terminated, or suspended in whole or in part, and the Operator may be declared ineligible for further Government contracts in accordance with procedures authorized in Executive Order 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in Executive Order 11246 of September 24, 1965, or by rule, regulation, or order of the Secretary of Labor, or as otherwise provided by law.

7. The Operator will include the provisions of paragraphs (1) through (7) in every subcontract or purchase order unless exempted by rules, regulations, or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order 11246 of September 24, 1965, so that such provisions will be binding upon each subcontractor or vendor. The Operator will take such action with respect to any subcontract or purchase order as the contracting agency may direct as a means of enforcing such provisions including sanctions for noncompliance: Provided, however, that in the event the Operator becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the contracting agency, the Operator may request the United States to enter into such litigation to protect the interests of the United States.

(b) at sixty-five percent (65%) of current new price, as determined by Paragraph 2A of this Section IV, if Material was originally charged to the Joint Account as good used Material at seventy-five percent (75%) of current new price.

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

C. Other Used Material (Condition C and D)

(1) Condition C

Material which is not in sound and serviceable condition and not suitable for its original function until after reconditioning shall be priced at fifty percent (50%) of current new price as determined by Paragraph 2A of this Section IV. The cost of reconditioning shall be charged to the receiving property, provided Condition C value plus cost of reconditioning does not exceed Condition B value.

(2) Condition D

All other Material, including junk, shall be priced at a value commensurate with its use or at prevailing prices. Material no longer suitable for its original purpose but usable for some other purpose, shall be priced on a basis comparable with that of items normally used for such other purpose. Operator may dispose of Condition D Material under procedures normally utilized by the Operator without prior approval of Non-Operators.

D. Obsolete Material

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

E. Pricing Conditions

(1) Loading and unloading costs may be charged to the Joint Account at the rate of fifteen cents (15¢) per hundred weight on all tubular goods movements, in lieu of loading and unloading costs sustained, when actual hauling cost of such tubular goods are equalized under provisions of Paragraph 5 of Section II.

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

3. Premium Prices

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

4. Warranty of Material Furnished by Operator

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

V. INVENTORIES

The Operator shall maintain detailed records of Controllable Material.

1. Periodic Inventories, Notice and Representation

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

2. Reconciliation and Adjustment of Inventories

Reconciliation of a physical inventory with the Joint Account shall be made, and a list of overages and shortages shall be furnished to the Non-Operators within six months following the taking of the inventory. Inventory adjustments shall be made by Operator with the Joint Account for overages and shortages, but Operator shall be held accountable only for shortages due to lack of reasonable diligence.

3. Special Inventories

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

4. Expense of Conducting Periodic Inventories

The expense of conducting periodic Inventories shall not be charged to the Joint Account unless agreed to by the Parties.

EXHIBIT "D"

Attached to and made a part of Operating Agreement
dated December 1, 1978 between HNG Oil Company, Operator,
and Phillips Petroleum Company, et al, Non-Operators

INSURANCE

Operator shall at all times during the term of this agreement carry insurance to protect the parties hereto as follows:

(1) Workman's compensation and occupational disease insurance as required by the laws of the state or states in which operations will be conducted and employers' liability insurance with a limit of not less than $100,000.00. Such insurance policy shall be endorsed to preclude exercise of rights of subrogation against parties to this agreement.

(2) Comprehensive general public liability insurance, excluding products, liability insurance, with limits of not less than $100,000.00 applicable to bodily injury, sickness or death of any one person and $300,000.00 for more than one person in any one accident, and $100,000.00 for loss of or damage to property in any one accident and $100,000.00 aggregate limit applicable to all loss of or damage to property during the policy period.

(3) Automobile public liability insurance covering all automotive equipment used in performance of work under this agreement with limits of not less than $100,000.00 applicable to bodily injury, sickness or death of any one person and $300,000.00 for more than one person in any one accident, and $100,000.00 for loss of or damage to property in any one accident.

If automotive equipment used is owned exclusively by Operator, no charge will be made to the Joint Account for premiums for this coverage except as provided in Section III, Paragraph 5 of the Accounting Procedure.

Operator shall require all contractors performing work under this agreement to carry the following insurance:

(1) Workmen's compensation and occupational disease insurance as required by the laws of the state or states in which operations will be conducted and employers' liability insurance with a limit of not less than $100,000.00.

(2) Comprehensive general public liability insurance with limits of not less than $100,000.00 applicable to bodily injury, sickness or death of any one person and $300,000.00 for more than one person in any one accident, and $100,000.00 for loss of or damage to property in any one accident and $100,000.00 aggregate limit applicable to all loss of or damage to property during the policy period.

(3) Automobile public liability insurance covering all automotive equipment used in performance of work under this agreement with limits of not less than $100,000.00 applicable to bodily injury, sickness or death of any one person and $300,000.00 for more than one person in any one accident, and $100,000.00 for loss of or damage to property in any one accident.

Operator acknowledges that it may be required to file Standard Form 100 (EEO-1) promulgated jointly by the Office of Federal Contract Compliance, the Equal Employment Opportunity Commission and Plans for Progress with Joint Reporting Committee, Federal Depot, Jeffersonville, Indiana, within thirty (30) days of the date of contract award if such report has not been filed for the current year and otherwise comply with or file such other compliance reports as may be required under Executive Order 11246, as amended and Rules and Regulations adopted thereunder.

Operator further acknowledges that he may be required to develop a written affirmative action compliance program as required by the Rules and Regulations approved by the Secretary of Labor under authority of Executive Order 11246 and supply Non-Operators with a copy of such program if they so request.

Operator assures Non-Operators that it does not and will not maintain or provide for its employees any segregated facilities at any of its establishments, and that it does not and will not permit its employees to perform their services at any location, under its control, where segregated facilities are maintained. For this purpose, it is understood that the phrase "segregated facilities" includes facilities which are in fact segregated on a basis of race, color, religion, or national origin, because of habit, local custom or otherwise. It is further understood and agreed that maintaining or providing segregated facilities for its employees or permitting its employees to perform their services at any location under its control where segregated facilities are maintained is a violation of the equal opportunity clause required by Executive Order 11246 of September 24, 1965.

Operator further understands and agrees that a breach of the assurance herein contained subjects it to the provisions of the Order at 41 CFR Chapter 60 of the Secretary of Labor dated May 21, 1968, and the provisions of the equal opportunity clause enumerated in contracts between the United States of America and Non-Operators.

Whoever knowingly and willfully makes any false, fictitious or fraudulent representation may be liable to criminal prosecution under 18 U.S.C. § 1001.

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Form 2636-S 1-77

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ASSIGNMENT AND AGREEMENT

THIS ASSIGNMENT AND AGREEMENT, made and entered into this 26th day of June, 19 78, by and between PHILLIPS PETROLEUM COMPANY, a Delaware corporation, with an operating office at Bartlesville, Oklahoma, Party of the First Part, hereinafter called "Phillips", and

HNG OIL COMPANY

P. O. Box 2267

Midland, Texas 79702

Party of the Second Part, hereinafter called "Second Party", whether one or more.

Phillips is the owner of a certain oil and gas lease (or leases) insofar as the same covers the lands described in Exhibit "A" hereto attached and by reference made a part hereof, which oil and gas lease (or leases) is briefly described in Exhibit "A". Reference is made to said lease (or leases) and to the record thereof for all of the terms and covenants thereof.

Phillips desires to have the lands above referred to tested for oil and gas production and Second Party has expressed its willingness to make such a test on the terms and under the conditions hereinafter set out.

NOW, THEREFORE, in consideration of the mutual covenants and agreements hereinafter set forth and further in consideration of the mutual benefits to Phillips and Second Party, the parties hereto agree as follows:

I

ASSIGNMENT

Phillips, subject to the conditions, exceptions, reservations, covenants and agreements hereinabove set forth, does hereby assign and transfer unto Second Party, without representation or warranty of title, either express or implied, all of its right, title and interest in and to the oil and gas lease (or leases) described in Exhibit "A" insofar as said oil and gas lease (or leases) covers and pertains to the oil, gas and casinghead gas, and all rights pertaining thereto, in those parts of Section 3, Township 24 South, Range 28E, N.M.P.M., Eddy County, New Mexico, only which are covered by said lease described in Exhibit "A" from the surface of the ground down to and including the base of the Pennsylvanian formation.

the rights so assigned being hereinafter sometimes referred to as the "assigned premises". This assignment is made subject to all overriding royalties, production payments and other encumbrances described in Exhibit "A" as well as any additional valid and existing overriding royalties, production payments and other encumbrances which may appear of record. It is expressly understood that all leasehold rights under said oil and gas lease (or leases) not herein specifically assigned are excepted from this assignment and reserved and retained unto Phillips, its successors and assigns.

II

RESERVATION OF OVERRIDING ROYALTY

Phillips hereby excepts from the within assignment and reserves and retains unto itself, its successors and assigns, as an overriding royalty: five percent (5%) of eight-eighths of all oil, gas and casinghead gas produced and save from the depths set out above which is attributable to the land described in Exhibit "A". In the event the interest assigned in the oil and gas leases described in Exhibit "A" cover less than the entire oil and gas leasehold estate in such land behind each well, then the overriding royalty herein reserved to Phillips shall be the same proportion of five percent of eight-eighths that the interest herein assigned in the oil and gas leases hereinabove assigned bear to the full oil and gas leasehold estate in each such proration unit. The overriding royalty reserved herein is over and above all currently existing lessors royalties, overriding royalties, production payments, other payments out of production from the depths herein assigned from the lands described in Exhibit "A".

Said overriding royalty shall be delivered to Phillips in the pipe line to which the well or wells on said assigned premises may be connected, free and clear of all risks incident to and all expense of drilling, testing, developing, operating and maintaining the assigned premises, and free and clear of all liens, transportation charges, storage charges and other charges and expenses, and free and clear of all taxes, except that said overriding royalty interest shall bear its proportionate part of any gross production, severance and/or ad valorem taxes. The proceeds of said overriding royalty interest shall be paid monthly direct to Phillips at its office at Bartlesville, Oklahoma, by the purchaser or purchasers of said production.

III

PERFORMANCE OF COVENANTS

Second Party accepts this assignment and agreement subject to all of the terms, provisions and conditions hereof and of the oil and gas lease (or leases) described in Exhibit "A" and of intermediate assignments thereof, if any, and Second Party assumes and agrees to fully comply with and timely perform each and every duty, obligation and covenant, both express and implied, provision and condition of said oil and gas lease (or leases) and of intermediate assignments thereof, if any, imposed upon the lessee and/or assignee thereby insofar as concerns the assigned premises, and Second Party agrees to drill any and all wells which may be necessary to protect the assigned premises from drainage by wells on adjacent lands. Second Party further agrees to save, protect and hold Phillips harmless at all times from all damages and all penalties which may arise or be adjudged against it on Second Party's failure or refusal to comply fully and faithfully with each and every duty, obligation and covenant of said lease (or leases) and of intermediate assignments thereof, if any, imposed upon the lessee and/or assignee thereby insofar as concerns the assigned premises.

IV

INSURANCE AND INDEMNITY

Second Party at all times during the life of this agreement shall:
Comply with all applicable Federal and State Workmen's Compensation Act or Acts; and shall purchase and maintain the following insurance:

(a) General Public Liability Insurance, including contractor's protective liability insurance, with bodily injury limits of not less than $100,000 each person, $300,000 any one accident and property damage limit of not less than $100,000 any one accident;
(b) Automobile Public Liability Insurance with bodily injury limits of not less than $100,000 each person and $300,000 any one accident and property damage limit of not less than $100,000 any one accident;
(c) Such additional insurance, if any, as may be required under Article XVIII.

No recitation of any amount or amounts herein shall be construed to in any manner limit Second Party's liability under this agreement.

Prior to commencing any operations under this agreement, Second Party shall furnish certificates satisfactory to Phillips certifying full compliance with the above requirements. Certificates of insurance shall specify that in the event of cancellation or material change in coverage at least ten (10) days' prior written notice shall be given Phillips at its Exploration office in Odessa, Texas.

Second Party agrees to indemnify Phillips and save and hold it harmless from and against any and all claims for property damage of all character including, but not limited to, damages caused to land, stock, crops, fences, buildings, structures and other improvements, from and against any and all claims for damages or injuries to persons including, but not limited to, employees of Second Party resulting from or arising out of the operations conducted or caused or permitted to be conducted by Second Party on or in connection with the lands described in Exhibit "A", and from and against any and all claims for labor and materials and any other costs and expense in connection with Second Party's operations hereunder which are not expressly assumed by Phillips in this agreement.

V

TEST WELL

Second Party agrees that on or before October 1, 1978 it will commence or cause to be commenced the actual drilling of a well for oil and gas at the following location: at a location 1980 feet from the west line and 660 feet from the south line of Section 3, Township 24 South, Range 28 East, Eddy County, New Mexico.

and that it will thereafter continue the drilling of said well with due diligence to the following depth: to a depth sufficient to thoroughly test the Morrow formation or to a total depth of thirteen thousand (13,000) feet, whichever is the shallower depth.

Said well shall be completed to produce into the tanks or pipe line to which it may be connected or, if a dry hole, shall be plugged and abandoned and the premises restored in a lawful manner with due diligence Said well shall be drilled, tested and completed or, if a dry hole, shall be plugged and abandoned and the premises restored in a good and workmanlike manner, including the removal of all leasehold material and debris placed on said premises by Second Party and the restoration of the property by filling and leveling the cellar and slush pits, and all drilling and other operations shall be performed at the sole cost, risk and expense of Second Party.

VI

DEFAULT

In the event Second Party shall fail or refuse to commence the well for which provision hereinabove is made within the time herein specified, or, having commenced said well, shall fail or refuse to drill and complete the same to the depth, within the time and in the manner provided in this agreement, then and thereupon, in addition to all other remedies which Phillips may have and notwithstanding anything in this agreement to the contrary, the aforesaid assignment and this agreement as to all of said assigned premises shall terminate and the lease (or leases) on the assigned premises shall revert to Phillips, if Phillips shall so elect and shall evidence such election by giving notice in writing to Second Party at its address hereinabove given or by filing such notice for record in any county or parish in which any lease described in Exhibit "A" is recorded. If Phillips shall so elect to terminate such assignment and this agreement, Second Party agrees that upon demand it will forthwith reassign the lease (or leases) on the assigned premises to Phillips, warranting the same to be free and clear of all liens, claims, clouds and encumbrances caused, suffered or created by, through or under Second Party; provided, however, that the termination of this assignment and agreement and the reassignment of said lease (or leases) on the assigned premises to Phillips shall not operate to relieve Second Party from liability to Phillips for any damage Phillips may sustain as a result of the breach by Second Party of the terms of this assignment and agreement.

VII

CONCURRENT RIGHTS OF INGRESS AND EGRESS

The parties hereto, their successors and assigns, shall have equal and concurrent rights of ingress and egress on the lands described in Exhibit "A" for the purpose of exploring for, drilling for, mining, producing and marketing the minerals owned by each of the parties hereto from their respective depths, as hereinabove defined, under the oil and gas lease (or leases) described in Exhibit "A". And further said parties shall own and hold equally any and all rights granted by said oil and gas lease (or leases) as incident to and for the purpose of mining, exploring for, drilling for and producing the minerals owned by them from said respective depths, including the right to lay and maintain pipe lines, water lines, dig pits, erect structures and to do and perform any and all other things incident to the rights and interests of the parties hereto in said respective depths, hereinabove defined. The aforesaid rights shall be exercised in such a manner as not to interfere unduly with the similar rights of the other party hereto.

VIII

RELINQUISHMENT OF RESERVED RIGHTS

In the event Phillips elects to surrender or relinquish the leasehold estate herein reserved unto it in numerical paragraph I hereof in all or any part of the lands described in Exhibit "A", it may, at its election, execute and deliver unto Second Party an assignment, without warranty of title, either express or implied, of said reserved leasehold estate in that part of said lands which Phillips desires to surrender or relinquish. Second Party agrees to accept such assignment and file the same for record in the county (ies) or parish (es) where said land is located; such assignment shall not affect any other interests, reservations or rights of Phillips provided for in this agreement.

IX

DELAY RENTALS AND SHUT-IN WELL PAYMENTS

So long as Phillips retains the leasehold estate reserved to it in Article I hereof in any of the lands described in Exhibit "A" Phillips shall pay all delay rentals which may become due and payable under the terms of the lease (or leases) described in Exhibit "A" necessary to maintain the same in force as to the lands in which the leasehold estate of Phillips is so retained; provided, Phillips shall not be liable to any extent for erroneous payment or inadvertent failure to pay any such delay rentals. Upon being billed therefor Second Party shall reimburse Phillips for one-half (1/2) of all delay rentals so paid on the acreage subject to this agreement. Second Party at its sole cost, agrees to timely pay any and all shut-in well payments necessary to maintain in force the oil and gas lease (or leases) described in Exhibit "A" with respect to any well or wells drilled by Second Party on the assigned premises. Second Party agrees to immediately notify Phillips by Western Union telegram, to its Exploration office at Bartlesville, Oklahoma, at any time a well is completed on the assigned premises which is capable of producing but is not produced and at any time production from the assigned premises ceases for any reason.

Second Party agrees to immediately furnish to Phillips at its Exploration office in Bartlesville, Oklahoma, a photostatic copy of any and all instruments of whatsoever character served on Second Party which evidence a change in the ownership of delay rentals or royalties payable under the oil and gas lease (or leases) described in Exhibit "A".

If after the completion of the test well provided for above one party hereto desires to continue a lease in force and effect by the payment of delay rentals and the other party does not desire to join in the payment of such rentals, then the party not desiring to join in the payment of such rentals shall notify the other party in writing at its address hereinabove given at least thirty (30) days prior to the rental payment date given in said lease. The party receiving said notice shall have fifteen (15) days after receipt thereof within which to elect to receive an assignment of the lease insofar as the same covers lands described in Exhibit "A" from the party who elects not to pay delay rentals. In the event Second Party does not elect to pay delay rentals and it is not then in default in the performance of its duties and obligations under the terms of said lease and under the terms of this agreement, and Phillips shall have elected to receive an assignment from Second Party, then Second Party, upon receipt of notice thereof, shall execute, acknowledge and deliver unto Phillips a proper assignment of said lease covering its entire interest therein, warranting the same to be free and clear of all liens, claims, clouds and encumbrances caused, suffered or created by, through or under Second Party. In the event Phillips shall elect not to pay delay rentals, then upon receipt of notice that Second Party desires an assignment, Phillips shall execute, acknowledge and deliver unto Second Party a proper assignment of the leasehold estate reserved unto Phillips in Article I hereof in and to said lease insofar as the same covers the lands described in Exhibit "A"; such assignment shall not affect any other interests, reservations or rights of Phillips provided for in this agreement. In the event, however, both parties elect not to pay delay rentals under said lease, they shall execute a joint release thereof.

X

GEOLOGICAL DATA

Representatives of Phillips shall have access to all wells, including the test well provided for above, which may be drilled, worked over, deepened or plugged back on the assigned premises and acreage pooled therewith and the logs thereof at any and all times and shall be furnished with samples from such horizons in such wells as may be requested by Phillips and such drilling reports, reports relating to work-over, deepening or plugging back operations and other information regarding the progress of said wells as may be desired by Phillips. If said test well shall be drilled with rotary tools, tests shall be made at intervals of five hundred (500) feet from the top of the hole to the ultimate depth thereof to determine the angle of deflection of the hole from vertical, and Second Party agrees to maintain the hole within four degrees (4°) of the vertical. Second Party agrees to save representative formation samples at approximately ten (10) foot intervals in said test well and all other wells drilled on the assigned premises and to keep the drilling mud in condition to bring representative samples to the surface. Phillips shall have the right to make velocity determinations or other physical measurements in any and all wells drilled on the assigned premises, said determinations or measurements to be made at the expense and upon the responsibility of Phillips. Second Party agrees to have an electrical log survey made, by a reputable and qualified service company, of the test well provided for above and all other wells drilled on the assigned premises from the base of the shallowest surface casing to the greatest depth to which each of said wells is finally drilled. Second Party shall furnish Phillips with copies of all logs made in connection with the drilling of said test well and all other wells drilled on the assigned premises, including drillers' logs, electrical logs and other logs containing information desired by Phillips; provided, however, that all electrical logs shall be furnished to Phillips immediately upon the completion of an electrical log survey. Second Party shall, in good and workmanlike manner, core or test promptly all prospective oil and/or gas formations which may be encountered in the drilling of said test well. If Second Party shall take any cores while drilling said test well, it shall furnish Phillips with representative samples thereof and Phillips shall have the right to run core analyses on all such samples. If Second Party shall make any drill stem tests in said test well, it shall furnish Phillips with the details of all such tests. In the event any show of oil and/or gas is encountered in the drilling of said test well, Second Party forthwith and before drilling or testing the formation where the show was encountered shall notify Phillips at its Exploration office at Odessa, Texas, in sufficient time that Phillips may, if it so desires, have a representative present when such formation is penetrated and/or tested.

In the event any well or wells drilled pursuant to this agreement shall be drilled on acreage other than the assigned premises, including but not limited to a unit well drilled on a unit of which the assigned premises or any portion thereof is a part, all of the provisions of the Article X relating to the test well shall apply to such well if it is the test well and all of such provisions relating to a well other than the test well shall apply to such well if it is a well other than the test well.

XI

LOCATION NOTICE

Second Party shall notify Phillips at its Exploration office at Odessa, Texas, in writing, at once, of (a) the location of the well for which provision is hereinbefore made, when fixed, by giving the distances and directions thereof from at least two governmental or recognized survey lines, and (b) the date of spudding (commencement of actual drilling) of said well.

XII

CALL ON PRODUCTION

Phillips shall have the right at all times and from time to time, at its election, to purchase all or any part of the crude oil and/or distillate production from any wells drilled on any portion of the assigned premises at price of highest bona fide offer for crude oil and/or distillate of like grade and gravity produced in the field.

In addition to the call on production provided for above, and in the event such call on production is not exercised as to gas well gas and/or casinghead gas, Phillips shall also have the exclusive right at all times and from time to time, at its election, to purchase the right to process, or have processed, all or any part of the gas well gas and/or casinghead gas production from any wells drilled on any portion of the assigned premises. In any sale or disposition of its share of gas from acreage covered hereby, Second Party will retain the right to process or have processed the natural gas stream for the extraction of natural gas liquids and to retain the liquids removed by such processing. Such right to process, or have processed, shall permit the location of processing facilities at any point selected by Phillips on the gas purchaser's system downstream from the wellhead, which point shall generally be in or near the field of production but which may be sufficiently removed from place of production as to permit the construction of a processing plant under normal conditions on hard ground (whether or not other gas may have been commingled with gas hereunder prior to such point of processing).

In the event Phillips elects to process, or have processed, the gas, then (a) Phillips shall own all natural gas liquids extracted and shall pay to Second Party, its successor or assign, a percentage of the value of the natural gas liquids extracted from Second Party's share of such gas which is equivalent to the highest bona fide offer made to Second Party, its successor or assign, by anyone else for such rights on said gas. In the absence of such bona fide offer for said rights, (b) Phillips shall own all natural gas liquids extracted and shall pay Second Party for the value of the volume of gas shrinkage (including plant fuel) resulting from processing Second Party's share of such gas (based upon the price specified in the gas sales contract as hereinafter defined), plus one-eighth of the value of the liquids so removed and saved and sold by Phillips, its successor or assign (said value to be the actual authorized sales price for all such products, f.o.b. processing plant fence, after deducting the payment for gas shrinkage, sales cost, discounts and allowances and, in the case of tank car shipments of LPG only, tank car rental of 3/8¢ per gallon); provided, however, that Second Party, its successor or assign, shall have the option of accepting the same basis for payment (reasonably adjusted for differences in quality and quantity of gas and conditions of delivery) as is made by Phillips, its successor or assign, to other parties for processing similar gas in said plant.

The price specified in the gas sales contract may be subject to regulation by state or federal regulatory bodies having jurisdiction. The phrase 'price specified in the gas sales contract' as used herein shall mean only that portion of the price then being collected by Second Party which is not subject to possible future refund by Second Party. If Second Party is later determined to be entitled to retain all or part of the amount collected subject to refund and is relieved from all further obligation to refund with respect thereto, Phillips shall recalculate the value of the volume of gas shrinkage based on the price Second Party is so permitted to retain and shall pay Second Party the difference, without interest, between the recalculated value and the amount previously paid Second Party therefor.

In the event Second Party, its successor or assign, desires to process, or have processed, its share of such gas, then within one hundred twenty (120) days after written notice of such desire by Second Party, its successor or assign, to Phillips, Phillips shall advise in writing whether or not Phillips elects to process, or have processed, said gas as herein provided. In the event Phillips does not elect to process, or have processed, such gas, then the gas processing rights granted to Phillips under this Article XII shall thereupon terminate, provided, however, that if within the period of one hundred and twenty (120) days following relinquishment of the processing rights by Phillips, Second Party shall not itself commence processing such gas or contract with a third party or parties for processing such gas, then the relinquishment of the processing rights by Phillips shall become ineffective and Phillips shall again have the right as provided above, to elect whether or not it will process or have processed such gas.

In the event Second Party, its successor or assign, enters into more than one contract for the sale or disposition of its share of such gas, or if any contract so made provides for delivery into two or more different systems of the purchaser, or if Second Party, its successor or assign, in any way makes more than one disposition of such gas, then the rights herein granted to Phillips, its successor or assign, shall be separate with respect to each such contract, system or disposition.

XIII
EXTENSIONS AND RENEWALS

All interests, reservations and rights of Phillips in and to the lands described in Exhibit "A" and the production therefrom provided for in this agreement shall extend not only to the oil and gas lease(or leases) described in Exhibit "A", but also to any and all extensions or renewals of said oil and gas lease (or leases) which may be acquired by Second Party. The term "extensions" of the aforesaid oil and gas lease (or leases) as used herein shall be deemed to include, but not by way of limitation, any agreement or agreements of whatsoever character acquired by Second Party under and by virtue of which said oil and gas lease (or leases) is continued in force. The term "renewals" of the aforesaid oil and gas lease (or leases) as used herein shall be deemed to include, but not by way of limitation, any lease or leases acquired by Second Party on all or any part of the lands described in Exhibit "A" within twelve (12) months from the date of termination or expiration of said lease (or leases) or any extensions or renewals thereof. Second Party agrees to execute such further grants and assurances as may be requisite to vest in Phillips under any such extensions or renewals the same rights and interests in and to the lands described in Exhibit "A" and the production therefrom as are reserved by or granted to Phillips under the provisions of this agreement.

XIV
PREFERENTIAL RIGHT TO PURCHASE

In the event Second Party (or any one or more of them, if more than one) shall at any time desire to sell all or any part of its interest in and to the assigned premises or shall have a bona fide offer from a purchaser to purchase all or any part of such interest at a price that is acceptable to Second Party, then Second Party shall furnish to Phillips at its Exploration office at Odessa, Texas, a copy of the signed bona fide offer or price that is acceptable to Second Party. Phillips shall have fifteen (15) days after receipt of such notice within which to elect to purchase said interest at the same bona fide price and under the same terms and conditions as offered by said prospective purchaser or at the price that is acceptable to Second Party. Such right of purchase shall be accepted or rejected by Phillips by letter posted in the United States post office and addressed to Second Party at its address hereinbefore given with said period of fifteen (15) days. If Phillips shall elect to purchase said interest, upon receipt of notice of such election to purchase Second Party shall duly execute, acknowledge and deliver unto Phillips a proper assignment of such interest and Phillips, upon approval of title thereto, shall pay the stipulated price therefor. If, within the time above specified, Phillips shall notify Second Party that it does not elect to purchase such interest or Phillips shall fail or neglect to notify Second Party, which failure or neglect shall be construed to mean that Phillips does not elect to purchase such interest, then, in either event, Second Party shall be at liberty to sell and assign such interest to some other purchaser at the same bona fide price and under the same terms and conditions as offered to Phillips for such interest; provided, however, that if such interest is not disposed of by Second Party within thirty (30) days after the expiration of said period of fifteen (15) days, Second Party shall not thereafter dispose of any part of its interest without again offering the same to Phillips as above provided.

The preferential right of Phillips to purchase as provided herein shall extend to any sale by a purchaser from Second Party and to any sale by any subsequent purchaser, and the waiver by Phillips of its rights hereunder as to any sale shall not constitute a waiver of such rights as to any subsequent sale and shall be conditioned upon (a) the assignee's delivery to Phillips, as soon as possible, of a certified copy of the assignment, (b) that the assignment be made expressly subject to all of the terms and conditions of this agreement, and (c) the express assumption by assignee of all of the obligations imposed by this agreement upon Second Party.

XV

ABANDONMENT

Second Party shall not at any time abandon, relinquish, surrender or let expire its leasehold estate in any part or all of the assigned premises or plug and abandon the last producing well or well capable of producing on the assigned premises without first giving Phillips written notice at its Exploration office in

Houston, Texas , of such

desire and intention at least sixty (60) days before said leasehold estate is to be abandoned, relinquished, surrendered or permitted to expire or the last producing well or well capable of producing is to be plugged and abandoned, and Phillips shall have thirty (30) days after receipt of such notice within which to notify Second Party at its address hereinabove given whether or not Phillips elects to take over said leasehold estate of Second Party; it being understood that in the event Phillips shall elect to take over said leasehold estate of Second Party and there shall be a well or wells thereon belonging to Second Party, Phillips shall have the right to take over any such well or wells by paying Second Party the salvage value of all materials in such well or wells so taken over by Phillips; provided, however, Phillips shall not be required to make payment therefor until Phillips shall have approved or accepted title to said leasehold interest of Second Party. If Phillips shall fail or neglect to so notify Second Party at its address hereinabove given of such election within said thirty (30) day period it shall be deemed that Phillips does not elect to take over said leasehold estate. If Phillips shall elect to take over said leasehold estate covering any part or all of said premises and accept an assignment thereof from Second Party, and Phillips elects not to take over any particular well or wells located thereon, then before assigning said leasehold interest to Phillips, Second Party shall plug and abandon any and all wells which Phillips does not elect to take over, and shall, within a reasonable time thereafter, remove all leasehold material and debris placed on said premises by Second Party and restore the property by filling and leveling the cellar and slush pits, all at the risk and expense of Second Party. Upon the election of Phillips to take over the leasehold interest of Second Party in any part or all of said premises, Second Party shall deliver unto Phillips a proper assignment of such leasehold estate, warranting the same to be free and clear of all liens, claims, clouds and encumbrances caused, suffered or created by, through or under Second Party.

Nothing herein contained, express or implied, shall ever be construed as relieving Second Party from any of its obligations under this agreement.

XVI

USE OF PHILLIPS PRODUCTS

Second Party agrees to purchase from Phillips, if available at competitive prices, terms and conditions, all gasoline, oil, greases and other products marketed by Phillips necessary for Second Party's drilling operations and other operations in connection with the well provided for above and in connection with all its further and future operations on the assigned premises.

XVII

AD VALOREM TAXES

If the assigned premises have been assessed for ad valorem taxes such taxes shall be prorated on a calendar year basis and Phillips shall pay such taxes for the current year, Second Party shall be liable for its proportionate share of the full amount of taxes so paid and shall reimburse Phillips upon being billed therefor. Second Party assumes the payment of all ad valorem taxes, if any, for all subsequent years.

XVIII
OTHER PROVISIONS

XVIII-A. Second Party agrees that in the event the well herein above provided for in Article V is completed as a gas well, it will within ninety (90) days after reaching total depth in said well commence or cause to be commenced the actual drilling of a well for oil and/or gas at a location of its selection in the north half of Section 3, Township 24 South, Range 28 East, and that it will continue the drilling of said well with due diligence to a depth sufficient to thoroughly test the deepest zone or horizon which is then producing or shall have produced oil and/or gas in the well provided for in Article V. Such well shall be drilled within the same time and in the same manner as provided above for the well provided for in Article V, and all other terms and provisions of this Assignment and Agreement shall apply to the well hereinabove provided for in Article V above and shall also apply to the well provided for in this Article XVIII-A.

XVIII-B. Second Party hereby agrees that, in the event the well hereinabove provided for in Article V above is completed as a gas well, it will forthwith allocate to said well a proration unit covering the south half (S/2) Section 3, Township 24 South, Range 28 East, Eddy County, New Mexico. Second Party further agrees that, in the event the well hereinabove provided for in Article XVIII-A above is completed as a gas well, it will forthwith allocate to said well a proration unit covering the north half of Section 3, Township 24 South, Range 28 East, Eddy County, New Mexico.

XVIII-C. In the event the well hereinabove provided for in Article V above is not completed as a gas well, Second Party agrees that it will, within ninety (90) days from reaching total depth in said well commence or cause to be commenced the actual drilling of a well for oil and/or gas at a location of Second Party's selection in Section 3, Township 24 South, Range 28 East, which is on some part of the land covered by the leases set out in Exhibit "A". Said well shall be drilled at the sole cost, risk and expense of Second Party and shall be drilled to a depth sufficient to thoroughly test the deepest zone or horizon from which the well provided for in Article V is then producing or shall have once produced oil and/or gas. In the event the well provided for in Article V shall not have produced oil and/or gas, the well provided for in this Article XVIII-C shall be drilled to the same depth as provided for said well.

XVIII-D. At such time as ninety (90) days have passed between reaching total depth in any well drilled under the provisions of this Assignment and Agreement without commencement of actual drilling of a well for oil and/or gas on some part of Section 3, T-24 South, Range 24 East, Second Party agrees that it will forthwith reassign to Phillips all right, title and interest assigned to it in Article I above in any non-producing half-section or half sections (north half and/or south half of Section 3, T-24S, R-28E) insofar as such right, title and interest is covered by the oil and gas leases described in Exhibit "A". "Non-producing half section" as used herein means any half section which does not have located thereon a well capable of producing oil or gas.

At the same time, Second Party agrees that, in the event any of the wells drilled and completed as a producer of oil and/or gas pursuant to the terms of Article V, XVIII-A or XVIII-C is not drilled to a depth sufficient that the top of the Mississippian formation is indicated on a log of the well bore, it will reassign to Phillips all right, title and interest in and to the oil and gas leases described in Exhibit "A" insofar as such leases cover any part of said Section 3 from one hundred feet below the total depth drilled in each such well down to and including the base of the Pennsylvanian formation as follows:

(1) In the event such well is the well provided for in Article V, the reassignment shall cover the rights set out above in the south half of said Section 3.

(2) In the event such well is the well provided for in Article XVIII-A, the reassignment shall cover the rights set out above in the north half of Section 3.

(3) In the event such well is the well provided for in Article XVIII-C, the reassignment shall cover the rights set out above as to all of said Section 3.

XVIII-E. In the event Second Party shall fail or refuse to drill, test and complete the well provided for in Article V (and the well provided for in Article XVIII-C if applicable) within the time and in the manner set out therein, Second Party shall forthwith reassign to Phillips all right, title and interest assigned to it in Article I above, insofar as such rights cover and pertain to any of the lands in Section 3, T-24 South, Range 28 East, Eddy County, New Mexico. In the event Second Party shall fail or refuse to drill, test and complete the well provided for in Article XVIII-A, above, Second Party shall forthwith reassign to Phillips all right, title and interest in the lands covered by the leases described in Exhibit "A" in the north half of said Section 3. Such reassignment(s) provided for in this Article XVIII-E shall constitute the sole remedy for default, and subject to the provisions of Article III above, Second Party shall not be liable in damages for failure to drill any well provided for in Article V, XVIII-A or XVIII-C.

XVIII-F. In each of the reassignments provided for in Articles XVIII-D and XVIII-E, Second Party agrees that it will warrant all rights reassigned to be free and clear of all liens, claims, clouds and encumbrances caused or created by, through or under Second Party or its assignees. Each such reassignment shall be on a form acceptable to Phillips' attorneys.

XVIII-G. Any provisions in Article XIV of this Assignment and Agreement to the contrary, notwithstanding, it is understood and agreed between the parties hereto that Second Party shall have the right to assign all or any part of its interest in the land in Section 3 covered by the leases described in Exhibit "A" without offering the same to Phillips at any time prior to commencement of the well provided for in Article V above, provided, that an executed copy of such assignment is furnished Phillips and such assignment is made expressly subject to all of terms and conditions of this Assignment and Agreement and the assignee expressly assumes all of the obligations imposed by this Assignment upon Second Party.

XVIII-H. At such time as Second Party shall have produced and saved from each of the wells hereinabove provided for in Articles V and XVIII-A or XVIII-C, oil, gas and casinghead gas of a total "market value" equal to 100% of the costs and expenses of drilling, testing and completing said well, plus 100% of the costs of operation of each said well, Second Party shall immediately notify Phillips in writing and Phillips shall have sixty (60) days following the receipt of each such notice to notify Second Party whether or not it elects to receive from Second Party an assignment of an undivided interest as follows:

(1) If the well which has produced the amount set out above is the well which shall have been drilled pursuant to Article V above, and the well has been completed as a gas well, the assignment shall convey an undivided one-half of the proportion obtained when the net oil and gas leasehold acres on the south half of Section 3, T-24S, R-28E, covered by the oil and gas leases described in Exhibit "A" is divided by the total acres in the south half of said Section 3. Such Assignment shall convey that interest in the south half of said Section 3.

(2) If the well which has produced the amount set out above is the well which shall have been drilled pursuant to Article XVIII-A, and said well has been completed as a gas well, the reassignment shall convey in the north half of Section 3, T-24S, R-28E one-half of the proportion obtained when the net oil and gas leasehold acres in the north half of said Section 3, T-24S, R-28E, which are covered by oil and gas leases described in Exhibit "A" is divided by the total acres in the north half of said Section 3. Such Assignment shall convey that interest in the north half of said Section 3.

(3) If the well which has produced the amount set out above is any well drilled pursuant to the terms and provisions of this Assignment and Agreement which has been completed as an oil well and the proration unit allocated to such well contains any part of the land in Section 3, T-24S, R-28E, which is covered by any of the leases described in Exhibit "A", such reassignment shall convey one-half of the proportion obtained when the net oil and gas leasehold acres in the proration unit which are covered by the leases described in Exhibit "A" is divided by the total acres in the proration unit allocated to such well. Such Assignment shall convey that interest in the proration unit allocated to the well.

In each reassignment as set out under (1), (2) or (3) above, such assignments shall also convey to Phillips an interest in the well and all lease equipment and personal property located thereon or appurtenant to the area reassigned equal to the interest in the proration unit which is reassigned.

Each such assignment shall become effective at 7:00 a.m. on the date each well has produced the amounts set out above. Each such assignment shall cover all depths held by Second Party in the land conveyed which are then owned by Second Party through the assignment in Article I.

If Phillips shall notify Second Party that it elects not to receive assignment of such interest in any such half section or proration unit and well located thereon, or if Phillips shall fail or neglect to notify Second Party within the sixty (60) day period hereinabove specified, then, and in either event, it shall be deemed that Phillips does not elect to receive an assignment of an interest in the land allocated to such well and the well on such land and all other terms and provisions of this Assignment and Agreement shall continue in full force and effect as to such well and half section the same as before such election. In the event Phillips shall elect to receive any or all of such assignments, the overriding royalty reserved to Phillips in Article II above shall terminate as to each such tract of land in which an interest is assigned on the effective date of such assignment.

In determining the "market value" of production from each such well for the purposes of this Article XVIII-H there shall be deducted the royalties paid to the lessors under terms of the Oil and Gas Leases set out in Exhibit "A" and the overriding royalty paid to Phillips pursuant to the terms and provisions of Article II above and gross production taxes paid by Second Party on such production, but no other deduction of any kind or character shall be made.

During the time Second Party is recovering its costs and expenses as set forth above, Second Party shall furnish Phillips, Attention: Director, Joint Interest Operations, Exploration and Production Division, 419 Frank Phillips Building, Bartlesville, Oklahoma 74004, a monthly itemized statement reflecting the costs and expenses incurred in the development, operation, and maintenance of each said well, the production sold, production on hand and run tickets fully disclosing the type, quality and quantity of production and disposition thereof. The costs incurred by Second Party in the development, operation and maintenance of each said well shall be determined in accordance with the provisions of the Accounting Procedure attached as Exhibit "C" to the Operating Agreement attached hereto and made a part hereof.

In the event Phillips elects to accept the assignment(s) hereinabove provided, it is understood and agreed that such assignment(s) from Second Party to Phillips may not be made and delivered until after the date Second Party shall have recovered the amounts herein specified. Nevertheless, as between the parties hereto, effective at 7:00 a.m. on the date Second Party has recovered it costs and expenses from the proceeds of production from a well as herein provided, Phillips shall be entitled to receive the proceeds of that part of the working interest production attributable to the interest assigned to Phillips less its share of the costs of operation of said well, and Second Party's obligation to pay Phillips an overriding royalty on production from the proration unit around said well pursuant to Article II above shall cease. An appropriate adjustment of accounts shall be made between the parties to accomplish the purposes herein set forth and Second Party shall pay to Phillips any and all amounts due it.

XVIII-I. In the event a assignment of any land described in Exhibit "A" is made pursuant to the provisions of Article XVIII-H, the Operating Agreement attached hereto as Exhibit "B" shall become effective as to said assigned acreage as of the date of the assignment to Phillips provided for above in Article XVIII-H. Upon the date the Operating Agreement becomes effective, Articles III, IV, X, XI and XV of this Assignment and Agreement will no longer apply to the acreage subject to the Operating Agreement, provided, however, that the last grammatical paragraph of Article IV shall remain in effect as to all matters covered therein arising prior to such date.

XVIII-J. It is understood and agreed between the parties hereto that, while Phillips is not retaining a call on gas production, the price of gas produced under terms of this Agreement shall be the highest of (a) highest market price paid or offered for gas of comparable quality in the field where produced when run; or (b) the gross price paid or offered to the producer.

XIX

ENTIRE AGREEMENT

The terms of this agreement constitute the entire contract of the parties and there are no agreements, undertakings, obligations, promises, assurances or conditions, whether precedent or otherwise, except those specifically set forth.

XX

HEADINGS FOR CONVENIENCE

The paragraph headings used in this agreement are inserted for convenience only and shall be disregarded in construing this agreement.

XXI

TIME FOR EXECUTION

If this agreement is not duly executed by Second Party and returned to Phillips within fifteen (15) days from the date hereof, then and thereupon, this assignment and agreement, at the option of Phillips, shall be null and void and of no effect.

XXII

SUCCESSORS AND ASSIGNS

The terms, covenants and conditions hereof shall be deemed to be covenants running with the leasehold estate hereinabove referred to and as such shall extend to, bind and inure to the benefit of the parties hereto, their heirs, administrators, executors, personal representatives, successors and assigns.

EXECUTED as of the day and year first above written.

HNG OIL COMPANY

By: J. Stewart Martin, Vice President

ATTEST:

Judy Walters
Asst. Secretary

PHILLIPS PETROLEUM COMPANY

By Cliff Ohr, Its Attorney In Fact

THE STATE OF TEXAS §

COUNTY OF MIDLAND §

BEFORE ME, the undersigned authority, a Notary Public in and for said County and State, on this day personally appeared J. Stewart Martin of HNG OIL COMPANY known to me to be the person whose name is subscribed to the fopregoing instrument, and acknowledged to me that the same was the act of the said HNG OIL COMPANY, a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the 19 day of July, 1978.

My Commission Expires:

1-28-79

Notary Public in and for Midland County, Texas

THE STATE OF TEXAS §

COUNTY OF HARRIS §

BEFORE ME, the undersigned authority, a Notary Public in and for said County and State, on this day personally appeared Cliff Ohr, of PHILLIPS PETROLEUM COMPANY, known to me to be the person whose name is subscribed to the fopregoing instrument, and acknowledged to me that the same was the act of the said PHILLIPS PETROLEUM COMPANY, a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the 28th day of June, 1978.

My Commission Expires:

E. LAMAR BRITTON
Notary Public in and for Harris County, Texas
My Commission Expires June 30, 1978
Bonded by Alexander Lovell, Lawyers Surety Corp.

EXHIBIT "A"

ATTACHED TO AND MADE A PART OF ASSIGNMENT AND AGREEMENT DATED JUNE 26, 1978,
BY AND BETWEEN PHILLIPS PETROLEUM COMPANY AND HNG OIL COMPANY

LEASE NO.	DATED	LESSOR	LESSEE	RECORDED BOOK	RECORDED PAGE
C-140636	June 10, 1971	S. F. Williams, et ux	L. D. Williams, Glen B. Williams and James W. Williams	82	192
G-140636-A01	June 29, 1971	Wayne Cowden, et al	" " "	82	567
G-140636-B01	June 24, 1971	Joe H. Beeman, et al	" " "	82	195
G-140636-C01	August 2, 1971	Ernest A. Hanson, et al	" " "	82	198
G-140636-D01	October 7, 1971	Dorothy Lee	" " "	82	570
G-140636-E01	October 7, 1971	A. S. Blauw, et ux	" " "	82	573
G-140636-F01	October 21, 1971	George W. Littlefield	" " "	82	576
G-143981-A01	September 10, 1973	The Bishop Whipple Schools Successor to Shattuck School	E. S. Grear	108	211
G-143984	September 10, 1973	Dean Chafee, Guardian of the Estate of Tressie E. Chafee, Widow of Harry Jay Chafee	E. S. Grear	107	121
G-143988	September 6, 1973	Addie Swearingen, a single woman	E. S. Grear	107	472
G-143981	August 15, 1973	Guillermo Ruiz, et ux	E. S. Grear	105	822

All book and page recording data on this Exhibit "A" refer to Miscellaneous Records of Eddy County, New Mexico.

A.A.P.L. FORM 610

MODEL FORM OPERATING AGREEMENT—1956

Non-Federal Lands

EXHIBIT "B"

ATTACHED TO AND MADE A PART OF ASSIGNMENT AND AGREEMENT DATED THE 26TH DAY OF JUNE, 1978, BY AND BETWEEN PHILLIPS PETROLEUM COMPANY AND HNG OIL COMPANY

OPERATING AGREEMENT

DATED

26th DAY OF JUNE, 19 78,

FOR UNIT AREA IN TOWNSHIP 24 SOUTH, RANGE 28 EAST,

EDDY COUNTY, STATE OF NEW MEXICO.

AMERICAN ASSOCIATION OF PETROLEUM LANDMEN
APPROVED FORM. A.A.P.L. NO. 610
MAY BE ORDERED DIRECTLY FROM THE PUBLISHER
ROSS - MARTIN COMPANY, BOX 800, TULSA 74101

A.A.P.L. FORM 610

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A.A.P.L. FORM 610

OPERATING AGREEMENT

THIS AGREEMENT, entered into this 26th day of JUNE, 19 78, between HNG OIL COMPANY,

hereafter designated as "Operator", and the signatory parties other than Operator.

WITNESSETH, THAT:

WHEREAS, the parties to this agreement are owners of oil and gas leases covering and, if so indicated, unleased mineral interests in the tracts of land described in Exhibit "A", and all parties have reached an agreement to explore and develop these leases and interests for oil and gas to the extent and as hereinafter provided;

NOW, THEREFORE, it is agreed as follows:

1. DEFINITIONS

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

(1) The words "party" and "parties" shall always mean a party, or parties, to this agreement.

(2) The parties to this agreement shall always be referred to as "it" or "they", whether the parties be corporate bodies, partnerships, associations, or persons real.

(3) The term "oil and gas" shall include oil, gas, casinghead gas, gas condensate, and all other liquid or gaseous hydrocarbons, unless an intent to limit the inclusiveness of this term is specifically stated.

(4) The term "oil and gas interests" shall mean unleased fee and mineral interests in tracts of land lying within the Unit Area which are owned by parties to this agreement.

(5) The term "Unit Area" shall refer to and include all of the lands, oil and gas leasehold interests and oil and gas interests intended to be developed and operated for oil and gas purposes under this agreement. Such lands, oil and gas leasehold interests and oil and gas interests are described in Exhibit "A".

(6) 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 Unit Area or as fixed by express agreement of the parties.

(7) All exhibits attached to this agreement are made a part of the contract as fully as though copied in full in the contract.

(8) The words "equipment" and "materials" as used here are synonymous and shall mean and include all oil field supplies and personal property acquired for use in the Unit Area.

2. TITLE EXAMINATION, LOSS OF LEASES AND OIL AND GAS INTERESTS

A. Title Examination:

~~Each party other than Operator shall promptly submit to Operator abstracts certified from beginning to~~ recent date, together with all title papers in its possession covering leases and oil and gas interests which it is subjecting to this contract. All of these abstracts and title records shall be examined for the benefit of all parties by Operator's attorneys.

Operator shall promptly submit abstracts certified from beginning to recent date, together with all title papers in its possession covering leases and oil and gas interests which it is subjecting to this agreement, to _____ for examination by the latter's attorney for the benefit of all parties.

All title examinations shall be made without charge. Each examining attorney shall prepare a complete title report on each separate tract based upon the abstract record and title papers submitted to him. Each title report shall contain a list of fee owners and their interests, shall state the attorney's opinion concerning validity of their interests, and shall contain an enumeration and description of title defects, if any, a report upon mortgages, taxes, pending suits, and judgments, and unreleased oil and gas leases, and a list of requirements, if any, upon which the examiner's approval of title to the lease or oil and gas interest is contingent. The title report shall also contain a specific description of the oil and gas lease being subjected to this contract, with a statement of its form, term (which will be satisfactory if it has a primary term expiring not sooner ~~than _____), amount of royalty, status of delay rental payments, and unusual drilling~~

"Joint Loss"

~~obligations and of excess royalty, oil payments, and other special burdens. A copy of each title opinion, and~~ of each supplemental opinion, and of all final opinions, shall be sent promptly to each party. The opinion of the examining attorney concerning the validity of the title to each oil and gas interest and each lease, and the amount of interest covered thereby shall be binding and conclusive on the parties, but the acceptability of leases as to primary term, royalty provisions, drilling obligations, and special burdens, shall be a matter for approval and acceptance by an authorized representative of each party.

All title examinations shall be made, and title reports submitted, within a period of_____days after the submission of abstracts and title papers. Each party shall, in good faith, try to satisfy the requirements of the examining attorneys concerning its leases and interests, and each shall have a period of_____ days from receipt of title report for this purpose. If the title to any lease, or oil and gas interest, is finally rejected by the examining attorney, all parties shall then be asked to state in writing whether they will waive the title defects and accept the leases or interests, or whether they will stand on the attorney's opinion. If one or more parties refuse to waive title defects, this agreement shall, in that case, be terminated and abandoned, and all abstracts and title papers shall be returned to their senders. If all titles are approved by the examining attorneys, or are accepted by all parties, and if all leases are accepted as to primary terms, royalty provisions, drilling obligations and special burdens, all subsequent provisions of this agreement shall become operative ~~immediately, and the parties shall proceed to their performance as they are hereinafter stated.~~

B. Failure of Title:

After all titles are approved or accepted, any defects of title that may develop shall be the joint responsibility of all parties and, if a title loss occurs, it shall be the loss of all parties, with each bearing its proportionate part of the loss and of any liabilities incurred in the loss. If such a loss occurs, there shall be no change in, or adjustment of, the interests of the parties in the remaining portion of the Unit Area.

C. Loss of Leases For Other Than Title Failure:

If any lease or interest subject to this agreement be lost through failure to develop or because express or implied covenants have not been performed, or if any lease be permitted to expire at the end of its primary term and not be renewed or extended, the loss shall not be considered a failure of title and all such losses shall be joint losses and shall be borne by all parties in proportion to their interests and there shall be no readjustment of interests in the remaining portion of the Unit Area.

3. UNLEASED OIL AND GAS INTERESTS

If any party owns an unleased oil and gas interest in the Unit Area, that interest shall be treated for the purpose of this agreement as if it were a leased interest under the form of oil and gas lease attached as Exhibit "B" and for the primary term therein stated. As to such interests, the owner shall receive royalty on production as prescribed in the form of oil and gas lease attached hereto as Exhibit "B". Such party shall, however, be subject to all of the provisions of this agreement relating to lessees, to the extent that it owns the lessee interest.

4. INTERESTS OF PARTIES

Exhibit "A" lists all of the parties, and their respective percentage or fractional interests under this agreement. Unless changed by other provisions, all costs and liabilities incurred in operations under this contract shall be borne and paid, and all equipment and material acquired in operations on the Unit Area shall be owned, by the parties as their interests are given in Exhibit "A". All production of oil and gas from the Unit Area, subject to the payment of lessor's royalties, shall also be owned by the parties in the same manner.

If the interest of any party in any oil and gas lease covered by this agreement is subject to an overriding royalty, production payment, or other charge over and above the usual one-eigthh (⅛) royalty, such party shall assume and alone bear all such excess obligations and shall account for them to the owners thereof out of its share of the working interest production of the Unit Area.

5. OPERATOR OF UNIT

HNG OIL COMPANY shall be the Operator of the Unit Area, and shall conduct and direct and have full control of all operations on the Unit Area as permitted and required by, and within the limits of, this agreement. It shall conduct all such operations in a good and workmanlike manner, but it shall have no liability as Operator to the other parties for losses sustained, or liabilities incurred, except such as may result from gross negligence or from breach of the provisions of this agreement.

6. EMPLOYEES

~~The number of employees and their selection, and the hours of labor and the compensation for services~~ performed, shall be determined by Operator. All employees shall be the employees of Operator.

7. TEST WELL

On or before the_____ day of_____, 19____, Operator shall commence the drilling of a well for oil and gas in the following location:

and shall thereafter continue the drilling of the well with due diligence to unless granite or other practically impenetrable substance is encountered at a lesser depth or unless all parties agree to complete the well at a lesser depth.

Operator shall make reasonable tests of all formations encountered during drilling which give indication of containing oil and gas in quantities sufficient to test, unless this agreement shall be limited in its application to a specific formation or formations, in which event Operator shall be required to test only the formation or formations to which this agreement may apply.

If in Operator's judgment the well will not produce oil or gas in paying quantities, and it wishes to plug and abandon the test as a dry hole, it shall first secure the consent of all parties to the plugging, and the ~~well shall then be plugged and abandoned as promptly as possible.~~

8. COSTS AND EXPENSES

Except as herein otherwise specifically provided, Operator shall promptly pay and discharge all costs and expenses incurred in the development and operation of the Unit Area pursuant to this agreement and shall charge each of the parties hereto with their respective proportionate shares upon the cost and expense basis provided in the Accounting Procedure attached hereto and marked Exhibit "C". If any provision of Exhibit "C" should be inconsistent with any provision contained in the body of this agreement, the provisions in the body of this agreement shall prevail.

Operator, at its election, shall have the right from time to time to demand and receive from the other parties payment in advance of their respective shares of the estimated amount of the costs to be incurred in operations hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an itemized statement of such estimated costs, together with an invoice for its share thereof. Each such statement and invoice for the payment in advance of estimated costs shall be submitted on or before the 20th day of the next preceding month. Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest at the rate of twelve percent (12%) per annum until paid. Proper adjustment shall be made monthly between advances and actual cost, to the end that each party shall bear and pay its proportionate share of actual costs incurred, and no more.

9. OPERATOR'S LIEN

Operator is given a first and preferred lien on the interest of each party covered by this contract, and in each party's interest in oil and gas produced and the proceeds thereof, and upon each party's interest in material and equipment, to secure the payment of all sums due from each such party to Operator.

In the event any party fails to pay any amount owing by it to Operator as its share of such costs and expense or such advance estimate within the time limited for payment thereof, Operator, without prejudice to other existing remedies, is authorized, at its election, to collect from the purchaser or purchasers of oil or gas, the proceeds accruing to the working interest or interests in the Unit Area of the delinquent party up to the amount owing by such party, and each purchaser of oil or gas is authorized to rely upon Operator's statement as to the amount owing by such party.

In the event of the neglect or failure of any non-operating party to promptly pay its proportionate part of the cost and expense of development and operation when due, the other non-operating parties and Operator, within thirty (30) days after the rendition of statements therefor by Operator, shall proportionately contribute to the payment of such delinquent indebtedness and the non-operating parties so contributing shall be entitled to the same lien rights as are granted to Operator in this section. Upon the payment by such delinquent or defaulting party to Operator of any amount or amounts on such delinquent indebtedness, or upon any recovery on behalf of the non-operating parties under the lien conferred above, the amount or amounts so paid or recovered shall be distributed and paid by Operator to the other non-operating parties and Operator proportionately in accordance with the contributions theretofore made by them.

10. TERM OF AGREEMENT

This agreement shall remain in full force and effect for as long as any of the oil and gas leases subjected to this agreement remain or are continued in force as to any part of the Unit Area, whether by production, extension, renewal or otherwise; provided, however, that in the event the first well drilled hereunder results in a dry hole and no other well is producing oil or gas in paying quantities from the Unit Area, then at the end of ninety (90) days after abandonment of the first test well, this agreement shall terminate unless one or more of the parties are then engaged in drilling a well or wells pursuant to Section 12 hereof, or all parties have agreed to drill an additional well or wells under this agreement, in which event this agreement shall continue in force until such well or wells shall have been drilled and completed. If production results therefrom this agreement shall continue in force thereafter as if said first test well had been productive in paying quantities, but if production in paying quantities does not result therefrom this agreement shall terminate at the end of ninety (90) days after abandonment of such well or wells. It is agreed, however, that the termination of this agreement shall not relieve any party hereto from any liability which has accrued or attached prior to the date of such termination.

11. LIMITATION ON EXPENDITURES

Without the consent of all parties: (a) No well shall be drilled on the Unit Area except any well expressly provided for in this agreement and except any well drilled pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the drilling of a well shall include consent to all necessary expenditures in the drilling, testing, completing, and equipping of the well, including necessary tankage; (b) No well shall be reworked, plugged back or deepened except a well reworked, plugged back or deepened pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the reworking, plugging back or deepening of a well shall include consent to all necessary expenditures in conducting such operations and completing and equipping of said well to produce, including necessary tankage; (c) Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of fifteen thousand and no/100---------- Dollars ($ 15,000.00) except in connection with a well the drilling, reworking, deepening, or plugging back of which has been previously authorized by or pursuant to this agreement; provided, however, that in case of explosion, fire, flood, or other sudden emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion are required to deal with the emergency and to safeguard life and property, but Operator shall, as promptly as possible, report the emergency to the other parties. Operator shall, upon request, furnish copies of its "Authority for Expenditures" for any single project costing in excess of $ 5,000.00 .

12. OPERATIONS BY LESS THAN ALL PARTIES

If all the parties cannot mutually agree upon the drilling of any well on the Unit Area other than the test well provided for in Section 7, or upon the reworking, deepening or plugging back of a dry hole drilled at the joint expense of all parties or a well jointly owned by all the parties and not then producing in paying quantities on the Unit Area, any party or parties wishing to drill, rework, deepen or plug back such a well may give the other parties written notice of the proposed operation, specifying the work to be performed, the location, proposed depth, objective formation and the estimated cost of the operation. The parties receiving such a notice shall have thirty (30) days (except as to reworking, plugging back or drilling deeper, where a drilling rig is on location, the period shall be limited to forty-eight (48) hours exclusive of Saturday or Sunday) after receipt of the notice within which to notify the parties wishing to do the work whether they elect to participate in the cost of the proposed operation. Failure of a party receiving such a notice to so reply to it within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.

If any party receiving such a notice elects not to participate in the proposed operation (such party or parties being hereafter referred to as "Non-Consenting Party"), then in order to be entitled to the benefits of this section, the party or parties giving the notice and such other parties as shall elect to participate in the operation (all such parties being hereafter referred to as the "Consenting Parties") shall, within thirty (30) days after the expiration of the notice period of thirty (30) days (or as promptly as possible after the expiration of the 48-hour period where the drilling rig is on location, as the case may be) actually commence work on the proposed operation and complete it with due diligence.

The entire cost and risk of conducting such operations shall be borne by the Consenting Parties in the proportions that their respective interests as shown in Exhibit "A" bear to the total interests of all Consenting Parties. Consenting Parties shall keep the leasehold estates involved in such operations free and clear of all liens and encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such an operation results in a dry hole, the Consenting Parties shall plug and abandon the well at their sole cost, risk and expense. If any well drilled, reworked, deepened or plugged back under the provisions of this section results in a producer of oil and/or gas in paying quantities, the Consenting Parties shall complete and equip the well to produce at their sole cost and risk, and the well shall then be turned over to Operator and shall be operated by it at the expense and for the account of the Consenting Parties. Upon commencement of operations for the drilling, reworking, deepening or plugging back of any such well by Consenting Parties in accordance with the provisions of this section, each Non-Consenting Party shall be deemed to have relinquished to Consenting Parties, and the Consenting Parties shall own and be entitled to receive, in proportion to their respective interests, all of such Non-Consenting Party's interest in the well, its leasehold operating rights, and share of production therefrom until the proceeds or market value thereof (after deducting production taxes, royalty, overriding royalty and other interests payable out of or measured by the production from such well accruing with respect to such interest until it reverts) shall equal the total of the following:

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

(B) 300% of that portion of the costs and expenses of drilling, reworking, deepening or plugging back, testing and completing, after deducting any cash contributions received under Section 25, and 300% of that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections), which would have been chargeable to such Non-Consenting Party if it had participated therein.

In the case of any reworking, plugging back or deeper drilling operation, the Consenting Parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all such equipment shall remain unchanged; and upon abandonment of a well after such reworking, plugging back or deeper drilling, the Consenting Parties shall account for all such equipment to the owners thereof, with each party receiving its proportionate part in kind or in value.

Within sixty (60) days after the completion of any operation under this section, the party conducting the operations for the Consenting Parties shall furnish each Non-Consenting Party with an inventory of the equipment in and connected to the well, and an itemized statement of the cost of drilling, deepening, plugging back, testing, completing, and equipping the well for production; or, at its option, the operating party, in lieu of an itemized statement of such costs of operation, may submit a detailed statement of monthly billings. Each month thereafter, during the time the Consenting Parties are being reimbursed as provided above, the Consenting Parties shall furnish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the operation of the well, together with a statement of the quantity of oil and gas produced from it and the amount of proceeds realized from the sale of the well's working interest production during the preceding month. Any amount realized from the sale or other disposition of equipment newly acquired in connection with any such operation which would have been owned by a Non-Consenting Party had it participated therein shall be credited against the total unreturned costs of the work done and of the equipment purchased, in determining when the interest of such Non-Consenting Party shall revert to it as above provided; if there is a credit balance it shall be paid to such Non-Consenting Party.

If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest the amounts provided for above, the relinquished interests of such Non-Consenting Party shall automatically revert to it and from and after such reversion such Non-Consenting Party shall own the same interest in such well, the operating rights and working interest therein, the material and equipment in or pertaining thereto, and the production therefrom as such Non-Consenting Party would have owned had it participated in the drilling, reworking, deepening or plugging back of said well. Thereafter, such Non-Consenting Party shall be charged with and shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this agreement and the accounting procedure schedule, Exhibit "C", attached hereto.

Notwithstanding the provisions of this Section 12, it is agreed that without the mutual consent of all parties, no wells shall be completed in or produced from a source of supply from which a well located elsewhere on the Unit Area is producing, unless such well conforms to the then-existing well spacing pattern for such source of supply.

~~The provisions of this section shall have no application whatsoever to the drilling of the initial test~~ well on the Unit Area, but shall apply to the reworking, deepening, or plugging back of the initial test well after it has been drilled to the depth specified in Section 7, ~~if it~~ is, or thereafter shall prove to be, a dry hole or non-commercial well, and to ~~all other~~ wells drilled, reworked, deepened, or plugged back, or proposed to be drilled, ~~reworked~~, deepened, or plugged back, upon the Unit Area subsequent to the drilling of ~~the initial test well.~~

13. RIGHT TO TAKE PRODUCTION IN KIND

Subject to the provisions of Article XII of the Assignment and Agreement to which this Operating Agreement is attached, each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the Unit Area, exclusive of production which may be used in development and producing operations and in preparing and treating oil for marketing purposes and production unavoidably lost. Each party shall pay or deliver, or cause to be paid or delivered, all royalties, overriding royalties, or other payments due on its share of such production, and shall hold the other parties free from any liability therefor. Any extra expenditure incurred in the taking in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party.

Each party shall execute all division orders and contracts of sale pertaining to its interest in production from the Unit Area, and shall be entitled to receive payment direct from the purchaser or purchasers thereof for its share of all production.

In the event any party shall fail to make the arrangements necessary to take in kind or separately dispose of its proportionate share of the oil and gas produced from the Unit Area, Operator shall have the right, subject to revocation at will by the party owning it, but not the obligation, to purchase such oil and gas or sell it to others for the time being, at not less than the market price prevailing in the area, which shall in no event be less than the price which Operator receives for its portion of the oil and gas produced from the Unit Area. Any such purchase or sale by Operator shall be subject always to the right of the owner of the production to exercise at any time its right to take in kind, or separately dispose of, its share of all oil and gas not previously delivered to a purchaser. Notwithstanding the foregoing, Operator shall not make a sale into interstate commerce of any other party's share of gas production without first giving such other party sixty (60) days notice of such intended sale.

14. ACCESS TO UNIT AREA

Each party shall have access to the Unit Area at all reasonable times, at its sole risk, to inspect or observe operations, and shall have access at reasonable times to information pertaining to the development or operation thereof, including Operator's books and records relating thereto. Operator shall, upon request, furnish each of the other parties with copies of all drilling reports, well logs, tank tables, daily gauge and run tickets and reports of stock on hand at the first of each month, and shall make available samples of any cores or cuttings taken from any well drilled on the Unit Area.

15. DRILLING CONTRACTS

All wells drilled on the Unit Area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. Operator, if it so desires, may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the field, 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 shall be customary and usual in the field in contracts of independent contractors who are doing work of a similar nature.

16. ABANDONMENT OF WELLS

No well, other than any well which has been drilled or reworked pursuant to Section 12 hereof for which the Consenting Parties have not been fully reimbursed as therein provided, which has been completed as a producer shall be plugged and abandoned without the consent of all parties; provided, however, if all parties do not agree to the abandonment of any well, those wishing to continue its operation shall tender to each of the other parties its proportionate share of the value of the well's salvable material and equipment, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. Each abandoning party shall then assign to the non-abandoning parties, without warranty, express or implied, as to title or as to quantity, quality, or fitness for use of the equipment and material, all of its interest in the well and its equipment, together with its interest in the leasehold estate as to, but only as to, the interval or intervals of the formation or formations then open to production. The assignments so limited shall encompass the "drilling unit" upon which the well is located. The payments by, and the assignments to, the assignees shall be in a ratio based upon the relationship of their respective percentages of participation in the Unit Area to the aggregate of the percentages of participation in the Unit Area of all assignees. There shall be no readjustment of interest in the remaining portion of the Unit Area.

After the assignment, the assignors shall have no further responsibility, liability, or interest in the operation of or production from the well in the interval or intervals then open. Upon request of the assignees, Operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and charges contemplated by this agreement, plus any additional cost and charges which may arise as the result of the separate ownership of the assigned well.

17. DELAY RENTALS AND SHUT-IN WELL PAYMENTS

Each party shall pay all delay rentals and shut-in well payments which may be required under the terms of its lease or leases and submit evidence of each payment to the other parties at least ten (10) days prior to the payment date. The paying party shall be reimbursed by Operator for 100% of any such delay rental payment and 100% of any such shut-in well payment. The amount of such reimbursement shall be charged by Operator to the joint account of the parties and treated in all respects the same as costs incurred in the development and operation of the Unit Area. Each party responsible for such payments shall diligently attempt to make proper payment, but shall not be held liable to the other parties in damages for the loss of any lease or interest therein if, through mistake or oversight, any rental or shut-in well payment is not paid or is erroneously paid. The loss of any lease or interest therein which results from a failure to pay or an erroneous payment of rental or shut-in well payment shall be a joint loss and there shall be no readjustment of interests in the remaining portion of the Unit Area. If any party secures a new lease covering the terminated interest, such acquisiton shall be subject to the provisions of Section 23 of this agreement.

Operator shall promptly notify each other party hereto of the date on which any gas well located on the Unit Area is shut in and the reason therefor.

18. PREFERENTIAL RIGHT TO PURCHASE

~~Should any party desire to sell all or any part of its interests under this contract, or its rights and interests~~ in the Unit Area, it shall promptly give written notice to the other parties, with full information concerning its proposed sale, which shall include the name and address of the prospective purchaser (who must be ready, willing and able to purchase), the purchase price, and all other terms of the offer. The other parties shall then have an optional prior right, for a period of ten (10) days after receipt of the notice, to purchase on the same terms and conditions the interest which the other party proposes to sell; and, if this optional right is exercised, the purchasing parties shall share the purchased interest in the proportions that the interest of each bears to the total interest of all purchasing parties. However, there shall be no preferential right to purchase in those cases where any party wishes to mortgage its interests, or to dispose of its interests by merger, reorganization, consolidation, or sale of all of its assets, or a sale or transfer of its interests to a subsidiary or parent company, or subsidiary of a parent company, or to any company in which any one party owns a majority of the stock.

19. SELECTION OF NEW OPERATOR

Should a sale be made by Operator of its rights and interests, the other parties shall have the right within sixty (60) days after the date of such sale, by majority vote in interest, to select a new Operator. If a new Operator is not so selected, the transferee of the present Operator shall assume the duties of and act as Operator. In either case, the retiring Operator shall continue to serve as Operator, and discharge its duties in that capacity under this agreement, until its successor Operator is selected and begins to function, but the present Operator shall not be obligated to continue the performance of its duties for more than 120 days after the sale of its rights and interests has been completed.

20. MAINTENANCE OF UNIT OWNERSHIP

For the purpose of maintaining uniformity of ownership in the oil and gas leasehold interests covered by this contract, and notwithstanding any other provisions to the contrary, no party shall sell, encumber, transfer or make other disposition of its interest in the leases embraced within the Unit Area and in wells, equipment and production unless such disposition covers either:

(1) the entire interest of the party in all leases and equipment and production; or

(2) an equal undivided interest in all leases and equipment and production in the Unit Area.

Every such sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement, and shall be made without prejudice to the rights of the other parties.

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

21. RESIGNATION OF OPERATOR

Operator may resign from its duties and obligations as Operator at any time upon written notice of not less than ninety (90) days given to all other parties. In this case, all parties to this contract shall select by majority vote in interest, not in numbers, a new Operator who shall assume the responsibilities and duties, and have the rights, prescribed for Operator by this agreement. The retiring Operator shall deliver to its successor all records and information necessary to the discharge by the new Operator of its duties and obligations.

22. LIABILITY OF PARTIES

The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the Unit Area. Accordingly, the lien granted by each party to Operator in Section 9 is given to secure only the debts of each severally. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership or association, or to render them liable as partners.

23. RENEWAL OR EXTENSION OF LEASES

If any party secures a renewal of any oil and gas lease subject to this contract, each and all of the other parties shall be notified promptly, and shall have the right to participate in the ownership of the renewal lease by paying to the party who acquired it their several proper proportionate shares of the acquisition cost, which shall be in proportion to the interests held at that time by the parties in the Unit Area.

If some, but less than all, of the parties elect to participate in the purchase of a renewal lease, it shall be owned by the parties who elect to participate therein, in a ratio based upon the relationship of their respective percentage of participation in the unit area to the aggregate of the percentages of participation in the unit area of all parties participating in the purchase of such renewal lease. Any renewal lease in which less than all the parties elect to participate shall not be subject to this agreement.

Each party who participates in the purchase of a renewal lease shall be given an assignment of its proportionate interest therein by the acquiring party.

The provisions of this section shall apply to renewal leases whether they are for the entire interest covered by the expiring lease or cover only a portion of its area or an interest therein. Any renewal lease taken before the expiration of its predecessor lease, or taken or contracted for within six (6) months after the expiration of the existing lease shall be subject to this provision; but any lease taken or contracted for more than six (6) months after the expiration of an existing lease shall not be deemed a renewal lease and shall not be subject to the provisions of this section.

The provisions in this section shall apply also and in like manner to extensions of oil and ga

24. SURRENDER OF LEASES

The leases covered by this agreement, in so far as they embrace acreage in the Unit Area, shall not be surrendered in whole or in part unless all parties consent.

However, should any party desire to surrender its interest in any lease or in any portion thereof, and other parties not agree or consent, the party desiring to surrender shall assign, without express or implied warranty of title, all of its interest in such lease, or portion thereof, and any well, material and equipment which may be located thereon and any rights in production thereafter secured, to the parties not desiring to surrender it. Upon such assignment, the assigning party shall be relieved from all obligations thereafter accruing, but not theretofore accrued, with respect to the acreage assigned and the operation of any well thereon, and the assigning party shall have no further interest in the lease assigned and its equipment and production. The parties assignee shall pay to the party assignor the reasonable salvage value of the latter's interest in any wells and equipment on the assigned acreage, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. If the assignment is in favor of more than one party, the assigned interest shall be shared by the parties assignee in the proportions that the interest of each bears to the interest of all parties assignee.

Any assignment or surrender made under this provision shall not reduce or change the assignors' or surrendering parties' interest, as it was immediately before the assignment, in the balance of the Unit Area; and the acreage assigned or surrendered, and subsequent operations thereon, shall not thereafter be subject to the terms and provisions of this agreement.

25. ACREAGE OR CASH CONTRIBUTIONS

If any party receives while this agreement is in force a contribution of cash toward the drilling of a well or any other operation on the Unit Area, such contribution shall be paid to the party who conducted the drilling or other operation and shall 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 the contribution is made shall promptly execute an assignment of the acreage, without warranty of title, to all parties to this agreement in proportion to their interests in the Unit Area at that time, and such acreage shall become a part of the Unit Area and be governed by all the provisions of this contract. Each party shall promptly notify all other parties of all acreage or money contributions it may obtain in support of any well or any other operation on the Unit Area.

26. PROVISION CONCERNING TAXATION

Each of the parties hereto elects, under the authority of Section 761(a) of the Internal Revenue Code of 1954, to be excluded from the application of all of the provisions of Subchapter K of Chapter 1 of Subtitle A of the Internal Revenue Code of 1954. If the income tax laws of the state or states in which the property covered hereby is located contain, or may hereafter contain, provisions similar to those contained in the Subchapter of the Internal Revenue Code of 1954 above referred to under which a similar election is permitted, each of the parties agrees that such election shall be exercised. Each party authorizes and directs the Operator to execute such an election or elections on its behalf and to file the election with the proper governmental office or agency. If requested by the Operator so to do, each party agrees to execute and join in such an election.

Operator shall render for ad valorem taxation all property subject to this agreement which by law should be rendered for such taxes, and it shall pay all such taxes lawfully assessed thereon.

Operator shall bill all other parties for their proportionate share of all tax payments in the manner provided in Exhibit "C".

If any tax assessment is considered unreasonable by Operator, it may at its discretion protest such valuation within the time and manner prescribed by law, and prosecute the protest to a final determination, unless all parties agree to abandon the protest prior to final determination. When any such protested valuation shall have been finally determined, Operator shall pay the assessment for the joint account, together with interest and penalty accrued, and the total cost shall then be assessed against the parties, and be paid by them, as provided in Exhibit "C".

27. INSURANCE

At all times while operations are conducted hereunder, Operator shall comply with the Workmen's Compensation Law of the State where the operations are being conducted. Operator shall also carry or provide insurance for the benefit of the joint account of the parties as may be outlined in Exhibit "D" attached to and made a part hereof. Operator shall require all contractors engaged in work on or for the Unit Area to comply with the Workmen's Compensation Law of the State where the operations are being conducted and to maintain such other insurance as Operator may require.

In the event Automobile Public Liability Insurance is specified in said Exhibit "D", or subsequently receives the approval of the parties, no direct charge shall be made by Operator for premiums paid for such insurance for operator's fully owned automotive equipment.

28. CLAIMS AND LAWSUITS

If any party to this contract is sued on an alleged cause of action arising out of operations on the Unit Area, or on an alleged cause of action involving title to any lease or oil and gas interest subjected to this contract, it shall give prompt written notice of the suit to the Operator and all other parties.

The defense of lawsuits shall be under the general direction of a committee of lawyers representing the parties, with Operator's attorney as Chairman. Suits may be settled during litigation only with the joint consent of all parties. No charge shall be made for services performed by the staff attorneys for any of the parties, but otherwise all expenses incurred in the defense of suits, together with the amount paid to discharge any final judgment, shall be considered costs of operation and shall be charged to and paid by all parties in proportion to their then interests in the Unit Area. Attorneys, other than staff attorneys for the parties, shall be employed in lawsuits involving Unit Area operations only with the consent of all parties; if outside counsel is employed, their fees and expenses shall be considered Unit Area expense and shall be paid by Operator and charged to all of the parties in proportion to their then interests in the Unit Area. The provisions of this paragraph shall not be applied in any instance where the loss which may result from the suit is treated as an individual loss rather than a joint loss under prior provisions of this agreement, and all such suits shall be handled by and be the sole responsibility of the party or parties concerned.

Damage claims caused by and arising out of operations on the Unit Area, conducted for the joint account of all parties, shall be handled by Operator and its attorneys, the settlement of claims of this kind shall be within the discretion of Operator so long as the amount paid in settlement of any one claim does not exceed one thousand ($1000.00) dollars and, if settled, the sums paid in settlement shall be charged as expense to and be paid by all parties in proportion to their then interests in the Unit Area.

29. 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 make money payments, 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 affected party shall use all possible diligence to remove the force majeure as quickly as possible.

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.

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, explosion, governmental restraint, 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.

30. NOTICES

All notices authorized or required between the parties, and required by any of the provisions of this agreement, shall, unless otherwise specifically provided, be given in writing by United States mail or Western Union Telegram, postage or charges prepaid, and addressed to the party to whom the notice is given at the

addresses listed on Exhibit "A". The originating notice to be given under any provision hereof shall be deemed given only when received by the party to whom such notice is directed and the time for such party to give any notice in response thereto shall run from the date the originating notice is received. The second or any responsive notice shall be deemed given when deposited in the United States mail or with the Western Union Telegraph Company, with postage or charges prepaid. 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.

31. OTHER CONDITIONS, IF ANY, ARE:

31-A. TAXES ON PRODUCTION

At and during such time or times as Non-Operator is exercising the right to take in kind or separately dispose of its proportionate part of the production as set forth in Section 13 hereof, Non-Operator shall pay or arrange for the payment of all production, severance, gathering, sales or similar taxes imposed upon such part.

At and during such time or times as Operator or any other party is purchasing or selling another Non-Operator's proportionate part of production, as set forth in said Section 13, Operator or the party or parties receiving or selling said production, shall pay or arrange for the payment of all production, severance, gathering, sales or similar taxes imposed upon such party and shall deduct the amount of tax so paid from any proceeds due the owner of such production.

31-B. BURDENS CREATED SUBSEQUENT TO THIS AGREEMENT

Notwithstanding anything herein to the contrary, if any working interest owner shall, subsequent to the execution of this agreement, create an overriding royalty, production payment, net proceeds interest, carried interest, or any other interest out of its working interest (hereinafter called "subsequently created interest"), such subsequently created interest shall be specifically made subject to all the terms and provisions of this agreement. If the working interest owner from which such subsequently created interest is created (a) fails to pay when due its share of costs and expenses chargeable hereunder, and its share of production accruing hereunder is insufficient to cover such costs and expenses, or (b) elects to go nonconsent under Section 12, or (c) elects to abandon a well under Section 16 hereof, elects to surrender a lease under Section 24 hereof, or otherwise withdraws from this agreement, the subsequently created interest shall be chargeable with a pro-rata portion of all costs and expenses hereunder in the same manner as if such subsequently created interest were a working interest, and operator shall have the right to enforce against such subsequently created interest the lien and all other rights granted in Section 9 hereof for the purpose of collecting costs and expenses chargeable to the subsequently created interest.

31-C. FAIR EMPLOYMENT PRACTICES

In connection with the performance of work under this Operating Agreement, Operator agrees to comply fully with all provisions of Executive Order 11246 of September 24, 1965. A copy of the Equal Employment Opportunity Provision as set out in said order is attached hereto as Exhibit "E".

31-D. COMPLIANCE WITH ALL LAWS, RULES AND REGULATIONS

Operator agrees to comply fully with all applicable laws, rules and regulations pertaining to operations conducted pursuant to this agreement.

31-E. DISPOSITION OF PRODUCTION

The right to take production in kind as set out in Section 13 is subject to the prior call on production retained by Phillips Petroleum Company under Article XII of the Assignment and Agreement to which this Operating Agreement is attached.

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

ATTEST:

_____ _____

OPERATOR

ATTEST:

_____ _____

ATTEST:

_____ _____

EXHIBIT "A"

ATTACHED TO AND MADE A PART OF OPERATING AGREEMENT DATED THE 26TH DAY OF JUNE, 1978, BY AND BETWEEN HNG OIL COMPANY AS OPERATOR AND PHILLIPS PETROLEUM COMPANY AS NON-OPERATOR

AREA AND DEPTHS SUBJECT TO THIS OPERATING AGREEMENT

The area covered by this Operating Agreement shall be the area reassigned to Phillips pursuant to the provisions of Article XVIII-H of the Assignment and Agreement to which this Operating Agreement is attached as an agreement. This Operating Agreement shall cover the depths conveyed by such reassignments. The interests of the parties shall be those reassigned to Phillips and are owned by Phillips; all other interest is owned by operators.

AREA AND ADDRESSES OF THE PARTIES

HNG OIL COMPANY (Operator)
P. O. BOX 2267
MIDLAND, TEXAS 79702

PHILLIPS PETROLEUM COMPANY
4001 PENBROOK
ODESSA, TEXAS 79762

PRODUCERS 88 REV.-TEX. A (2-64)

EXHIBIT "B"

ATTACHED TO AND MADE A PART OF OPERATING AGREEMENT DATED THE 26TH DAY OF JUNE, 1978, BY AND BETWEEN HNG OIL COMPANY AS OPERATOR AND PHILLIPS PETROLEUM COMPANY AS NON-OPERATOR.

1. Lessor, in consideration of _____ Dollars ($_____) in hand paid, receipt of which is here acknowledged, and of the royalties herein provided and of the agreements of the lessee herein contained, hereby grants, leases and lets exclusively unto lessee for the purpose of investigating, exploring, prospecting, drilling, mining and operating for and producing oil, gas, and all other minerals, injecting gas, waters, other fluids, and air into subsurface strata, laying pipe lines, storing oil, building tanks, power stations, telephone lines and other structures and things thereon to produce, save, take care of, treat, process, store and transport said minerals and other products manufactured therefrom, and housing and otherwise caring for its employees, the following described land in _____ County, Texas, to-wit:

EXHIBIT "B"

Notwithstanding the reference to "oil" and "other minerals" this lease shall cover gas and all associated liquid hydrocarbons only.

[redacted]

[redacted] one (1) year

2. Subject to the other provisions herein contained, this lease shall remain in force for a term of [redacted] from this date (called "primary term"), and as long thereafter as oil, gas, or other mineral is produced from said land or land with which said land is pooled.

3. The royalties to be paid by lessee are: (a) on oil, and on other liquid hydrocarbons saved at the well, one-eighth of that produced and saved from said land, same to be delivered at the wells or to the credit of lessor in the pipe line to which the wells may be connected; lessor's interest in either case shall bear its proportion of any expenses for treating oil to make it marketable as crude; (b) on gas, including casinghead gas and all gaseous substances, produced from said land and sold or used off the premises or in the manufacture of gasoline or other product therefrom, the market value at the mouth of the well of one-eighth of the gas so sold or used, provided that on gas sold at the wells the royalty shall be one-eighth of the amount realized from such sale; (c) on all other minerals mined and marketed, one-eighth, either in kind or value at the well or mine, at lessee's election, except that on sulphur the royalty shall be One Dollar ($1.00) per long ton; and (d) at any time, either before or after the expiration of the primary term of this lease, if there is a gas well or wells on the above land (and for the purposes of this clause (d) the term "gas well" shall include wells capable of producing natural gas, condensate, distillate or any gaseous substance and wells classified as gas wells by any governmental authority) and such well or wells are shut in before or after production therefrom, lessee or any assignee hereunder may pay or tender an annual royalty equal to the amount of [redacted] for in this lease for the acreage then held under this lease by the party making such payment or tender, and if such payment or tender is made, it shall be considered under all provisions of this lease that gas is being produced from the leased premises in paying quantities for one (1) year from the date such payment or tender is made, and in like manner subsequent annual royalty payments may be made or tendered and it will be considered under all provisions of this lease that gas is being produced from the leased premises in paying quantities during any annual period for which such royalty is paid or tendered; such royalty may be paid or tendered [redacted] payment or tender of delay rentals; and when there is a shut-in gas well or wells on the leased premises if this lease is not continued in force under some other provision thereof, it shall nevertheless continue in force for a period of ninety (90) days from the last date on which a gas well located on the leased premises is shut in, or for ninety (90) days following the date to which this lease is continued in force by some other provision thereof, as the case may be, within which ninety-day period lessee or any assignee hereunder may commence or resume the payment or tender of the royalty as herein provided.

$1.00 per acre

by check or draft of lessee mailed or delivered to lessor.

[redacted]

[redacted]

[redacted]

5. Lessee is hereby granted the right to pool or unitize this lease, the land covered by it or any part thereof with any other land, lease, leases, mineral estates or parts thereof for the production of oil, gas, or any other minerals. Units pooled for oil hereunder shall not exceed forty (40) acres plus a tolerance of ten per cent (10%) thereof, and units pooled for gas hereunder shall not exceed six hundred forty (640) acres plus a tolerance of ten per cent (10%) thereof, provided that if any Federal or State law, Executive order, rule or regulation shall prescribe a spacing pattern for the development of the field or allocate a producing allowable on acreage per well, then any such units may embrace as much additional acreage as may be so prescribed or as may be used in such allocation or allowable. Lessee shall file written unit designations in the county in which the premises are located. Such units may be designated either before or after the completion of wells. Drilling operations and production on any part of the pooled acreage shall be treated as if such drilling operations were upon or such production was from the land described in this lease whether the well or wells be located on the land covered by this lease or not. The entire acreage pooled into a unit shall be treated for all purposes, except the payment of royalties on production from the pooled unit, as if it were included in this lease. In lieu of the royalties herein provided, lessor shall receive on production from a unit so pooled only such portion of the royalty stipulated herein as the amount of his acreage placed in the unit or his royalty interest therein on an acreage basis bears to the total acreage so pooled in the particular unit involved.

6. If, prior to discovery of oil, gas, or other minerals on said land or land pooled therewith lessee should drill and abandon a dry hole or holes thereon, or if, after discovery of oil, gas, or other minerals, the production thereof should cease from any cause, this lease shall not terminate if lessee commences reworking or additional drilling operations within sixty (60) days thereafter, [redacted]. If a dry hole is completed and abandoned at any time during the [redacted] primary term and prior to discovery of oil, gas, or other mineral on said land or land pooled therewith, no [redacted] operations are necessary in order to keep the lease in force during the remainder of the primary term. If, at the expiration of the primary term, oil, gas, or other mineral is not being produced on said land or land pooled therewith but lessee is then engaged in operations for drilling, mining, or reworking of any well or mine thereon, this lease shall remain in force so long as drilling, mining, or reworking operations are prosecuted (whether on the same or different wells) with no cessation of more than sixty (60) consecutive days, and if they result in production, so long thereafter as oil, gas, or other mineral is produced from said land or land pooled therewith. In the event a well or wells producing oil or gas in paying quantities should be brought in on adjacent land and within three hundred thirty (330) feet of and draining the leased premises, lessee agrees to drill such offset wells as a reasonably prudent operator would drill under the same or similar circumstances.

7. Lessee shall have free use of oil, gas, and water from said land, except water from lessor's wells and tanks, for all operations hereunder, including repressuring, pressure maintenance, cycling, and secondary recovery operations, and the royalty shall be computed after deducting any so used. Lessee shall have the right at any time during or after the expiration of this lease to remove all property and fixtures placed by lessee on said land, including the right to draw and remove all casing.

8. The rights of either party hereunder may be assigned in whole or in part and the provisions hereof shall extend to the heirs, executors, administrators, successors, and assigns, but no change or division in ownership of the land, [redacted] or royalties, however accomplished, shall operate to enlarge the obligations or diminish the rights of lessee. No such change or division in the ownership of the land, [redacted] or royalties shall be binding upon lessee for any purpose until such person acquiring any interest has furnished lessee with the instrument or instruments, or certified copies thereof, constituting his chain of title from the original lessor. [redacted]. An assignment of this lease, in whole or in part, shall, to the extent of such assignment, relieve and discharge lessee of any obligations hereunder, and, if lessee or assignee of part or parts hereof [redacted] fail to comply with any [redacted] provision of the lease, such default shall not affect this lease in so far as it covers a part of said lands upon which lessee or any assignee thereof shall [redacted] have complied.

9. Lessee shall not be liable for delays or defaults in its performance of any agreement or covenant hereunder due to force majeure. The term "force majeure" as employed herein shall mean: any act of God including but not limited to storms, floods, washouts, landslides, and lightning; acts of the public enemy; wars, blockades, insurrections or riots; strikes or lockouts; epidemics or quarantine regulations; laws, acts, orders or requests of federal, state, municipal or other governments or governmental officers or agents under color of authority; freight embargoes or failures; exhaustion or unavailability or delays in delivery of any product, labor, service, or material. If lessee is required, ordered or directed by any federal, state or municipal law, executive order, rule, regulation or request enacted or promulgated under color of authority to cease drilling operations, reworking operations or producing operations on the land covered by this lease or if lessee by force majeure is prevented from conducting drilling operations, reworking operations or producing operations, then until such time as such law, order, rule, regulation, request or force majeure is terminated and for a period of ninety (90) days after such termination each and every provision of this lease that might operate to terminate it or the estate conveyed by it shall be suspended and inoperative and this lease shall continue in full force. If any period of suspension occurs during the primary term, the time thereof shall be added to such term.

10. Lessor hereby warrants and agrees to defend the title to said land, and agrees that lessee, at its option, may discharge any tax, mortgage, or other lien upon said land, and in the event lessee does so, it shall be subrogated to such lien with the right to enforce same and apply [redacted] royalties accruing hereunder toward satisfying same. Without impairment of lessee's rights under the warranty in the event of failure of title, it is agreed that, if lessor owns an interest in said land less than the entire fee simple estate, then the royalties [redacted] to be paid lessor shall be reduced proportionately; should any one or more of the parties named above as lessors fail to execute this lease, it shall nevertheless be binding upon the party or parties executing the same.

11. Lessee, its/his successors and assigns, shall have the right at any time to surrender this lease, in whole or in part, to lessor or his heirs and assigns by delivering or mailing a release thereof to the lessor, or by placing a release thereof of record in the county in which said land is situated; thereupon lessee shall be relieved from all obligations, expressed or implied, of this agreement as to the acreage so surrendered. [redacted]

IN WITNESS WHEREOF, we sign the day and year first above written.

_____ _____

_____ _____

_____ _____

_____ _____

THE STATE OF TEXAS }
COUNTY OF..... }

BEFORE ME, the undersigned authority, a Notary Public in and for.....County, Texas, on this day personally appeared....., known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that .....he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this.....day of ....., A. D. 19.....

.....

Notary Public,.....County, Texas.

THE STATE OF TEXAS }
COUNTY OF..... }

BEFORE ME, the undersigned authority, a Notary Public in and for.....County, Texas, on this day personally appeared.....and.....,
his wife, both known to me to be the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that they executed the same for the purposes and consideration therein expressed; and the said.....
....., wife of the said.....
having been examined by me privily and apart from her husband, and having the same fully explained to her, she, the said
....., acknowledged such instrument to be her act and deed, and declared that she had willingly signed the same for the purposes and consideration therein expressed, and that she did not wish to retract it.

Given under my hand and seal of office this.....day of.....A. D. 19.....

.....

Notary Public,.....County, Texas.

No.....

OIL, GAS AND MINERAL LEASE

TEXAS

.....

.....

TO

.....

.....

Filed for Record this the.....
day of.....A. D. 19.....
at.....o'clock.....M.
.....County Clerk.
By.....Deputy.

Recorded.....A. D. 19.....
in.....County
Record of.....
Book.....Page.....
.....County Clerk.
By.....Deputy.

THE STATE OF TEXAS }
COUNTY OF..... }

BEFORE ME, the undersigned authority, a Notary Public in and for.....County, Texas, on this day personally appeared.....and.....,
his wife, both known to me to be the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that they executed the same for the purposes and consideration therein expressed; and the said.....
....., wife of the said.....
having been examined by me privily and apart from her husband, and having the same fully explained to her, she, the said
....., acknowledged such instrument to be her act and deed, and declared that she had willingly signed the same for the purposes and consideration therein expressed, and that she did not wish to retract it.

Given under my hand and seal of office this.....day of.....A. D. 19.....

.....

Notary Public,.....County, Texas.

COPAS — 1974
Recommended by the Council of Petroleum Accountants Societies of North America

COPAS FORM

EXHIBIT "C"

Attached to and made a part of Operating Agreement dated the 26th day of June, 1978, by and between HNG Oil Company as Operator and Phillips Petroleum Company as Non-Operator.

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 of North America.

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

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. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.

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 rate of twelve percent (12%) per annum 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.

5. Audits

A. Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit Operator's accounts and records relating to the Joint Account for any calendar year within the twenty-four (24) month period following the end of such calendar year; provided, however, the making of an audit shall not extend the time for the taking of written exception to and the adjustments of accounts as provided for in Paragraph 4 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make every reasonable effort to conduct joint or simultaneous audits in a manner which will result in a minimum of inconvenience to the Operator. Operator shall bear no portion of the Non-Operators' audit cost incurred under this paragraph unless agreed to by the Operator.

6. Approval by Non-Operators

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

II. DIRECT CHARGES

Operator shall charge the Joint Account with the following items:

1. Rentals and Royalties

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

2. Labor

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

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

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

B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II. Such costs under this Paragraph 2B may be charged on a "when and as paid basis" or by "percentage assessment" on the amount of salaries and wages chargeable to the Joint Account under Paragraph 2A of this Section II. If percentage assessment is used, the rate shall be based on the Operator's cost experience.

C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are applicable to Operator's costs chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II.

D. Personal Expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II.

3. Employee Benefits

Operator's current costs of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II shall be Operator's actual cost not to exceed twenty per cent (20%).

4. Material

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

5. Transportation

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

A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be made to the Joint Account for a distance greater than the distance from the nearest reliable supply store, recognized barge terminal, or railway receiving point where like material is normally available, unless agreed to by the Parties.

B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint Account for a distance greater than the distance to the nearest reliable supply store, recognized barge terminal, or railway receiving point unless agreed to by the Parties. No charge shall be made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by the Parties.

C. In the application of Subparagraphs A and B above, there shall be no equalization of actual gross trucking cost of $200 or less excluding accessorial charges.

6. Services

The cost of contract services, equipment and utilities provided by outside sources, except services excluded by Paragraph 9 of Section II and Paragraph 1. ii of Section III. The cost of professional consultant services and contract services of technical personnel directly engaged on the Joint Property if such charges are excluded from the Overhead rates. The cost of professional consultant services or contract services of technical personnel not directly engaged on the Joint Property shall not be charged to the Joint Account unless previously agreed to by the Parties.

7. Equipment and Facilities Furnished by Operator

A. Operator shall charge the Joint Account for use of Operator owned equipment and facilities at rates commensurate with costs of ownership and operation. Such rates shall include costs of maintenance, repairs, other operating expense, insurance, taxes, depreciation, and interest on investment not to exceed eight per cent (8%) per annum. Such rates shall not exceed average commercial rates currently prevailing in the immediate area of the Joint Property.

B. In lieu of charges in Paragraph 7A above, Operator may elect to use average commercial rates prevailing in the immediate area of the Joint Property less 20%. For automotive equipment, Operator may elect to use rates published by the Petroleum Motor Transport Association.

8. Damages and Losses to Joint Property

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

9. Legal Expense

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

10. Taxes

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

11. Insurance

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

12. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator in the necessary and proper conduct of the Joint Operations.

III. OVERHEAD

1. Overhead - Drilling and Producing Operations

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

(X) Fixed Rate Basis, Paragraph 1A, or
( ) Percentage Basis, Paragraph 1B.

Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under Paragraph 2A, Section II. The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the Overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by the Parties as a direct charge to the Joint Account.

ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant services and contract services of technical personnel directly employed on the Joint Property shall ( ) shall not (X) be covered by the Overhead rates.

A. Overhead - Fixed Rate Basis

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

Drilling Well Rate $ 2578.
Producing Well Rate $ 318.

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

(a) Drilling Well Rate

[1] Charges for onshore drilling wells shall begin on the date the well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days.

[2] Charges for offshore drilling wells shall begin on the date when drilling or completion equipment arrives on location and terminate on the date the drilling or completion equipment moves off location or rig is released, whichever occurs first, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days

[3] Charges for wells undergoing any type of workover or recompletion for a period of five (5) consecutive days or more shall be made at the drilling well rate. Such charges shall be applied for the period from date workover operations, with rig, commence through date of rig release, except that no charge shall be made during suspension of operations for fifteen (15) or more consecutive days.

(b) Producing Well Rates

[1] An active well either produced or injected into for any portion of the month shall be considered as a one-well charge for the entire month.

[2] Each active completion in a multi-completed well in which production is not commingled down hole shall be considered as a one-well charge providing each completion is considered a separate well by the governing regulatory authority.

[3] An inactive gas well shut in because of overproduction or failure of purchaser to take the production shall be considered as a one-well charge providing the gas well is directly connected to a permanent sales outlet.

[4] A one-well charge may be made for the month in which plugging and abandonment operations are completed on any well.

[5] All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease allowable, transferred allowable, etc.) shall not qualify for an overhead charge.

(3) The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the calendar year preceding as shown by the index of average weekly earnings of Crude Petroleum and Gas Fields Production Workers as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian index as published by Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

B. Overhead - Percentage Basis

(1) Operator shall charge the Joint Account at the following rates:

(a) Development

_____ Percent (%) of the cost of Development of the Joint Property exclusive of costs provided under Paragraph 9 of Section II and all salvage credits.

(b) Operating

_____ Percent (%) of the cost of Operating the Joint Property exclusive of costs provided under Paragraphs 1 and 9 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

(2) Application of Overhead - Percentage Basis shall be as follows:
For the purpose of determining charges on a percentage basis under Paragraph 1B of this Section III, development shall include all costs in connection with drilling, redrilling, deepening or any remedial operations on any or all wells involving the use of drilling crew and equipment; also, preliminary expenditures necessary in preparation for drilling and expenditures incurred in abandoning when the well is not completed as a producer, and original cost of construction or installation of fixed assets, the expansion of fixed assets and any other project clearly discernible as a fixed asset, except Major Construction as defined in Paragraph 2 of this Section III. All other costs shall be considered as Operating.

2. Overhead - Major Construction

To compensate Operator for overhead costs incurred in the construction and installation of fixed assets, the expansion of fixed assets, and any other project clearly discernible as a fixed asset required for the development and operation of the 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 $ * : *To be negotiated

A. * % of total costs if such costs are more than $_____ but less than $_____; plus

B. * % of total costs in excess of $_____ but less than $1,000,000; plus

C. * % of total 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 shall be excluded.

3. 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 reason, 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 bases exclusive of cash discounts:

A. New Material (Condition A)

(1) Tubular goods, except line pipe, shall be priced at the current new price in effect on date of movement on a maximum carload or barge load weight basis, regardless of quantity transferred, equalized to the lowest published price f.o.b. railway receiving point or recognized barge terminal nearest the Joint Property where such Material is normally available.

(2) Line Pipe

(a) Movement of less than 30,000 pounds shall be priced at the current new price, in effect at date of movement, as listed by a reliable supply store nearest the Joint Property where such Material is normally available.

(b) Movement of 30,000 pounds or more shall be priced under provisions of tubular goods pricing in Paragraph 2A (1) of this Section IV.

(3) Other Material shall be priced at the current new price, in effect at date of movement, as listed by a reliable supply store or f.o.b. railway receiving point nearest the Joint Property where such Material is normally available.

B. Good Used Material (Condition B)

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

(1) Material moved to the Joint Property

(a) At seventy-five percent (75%) of current new price, as determined by Paragraph 2A of this Section IV.

(2) Material moved from the Joint Property

(a) At seventy-five percent (75%) of current new price, as determined by Paragraph 2A of this Section IV, if Material was originally charged to the Joint Account as new Material, or

(b) at sixty-five percent (65%) of current new price, as determined by Paragraph 2A of this Section IV, if Material was originally charged to the Joint Account as good used Material at seventy-five percent (75%) of current new price.

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

C. Other Used Material (Condition C and D)

(1) Condition C

Material which is not in sound and serviceable condition and not suitable for its original function until after reconditioning shall be priced at fifty percent (50%) of current new price as determined by Paragraph 2A of this Section IV. The cost of reconditioning shall be charged to the receiving property, provided Condition C value plus cost of reconditioning does not exceed Condition B value.

(2) Condition D

All other Material, including junk, shall be priced at a value commensurate with its use or at prevailing prices. Material no longer suitable for its original purpose but usable for some other purpose, shall be priced on a basis comparable with that of items normally used for such other purpose. Operator may dispose of Condition D Material under procedures normally utilized by the Operator without prior approval of Non-Operators.

D. Obsolete Material

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

E. Pricing Conditions

(1) Loading and unloading costs may be charged to the Joint Account at the rate of fifteen cents (15¢) per hundred weight on all tubular goods movements, in lieu of loading and unloading costs sustained, when actual hauling cost of such tubular goods are equalized under provisions of Paragraph 5 of Section II.

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

3. Premium Prices

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

4. Warranty of Material Furnished by Operator

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

V. INVENTORIES

The Operator shall maintain detailed records of Controllable Material.

1. Periodic Inventories, Notice and Representation

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

2. Reconciliation and Adjustment of Inventories

Reconciliation of a physical inventory with the Joint Account shall be made, and a list of overages and shortages shall be furnished to the Non-Operators within six months following the taking of the inventory. Inventory adjustments shall be made by Operator with the Joint Account for overages and shortages, but Operator shall be held accountable only for shortages due to lack of reasonable diligence.

3. Special Inventories

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

4. Expense of Conducting Periodic Inventories

The expense of conducting periodic Inventories shall not be charged to the Joint Account unless agreed to by the Parties.

EXHIBIT "D"

ATTACHED TO AND MADE A PART OF OPERATING AGREEMENT DATED THE 26TH DAY OF JUNE, 1978, BY AND BETWEEN HNG OIL COMPANY AS OPERATOR AND PHILLIPS PETROLEUM COMPANY AS NON-OPERATOR

INSURANCE

Operator shall carry Workmen's Compensation Insurance to comply fully with the Workmen's Compensation Act or acts applicable to all operations conducted hereunder, provided Operator may qualify as a self-insurer if permitted under such act or acts. No other insurance shall be carried by the Operator for the benefit of the parties hereto except by mutual consent of the parties.

EXHIBIT "E"

ATTACHED TO AND MADE A PART OF OPERATING AGREEMENT DATED THE 26TH DAY OF JUNE, 1978, BY AND BETWEEN HNG OIL COMPANY AS OPERATOR AND PHILLIPS PETROLEUM COMPANY AS NON-OPERATOR.

Equal Employment Opportunity Provision

During the performance of this contract, Operator (HNG OIL COMPANY) agrees as follows:

1. The Operator will not discriminate against any employees or applicant for employment because of race, color, religion, sex, or national origin. The Operator will take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex, or national origin. Such action shall include, but not be limited to, the following: employment, upgrading, demotion, or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The Operator agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided by the contracting officer setting forth the provisions of this nondiscrimination clause.

2. The Operator will, in all solicitations or advertisements for employees placed by or on behalf of the Operator, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex, or national origin.

3. The Operator will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice to be provided by the agency contracting officer, advising the labor union or workers' representative of the Operator's commitments under Section 202 of Executive Order 11246 of September 24, 1965, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

4. The Operator will comply with all provisions of Executive Order 11246 of September 24, 1965, and of the rules, regulations, and relevant orders of the Secretary of Labor.

5. The Operator will furnish all information and reports required by Executive Order 11246 of September 24, 1965, and by the rules, regulations, and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records, and accounts by the contracting agency and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations, and orders.

6. In the event of the Operator's noncompliance with the nondiscrimination clauses of this contract or with any of such rules, regulations, or orders, this contract may be cancelled, terminated, or suspended in whole or in part, and the Operator may be declared ineligible for further Government contracts in accordance with procedures authorized in Executive Order 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in Executive Order 11246 of September 24, 1965, or by rule, regulation, or order of the Secretary of Labor, or as otherwise provided by law.

7. The Operator will include the provisions of paragraphs (1) through (7) in every subcontract or purchase order unless exempted by rules, regulations, or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order 11246 of September 24, 1965, so that such provisions will be binding upon each subcontractor or vendor. The Operator will take such action with respect to any subcontract or purchase order as the contracting agency may direct as a means of enforcing such provisions including sanctions for noncompliance: Provided, however, that in the event the Operator becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the contracting agency, the Operator may request the United States to enter into such litigation to protect the interests of the United States.

Operator acknowledges that it may be required to file Standard Form 100 (EEO-1) promulgated jointly by the Office of Federal Contract Compliance, the Equal Employment Opportunity Commission and Plans for Progress with Joint Reporting Committee, Federal Depot, Jeffersonville, Indiana, within thirty (30) days of the date of contract award if such report has not been filed for the current year and otherwise comply with or file such other compliance reports as may be required under Executive Order 11246, as amended and Rules and Regulations adopted thereunder.

Operator further acknowledges that he may be required to develop a written affirmative action compliance program as required by the Rules and Regulations approved by the Secretary of Labor under authority of Executive Order 11246 and supply Non-Operators with a copy of such program if they so request.

Operator assures Non-Operators that it does not and will not maintain or provide for its employees any segregated facilities at any of its establishments, and that it does not and will not permit its employees to perform their services at any location, under its control, where segregated facilities are maintained. For this purpose, it is understood that the phrase "segregated facilities" includes facilities which are in fact segregated on a basis of race, color, religion, or national origin, because of habit, local custom or otherwise. It is further understood and agreed that maintaining or providing segregated facilities for its employees or permitting its employees to perform their services at any location under its control where segregated facilities are maintained is a violation of the equal opportunity clause required by Executive Order 11246 of September 24, 1965.

Operator further understands and agrees that a breach of the assurance herein contained subjects it to the provisions of the Order at 41 CFR Chapter 60 of the Secretary of Labor dated May 21, 1968, and the provisions of the equal opportunity clause enumerated in contracts between the United States of America and Non-Operators.

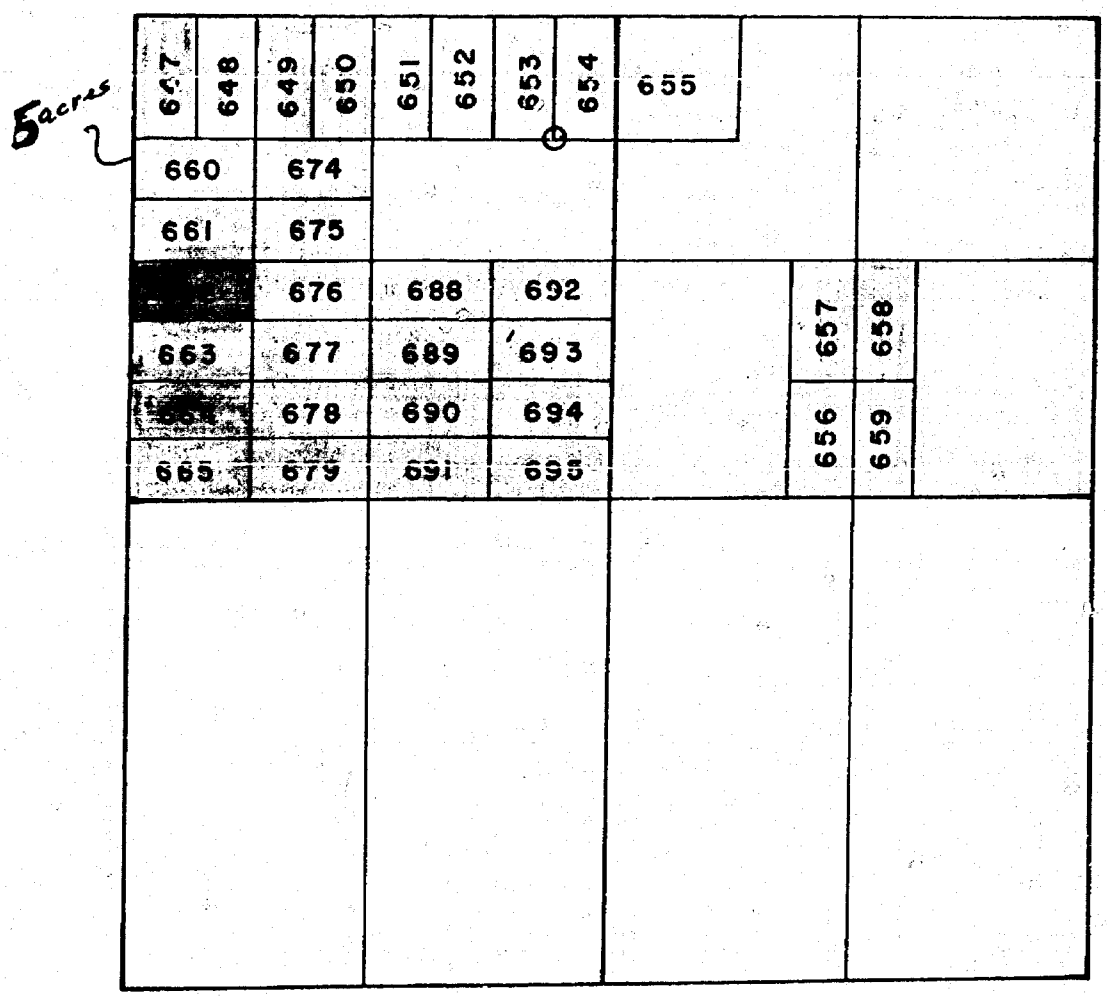
Whoever knowingly and willfully makes any false, fictitious or fraudulent representation may be liable to criminal prosecution under 18 U.S.C. § 1001.

EDDY COUNTY, NEW MEXICO

T-23-S, R-28-E

North 1/2

Section 35:



- HNG Oil Co.
- Phillips Petr.
- J. E. Russell, et al
- Enderud & Larson
- Heirs of Burt Schurr

N

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 1
CASE NO. 6431
Submitted by
Hearing Date

CASE NO. 6431
HNG OIL COMPANY
Williams Com "35" #1
N/2 of Section 35, T-23-S, R-28-E
Eddy County, New Mexico

1.875 mineral acres in and under the N/2 SW/4 SW/4 NW/4 (Farm Tract 664) containing 5 acres.

Ownership of 1.875 acres:

Heirs of Albert Larson	1.0417 acres
Olaf Enderud	0.8333 acres
	1.8750 acres

Last Known Address: Caldwell, Kansas

5 acres being N/2 SW/4 NW/4 NW/4 (Farm Tract 660).

Ownership of 5 acres:

Heirs of Burt Schurr

Last Known Address: LeRoy, Kansas

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 2
CASE NO. 6431
Submitted by
Hearing Date

P. O. BOX 2267, MIDLAND, TEXAS 79702 (915) 683-4871

January 24, 1979

Mr. Robert B. Coleman
P. O. Box 501
Midland, Texas 79702

RE: HNG-Williams "35" Com. #1
Eddy County, New Mexico

Dear Mr. Coleman:

You have advised us verbally that you are acquiring an oil and gas lease from the heirs of Burt Schurr covering the N/2 SW/4 NW/4 NW/4 of Section 35, T-23-S, R-28-E, Eddy County, New Mexico.

This company failed in its efforts to locate the present owners of the above described 5 acre tract and elected to proceed with the drilling of its Williams "35" Com. #1 Well located 660' FNL and 2310' FWL of Section 35, T-23-S, R-28-E, Eddy County, New Mexico. This test well will be drilled to sufficiently test the Morrow formation at an estimated depth of 13,400'.

On January 9, 1979 application was made (copy attached) to the Oil Conservation Division of New Mexico for compulsory pooling of all oil and gas mineral interests in the Pennsylvanian formation in and under the N/2 of said Section 35. A hearing is set for January 31, 1979 in Santa Fe, New Mexico.

Assuming you do have a valid lease covering the interests of the owners of the above mentioned 5 acre tract, we invite you to commit same to a 320 acre unit covering the N/2 of said Section 35 and to participate in the drilling of the HNG-Williams "35" Com. #1 as a working interest (1.5625%) owner. In lieu thereof, we would be agreeable to assuming your position on a farmout basis with you retaining a 1/16th overriding royalty interest with the option to convert same to a 1/2 working interest at payout of the well, both proportionately reduced.

A copy of our AFE for the drilling of the Williams "35" Com. #1 is enclosed herewith.

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 3
CASE NO. 6431
Submitted by
Hearing Date
encls.

Yours very truly,

HNG OIL COMPANY

Raymond Parker

Raymond Parker
Manager of Lands

Blank

AFFIDAVIT

State of Kansas)
County of Sedgwick)

Tom Burden, being first duly sworn, on h is oath states, that he is a person of lawful age; that he is and has been for 18 years last past a resident of Sedgwick County, State of Kansas, and further deposes and states:

That affiant has made a thorough investigation in an attempt to locate Mr. Albert Larson and/or his heirs at law, said party being the owner of a 5/24 mineral interest in and under the N½SW¼SW¼NW¼ of Section 35-23 South, 28 East, Eddy County, New Mexico. Investigation attempts led the Affiant to Mr. D. B. Stalling, attorney at Law of Caldwell, Kansas, who knew the party in question and who at one time was a resident of Kiowa, Kansas. Affiant was advised to contact Mr. Carl McNally of Kiowa, Kansas for information regarding the whereabouts of Mr. Larson. Mr. McNally had been a long time friend of Mr. Larson. Affiant discovered Mr. McNally to be deceased, however, his surviving widow was still living, but quite elderly. She recalled that Mr. Larson had some brothers and sisters, but she did not know their whereabouts. She stated that she thought that Mr. Larson had moved to Los Angeles around 1949 and that she had not heard of or from him since nor from his brothers or sisters. She stated that Mr. Larson had a wife and several children, but they moved when Mr. Larson did. Affiant then checked with various government agencies in Sacramento, California in an attempt to locate Mr. Larson to no avail. Affiant then re-contacted Mr. Stalling for additional information without success. Therefore, affiant considers the above as representative of a thorough investigation to locate Mr. Larson, or his heirs at law, and that same are not locatable.

Further, Affiant saith not:

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 4
CASE NO. 6431
Submitted by
Hearing Date

STATE OF KANSAS DORENE K. DUNN Sedgwick County, Ks. My Appmt. Exp. 1-13-80
(SEAL)

Signed: Tom Burden
Tom Burden

Subscribed and sworn to before me this 5th day of January, A. D. 19 79.

Dorene K. Dunn
Notary Public.

My Commission Expires ....., 19.....

STATE OF Kansas }
COUNTY OF Sedgwick } ss. ACKNOWLEDGMENT FOR INDIVIDUAL (Kans. Okla. and Colo.)

Before me, the undersigned, a Notary Public, within and for said County and State, on this 5th day of January, 19 79, personally appeared Tom Burden and .....

to me personally known to be the identical person who executed the within and foregoing instrument and acknowledged to me that he executed the same as his free and voluntary act and deed for the uses and purposes therein set forth.

IN WITNESS WHEREOF, I have hereunto set my hand and official seal the day and year last above written.

My commission expires .....

STATE OF KANSAS DORENE K. DUNN Sedgwick County, Ks. My Appmt. Exp. 1-13-80

Dorene K. Dunn
Notary Public

Blank

AFFIDAVIT

State of Kansas)
) ss
County of Sedgwick)

Tom Burden, being first duly sworn, on h is oath states, that he is a person of lawful age; that he is and has been for 18 years last past a resident of Sedgwick County, State of Kansas, and further deposes and states: That affiant has made a thorough investigation in an attempt to locate Mr. Olaf Enderud and/or his wife, Cora Enderud, or any heirs at law of same, said parties being owners of a 4/24 mineral interest in and under the N½SW¼SW¼NW¼ of Section 35-23S-28E, Eddy County, New Mexico. Investigation attempts led the affiant to Mr. D. B. Stalling, attorney at law, in the City of Caldwell, State of Kansas. Mr. Stalling stated that Mr. and Mrs. Enderud were at one time residents of Caldwell, Kansas, but that they moved to San Diego, California in the early part of the 1940's to work in the naval shipyards in that city. However, Mr. Stalling was fairly certain that both parties are now deceased. Mr. Stalling stated that Mr. Enderud had one brother and no children. His brother's name was Ekrun Enderud and was also a resident of San Diego, California. Since the two brothers were approximately the same age, it was assumed by Mr. Stalling that Ekrun Enderud is also deceased. The affiant checked with the Department of Motor Vehicles in Sacramento, California in an attempt to locate any of the previously mentioned parties since they would probably own an automobile titled to them with an address on the State records. No such parties were listed. Affiant also checked with the Bureau of Vital Statistics in Sacramento to ascertain if any of the parties in question died a resident of the State of California since any death certificate would indicate the name and address of the next of kin. However, there were no such parties listed on the state records. Thereupon, the affiant re-contacted Mr. Stalling for additional information to no avail. Therefore, affiant feels that a thorough investigation has been made in an effort to locate Mr. and Mrs. Olaf Enderud and/or their heirs at law without results and that they are not locatable.

Further, Affiant saith not:

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 5
CASE NO. 6431
Submitted by
Hearing Date

STATE NOTARY PUBLIC KANSAS
DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80
(SEAL)

Signed: Tom Burden
Tom Burden

Subscribed and sworn to before me this 5th day of January, A. D. 19 79

Dorene K. Dunn
Notary Public.

My Commission Expires ....., 19.....

STATE OF Kansas }
COUNTY OF Sedgwick } ss. ACKNOWLEDGMENT FOR INDIVIDUAL (Kans. Okla. and Colo.)

Before me, the undersigned, a Notary Public, within and for said County and State, on this 5th day of January, 19 79, personally appeared Tom Burden and .....

to me personally known to be the identical person who executed the within and foregoing instrument and acknowledged to me that he executed the same as his free and voluntary act and deed for the uses and purposes therein set forth.

IN WITNESS WHEREOF, I have hereunto set my hand and official seal the day and year last above written.

My commission expires .....

STATE NOTARY PUBLIC KANSAS
DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80

Dorene K. Dunn
Notary Public

15

14

Drilling

Delta

Strawn Sd

22

Amoco

Strawn Sd

Amoco
Brantley
1

Morrow Sd
(12264-430)
Comp 1-18-79

23

Delta

Strawn Sd

Delta

Blow-Out Well
Atoka Sd T

27

Moddox
Pardue Farms
1-27

Morrow Sd
(12480-661)
Dry gas sales
to El Paso
1-16-79

26

Moddox

Dual
Strawn Sd (11468-74)
Atoka Sd (11756-80)

Amoco

Strawn Sd
(11484-91)

S

34

35

HNG
84-01 thru 84-04
1-S-81

(155.762 Net)

E

HNG L-35
HNG
01, 89-02
1-9-81
(330 Net)

Drilling

Williams Com"

89-03, -04, -05, -06
1-9-81
(165.90 Net)

3

2

NO MALAGA

HNG
90-01, -02, -03, -04
1-9-81
(44 Net)

PV & NE Ry.
(Approx)

Phillips
Malaga
1-A

Rich-Boss
Beeman
1

Morrow Sd
(12310-658)

30

10

11

Schobel

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 6
CASE NO. 6431
Submitted by
Hearing Date

hng
Oil Company

Case No. 6431
HNG Oil Company
Williams Com "35" #1
N/2 Sec. 35, 23S-28E
Eddy County, New Mexico

DRILLING OR WORKOVER AFE

hng Oil Company

AFE NO.

LSE. NO.

HNG W.I.

HNG EST. COST

AFE DATE

[X] WILDCAT
- [X] DRILLING
- [X] COMPLETION
- [ ] RE-ENTRY

[ ] DEVELOPMENT
- [ ] DRILLING
- [ ] COMPLETION
- [ ] RE-ENTRY

[ ] WORKOVER
- [ ] SAME ZONE
- [ ] NEW ZONE
- [ ] P & A

LEASE & WELL NO. Williams Com 35-1	DEPTH & FORM 13,400 Morrow
LOCATION, 660' FNL & 2310' FWL, Sec. 35, T-23-S, R-28-E	
COUNTY & STATE Eddy, New Mexico	FIELD Wildcat
OPERATOR HNG Oil	SPUD DATE 12-10-78

	INTANGIBLE WELL COST			
	DESCRIPTION	DRILLING	COMPLETION	TOTAL
1	Access, Location & Roads	40,000		40,000
2	Rig Move	70,000		70,000
3	Footage Cost			
4	Day Work Cost 70 days @ 4,650	325,500		325,500
5	Bits & Reamers	42,500		42,500
6	Fuel	42,000	4,200	46,200
7	Water	5,000		5,000
8	Mud & Chemicals	65,000	5,000	70,000
9	Cementing & Service	42,500		42,500
10	Coring			
11	Surveying & Testing	40,000		40,000
12	Mud Logging	17,500		17,500
13	Perforating		5,000	5,000
14	Stimulation		30,000	30,000
15	Transportation	6,000	6,000	12,000
16	Drilling Overhead & Supervision	10,500	1,050	11,550
17	Equipment Rental	12,000	7,000	19,000
18	Completion Rig 7 days @		32,550	32,550
19	Other Drilling Expense			
20	Contingencies (10% of Intangibles)	71,850	9,080	80,930
21				
22				
23	TOTAL INTANGIBLES	790,350	99,880	890,230

TANGIBLE WELL COST

24	40 ' Of 20 " Conductor Casing	2,750		2,750
25	600 ' Of 13 3/8 " Surface Casing	10,275		10,275
26	3100 ' Of 9 5/8 " Intermediate Casing	37,925		37,925
27	' Of " Intermediate Casing			
28	11,200 ' Of 7 " Intermediate Casing	141,960		141,960
29	2200 ' Of 4 1/2 " Production Casing		22,000	22,000
30	' Of " Tie-Back Casing			
31	11,000 ' Of 2 7/8 " Tubing		107,150	107,150
32	' Of " Tubing			
33	' Of " Tubing			
34	Liner Equipment		12,500	12,500
35	Wellhead Equipment	15,000	20,000	35,000
36	Producing Facilities, Tank Battery, Flowline		30,000	30,000
37	Packers & Other Subsurface Tools			
38	Contingencies (10% of Tangibles)	20,791	19,165	39,956
39				
40				
41	TOTAL TANGIBLES	228,701	210,815	439,516
42	TOTAL WELL COST	1,019,051	310,695	1,329,746

HNG OIL COMPANY APPROVAL

By	Date	By	Date	By	Date	By	Date	By	Date

JOINT OPERATOR APPROVAL

Firm _____ By _____ Title _____ Date _____

AFE No. _____

BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 2
CASE NO. 6431
Submitted by
Hearing Date

10. Taxes

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

11. Insurance

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

12. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator in the necessary and proper conduct of the Joint Operations.

III. OVERHEAD

1. Overhead - Drilling and Producing Operations

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

(X) Fixed Rate Basis, Paragraph 1A, or
( ) Percentage Basis, Paragraph 1B.

Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under Paragraph 2A, Section II. The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the Overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by the Parties as a direct charge to the Joint Account.

ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant services and contract services of technical personnel directly employed on the Joint Property shall ( ) shall not ( ) be covered by the Overhead rates.

A. Overhead - Fixed Rate Basis

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

Drilling Well Rate $ 2398.00
Producing Well Rate $ 318.00

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

(a) Drilling Well Rate

[1] Charges for onshore drilling wells shall begin on the date the well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days.

[2] Charges for offshore drilling wells shall begin on the date when drilling or completion equipment arrives on location and terminate on the date the drilling or completion equipment moves off location or rig is released, whichever occurs first, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days

[3] Charges for wells undergoing any type of workover or recompletion for a period of five (5) consecutive days or more shall be made at the drilling well rate. Such charges shall be applied for the period from date workover operations, with rig, commence through date of rig release, except that no charge shall be made during suspension of operations for fifteen (15) or more consecutive days.

(b) Producing Well Rates

[1] An active well either produced or injected into for any portion of the month shall be considered as a one-well charge for the entire month.

[2] Each active completion in a multi-completed well in which production is not commingled down hole shall be considered as a one-well charge providing each completion is considered a separate well by the governing regulatory authority.

[3] An inactive gas well shut in because of overproduction or failure of purchaser to take the production shall be considered as a one-well charge providing the gas well is directly connected to a permanent sales outlet.

[4] A one-well charge may be made for the month in which plugging and abandonment operations are completed on any well.

[5] All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease allowable, transferred allowable, etc.) shall not qualify for an overhead charge.

(3) The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the calendar year preceding as shown by the index of average weekly earnings of Crude Petroleum and Gas Fields Production Workers as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian index as published by Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

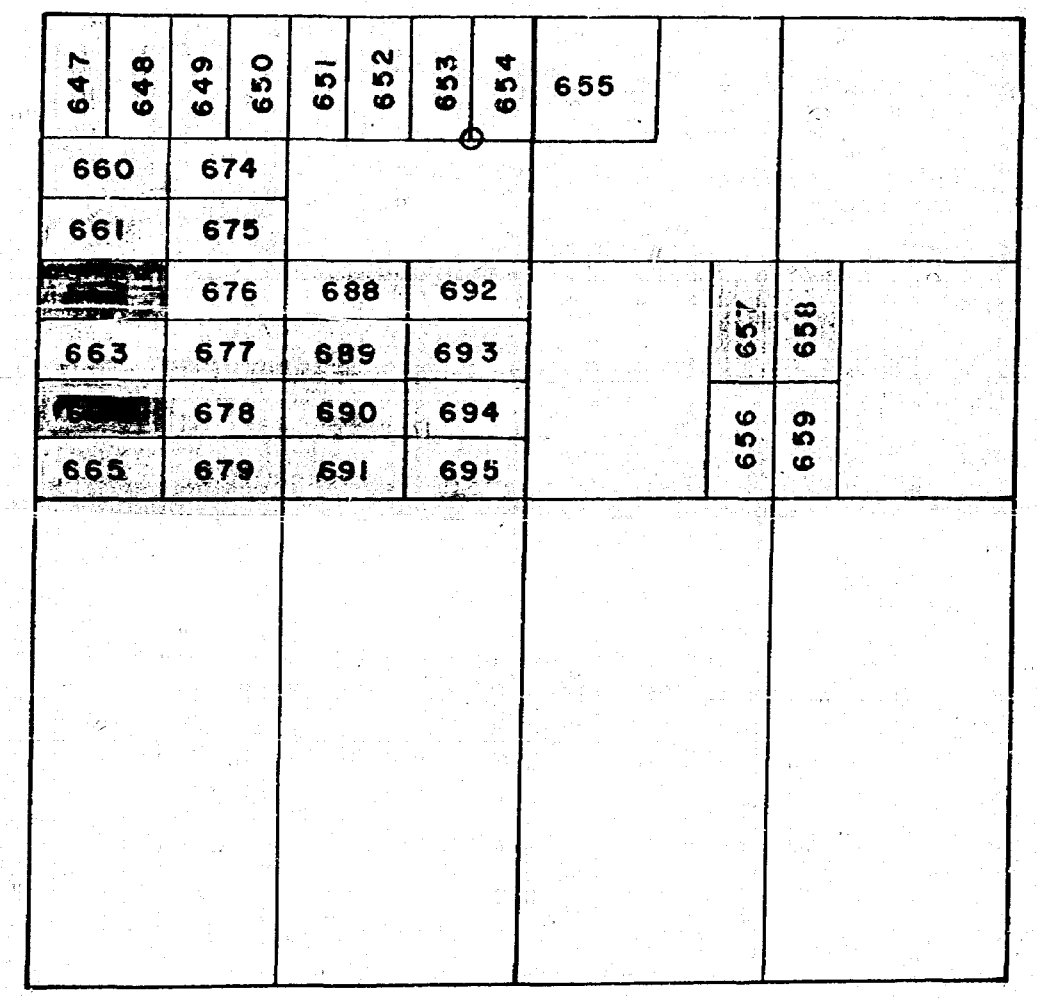
BEFORE EXAMINER STAMETS
OIL CONSERVATION DIVISION
HNG EXHIBIT NO. 8
CASE NO. 6431
Submitted by:
Hearing Date

EDDY COUNTY, NEW MEXICO

T-23-S, R-28-E

North 1/2

Section 35:



— HNG Oil Co.

— Phillips Petr.

— J. E. Russell, et al

— Enderud & Larson

— Heirs of Burt Schurr

N

Case 6451
Ex 1

CASE NO. 6431
HNG OIL COMPANY
Williams Com "35" #1
N/2 of Section 35, T-23-S, R-28-E
Eddy County, New Mexico

1.875 mineral acres in and under the N/2 SW/4 SW/4 NW/4 (Farm Tract 664) containing 5 acres.

Ownership of 1.875 acres:

Heirs of Albert Larson	1.0417 acres
Olaf Enderud	0.8333 acres
	1.8750 acres

Last Known Address: Caldwell, Kansas

5 acres being N/2 SW/4 NW/4 NW/4 (Farm Tract 660).

Ownership of 5 acres:

Heirs of Burt Schurr

Last Known Address: LeRoy, Kansas

Case 6431
Ex. 2

HNG Oil Company
P. O. BOX 2267, MIDLAND, TEXAS 79702 (915) 683-4871

January 24, 1979

Mr. Robert B. Coleman
P. O. Box 501
Midland, Texas 79702

RE: HNG-Williams "35" Com. #1
Eddy County, New Mexico

Dear Mr. Coleman:

You have advised us verbally that you are acquiring an oil and gas lease from the heirs of Burt Schurr covering the N/2 SW/4 NW/4 NW/4 of Section 35, T-23-S, R-28-E, Eddy County, New Mexico.

This company failed in its efforts to locate the present owners of the above described 5 acre tract and elected to proceed with the drilling of its Williams "35" Com. #1 Well located 660' FNL and 2310' FWL of Section 35, T-23-S, R-28-E, Eddy County, New Mexico. This test well will be drilled to sufficiently test the Morrow formation at an estimated depth of 13,400'.

On January 9, 1979 application was made (copy attached) to the Oil Conservation Division of New Mexico for compulsory pooling of all oil and gas mineral interests in the Pennsylvanian formation in and under the N/2 of said Section 35. A hearing is set for January 31, 1979 in Santa Fe, New Mexico.

Assuming you do have a valid lease covering the interests of the owners of the above mentioned 5 acre tract, we invite you to commit same to a 320 acre unit covering the N/2 of said Section 35 and to participate in the drilling of the HNG-Williams "35" Com. #1 as a working interest (1.5625%) owner. In lieu thereof, we would be agreeable to assuming your position on a farmout basis with you retaining a 1/16th overriding royalty interest with the option to convert same to a 1/2 working interest at payout of the well, both proportionately reduced.

A copy of our AFE for the drilling of the Williams "35" Com. #1 is enclosed herewith.

Yours very truly,

HNG OIL COMPANY

Raymond Parker

Raymond Parker
Manager of Lands

RP/jw
encls.

1/31
Ex 5

Blank

AFFIDAVIT

Kansas Blue Print Co.

State of Kansas)
County of Sedgwick)ss.

Tom Burden, being first duly sworn, on h is oath states, that he is a person of lawful age; that he is and has been for 18 years last past a resident of Sedgwick County, State of Kansas, and further deposes and states:

That affiant has made a thorough investigation in an attempt to locate Mr. Albert Larson and/or his heirs at law, said party being the owner of a 5/24 mineral interest in and under the N½SW¼SW¼NW¼ of Section 35-23 South, 28 East, Eddy County, New Mexico. Investigation attempts led the Affiant to Mr. D. B. Stalling, attorney at Law of Caldwell, Kansas, who knew the party in question and who at one time was a resident of Kiowa, Kansas. Affiant was advised to contact Mr. Carl McNally of Kiowa, Kansas for information regarding the whereabouts of Mr. Larson. Mr. McNally had been a long time friend of Mr. Larson. Affiant discovered Mr. McNally to be deceased, however, his surviving widow was still living, but quite elderly. She recalled that Mr. Larson had some brothers and sisters, but she did not know their whereabouts. She stated that she thought that Mr. Larson had moved to Los Angeles around 1949 and that she had not heard of or from him since nor from his brothers or sisters. She stated that Mr. Larson had a wife and several children, but they moved when Mr. Larson did. Affiant then checked with various government agencies in Sacramento, California in an attempt to locate Mr. Larson to no avail. Affiant then re-contacted Mr. Stalling for additional information without success. Therefore, affiant considers the above as representative of a thorough investigation to locate Mr. Larson, or his heirs at law, and that same are not locatable.

Further, Affiant saith not:

DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80

(SEAL)

Signed: Tom Burden
Tom Burden

Subscribed and sworn to before me this 5th day of January, A. D. 19 79.

Dorene K. Dunn
Notary Public.

My Commission Expires ....., 19.....

STATE OF Kansas }
COUNTY OF Sedgwick } ss. ACKNOWLEDGMENT FOR INDIVIDUAL (Kans. Okla. and Colo.)

Before me, the undersigned, a Notary Public, within and for said County and State, on this 5th day of January, 19 79, personally appeared Tom Burden and .....

to me personally known to be the identical person who executed the within and foregoing instrument and acknowledged to me that he executed the same as his free and voluntary act and deed for the uses and purposes therein set forth.

IN WITNESS WHEREOF, I have hereunto set my hand and official seal the day and year last above written.

My commission expires .....

DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80

Dorene K. Dunn
Notary Public

Case 6431
Ex 4

Blank

AFFIDAVIT

State of Kansas)
County of Sedgwick)ss.

Tom Burden, being first duly sworn, on h is oath states, that he is a person of lawful age; that he is and has been for 18 years last past a resident of Sedgwick County, State of Kansas, and further deposes and states: That affiant has made a thorough investigation in an attempt to locate Mr. Olaf Enderud and/or his wife, Cora Enderud, or any heirs at law of same, said parties being owners of a 4/24 mineral interest in and under the N½SW¼SW¼NW¼ of Section 35-23S-28E, Eddy County, New Mexico. Investigation attempts led the affiant to Mr. D. B. Stalling, attorney at law, in the City of Caldwell, State of Kansas. Mr. Stalling stated that Mr. and Mrs. Enderud were at one time residents of Caldwell, Kansas, but that they moved to San Diego, California in the early part of the 1940's to work in the naval shipyards in that city. However, Mr. Stalling was fairly certain that both parties are now deceased. Mr. Stalling stated that Mr. Enderud had one brother and no children. His brother's name was Ekrun Enderud and was also a resident of San Diego, California. Since the two brothers were approximately the same age, it was assumed by Mr. Stalling that Ekrun Enderud is also deceased. The affiant checked with the Department of Motor Vehicles in Sacramento, California in an attempt to locate any of the previously mentioned parties since they would probably own an automobile titled to them with an address on the State records. No such parties were listed. Affiant also checked with the Bureau of Vital Statistics in Sacramento to ascertain if any of the parties in question died a resident of the State of California since any death certificate would indicate the name and address of the next of kin. However, there were no such parties listed on the state records. Thereupon, the affiant re-contacted Mr. Stalling for additional information to no avail. Therefore, affiant feels that a thorough investigation has been made in an effort to locate Mr. and Mrs. Olaf Enderud and/or their heirs at law without results and that they are not locatable.

Further, Affiant saith not:

DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80
(SEAL)

Signed: Tom Burden
Tom Burden

Subscribed and sworn to before me this 5th day of January, A. D. 19 79

Dorene K. Dunn
Notary Public.

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STATE OF Kansas }
COUNTY OF Sedgwick } ss. ACKNOWLEDGMENT FOR INDIVIDUAL (Kans. Okla. and Colo.)

Before me, the undersigned, a Notary Public, within and for said County and State, on this 5th day of January, 19 79, personally appeared Tom Burden and .....

to me personally known to be the identical person who executed the within and foregoing instrument and acknowledged to me that he executed the same as his free and voluntary act and deed for the uses and purposes therein set forth.

IN WITNESS WHEREOF, I have hereunto set my hand and official seal the day and year last above written.

My commission expires .....

DORENE K. DUNN
Sedgwick County, Ks.
My Appmt. Exp. 1-13-80

Dorene K. Dunn
Notary Public

6431
E & S

Drilling

Delto
Strawn Sd

22

Amoco
Strawn Sd

Amoco
Brantley
I
Morrow Sd
(12264-430)
Comp 1-18-79

23

Delto
Strawn Sd

Delto

Blow-Out Well
Atoka Sd T

27

Maddox
Pardue Farms
I-27
Morrow Sd
(12480-661)
On gas sales
to El Paso
1-16-79

26

Maddox

Dual
Strawn Sd (11468-74)
Atoka Sd (11756-80)

Amoco

Strawn Sd S
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HNG
90-01, 89-02
1-9-81
(330 Net)

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"Williams Com"

84-01 thru 84-06
1-9-81
(155.762 Net)

89-03, -04, -05, -06
1-9-81
(165.90 Net)

E

3

2

NO MEXICO

HNG
90-01, -02, -03, -0
1-9-81
(44 Net)

Phillips
Mologa
I-A

Rich-Boss
Beeman
I

Morrow Sd
(12310-658)

PV & NE Ry.
(Approx)

30

10

Schobel
Beeman
11

hng
Oil Company

Case No. 6431

HNG Oil Company

Williams Com "35" #1

N/2 Sec. 35, 23S-28E

Eddy County, New Mexico

6431

Ex. 6

DRILLING OR WORKOVER AFE

HNG Oil Company

AFE NO.

LSE. NO.

HNG W.I.

HNG EST. COST

AFE DATE

[X] WILDCAT
- [X] DRILLING
- [X] COMPLETION
- [ ] RE-ENTRY

[ ] DEVELOPMENT
- [ ] DRILLING
- [ ] COMPLETION
- [ ] RE-ENTRY

[ ] WORKOVER
- [ ] SAME ZONE
- [ ] NEW ZONE
- [ ] P & A

LEASE & WELL NO. Williams Com 35-1	DEPTH & FORM 13,400 Morrow
LOCATION, 660' FNL & 2310' FWL, Sec. 35, T-23-S, R-28-E	
COUNTY & STATE Eddy, New Mexico	FIELD Wildcat
OPERATOR HNG Oil	SPUD DATE 12-10-78

	INTANGIBLE WELL COST			
	DESCRIPTION	DRILLING	COMPLETION	TOTAL
1	Access, Location & Roads	40,000		40,000
2	Rig Move	70,000		70,000
3	Footage Cost			
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5	Bits & Reamers	42,500		42,500
6	Fuel	42,000	4,200	46,200
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8	Mud & Chemicals	65,000	5,000	70,000
9	Cementing & Service	42,500		42,500
10	Coring			
11	Surveying & Testing	40,000		40,000
12	Mud Logging	17,500		17,500
13	Perforating		5,000	5,000
14	Stimulation		30,000	30,000
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18	Completion Rig 7 days @		32,550	32,550
19	Other Drilling Expense			
20	Contingencies (10% of Intangibles)	71,850	9,080	80,930
21				
22				
23	TOTAL INTANGIBLES	790,350	99,880	890,230

TANGIBLE WELL COST

24	40 ' Of 20" " Conductor Casing	2,750		2,750
25	600 ' Of 13 3/8 " Surface Casing	10,275		10,275
26	3100 ' Of 9 5/8 " Intermediate Casing	37,925		37,925
27	' Of " Intermediate Casing			
28	11,200 ' Of 7 " Intermediate Casing	141,960		141,960
29	2200 ' Of 4 1/2 " Production Casing		22,000	22,000
30	' Of " Tie-Back Casing			
31	11,000 ' Of 2 7/8 " Tubing		107,150	107,150
32	' Of " Tubing			
33	' Of " Tubing			
34	Liner Equipment		12,500	12,500
35	Wellhead Equipment	15,000	20,000	35,000
36	Producing Facilities, Tank Battery, Flowline		30,000	30,000
37	Packers & Other Subsurface Tools			
38	Contingencies (10% of Tangibles)	20,791	19,165	39,956
39				
40				
41	TOTAL TANGIBLES	228,701	210,815	439,516
42	TOTAL WELL COST	1,019,051	310,695	1,329,746

HNG OIL COMPANY APPROVAL

By	Date	By	Date	By	Date	By	Date	By	Date

JOINT OPERATOR APPROVAL

6431
Ex 7

Firm _____ By _____ Title _____ Date _____

AFE No. _____

10. Taxes

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

11. Insurance

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

12. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator in the necessary and proper conduct of the Joint Operations.

III. OVERHEAD

1. Overhead - Drilling and Producing Operations

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

(X) Fixed Rate Basis, Paragraph 1A, or
( ) Percentage Basis, Paragraph 1B.

Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under Paragraph 2A, Section II. The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the Overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by the Parties as a direct charge to the Joint Account.

ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant services and contract services of technical personnel directly employed on the Joint Property shall ( ) shall not ( ) be covered by the Overhead rates.

A. Overhead - Fixed Rate Basis

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

Drilling Well Rate $ 2398.00
Producing Well Rate $ 318.00

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

(a) Drilling Well Rate

[1] Charges for onshore drilling wells shall begin on the date the well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days.

[2] Charges for offshore drilling wells shall begin on the date when drilling or completion equipment arrives on location and terminate on the date the drilling or completion equipment moves off location or rig is released, whichever occurs first, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days

[3] Charges for wells undergoing any type of workover or recompletion for a period of five (5) consecutive days or more shall be made at the drilling well rate. Such charges shall be applied for the period from date workover operations, with rig, commence through date of rig release, except that no charge shall be made during suspension of operations for fifteen (15) or more consecutive days.

(b) Producing Well Rates

[1] An active well either produced or injected into for any portion of the month shall be considered as a one-well charge for the entire month.

[2] Each active completion in a multi-completed well in which production is not commingled down hole shall be considered as a one-well charge providing each completion is considered a separate well by the governing regulatory authority.

[3] An inactive gas well shut in because of overproduction or failure of purchaser to take the production shall be considered as a one-well charge providing the gas well is directly connected to a permanent sales outlet.

[4] A one-well charge may be made for the month in which plugging and abandonment operations are completed on any well.

[5] All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease allowable, transferred allowable, etc.) shall not qualify for an overhead charge.

(3) The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the calendar year preceding as shown by the index of average weekly earnings of Crude Petroleum and Gas Fields Production Workers as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian Index as published by Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

(M31
Ex 8

Dockets Nos. 5-79 and 6-79 are tentatively set for hearing on February 14 and 28, 1979. Applications for hearing must be filed at least 22 days in advance of hearing date.

DOCKET: EXAMINER HEARING - WEDNESDAY - JANUARY 31, 1979

9 A.M. - OIL CONSERVATION DIVISION CONFERENCE ROOM,
STATE LAND OFFICE BUILDING, SANTA FE, NEW MEXICO

The following cases will be heard before Richard L. Stamets, Examiner, or Daniel S. Nutter, Alternate Examiner:

CASE 6422: In the matter of the hearing called by the Oil Conservation Division on its own motion to permit Helton Engineering & Geological Services, Inc., Travelers Indemnity Company, and all other interested parties to appear and show cause why the Brent Well No. 1 located in Unit M of Section 29 and the Brent Well No. 3 located in Unit G of Section 19, both in Township 13 North, Range 6 East, Sandoval County, New Mexico, should not be plugged and abandoned in accordance with a Division-approved plugging program.

CASE 6415: (Continued from January 17, 1979, Examiner Hearing)

Application of Yates Petroleum Corporation for compulsory pooling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Wolfcamp thru Devonian formations underlying the W/2 of Section 20, Township 14 South, Range 36 East, Lea County, New Mexico, to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the well and a charge for risk involved in drilling said well.

CASE 6419: (Continued from January 17, 1979, Examiner Hearing)

Application of Yates Petroleum Corporation for a dual completion, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion (conventional) of its Lanning JC Well No. 1 located in Unit B of Section 7, Township 18 South, Range 26 East, Eagle Creek Field, Eddy County, New Mexico, to produce gas from the Strawn formation through the casing-tubing annulus and from the Morrow formation through tubing.

CASE 6423: Application of Yates Petroleum Corporation for an unorthodox well location, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of its Jackson AT Well No. 9 located 660 feet from the South and West lines of Section 13, Township 17 South, Range 25 East, Eddy County, New Mexico, to test the Wolfcamp, Pennsylvanian, and Mississippian formations, the S/2 of said Section 13 to be dedicated to the well.

CASE 6424: Application of Yates Petroleum Corporation for an unorthodox well location, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of its Superior Fed. KJ Well No. 1 located 990 feet from the North and West lines of Section 7, Township 20 South, Range 29 East, Eddy County, New Mexico, to test the Wolfcamp and Pennsylvanian formations, the N/2 of said Section 7 to be dedicated to the well.

CASE 6425: Application of T. B. Knox Estate for exception to Order No. R-111-A, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks an exception to the casing/cementing rules for the Oil-Potash Area as promulgated by Order No. R-111-A to permit its Lucia Brookes Well No. 2 located in Unit K of Section 14, Township 18 South, Range 30 East, Eddy County, New Mexico, to be completed in the following manner: set surface casing and circulate cement; eliminate salt protection string; and do not circulate cement on production casing.

CASE 6426: Application of C. W. Trainer for an unorthodox gas well location, Lea County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of a well to be located 660 feet from the North and West lines of Section 24, Township 20 South, Range 32 East, South Salt Lake-Morrow Pool, Lea County, New Mexico, the N/2 of said Section 24 to be dedicated to the well.

CASE 6427: Application of Caribou Four Corners, Inc., for an unorthodox well location, San Juan County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of its Caribou/Kirtland Well No. 1 to be located 1214 feet from the North line and 650 feet from the East line of Section 13, Township 29 North, Range 15 West, Cha Cha-Gallup Pool, San Juan County, New Mexico, the E/2 NE/4 to be dedicated to the well.

CASE 6428: Application of Mobil Oil Corporation for the amendment of Order No. R-5801, Lea County, New Mexico. Applicant, in the above-styled cause, seeks the amendment of Order No. R-5801 to delete the requirements for lined tubing in injection wells in the North Vacuum Abo East Pressure Maintenance Project, Lea County, New Mexico.

CASE 6429: Application of Zia Energy, Inc., for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its Elliott State Well No. 2 to be located in Unit B of Section 34, Township 20 South, Range 36 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

CASE 6430: Application of Phoenix Resources Company for a unit agreement, Chaves County, New Mexico. Applicant, in the above-styled cause, seeks approval for its Buckhorn Canyon Unit Area comprising 23,009 acres, more or less, of Federal and state lands in Township 19 South, Ranges 19 and 20 East, Chaves County, New Mexico.

CASE 6431: Application of HNG Oil Company for compulsory pooling, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East, Eddy County, New Mexico, to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the well and a charge for risk involved in drilling said well.

CASE 6432: Application of John Yuronka for compulsory pooling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Langlie Mattix Pool underlying the NE/4 NW/4 and the SE/4 NW/4 of Section 29, Township 24 South, Range 37 East, Lea County, New Mexico, to form two 40-acre units, each to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said wells and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the wells and a charge for risk involved in drilling said wells.

CASE 6433: Application of Cities Service Company for compulsory pooling, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Pennsylvanian formations underlying the S/2 of Section 8, Township 23 South, Range 28 East, Eddy County, New Mexico, to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the well and a charge for risk involved in drilling said well.

CASE 6434: Application of Amerada Hess Corporation for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its State "O" Well No. 5 to be located in Unit H of Section 30, Township 19 South, Range 37 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

CASE 6435: Application of Amerada Hess Corporation for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its W. A. Weir "B" Well No. 3 located in Unit B of Section 26, Township 19 South, Range 36 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

CASE 6436: Application of Amerada Hess Corporation for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its State "U" Gas Com Well No. 2 to be located in Unit C of Section 32, Township 19 South, Range 37 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

CASE 6437: Application of Curtis Little for approval of infill drilling and a non-standard proration unit, San Juan County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of a well to be located 1085 feet from the South line and 285 feet from the West line of Section 12, Township 28 North, Range 13 West, Basin-Dakota Pool, San Juan County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well. Applicant further seeks rescission of Order No. R-4556 and approval of a 344.36-acre non-standard gas proration unit comprising all of Section 11, and Lot 4 and the SW/4 SW/4 of Section 12 for said well.

CASE 6438: Application of Caulkins Oil Company for dual completions and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion of its Breech Well No. 812 located in Unit N of Section 18, Township 26 North, Range 6 West, and its Breech Well No. 224-A located in Unit B of Section 13, Township 26 North, Range 7 West, Rio Arriba County, New Mexico, to produce gas from the Dakota formation through a separate string of tubing and to commingle Chacra and Mesaverde production in the wellbores of said wells.

CASE 6439: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Mesaverde and Dakota production in the wellbore of its Breech A Well No. 229 located in Unit D of Section 17, Township 26 North, Range 6 West, Rio Arriba County, New Mexico.

CASE 6440: Application of Caulkins Oil Company for a dual completion and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion of its Breech F Well No. 8 located in Unit A of Section 34, Township 27 North, Range 6 West, Rio Arriba County, New Mexico, to produce gas from the Pictured Cliffs formation through a separate string of tubing and to commingle Mesaverde and Dakota production in the wellbore of said well.

CASE 6441: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs and Mesaverde production in the wellbore of its Breech F Well No. 12 located in Unit A of Section 35, Township 27 North, Range 6 West, Rio Arriba County, New Mexico.

CASE 6442: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs, Chacra and Mesaverde production in the wellbore of its Breech E Well No. 109 located in Unit M of Section 3, Township 26 North, Range 6 West, Rio Arriba County, New Mexico.

CASE 6443: Application of Caulkins Oil Company for a dual completion and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion (conventional) of its Breech B Well No. 220-R located in Unit B of Section 14, Township 26 North, Range 7 West, to produce gas from the Dakota formation through a separate string of tubing and to commingle Pictured Cliffs, Chacra and Mesaverde production in the wellbore of said well.

CASE 6444: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs, Mesaverde, Chacra and Greenhorn production in the wellbore of its Breech Well No. 224 located in Unit A of Section 13, Township 26 North, Range 7 West, Rio Arriba County, New Mexico.

Dockets Nos. 5-79 and 6-79 are tentatively set for hearing on February 14 and 28, 1979. Applications for hearing must be filed at least 22 days in advance of hearing date.

DOCKET: EXAMINER HEARING - WEDNESDAY - JANUARY 31, 1979

9 A.M. - OIL CONSERVATION DIVISION CONFERENCE ROOM,
STATE LAND OFFICE BUILDING, SANTA FE, NEW MEXICO

The following cases will be heard before Richard L. Stamets, Examiner, or Daniel S. Nutter, Alternate Examiner:

CASE 6422: In the matter of the hearing called by the Oil Conservation Division on its own motion to permit Helton Engineering & Geological Services, Inc., Travelers Indemnity Company, and all other interested parties to appear and show cause why the Brent Well No. 1 located in Unit M of Section 29 and the Brent Well No. 3 located in Unit G of Section 19, both in Township 13 North, Range 6 East, Sandoval County, New Mexico, should not be plugged and abandoned in accordance with a Division-approved plugging program.

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Application of Yates Petroleum Corporation for compulsory pooling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Wolfcamp thru Devonian formations underlying the W/2 of Section 20, Township 14 South, Range 36 East, Lea County, New Mexico, to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the well and a charge for risk involved in drilling said well.

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CASE 6423: Application of Yates Petroleum Corporation for an unorthodox well location, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of its Jackson AT Well No. 9 located 660 feet from the South and West lines of Section 13, Township 17 South, Range 25 East, Eddy County, New Mexico, to test the Wolfcamp, Pennsylvanian, and Mississippian formations, the S/2 of said Section 13 to be dedicated to the well.

CASE 6424: Application of Yates Petroleum Corporation for an unorthodox well location, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of its Superior Fed. KJ Well No. 1 located 990 feet from the North and West lines of Section 7, Township 20 South, Range 29 East, Eddy County, New Mexico, to test the Wolfcamp and Pennsylvanian formations, the N/2 of said Section 7 to be dedicated to the well.

CASE 6425: Application of T. B. Knox Estate for exception to Order No. R-111-A, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks an exception to the casing/cementing rules for the Oil-Potash Area as promulgated by Order No. R-111-A to permit its Lucia Brookes Well No. 2 located in Unit K of Section 14, Township 18 South, Range 30 East, Eddy County, New Mexico, to be completed in the following manner: set surface casing and circulate cement; eliminate salt protection string; and do not circulate cement on production casing.

CASE 6426: Application of C. W. Trainer for an unorthodox gas well location, Lea County, New Mexico. Applicant, in the above-styled cause, seeks approval for the unorthodox location of a well to be located 660 feet from the North and West lines of Section 24, Township 20 South, Range 32 East, South Salt Lake-Morrow Pool, Lea County, New Mexico, the N/2 of said Section 24 to be dedicated to the well.

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CASE 6431: Application of HNG Oil Company for compulsory pooling, Eddy County, New Mexico. Applicant, in the above-styled cause, seeks an order pooling all mineral interests in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East, Eddy County, New Mexico, to be dedicated to a well to be drilled at a standard location thereon. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof as well as actual operating costs and charges for supervision. Also to be considered will be the designation of applicant as operator of the well and a charge for risk involved in drilling said well.

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CASE 6435: Application of Amerada Hess Corporation for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its W. A. Weir "B" Well No. 3 located in Unit B of Section 26, Township 19 South, Range 36 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

CASE 6436: Application of Amerada Hess Corporation for approval of infill drilling, Lea County, New Mexico. Applicant, in the above-styled cause, seeks a finding that the drilling of its State "U" Gas Com Well No. 2 to be located in Unit C of Section 32, Township 19 South, Range 37 East, Eumont Gas Pool, Lea County, New Mexico, is necessary to effectively and efficiently drain that portion of the proration unit which cannot be so drained by the existing well, and further seeks approval of a waiver of existing well-spacing requirements.

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CASE 6438: Application of Caulkins Oil Company for dual completions and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion of its Breech Well No. 812 located in Unit N of Section 18, Township 26 North, Range 6 West, and its Breech Well No. 224-A located in Unit B of Section 13, Township 26 North, Range 7 West, Rio Arriba County, New Mexico, to produce gas from the Dakota formation through a separate string of tubing and to commingle Chacra and Mesaverde production in the wellbores of said wells.

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CASE 6440: Application of Caulkins Oil Company for a dual completion and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion of its Breech F Well No. 8 located in Unit A of Section 34, Township 27 North, Range 6 West, Rio Arriba County, New Mexico, to produce gas from the Pictured Cliffs formation through a separate string of tubing and to commingle Mesaverde and Dakota production in the wellbore of said well.

CASE 6441: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs and Mesaverde production in the wellbore of its Breech F Well No. 12 located in Unit A of Section 35, Township 27 North, Range 6 West, Rio Arriba County, New Mexico.

CASE 6442: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs, Chacra and Mesaverde production in the wellbore of its Breech E Well No. 109 located in Unit M of Section 3, Township 26 North, Range 6 West, Rio Arriba County, New Mexico.

CASE 6443: Application of Caulkins Oil Company for a dual completion and downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the dual completion (conventional) of its Breech B Well No. 220-R located in Unit B of Section 14, Township 26 North, Range 7 West, to produce gas from the Dakota formation through a separate string of tubing and to commingle Pictured Cliffs, Chacra and Mesaverde production in the wellbore of said well.

CASE 6444: Application of Caulkins Oil Company for downhole commingling, Rio Arriba County, New Mexico. Applicant, in the above-styled cause, seeks approval for the downhole commingling of Pictured Cliffs, Mesaverde, Chacra and Greenhorn production in the wellbore of its Breech Well No. 224 located in Unit A of Section 13, Township 26 North, Range 7 West, Rio Arriba County, New Mexico.

KELLAHIN and KELLAHIN
ATTORNEYS AT LAW
500 DON GASPAR AVENUE
P. O. BOX 1769
SANTA FE, NEW MEXICO 87501

JASON W. KELLAHIN
W. THOMAS KELLAHIN
KAREN AUBREY

TELEPHONE 982-4285
AREA CODE 505

January 9, 1979

Mr. Joe Ramey
Oil Conservation Division
P. O. Box 2088
Santa Fe, New Mexico 87501

Re: HNG Oil Company

Dear Joe:

I would appreciate you setting the enclosed application for hearing on January 31, 1979.

Very truly yours,

W. Thomas Kellahin

WTK/ma

Enclosure

CC: Mr. Raymond Parker

Pend docket for:
see 2 of application

JAN - 9 1979

BEFORE THE

ENERGY AND MINERAL DEPARTMENT

STATE OF NEW MEXICO

IN THE MATTER OF THE APPLICATION
OF HNG OIL COMPANY FOR COMPULSORY
POOLING, EDDY COUNTY, NEW MEXICO

Case 6431

A P P L I C A T I O N

Comes now HNG Oil Company and applies to the Oil Conservation Division of New Mexico for an order pooling all oil and gas mineral interests, whatever they may be, in the N/2 of Section ~~23,~~ 35 Township 23 South, Range 28 East, N.M.P.M., Eddy County, New Mexico, in the Pennsylvanian formation including but not limited to Morrow, Strawn and Atoka, underlying said tract, and in support thereof would show the Commission:

1. Applicant proposes to drill a well to the Pennsylvanian formation at an orthodox location 2310 feet from West line and 660 feet from the North line, dedicating the above-described 320 acre tract to the well.

2. Applicant has obtained leases, or participation in the drilling of the well from all interest owners in said 320 acre unit with the exception of the following persons, whose interest, names and addresses, to the best of applicant's information and belief, are as follows:

1.875 acre tract, designated as Farm Tract 664, located in the N/2 SW/4 SW/4 NW/4 of Section 23 Owned by Heirs of Albert Larson, and by Olaf Enderud. Last known address, Caldwell, Kansas, no other address found

5 acre tract known as Farm Tract 660, located in the N/2 SW/4 NW/4 NW/4 of Section 23

Owned by Heirs of Burt Schurr, last know address Leroy, Kansas

Heirs of Albert Larson and Olaf Inderud believed to be represented by Don B. Stallings, Attorney, Stock Exchange Building, 103 South Main Street, Caldwell, Kansas 67022

3. Applicant has made diligent effort to obtain the participation of said nonconsenting parties in the drilling of the proposed well, or, in the alternative, obtain a lease or farmout from them, but has been unable to do so.

WHEREFORE applicant prays the Division compulsory pool all of the mineral interests to the Pennsylvanian formation underlying the above tract, designating applicant as operator, and making provision in such order for applicant to recover out of production its costs of drilling, completing and equipping the proposed well, with costs of supervision while drilling, together with provisions for recovery of the costs of operation, including costs of supervision, upon completion of the well, and for a risk factor of 200% for the risk assumed in drilling the well, and for such other and further relief as proper.

Respectfully submitted,

HNG Oil Company

By W. F. Kellahin

Kellahin & Kellahin
P. O. Box 1769
Santa Fe, New Mexico 87501

ATTORNEYS FOR APPLICANT

Case 6432

JAN - 9 1979

BEFORE THE

ENERGY AND MINERAL DEPARTMENT

STATE OF NEW MEXICO

IN THE MATTER OF THE APPLICATION
OF HNG OIL COMPANY FOR COMPULSORY
POOLING, EDDY COUNTY, NEW MEXICO

A P P L I C A T I O N

Comes now HNG Oil Company and applies to the Oil Conservation Division of New Mexico for an order pooling all oil and gas mineral interests, whatever they may be, in the N/2 of Section 23, Township 23 South, Range 28 East, N.M.P.M., Eddy County, New Mexico, in the Pennsylvanian formation including but not limited to Morrow, Strawn and Atoka, underlying said tract, and in support thereof would show the Commission:

1. Applicant proposes to drill a well to the Pennsylvanian formation at an orthodox location 2310 feet from West line and 660 feet from the North line, dedicating the above-described 320 acre tract to the well.

2. Applicant has obtained leases, or participation in the drilling of the well from all interest owners in said 320 acre unit with the exception of the following persons, whose interest, names and addresses, to the best of applicant's information and belief, are as follows:

1.875 acre tract, designated as Farm Tract 664, located in the N/2 SW/4 SW/4 NW/4 of Section 23 Owned by Heirs of Albert Larson, and by Olaf Enderud. Last known address, Caldwell, Kansas, no other address found

5 acre tract known as Farm Tract 660, located in the N/2 SW/4 NW/4 NW/4 of Section 23

Owned by Heirs of Burt Schurr, last know address Leroy, Kansas

Heirs of Albert Larson and Olaf Enderud believed to be represented by Don B. Stallings, Attorney, Stock Exchange Building, 103 South Main Street, Caldwell, Kansas 67022

3. Applicant has made diligent effort to obtain the participation of said nonconsenting parties in the drilling of the proposed well, or, in the alternative, obtain a lease or farmout from them, but has been unable to do so.

WHEREFORE applicant prays the Division compulsory pool all of the mineral interests to the Pennsylvanian formation underlying the above tract, designating applicant as operator, and making provision in such order for applicant to recover out of production its costs of drilling, completing and equipping the proposed well, with costs of supervision while drilling, together with provisions for recovery of the costs of operation, including costs of supervision, upon completion of the well, and for a risk factor of 200% for the risk assumed in drilling the well, and for such other and further relief as proper.

Respectfully submitted,

HNG Oil Company

By _____
Kellahin & Kellahin
P. O. Box 1769
Santa Fe, New Mexico 87501

ATTORNEYS FOR APPLICANT

BEFORE THE

ENERGY AND MINERAL DEPARTMENT

STATE OF NEW MEXICO

JAN - 9 1979

IN THE MATTER OF THE APPLICATION
OF HNG OIL COMPANY FOR COMPULSORY
POOLING, EDDY COUNTY, NEW MEXICO

Case 6434

A P P L I C A T I O N

Comes now HNG Oil Company and applies to the Oil Conservation Division of New Mexico for an order pooling all oil and gas mineral interests, whatever they may be, in the N/2 of Section 23, Township 23 South, Range 28 East, N.M.P.M., Eddy County, New Mexico, in the Pennsylvanian formation including but not limited to Morrow, Strawn and Atoka, underlying said tract, and in support thereof would show the Commission:

1. Applicant proposes to drill a well to the Pennsylvanian formation at an orthodox location 2310 feet from West line and 660 feet from the North line, dedicating the above-described 320 acre tract to the well.

2. Applicant has obtained leases, or participation in the drilling of the well from all interest owners in said 320 acre unit with the exception of the following persons, whose interest, names and addresses, to the best of applicant's information and belief, are as follows:

1.875 acre tract, designated as Farm Tract 664, located in the N/2 SW/4 SW/4 NW/4 of Section 23 Owned by Heirs of Albert Larson, and by Olaf Enderud. Last known address, Caldwell, Kansas, no other address found

5 acre tract known as Farm Tract 660, located in the N/2 SW/4 NW/4 NW/4 of Section 23

Owned by Heirs of Burt Schurr, last know address Leroy, Kansas

Heirs of Albert Larson and Olaf Enderud believed to be represented by Don B. Stallings, Attorney, Stock Exchange Building, 103 South Main Street, Caldwell, Kansas 67022

3. Applicant has made diligent effort to obtain the participation of said nonconsenting parties in the drilling of the proposed well, or, in the alternative, obtain a lease or farmout from them, but has been unable to do so.

WHEREFORE applicant prays the Division compulsory pool all of the mineral interests to the Pennsylvanian formation underlying the above tract, designating applicant as operator, and making provision in such order for applicant to recover out of production its costs of drilling, completing and equipping the proposed well, with costs of supervision while drilling, together with provisions for recovery of the costs of operation, including costs of supervision, upon completion of the well, and for a risk factor of 200% for the risk assumed in drilling the well, and for such other and further relief as proper.

Respectfully submitted,

HNG Oil Company

By _____

Kellahin & Kellahin
P. O. Box 1769
Santa Fe, New Mexico 87501

ATTORNEYS FOR APPLICANT

DRAFT

dr/

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION DIVISION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 6431

Order No. R- 5994

APPLICATION OF HNG OIL COMPANY FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 9 a.m. on January 31, 19 79, at Santa Fe, New Mexico, before Examiner Richard L. Stamets.

NOW, on this _____ day of February, 1979, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS:

(1) That due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) That the applicant, HNG Oil Company, seeks an order pooling all mineral interests in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East NMPM, _____, Eddy County, New Mexico.

(3) That the applicant has the right to drill and proposes to drill a well at a standard location thereon.

(4) That there are interest owners in the proposed proration unit who have not agreed to pool their interests.

(5) That to avoid the drilling of unnecessary wells, to protect correlative rights, and to afford to the owner of each interest in said unit the opportunity to recover or receive without unnecessary expense his just and fair share of the gas in said pool, the subject application should be approved by pooling all mineral interests, whatever they may be, within said unit.

(6) That the applicant should be designated the operator of the subject well and unit.

(7) That any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(8) That any non-consenting working interest owner that does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(9) That any non-consenting interest owner should be afforded the opportunity to object to the actual well costs but that actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(10) That following determination of reasonable well costs, any non-consenting working interest owner that has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(11) That $2388.00 per month should be fixed as a reasonable charge for supervision (combined fixed rates) while drilling and that $318.00 per month should be fixed as a reasonable charge for supervision while producing; that this charge should be adjusted annually based upon the percentage increase or decrease in the average weekly earnings of crude petroleum and gas production workers; that the operator should be authorized to withhold from production the proportionate share of such supervision charge attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

~~attributable to each non-consenting working interest.~~

(12) That all proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(13) That upon the failure of the operator of said pooled unit to commence drilling of the well to which said unit is dedicated on or before August 1, 1979, the order pooling said unit should become null and void and of no effect whatsoever.

IT IS THEREFORE ORDERED:

(1) That all mineral interests, whatever they may be, in the Pennsylvanian formation underlying the N/2 of Section 35, Township 23 South, Range 28 East, NMPM, ~~[illegible]~~, Eddy County, New Mexico, are hereby pooled to form a standard 320- acre gas spacing and proration unit to be dedicated to a well to be drilled at a standard location thereon.

PROVIDED HOWEVER, that the operator of said unit shall commence the drilling of said well on or before the 1st day of August, 1979, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Pennsylvanian formation;

PROVIDED FURTHER, that in the event said operator does not commence the drilling of said well on or before the 1st day of August, 1979, Order (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division for good cause shown.

PROVIDED FURTHER, that should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Order (1) of this order should not be rescinded.

(2) That HNG Oil Company is hereby designated the operator of the subject well and unit.

(3) That after the effective date of this order and within ~~30~~ 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject unit an itemized schedule of estimated well costs.

(4) That within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and that any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(5) That the operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the well; that if no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, that if there is an objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(6) That within 60 days following determination of reasonable well costs, any non-consenting working interest owner that has paid his share of estimated costs in advance as provided

above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

(7) That the operator is hereby authorized to withhold the following costs and charges from production:

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(8) That the operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(9) That $2398.00 per month is hereby fixed as a reasonable charge for supervision (combined fixed rates) while drilling, and that $318.00 per month is hereby fixed as a reasonable charge for supervision while producing, provided that this rate shall be adjusted on the first day of April of each year following the effective date of this order; that the adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the preceding calendar year as shown by "The Index of Average Weekly Earnings of Crude Petroleum and Gas Production Workers" as published by the United States Department of Labor, Bureau of Labor Statistics, and the adjusted rate shall be the rates currently in use, plus or minus the computed adjustment; that the operator is hereby authorized to withhold from production the proportionate share of such supervision charge attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(10) That any unsevered mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(11) That any well costs or charges which are to be paid out of production shall be withheld only from the working interests share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(12) That all proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Eddy County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; that the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

(13) That jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.