



RICHARDSON OPERATING COMPANY

4601 DTC Blvd., Suite 470
Denver, Colorado 80237 (303) 830-8000
Fax (303) 830-8009

RECEIVED

FEB 14 2003

OIL CONSERVATION
DIVISION

February 12, 2003

Mr. Evan Jones
Vice President
San Juan Coal Company
300 West Arrington, Suite 200
Farmington, New Mexico 87401

Re: San Juan Coal Company "Gas Recovery Proposal"

Dear Mr. Jones:

Richardson Operating Company ("Richardson") is in receipt of the so-called "Gas Recovery Proposal" proffered by San Juan Coal Company ("San Juan") in your letter dated February 5, 2003. While this proposal is purportedly intended to "improve[] recovery of the resources in question," in fact, it is only the latest in a long series of attempts by San Juan to advance its own interests at the expense of other senior interests which it continues to disregard. With all due respect, this proposal smacks of the same arrogance which caused this conflict in the first place. In essence, San Juan offers to provide Richardson with whatever portion of Richardson's senior right San Juan can manage not to destroy by its junior-in-right coal mining operations. The premise upon which your proposal is based, *e.g.*, that San Juan has a right to conduct its coal mining operation at the expense of Richardson's senior rights, is fundamentally flawed for a number of reasons.

As you know, the oil and gas leases under which Richardson has developed, and intends to continue developing, valuable coalbed gas reserves are substantially prior in time to the coal lease held by San Juan. As you are also well aware, the relevant coal lease held by San Juan is expressly made subject to the rights of senior existing leaseholders in the same lands. Thus, when San Juan acquired this coal lease, it knew that Richardson held senior oil and gas leases on

the same lands and acknowledged that it was subject to Richardson's senior rights pursuant to those leases. Nevertheless, San Juan now maintains that the rights of Richardson and other senior interest holders must yield to San Juan's junior interests based, primarily, on the fact that San Juan is San Juan. This most recent proposal (to provide Richardson with the degraded leftovers of its interest that San Juan doesn't destroy) is only the latest affront by San Juan premised on the notion that the normal rules don't apply in this situation for some reason.

This proposal is particularly insulting because it parades as an attempt to maximize resource recovery when, in fact, it will result in just the opposite. Rather than facilitating the development of all recoverable reserves, San Juan's proposal is a thinly-veiled ploy to appease Richardson by offering enough of its own gas (although significantly degraded in quality) that it would stand idly by and watch San Juan destroy the remainder (*e.g.*, the majority of the potential gas reserves) in order to develop its junior coal interests. The absurdity of this proposition reveals the true depth of San Juan's presumptuousness.

As an alternative to your euphemistic proposal for "simultaneous mineral development," San Juan suggests that Richardson may prefer a buyout instead. Thus, rather than agreeing to the complete destruction of its interest, save the small volume of contaminated gas San Juan may be able to capture, Richardson may instead capitulate to the insistent demands of a junior interest holder and accept a dollar amount for its troubles. San Juan apparently fails to apprehend the fact that Richardson does not want a buyout; it wants San Juan to stop conducting any operations which interfere with Richardson's senior right to develop its oil and gas leases until those resources have been fully developed. Even if Richardson did want a buyout, which it does not, San Juan's prior proposals have bordered on the ridiculous. For example, San Juan said there was no gas in Section 36, T30N R15W, and therefore offered Richardson a few hundred dollars for its wells. Richardson deemed this offer to be somewhat inadequate, given the fact that it had already invested more than a million dollars in that section alone. The several million dollars worth of gas Richardson has since developed from Section 36 also tends to support its decision to reject San Juan's token offer.

It is not Richardson's fault that San Juan has engaged in shortsighted development of junior coal leases which are expressly subject to Richardson's senior rights in the same lands. Neither is it Richardson's problem that San Juan drastically underestimated Richardson's desire to develop its senior interests, which it has every legal right and every intention to do. Richardson will not agree to this proposal, nor any other, which sacrifices its senior oil and gas interests and the valuable resources they represent on the altar of efficiency or for the principle that might makes right. By this proposal, San Juan offers Richardson little more than the contaminated remains of gas it already owns. Alternatively, San Juan proposes a buyout which it has previously given Richardson meager cause to consider. Richardson wants to develop its senior oil and gas interests, and intends to do just that. Richardson will therefore not consent to any negotiation of "fair market value," which, of course, is predicated on the existence of a willing seller. Richardson is not a willing seller, it is a senior interest holder who will not

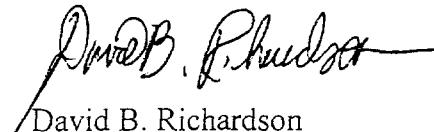
tolerate the impairment of its senior rights by San Juan nor any attempt destroy those rights through any process which would amount to a private right of condemnation.

Richardson's rights are senior in time. San Juan's junior coal leases are expressly made subject to such senior rights. San Juan's most recent proposal stands these principles on their head and is, therefore, rejected. Several months ago, in an effort to resolve the disparity between San Juan's expressed development intentions and its legal right to accomplish those objectives, Richardson offered an engineered proposal for settlement of this conflict. If your letter of February 5 constitutes San Juan's best response to that good faith proposal, then there is no point in any further negotiations unless and until San Juan recognizes the primacy of Richardson's right to develop its oil and gas interests in these lands and modifies its approach accordingly.

At this point, Richardson fully intends to continue developing its senior interests and will aggressively defend against any impairment of its legal right to do so. Richardson has already been forced to expend an inordinate amount of time and money responding to San Juan's refusal to recognize its presumptively senior right. Because Richardson's right is undeniably first in time and San Juan expressly made itself subject to senior interests in the same lands, please be advised that Richardson will hold San Juan accountable for all costs incurred to vindicate its right to develop its senior leasehold interests.

Sincerely,

RICHARDSON OPERATING COMPANY


David B. Richardson
President

cc: Steve Henke, BLM Farmington Field Office
Carston Goff, Deputy State Director, BLM NM State Office
Arthur Arguedas, Department of Interior Solicitor
✓ Lori Wrotenbery, Chairman, State of New Mexico Oil Conservation Commission
Jenifer Prokup, Secretary, NM Energy, Minerals, and Natural Resources Department
Patrick Lyons, Commissioner, NM State Land Office
Peter Bjork, Esq., Bjork, Lindley, Danielson & Little, P.C
Steve Ross, Esq., Oil Conservation Commission