

San Juan Coal Company

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OIL CONSERVATION
DIVISION



March 18, 2003

Mr. David B. Richardson, President
Richardson Operating Company
1700 Lincoln, Suite 1700
Denver CO 80203

BHP Billiton Limited
300 West Arrington, Suite 200
Farmington, New Mexico 87401 USA
Tel +1 505 598 4350 Fax +1 505 598 4300
bhpbilliton.com

RE: Richardson Operating Company's February 12, 2003 letter

Dear Mr. Richardson,

I considered not responding at all to the above referenced letter, given its content and tone. However, I thought it would be helpful to address some of the matters in your letter, without necessarily conceding or agreeing with those matters that are not addressed here. I am disappointed that Richardson Operating Company appears to be unwilling to discuss any amicable resolution of this matter at this time. Nonetheless, on behalf of San Juan Coal Company ("San Juan"), I would offer to maintain lines of communication between our companies to promote better understanding of the resource development conflict with which we are dealing. It is my hope that over time this enhanced understanding may contribute to a resolution of the conflict.

San Juan continues to seek ways to resolve the differences that separate our Companies. Because of mine safety and coal recovery issues caused by hydro-fracturing the coal seam during "conventional" gas well recovery operations, we have not wanted any additional "conventional" gas wells to be established in the mine area. As indicated in our February 5 letter, San Juan believes it may be able to safely develop some coal bed methane in advance of and during mining. You want to recover as much of the gas as possible, as inexpensively as possible. San Juan also wants the gas removed to reduce mine safety risks with as little an impact to the coal as possible. We have very similar goals; our differences lie, at least partially, in the method to be used to extract the gas that is present in the coal. It seems that these goals could be mutually best met by:

- You maximizing your gas extraction ahead of coal mining without damaging the coal using existing wells with no further hydro fracturing. Any new wells could use extraction technologies that are available that would allow gas recovery without damaging the coal seam or adjacent strata.
- San Juan recovering as much gas as safely and economically feasible in conjunction with its operations and delivering that gas to you (or the appropriate gas lessee) at the surface. A substantial amount of useable gas may be made available in conjunction with the mining operation that otherwise would not be available. Two of the possibilities are:
 - Gob vent boreholes - The mining process breaks up the strata above the No. 8 coal seam, including the coal left in the roof of the mine, far more than any conventional gas well drilling, completion and extraction activities. This greater "rubblizing" of the

A member of the BHP Billiton group
which is headquartered in Australia
Registered Office: 600 Bourke Street
Melbourne Victoria 3000 Australia
ABN 49 004 028 077
Registered in Australia

formations above the target coal seam allows a higher percentage of gas to be released from the rock that remains after mining. This gas could be delivered to the surface and potentially gathered by oil and gas lessees.

- o Horizontal holes - Holes can be drilled directly into the face of the No. 8 coal seam to extract methane existing in the coal. While San Juan does not yet have specific experience with how much gas such horizontal drilling might produce, this method may recover gas that could be delivered to the surface for collection as well.


The coal outcrop areas are marginal sources for coalbed methane production when compared to other areas in the San Juan Basin. Because of this, it has only been recently that you have targeted these areas for coalbed methane development, despite the fact that your leases were issued some time ago. While San Juan understands generally that your oil and gas leases were issued by the BLM and State prior to the coal leases that San Juan holds, San Juan asserts that the issuance of a lease is not the only or primary factor to consider in determining how a resource is developed. In this instance, since multiple overlapping resources have been leased, it is San Juan's position that the a number of factors including permit issuance date, land use designation, primary resource designation, public good, and resource utilization among others need to be considered. To this end San Juan would like to work with you and the BLM and State of NM to resolve this conflict.

SJCC has been desirous from the beginning to pay you the fair market value for the gas leases you hold in the mining areas. "Fair market value" should take into account not only the value of the gas but also the capital and operating costs required to produce it. To this end, San Juan engaged a reputable firm, Netherland, Sewell & Associates, Inc. (NSAI), with expertise in valuing gas properties to establish a value for the gas reserves in question. Given your reference to prior negotiations, I must state that the offer San Juan made to you for your leases was above the value calculated by NSAI. Given that our negotiations are covered by a confidentiality agreement, I refrain from further comment concerning those negotiations, and trust that you will do the same.

In any event, SJCC continues to be willing to settle at a fair market value of the reserves and/or work with you so that as much gas as possible can be produced ahead of, and in conjunction with, mining. Conceivably, we could discuss a partial buy-out combined with an arrangement by which San Juan would deliver gas to the surface for your collection.

We have met before and it may be productive to meet again. Please feel free to contact me at (505) 598-4360.

Sincerely Yours,



Evan Y. Jones
Vice-President
San Juan Coal Company

cc: Joanna Prokup, Secretary, New Mexico Energy, Minerals and Natural Resources
Department
Carston Goff, Deputy State Director, BLM
Steve Henke, BLM Farmington Field Office
Arthur Arguedas, Department of Interior Field Solicitor
Lori Wrotenbery, Chair, New Mexico Oil Conservation Commission
Patrick Lyons, Commissioner, New Mexico State Land Office
Steve Ross, Esq., Oil Conservation Commission