



United States Department of the Interior

MINERALS MANAGEMENT SERVICE

Royalty Management Program
P.O. Box 25165
Denver, Colorado 80225-0165



MMS/MRM/RIK
Mail Stop 330G5

NOV 15 2001

Dear :

The Minerals Management Service (MMS) has selected one or more offshore Federal leases in the Pacific that you operate to be included in a Royalty in Kind (RIK) program in which we will take crude oil royalties in kind beginning January 1, 2002.

This letter provides the procedures and establishes the terms and conditions under which the United States (Lessor) will take crude oil royalties in kind. Our authority is the Outer Continental Shelf Lands Act of 1953 (43 U.S.C. § 1353) and the royalty provisions contained in your Federal lease. For the purposes of this letter, Royalty Oil means the Federal lease oil and condensate production multiplied by the lease royalty rate. The volumes of crude oil taken in kind by the Lessor will reflect and be consistent with all grants of royalty relief.

Term

The Lessor will take all Royalty Oil in kind from the properties listed in the enclosure beginning January 1, 2002, and will continue taking royalties in kind until we notify you that in-kind status is terminated. We will provide Lessees and Operators with at least a 45-day prior written notice of termination of in-kind status.

Royalty Oil Delivery

You must deliver all Royalty Oil from the selected leases, including Royalty Oil from newly producing wells on these leases. In addition, you will make best efforts to notify the Lessor's designated point of contact of leases that, during this period of in-kind status, begin producing crude oil that flows to the facility measurement points (FMP) identified in the enclosure. Royalty oil from such new properties will be added to the RIK volumes at the existing delivery points only upon mutual consent of the purchaser and the Lessor.

Royalty Oil must be placed in marketable condition at no cost to the Lessor. Marketable condition means the condition generally acceptable to purchasers in the field or area. Questions on marketable condition should be directed to the Lessor's points of contact identified in this letter.

The delivery point for Royalty Oil produced from the properties in the enclosure is at the FMP or first interconnect into a main pipeline, as identified in the enclosure. The Lessor will take custody and responsibility for Royalty Oil beyond the delivery point. You can be reimbursed for transportation of Royalty Oil to any delivery points identified in the enclosure that are downstream of the FMP, as allowed in applicable MMS regulations, by taking a transportation deduction on the Report of Sales and Royalty Remittance (Form MMS-2014).

Fulfillment of Royalty Obligations

Delivery of the accurate volume of Royalty Oil (taking into account the effects of normal operational imbalances) in accordance with the terms of this letter will satisfy in full the Lessee's royalty obligation to the Lessor.

For properties where the Lessee has applied for deepwater royalty rate relief, you may use the proposed royalty rate in the interim before MMS/Offshore Minerals Management (OMM) approves the reduction. If OMM does not approve the royalty rate reduction, the resulting imbalance will be resolved in the same manner as described below for imbalances not remedied within 90 days (see "Balancing Account and Imbalances").

All rent or minimum royalty obligations remain the responsibility of the Lessee. If the Lessee owes minimum royalties, the Lessor will issue a bill including information supporting the calculation. The Lessee will have 30 days to review the bill and make payment or appeal the bill.

Lessor Obligation to Take

We agree to take 100 percent of the Royalty Oil delivered to the delivery point for the account of the Lessor. Using reasonable and customary industry practices, we will try to minimize imbalances with Operators and Lessees.

To facilitate timely and accurate custody transfer of Royalty Oil, we will communicate with you regarding arrangements for the transfer of Royalty Oil from the delivery point. The Lessee will not incur royalty-related penalties because of the Lessor's failure to take delivery of oil volumes as communicated by the Operator.

Communication with Lessor

No later than 10 calendar days before the first day of each month, you must notify the Lessor in writing via facsimile (303-275-7136) or e-mail addressed to our mailbox (rik.project@mms.gov) of the daily Royalty Oil volumes (Avails) anticipated for the following month of production for each of the delivery points identified in the enclosure. On this same schedule, for each of the delivery points, you will also provide any anticipated volume adjustments to resolve previous months' imbalances. The total volumes to be delivered to our purchaser at each of the delivery

points must be indicated on the same schedule as a **volume net** of anticipated production plus or minus any adjustments. The Lessor understands that any such estimates are not warranties of actual deliveries but are provided to facilitate planning.

You must also use reasonable efforts, consistent with industry practice, to inform the Lessor as soon as practical regarding significant changes to the information listed in the enclosure; e.g., oil production levels, oil type, and/or royalty rates for the RIK contract properties.

Volume Reconciliation

You must send all volume allocation schedules provided to pipeline companies that address crude oil volumes at the delivery points in the enclosure within 5 days of their submittal to the pipeline companies. You, as the Operator, must provide the lease imbalance statement to MMS no later than 45 days after the end of the month of production, unless MMS approves an alternative timeframe for submission of the statement. We will monitor and reconcile royalty entitlements with the Royalty Oil deliveries you make. Reconciliation will involve communication between you and the Lessor. Upon project termination, you, as the Operator, must issue a final oil imbalance statement. You will settle in accordance with the section "Balancing Account and Imbalances." Volume allocation schedules and lease imbalance statements should be submitted to the rik.project@mms.gov mailbox.

Balancing Account and Imbalances

Imbalances between delivered and entitled volumes of royalty oil will be jointly monitored by you and MMS. You will take timely action to remedy such imbalances through adjustments to royalty oil volumes delivered to MMS. Such volume adjustments will be identified in your communication of royalty oil volumes anticipated before the month of production (see above under "Communication with Lessor").

Imbalances will be remedied in the production month following the month that the imbalance is identified. Imbalances not remedied within 90 days of the end of the production month will be resolved as follows:

- Mutually agreed upon make-up delivery schedule, or
- Cash out payment based on the contract price (at the delivery point) that MMS actually received (or would have received) from its Purchaser during the month or months that the imbalance occurred. Interest will accrue from 60 days after notification that cash out payment is due.

When the lease is no longer taken in kind or after cessation of production from a lease, imbalances will be cashed out based on the MMS contract price (at the delivery point) for the last month the lease is taken in kind. Interest will accrue from 60 days after the final month of delivery. Imbalances remaining at the time of any sale/assignment of properties identified in the enclosure will be settled in compliance with your Purchase and Sale Agreement assignments. Imbalance provisions will be reviewed 6 months from initial contract date.

Reporting

You must continue to report crude oil production on the Oil and Gas Operations Report (OGOR) under requirements specified in MMS regulations and the MMS *Minerals Revenue Reporter Handbook* at <http://www.mrm.mms.gov/ReportingServices/PDFDocs/RevenueHandbook.pdf>. You will not be required to report Royalty Oil for the RIK properties listed in the enclosure on the Form MMS-2014 for the term during which the Lessor takes royalty in kind. Reporting does not change for non-RIK leases.

Lessor's Designee

The Lessor may act by or through a duly authorized designee. In such event, we will provide prior written notification of a designee, including the person to contact. Notification will include specific duties that will be handled by the designee on our behalf. The Lessor also will provide written notification when the designee is no longer authorized to act on our behalf for the purposes of this letter. You are authorized to communicate with the designee as specified in the notification. You will not be required to direct communications to both the Lessor and our designee. For purposes of this letter, if we notify you that we will use a designee in the contract, references to the Lessor shall refer to such designee. The designee will agree in writing to comply with all provisions of this letter that are applicable to the Lessor when the designee acts on our behalf.

Audit

The Lessor may audit your records regarding all information relevant to volumes and qualities of Royalty Oil produced, measured, delivered, and, if applicable, transported. We reserve the right to examine your financial records for the subject properties related to any transportation allowances and quality banks prior to the delivery point.

Lessees, Operators, and revenue payors must maintain all records of transactions mentioned in the above paragraph in accordance with the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (Public Law 104-185 Section 115(f)).

Lessor Point of Contact

Copies of all correspondence between Operator and Lessor should be kept on file by the Operator. Points of contact for the Lessor are listed below:

Volume Avails (Anticipated Volumes) and Operator Imbalance Statements:

Mr. Larry Barker

Telephone: 303-275-7296; Fax: 303-275-7136;

E-mail: Larry.Barker@mms.gov

Or

Mr. Ted Drescher
Telephone: 303-275-7297; Fax: 303-275-7136;
E-mail: Theodore.Drescher@mms.gov

New Lease Production:

Ms. Crystel Tobar
Telephone: 303-275-7282; Fax: 303-275-7136;
E-mail: Crystel.Tobar@mms.gov

Or

Ms. Stacy Leyshon
Telephone: 303-275-7469; Fax: 303-275-7137;
E-mail: Stacy.Leyshon@mms.gov

Reporting Issues:

Mr. Andy Sandoval
Telephone: 303-231-3777; Fax: 303-231-3700
E-mail: Alfonso.Sandoval@mms.gov

Electronic Funds Transfer:

Mr. Joe Romero
Telephone: 303-231-3123; Fax: 303-231-3501;
E-mail: Joseph.Romero@mms.gov

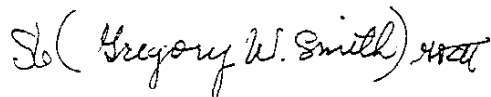
We acknowledge that Operators and Lessees have given proper notice when using the telephone number or fax number provided to communicate with the Lessor. Any telephone communication regarding volumes must be confirmed by fax or e-mail no later than 1 business day after telephone communication occurs. The Lessor further agrees to make arrangements to receive such communications regarding oil scheduling issues during normal business hours. Operators and Lessees should communicate with one of the points of contact to answer any further questions.

The Paperwork Reduction Act

The Paperwork Reduction Act of 1995 requires us to inform you that this information is being collected by MMS to document fulfillment of royalty obligations on minerals removed from Federal lands and that we will use this information to maintain and audit lease accounts. We estimate the burden for reporting is 10 minutes per property per month. Comments on the accuracy of this estimate or suggestions for reducing this burden should be directed to the Information Collection Clearance Officer, Minerals Management Service, 1849 C Street, NW, MS 4230, Washington, DC 20240. Proprietary information submitted to the U.S. Department of the Interior is protected in accordance with standards established by the Federal Oil and Gas

Royalty Management Act of 1982 (30 U.S.C. 1733), the Freedom of Information Act (5 U.S.C. 552(1,) (4)), and the Departmental Regulations (43 CFR 2). An agency may not conduct or sponsor and a person is not required to respond to a collection of information unless it displays a currently valid OMB control number.

Sincerely,

A handwritten signature in black ink that reads "Gregory W. Smith". The signature is written in a cursive style with a large initial "G".

for Milton K. Dial
Assistant Program Director
for Royalty In Kind

Enclosure

Minerals Management Service						Enclosure
Pacific Listing of RIK Oil Properties						
January 1, 2002 through December 31, 2002						
Producing MMS Properties	Crude Type	Delivery Point	MMS Facility Measurement Point	Operator	MMS Purchaser	Start Date
891-008979-A	Santa Ynez	Las Flores Canyon	20040833500	ExxonMobil	US Oil	1/1/2002
891-008979-B	Santa Ynez	Las Flores Canyon	20040833500	ExxonMobil	Paramount Petroleum	1/1/2002
891-008979-C	Santa Ynez	Las Flores Canyon	20040833500	ExxonMobil	US Oil	1/1/2002
891-008979-D	Santa Ynez	Las Flores Canyon	20040833500	ExxonMobil	US Oil	1/1/2002
088-000240-0						
088-000241-0	Dos Cuadras	Rincon Plant	20041113000	Nuevo Energy Co.	Gary-Williams Energy	1/1/2002