

dugan production corp.

November 25, 1997

Mr. Bill LeMay, Director
New Mexico Oil Conservation Div.
2040 South Pacheco Street
Santa Fe, NM 87505

Mr. Ray Powell, Commissioner
New Mexico State Land Office
P. O. Box 1148
Santa Fe, NM 87504-1148

Mr. Duane Spencer, Fluid Minerals, Manager
Bureau of Land Management
1235 La Plata Highway
Farmington, NM 87401

Re: Request for Surface Commingling, Off-lease Measurement and
Sale of Produced Natural Gas - Three Additional Wells
Dugan Production's Topaz Gas Gathering System
Federal Lease SF-078156 (Sections 33 & 34, T26N, R13W)
State Lease LG-3734 (Section 2, T25N, R13W)
San Juan County, New Mexico

Dear Mr. LeMay, Mr. Powell, and Mr. Spencer:

We are writing to request approval for the surface commingling, plus off-lease measurement and sale of gas produced from three additional natural gas wells to be connected to our Topaz Gas Gathering System.

Dugan Production's Topaz Gas Gathering Systems currently receives gas from nine Basin Fruitland Coal wells and during September 1997 production totalled 14,668 MCF (@ 15.025 psi) for an average of 489 MCFD. The operation of the gas gathering system which delivers gas to a CDP sales meter on El Paso Field Services' system in the NW/4 SE/4 of Section 25, T26N, R13W was initially authorized for six wells in 1994 and has been expanded two times. The dates of approval for each expansion are included on Attachment No. 2.

Attachment No. 1 presents the Topaz Gas Gathering System with the addition of Dugan Production's Bisti State #1, and Salge Federal A wells #94 and #95 which are the three wells to be added with this application.

The pertinent lease and well information for these three wells along with the nine other wells currently delivering gas into the Topaz Gas Gathering System is presented on Attachments No. 1 & 2. The Bisti State #1 was initially completed by Hicks Oil & Gas in the Bisti Gallup oil pool and upon acquiring this well from Hicks, Dugan Production plugged back the Gallup completion and completed the Basin Fruitland Coal interval on 9-11-97. This well has been connected to the Topaz Gas Gathering System and the connecting line was pressure tested to the maximum system pressure of 100 psi with no loss of pressure.

The Salge Federal A #94 has been drilled and 4½" casing was cemented through the Fruitland Coal on 11-12-97. The completion procedure is currently being prepared and this well will be completed in the Basin Fruitland Coal in the very near future.

The Salge Federal A #95 has not been drilled but an APD for a Fruitland Coal completion was submitted on 6-3-97 and will be the 4th Basin Fruitland Coal well on Federal Lease SF-078156. The surface for this location is controlled by the Navajo Tribe as part of the Navajo Indian Irrigation Project and as such also requires tribal approval which hopefully will not take too much longer. We are including this well with this application since we plan to commence drilling operations upon receiving approval of our APD.

The three subject wells either are or will all be completed in the Basin Fruitland Coal at intervals correlative to the producing interval in the nine other wells currently approved and delivering gas into the Topaz Gas Gathering System and we anticipate the production performance from these three wells to be similar to other wells currently connected to the gathering system, i.e., primarily dry natural gas and possibly a small amount of water. We do not anticipate any liquid hydrocarbons to be produced from any of the wells. All gas production will be metered at the individual wells utilizing conventional metering equipment. As with the other nine wells, the measurements from the wellsite meters will be utilized to determine factors for allocating sales volumes, BTUs and revenues from the CDP back to the individual wells. The procedures currently approved for the nine existing wells on the Topaz Gas Gathering System is presented on Attachment No. 3 and will also be utilized for the Bisti State #1 and the Salge Federal A wells #94 and #95.

Dugan Production Corp. is the operator of all wells connected to the Topaz Gas Gathering System, and only State and Federal mineral interest is involved in any of the 12 spacing units. There is no Indian or Fee mineral ownership.

Many of the wells presented on Attachment No. 1 are part of Dugan Production's West Bisti Unit which produces oil from the Gallup formation with very little casinghead gas. These wells are not connected to the Topaz Gas Gathering System. For clarification, the nine wells connected to the Topaz Gas Gathering System have been highlighted in blue, and the three wells proposed to be connected are highlighted in orange.

The commingling of the natural gas production from each lease is the result of using a common system to gather and transport the produced gas to the CDP sales meter. All gas volumes will be continuously measured at each well using conventional metering equipment installed and maintained by Dugan Production.

Currently, the Alamo Com No. 90 and Cisco Com No. 91 are the only well that has equipment requiring lease fuel, and since the Topaz Gas Gathering System is connected to EPNG's low pressure pipeline (100 psi or less), we do not anticipate the installation of any equipment which would require fuel in the near future. Should it become necessary to supply fuel to lease or system equipment, all volumes will be accounted for and allocated to the wells benefiting from the operation of the equipment. The current lease fuel requirements are presented on Attachment No. 4.

In summary, Dugan Production Corp. is requesting approval to add three wells (two on Federal and one on State leases), to the Topaz Gas Gathering System which will require surface commingling, plus off-lease measurement and sale of produced gas. These wells will be operated in the same manner that has been approved by the BLM, NMOCD and the State Land Office for the nine wells currently delivering gas into the system. Dugan Production Corp. has incurred a substantial investment in installing this gathering system, following extensive negotiations with EPNG upon their refusal to make wellhead connections for any of these wells. The only way EPNG (now El Paso Field Services) would consider accepting the gas produced from the subject wells was if we gathered and delivered the gas to a central point on their existing system, which has necessitated the installation and operation of the Topaz Gas Gathering System.

Should you need additional information or have questions regarding any of this information, please feel free to contact me or Barbara Williams at the letterhead address.

Sincerely,

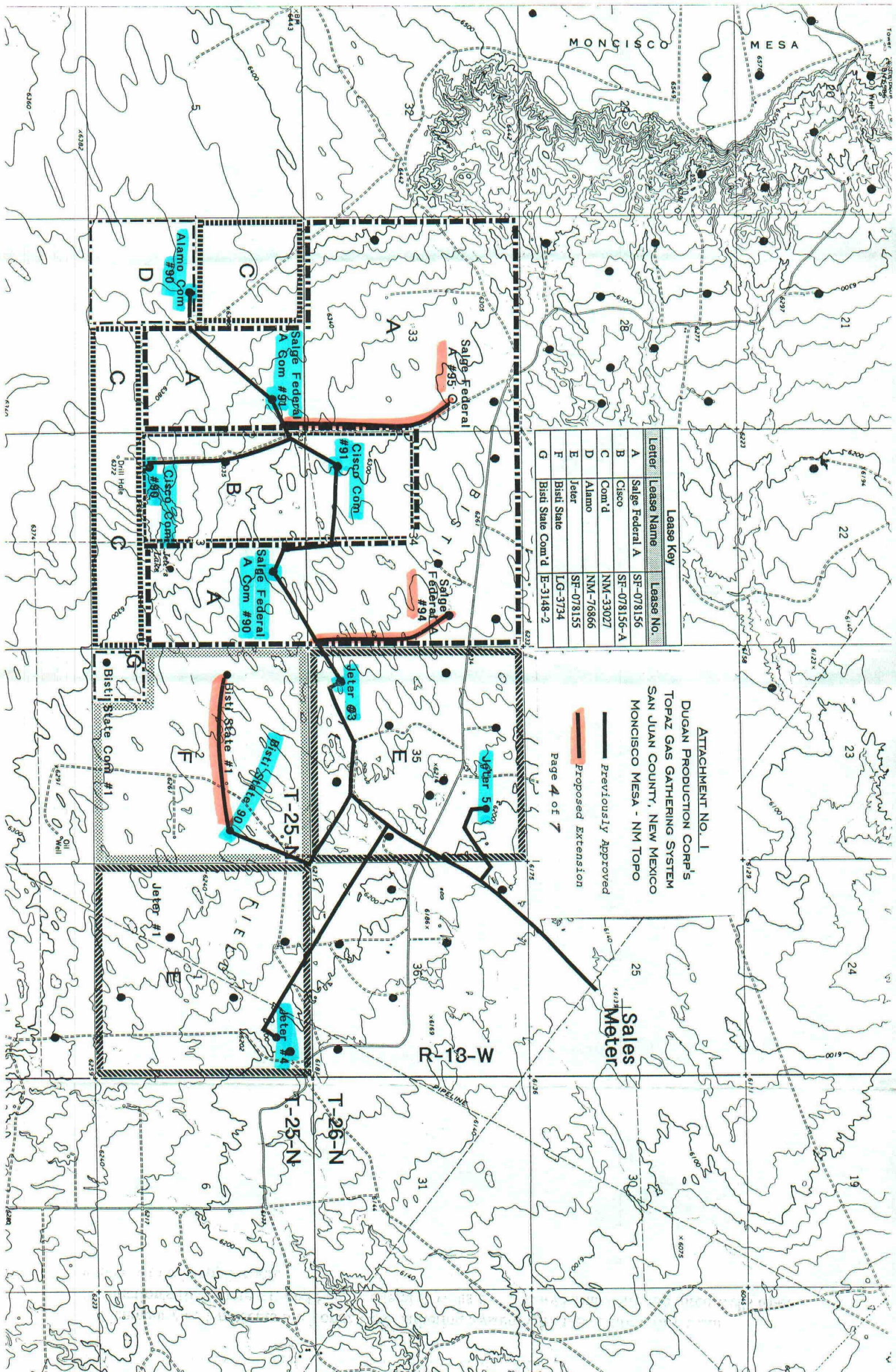


John D. Roe
Engineering Manager

JDR/tmf

attachs.

cc: NMOCD - Aztec



MONCISCO MESA

Lease Key	
Letter	Lease Name
A	Salge Federal A
B	Cisco
C	Com'd
D	Alamo
E	Jeter
F	Bisti State
G	Bisti State Com'd

ATTACHMENT NO. 1
DUGAN PRODUCTION CORP'S
TOPAZ GAS GATHERING SYSTEM
SAN JUAN COUNTY, NEW MEXICO
MONCISCO MESA - NM TOPO

Previously Approved
Proposed Extension

ATTACHMENT NO. 2
DUGAN PRODUCTION CORP.
TOPAZ GAS GATHERING SYSTEM 11-21-97
SAN JUAN COUNTY, NEW MEXICO

Well Name	API No.	Well Location		Lease Number	Type Lease	Communization Agreement Number	Producing Interval	Completion Date	Current Average Production		Spacing Unit	Dates for Surface Commingling, Off-Lease Measurement & Sales			
		¼ ¼	Sec-Twn-Rng						①	BWPD		Application	BLM	SLO	APPROVAL
Bisti State #1	25834	SWNW	02-25N-13W	LG-3734	State	State Com.	Basin Fruitland Coal	09-11-97	74*	0.3*	E/2-319.57A	11-24-97			
Salge Federal A #94	29501	SENE	34-26N-13W	SF 078156	Fed.	N/A	Basin Fruitland Coal	Note ③	---	---	E/2-320A	11-24-97			
Salge Federal A #95	NR	SENE	33-26N-13W	SF 078156	Fed.	N/A	Basin Fruitland Coal	Note ④	---	---	E/2-320A	11-24-97			

WELLS PREVIOUSLY APPROVED FOR SYSTEM

Alamo Com #90	28806	NESW	04-25N-13W	NM 76866	Fed.	NM NM 91217	Basin Fruitland Coal	08-15-93	28*	19*	W/2-320A	08-26-94	②	10-11-94	10-09-96	a
Bisti State #90	29216	SENE	02-25N-13W	LG-3734	State	N/A	Basin Fruitland Coal	09-18-96	53	1.1	E/2-319.67A	09-26-96		12-12-96	10-09-96	c
Cisco Com #90	28662	NWSW	03-25N-13W	SF 078156-A	Fed.	NM NM 89398	Basin Fruitland Coal	02-22-93	7	0.7	W/2-320A	08-26-94	②	10-11-94	10-09-96	a
Cisco Com #91	28805	SWSW	34-26N-13W	SF 078156-A	Fed.	NM NM 89374	Basin Fruitland Coal	04-15-93	45	1.4	W/2-320A	08-26-94	②	10-11-94	10-09-96	a
Jeter #3	28860	SWSW	35-26N-13W	SF 078155	Fed.	N/A	Basin Fruitland Coal	04-12-93	142	0.6	S/2-320A	08-26-94	②	10-11-94	10-09-96	a
Jeter #4	28804	NENE	01-25N-13W	SF 078155	Fed.	N/A	Basin Fruitland Coal	12-21-92	52	0.3	N/2-320A	12-29-94		01-09-95	10-09-96	b
Jeter #5	29390	NENE	35-26N-13W	SF 078155	Fed.	N/A	Basin Fruitland Coal	09-17-96	33	0.2	N/2-320A	09-26-96		12-12-96	10-09-96	c
Salge Federal A Com #90	28587	NWNE	03-25N-13W	SF 078156	Fed.	NM NM 88297	Basin Fruitland Coal	02-12-92	100	1.0	E/2-320A	08-26-94	②	10-11-94	10-09-96	a
Salge Federal A Com #91	28663	NENE	04-25N-13W	SF 078156	Fed.	NM NM 89362	Basin Fruitland Coal	02-14-93	13	1.5	E/2-320A	08-26-94	②	10-11-94	10-09-96	a

N/A - Not Applicable

NR - None Reported

- ① - Average production 8/97 & 9/97. * = well not producing 8/97 & 9/97. Rates are estimated from subsequent testing.
- ② - Application Supplemented 9/19/94, 9/30/94 and 10/19/94
- ③ - Well not completed. Spudded 11/7/97 & currently waiting to be completed.
- ④ - Well location, APD submitted 6/03/97.
- ⑤ - NMOCDC Commingling order CTB-407: a = 02-09-95; b = 05-16-95; c = 12-04-96

Attachment No. 3
Allocation Procedures
Dugan Production Corp.'s
Topaz Gas Gathering System
CPD - NWSE 25, T-26N, R-13W
San Juan County, New Mexico

Base Data:

W=Volume (MCF) from Well Allocation Meter

X=Volume (MCF) from CPD Sales Meter

Y=BTU's from CPD Sales Meter

Z=Gas Revenue (\$) from CPD Sales Meter

1. Individual Well Production = A+B+C+D+E

A = Allocated Sales Volume, MCF.

= (W/SUM W) x X

B = On lease fuel usage, MCF. Determined from equipment specifications and operating conditions.

C = Purged and/or vented gas from well and/or lease equipment, MCF. Calculated using equipment specifications and pressures.

D = Allocated fuel from gathering system equipment, MCF. The total fuel required to operate gathering system equipment will be allocated to the individual wells benefiting from the equipment using allocation factors determined by W / Sum W for the wells involved.

E = Allocated volume of gas lost and/or vented from the gathering system and/or gathering system equipment, MCF. The total volume will be determined using industry accepted procedures for the conditions existing at the time of the loss. All volumes corresponding to liquid condensation within the gathering system will also be determined. The total volume lost and/or vented will be allocated to the individual wells affected using factors determined by W / Sum W.

2. Allocated Individual Well BTU's = ((W x Individual well BTU) / Sum (W x individual well BTU)) x Y.

Individual well gas heating values to be determined in accordance with BLM's On Shore Order No. 5.

3. Allocated Individual Well Gas Revenues = (Allocated Individual well BTU's / Sum Allocated individual well BTU's) x Z

GAS USE (1)

DUGAN PRODUCTION CORP.

TOPAZ GAS GATHERING SYSTEM

SAN JUAN COUNTY, NEW MEXICO

Well Location	Equipment						Gas Purged to Unload Accumulated Liquids		
	Separator Burner BTU/hr	HP of Pump Unit Engine	HP of Compressor Engine	Lease Fuel MCFD (2)		Normal Tubing Size -Inch	Average Wellhead Press - psia	MCF per Cycle	
				Summer Months	Winter Months				
WELLS TO BE ADDED TO SYSTEM									
Bisti State #1	---	---	---	0	0	1-1/4"	71	0.06	
Salge Federal A #94	---	---	---	Note(3)	Note(3)	---	---	---	
'Salge Federal A #95	---	---	---	Note(3)	Note(3)	---	---	---	
WELLS PREVIOUSLY APPROVED FOR SYSTEM									
Alamo Com #90	---	7 (4)	---	1.76 (4)	1.76 (4)	2-3/8"	60	0	
Bisti State #90	---	---	---	0	0	1-1/4"	61	0.05	
Cisco Com #90	---	---	---	0	0	1-1/2"	60	0.08	
Cisco Com #91	90M	---	---	0	0.49	1-1/2"	54	0.07	
Jeter #3	---	---	---	0	0	1-1/2"	69	0.08	
Jeter #4	---	---	---	0	0	1-1/2"	54	0.06	
Jeter #5	---	---	---	0	0	1-1/4"	61	0.05	
Salge Fed A Com #90	---	---	---	0	0	2-3/8"	68	0.13	
Salge Fed A Com #91	---	---	---	0	0	1-1/2"	59	0.07	
System Equipment	---	---	---	0	0	---	---	---	

Notes:

- (1) Data reflects information as of 11-25-97. As descriptions &/or equipment change, fuel uses will also change.
- (2) Summer Months = May thru October. Winter Months = November thru April. Lease fuel is calculated from stated burner requirements and horsepower.
- (3) Well not completed - None anticipated.
- (4) Rod pump equipment installed 11-12-97. No fuel use prior to rod pump installation.