

## Oil and Gas Joint Operating and Farmout Agreements

Crafting Instruments That Address Modern Exploration and Production Challenges

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Today's faculty features:

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**JOINT OPERATING AGREEMENTS,  
FARMOUT AGREEMENTS AND  
OTHER MATERIAL AGREEMENTS**

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## INTRODUCTION

In the oil business and, frequently, when a Buyer acquires oil and gas interests, unless an agreement is personal between the parties, or the buyer can invoke the protection of a bona fide purchaser, the Buyer will be subject to unrecorded agreements between the seller and third parties.

Two types are the following:

### I. JOINT OPERATING AGREEMENTS

Joint operations are common in the oil and gas industry. When the interest in a property or group of properties is divided among more than one owner, the relationship between these co-owners is commonly governed by the AAPL Form 610 Model form Operating Agreement (“JOA”), which standardizes the recurring problem of how to unify, control and operate among the different participants in the project.<sup>1</sup> A JOA provides for the development and operation of certain leasehold interests for the joint account of concurrent owners who share in the expense of drilling and operations in accordance with the terms of the agreement.<sup>2</sup> It covers such diverse problems as the examination of title, the rendering of the property for ad valorem tax purposes, elections under the Internal Revenue Code, and the sale or transfer of any interest subject to the JOA.<sup>3</sup> The JOA is an important document to be considered and reviewed by a potential purchaser of a producing oil and gas property.

The main functions of the JOA are pooling the parties’ interest in the contract area, allocation of costs, expenses, and production within the contract area, the conduct of operations within the contract area, including the designation of the operator, and defining the respective rights, duties and responsibilities of the parties to each other and third parties.

#### [A] Designation of Operator

One purpose of a JOA is the appointment of an entity to be responsible for all operations in the contract area. That entity or individual is designated as the operator. The operator is given “full control” over all operations. There is a misconception among some buyers that if they are buying from the operator, then they will automatically acquire the right to operate the purchased properties. However, this only happens when the Seller owns the entire working interest in

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<sup>1</sup> J. David Heaney, “The Joint Operating Agreement, The AFE and COPAS—What They Fail to Provide,” 29 *Rocky Mt. Min. L. Inst.* 743 (1983).

<sup>2</sup>*Id.*

<sup>3</sup> Homer J. Penn, “Cotenancy Problems: Is the Gas Balancing Agreement the Answer?,” 33 *Rocky Mt. Min. L. Inst.* 18-1, 18-7, (1987).

the purchased properties.<sup>4</sup> If the Seller owns only an undivided interest, even if it is the majority interest, it is necessary to review the provisions of the operating agreement to determine if the operations can or will be acquired.<sup>5</sup>

The right to operate is predicated in part on the operator's ownership of an interest in the contract area. The right is extinguished upon the sale of the contract area and, therefore, cannot be assigned.<sup>6</sup>

Unless modified, the party who acquires the majority of votes is selected as the operator. The 1989 Model Form requires an affirmative vote of non-operators owning a majority interest, as shown on Exhibit "A" with JOA.<sup>7</sup> The 1982 Model Form anticipates three or more parties to the agreement. It requires the affirmative vote of *two* or more non-operators. If the AAPL Model Form Operating Agreement is not used, it is possible that the operating agreement utilized does not contain provisions detailing successorship to the operator.<sup>8</sup> Older operating agreements may not contain any provisions regarding the succession of the operator. It then becomes a matter of negotiation with the other working interest owners to determine who will succeed as operator once the operator has sold his interests.<sup>9</sup>

## **[B] In-Kind Provisions**

An in-kind provision in a JOA, governed by Article VI.G. of the 1989 agreement, requires that each party take his natural gas in-kind and separately dispose of his proportionate share produced from the contract acreage.<sup>10</sup> The provision states that if any party fails to so take, the terms of the gas balancing agreement, which is discussed below, will automatically become effective.<sup>11</sup> Primarily the major and larger independent oil companies utilize this provision, because they have the ability to market their share of production separately.<sup>12</sup> An in-kind provision also serves to maintain a non-corporate status between the

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<sup>4</sup> Heaney, *supra* note 1, at 744-745.

<sup>5</sup> *Id.*

<sup>6</sup> Under the 1977, 1982 and 1989 Model Form Agreements, the operator will be deemed to have resigned as operator when he no longer owns an interest in the contract area; *contra* Santa Fe Energy Operating Partners, L.P. v. Universal Resources Corp., No. 07-95-0342-CV, 1996 Tex. App. LEXIS 3540 (Tex. Ct. App. Aug. 14, 1996) (unpublished opinion) holding, as a matter of law, that the operator's rights to operate were assignable to its purchaser. The court reasoned that contract rights are assignable unless the contract relies on the personal trust, confidence, skill, character or credit of the parties.

<sup>7</sup> The assignee of an operator's working interest is one of the parties allowed to vote for a new operator. Duncan Oil Properties, Inc. v. Vastar Resources, Inc., 16 P.3d 465, 468 (Okla. Civ. App. 2000).

<sup>8</sup> George A. Snell, "Due Diligence Title Review: The Problem Areas, Where to Look and How to Solve," *Sixth Annual Dallas Energy Symposium* 31 (1994).

<sup>9</sup> *Id.*

<sup>10</sup> Model Form Operating Agreement, A.A.P.L. Form 610 – 1989, Article VI. G.

<sup>11</sup> Albert D. Hoppe, "Producer Gas Balancing, With and Without Formal Agreement," *Oil and Gas Law and Taxation*, 2-19, §2.05[3][c] (1991).

<sup>12</sup> Heaney, *supra* note 1, at 775.

parties for federal income tax purposes.<sup>13</sup> If the operator had a duty to dispose of his non-operators' gas, the entities would be classified and taxed as one corporate entity.

Under the JOA, if the non-operator fails to take its share of production in kind, the operator has the right, but not the obligation, to purchase and sell the non-operator's share of production for the account of the non-operator.<sup>14</sup>

The JOA states that the purchase and sale of the non-operator's production by the operator is always subject to the non-operator's exercise of their right to take in-kind at any time.<sup>15</sup>

### **[C] Non-Consent Provisions**

Non-consent operations under a JOA can result in a party not being entitled to proceeds of production from a particular well because he did not agree to bear the costs, drilling, reworking or other remedial operations.<sup>16</sup> In almost all situations, non-consent status is not reflected in the county clerk's records.

Typically, the penalty for not participating in the drilling, reworking or other operations is that the non-consenting party does not share in the revenues from the successful well until the consenting parties have recovered a penalty ranging from 100 percent to 600 percent of the operation.<sup>17</sup>

In any well or property to be purchased, there is the possibility that the Seller went non-consent or that the Seller has committed to bear a greater share of costs than indicated from record title.<sup>18</sup> The Purchase and Sale Agreement should undertake to identify any well in the transaction in which either the Seller or any other working interest owner has gone non-consent.<sup>19</sup>

Furthermore, non-consent operations may result in the Seller receiving a greater interest in production than he is normally entitled. A review of the revenue or working interest deck may show that the Seller owns a greater interest than what is shown from an examination of the county clerk's records. One frequent reason for the discrepancy in the decimal number is the Seller's acquisition of a non-consent interest. If the Buyer is assuming that this interest is perpetual, the Buyer will be unpleasantly surprised when the non-consent payout occurs.

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<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

<sup>15</sup> *Id.* at 776.

<sup>16</sup> Robert C. Bledsoe, "Ten Most Common Defects that Impede Closing and What To Do," 43rd Oil and Gas Inst., 2-14, §2.05[1], (Sw. L. Fdn.1992).

<sup>17</sup> Penn, *supra* note 3, at 18-8.

<sup>18</sup> *Id.*

<sup>19</sup> Bledsoe, *supra* note 16, at 2-14.

Unfortunately, there isn't a typical or easy way to determine the nonconsent interest acquired by a party. Many times, it is a function of 1) reviewing the proposal letters from the operator regarding the nonconsent interest and 2) a review of the election letters and a determination of who did not respond to the nonconsent proposals. After the review, follow-up conversations with the operator's accountant may be necessary to determine the number of wells not in full pay status.

#### **[D] Maintenance of Uniform Interest Provision**

Another provision that needs to be considered in connection with producing property transfers is the Maintenance of Uniform Interest ("MUI") provision.<sup>20</sup> This provision, like the preferential right to purchase provision, is a restraint on alienation. The MUI provision restricts transfers of non-uniform interests within the contract area of the JOA. A sale of deep rights, of shallow rights of an individual formation, or an assignment or reservation of all or part of a particular drilling and spacing unit, drill site or wellbore within a multi-well unit, subject to a JOA with no depth limitations, creates a non-uniform interest. The relevant language in all four versions of the JOA is substantially the same and generally reads as follows:

...no party shall sell, encumber, transfer or make other disposition of its interest in the leases embraced within the Contract 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 Contract Area.

The MUI provision applies to a much broader range of transfers than the preferential right provision. The MUI provision embraces not only sales, but also gifts, exchanges, mortgages and any other encumbrance, transfer or disposition.<sup>21</sup> It can be argued that even a non-uniform transfer of an overriding royalty, production payment, net profits interest and the like would violate the provision.<sup>22</sup> The language in the provision is probably broad enough to also apply to involuntary transfers as well as voluntary ones.

When performing due diligence, the Purchase and Sale Agreement needs to be reviewed to determine if a provision, such as a reservation of all existing

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<sup>20</sup> For the text, see 1956 JOA, Section 20 (styled the "Maintenance of Unit Ownership"), 1977 JOA, Article VIII.E., 1982 JOA, Article VIII.D. and 1989 JOA, Article VIII.D.

<sup>21</sup> Gary B. Conine, "Property Provisions of the Operating Agreement-Interpretation, Validity and Enforceability," 19 *Tex. Tech L. Rev.* 1263, 1326 (1988).

<sup>22</sup> Terry I. Cross, "Ties That Bind: Preemptive Rights and Restraints on Alienation That Commonly Burden Oil and Gas Properties," 5 *Tex. Wesleyan L. Rev.* 193, 213 (1999)

producing wellbores, may violate an applicable MUI. In such an event, a waiver of the application of the MUI should be sought from the other parties to the JOA.

## II. FARMOUTS AND RELATED AGREEMENTS

A farmout agreement is a transaction wherein the owner of an oil and gas lease (farmor) agrees to an assignment of a part of a lease to a party (farmee) who agrees, as consideration for the assignment, to drill a well to a certain depth or condition.<sup>23</sup> Some agreements require the farmee to drill to a minimum depth, where either a producing well or a dry hole will earn an assignment. In others, an assignment may be earned by drilling a producing well, regardless of the depth drilled. Still others require drilling to a minimum depth and completion as a producer.

Typically, the farmout agreement allows that the farmee “earns” its interest upon either drilling (“drill to earn”) or production (“produce to earn”).

Under a drill to earn farmout, the farmee earns the interest under the Farmout Agreement once drilling commences or reaches the contracted depth.<sup>24</sup>

Under a produce to earn farmout, the farmee must, generally, drill a well that produces in paying quarterly to earn the interest in the farmout acreage.<sup>25</sup>

### [A] Back-In Interests

It is common for the farmor to retain a non-operating interest in the farmed out acreage.

The conversion provision of a farmout agreement addresses whether the retained non-operating interest, i.e., an overriding royalty interest or a net profits interests that the farmor retains, will be converted at some point in time to a share of the working interest.<sup>26</sup> The farmor may have reserved the right to convert his overriding royalty interest into a working interest at payout of the well (“back-in after payout”). There are three possibilities: no conversion, mandatory conversion, and optional conversion.<sup>27</sup> The circumstances and goals of the farmor and farmee will determine which of the three possibilities are chosen.

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<sup>23</sup> Richard W. Hemingway, “The Farmout Agreement; A Story Short But Not Always Sweet,” 1 *Natural Resources and Environment* 3 (Spring 1985); *Avien Corp v. First Nat’l Oil, Inc.* 79 P.3d 223, 228 (Kan App. 2003).

<sup>24</sup> John S. Lowe, “Analyzing Oil and Gas Farmout Agreements,” 41 *Sw. L.J.* 759, 793 (1987).

<sup>25</sup> *Moncrief v. Louisiana Land and Expl. Co.* 861 P.2d 500, 504 (Wyo. 1993).

<sup>26</sup> Lowe, *supra* note 24, at 832.

<sup>27</sup> *Id.*

During the process of due diligence, the Buyer should examine the farmout agreements to determine if any of the purchased interests are subject to a reduction due to a farmout conversion or a back-in. At the same time, the Buyer may be purchasing an interest that has been farmed out by the Seller to a third party in which the Buyer will be entitled to convert his non-operating interest into a working interest.

## **[B] Assignments**

Few farmout agreements are recorded. However, once an agreement has been fully performed, the farmee is entitled to a recordable assignment of interest. It is important that the terms of the farmout agreement and the terms of the assignment do not conflict, or a dispute may arise as to which prevails. The Mississippi case of *Phillips Petroleum Co. v. Stack*<sup>28</sup> illustrates this problem. In *Stack*, an assignment followed the farmout agreement by a day, before the drilling of either of the two required wells under the agreement. Subsequently, Stack, the farmee, refused to assign Phillips the overriding royalty interests on lease extensions and renewal leases that were required by the farmout, but not referenced in the assignment. Stack contended that the agreement had merged into the assignment, or that the assignment had superseded the agreement. The Mississippi Supreme Court focused on Stack's admission that he had been obligated to drill the two wells provided for by the farmout agreement, even though the assignment did not mention that requirement.<sup>29</sup> The court concluded that the intent of the parties was that the two instruments together constituted the contract between the parties.<sup>30</sup>

After the drilling of the subject well, it is not unusual for the farmee to forget to request the earned assignment. A frequent reason for a discrepancy between record title as shown in the County Clerk's records and the interest shown to be paid in the deck is the absence of an executed assignment pursuant to a farmout agreement.

## **[C] Term Assignments**

To resolve the problem of assignments that don't get executed, and so as to put third parties on notice, companies have frequently turned to term assignments instead of farmout agreements. The term assignments convey an interest from the assignor/farmor to the assignee/farmee for a specific term. The assigned interest is to revert to the assignor if the assignee doesn't drill a producing well to a certain depth by a certain date.

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<sup>28</sup> 231 So. 2d 475 (Miss. 1969).

<sup>29</sup> *Id.* at 481.

<sup>30</sup> *Id.* at 482.

In such an instance, the Buyer should determine if the Seller is entitled to a reversion of the term assignment, or whether the Seller is obligated to reassign an interest because the interest was not earned under a term assignment.

### III. AREA OF MUTUAL INTEREST AGREEMENTS

Area of Mutual Interest Agreements (“AMI”) regulate the acquisition of oil and gas interests between parties to the agreement. In an Area of Mutual Interest Agreement, the parties attempt to describe a geographic area within which they agree to share certain additional leases acquired by either of them in the future.<sup>31</sup>

AMI’s are frequently included in JOAs. The parties to the JOA create an AMI agreement in order to protect themselves against another party to the JOA competing to buy leases near or in the contract area. AMI provisions can also be included in farmout agreements. An AMI provision gives the farmor and the farnee the right to share in interests acquired by the other in a designated contract area, which may be the same as or larger, than the farmout contract area.<sup>32</sup> AMIs are in the nature of a contract to convey interests in oil and gas leases.<sup>33</sup>

Whether a party is bound to an AMI agreement depends on the application of specific facts. First, there must be a sufficient description of the area that is subject to the AMI agreement.<sup>34</sup> The description must meet the statute of frauds.<sup>35</sup> Therefore, the agreement must be in writing and signed by the party to be charged with a specific description of the area. Second, there must be sufficient notice.<sup>36</sup> When a party to the AMI agreement acquires any right, title, interest or claim in an oil and/or gas interest in the area of mutual interest, the acquiring party must notify the non-acquiring parties of the acquisition.<sup>37</sup> The mode of notification can be determined by the parties and set out in the agreement.<sup>38</sup> Third, the AMI must state whether or not the agreement is a covenant that is going to run with the land or will be a personal covenant.<sup>39</sup>

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<sup>31</sup> Conine, *supra* note 21, at 1345-46; No. Central Oil v. Louisiana Land and Expl. Co., 22 S.W.3d 572, 577 (Tex. App. 2000).

<sup>32</sup> Lowe, *supra* note 24, at 844.

<sup>33</sup> *Id.*

<sup>34</sup> Allen D. Cummings, “Old Area of Mutual Interest and Dedication Agreements – New Problems,” 52 *Rocky Mt. Min. L. Inst.* 27-1, 27-3 (2006).

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> Cummings, *supra* note 34, at 27-3; see *Westland Oil Development Corp. v. Gulf Oil Corp.*, 637 S.W.2d 903 (Tex. 1982) (holding that the AMI provision related to and “touched and concerned” leases in existence at the time of the AMI agreement. Therefore, there was privity of estate amount the parties which was a covenant running with the land); *but contra Grimes v. Walsh & Watts, Inc.*, 649 S.W.2d 724 (Tex. App. 1983) (holding that an AMI covenant, not expressly made binding on successors and assigns was a personal covenant, where the lease

Next, the AMI must conform to the rule against perpetuities.<sup>40</sup> Fifth, the AMI must specify the time of performance, meaning that the agreement should provide a time in which a party must pay his share of acquisition costs.<sup>41</sup> Finally, the AMI agreement should be specific in defining what acquired interests will be subjected to the agreement.<sup>42</sup>

Area of mutual interest problems most often arise in a sale situation because the Buyer is subject to an AMI agreement and his purchase must be shared with third parties.<sup>43</sup> In analyzing such a purchase, early in the transaction, it is important to ask if the Buyer has interests in the area in order to determine whether or not the acquisition will trigger an AMI.<sup>44</sup> The party examining JOAs and other agreements should always be looking for this restriction.

It is also important to note that a Buyer may “buy” his way into an AMI, because the Seller is subject to an AMI with a third party.

Another concern in the use of the AMIs is the danger that large companies highly active in the vicinity of the contract area may enter into separate operating agreements or instruments with overlapping areas of mutual interest.

#### IV. PREFERENTIAL RIGHTS TO PURCHASE

##### [A] Introduction

One frequent obstacle in the JOA, farm-out agreement, or a prior assignment in the chain of title, is a preferential right to purchase provision.<sup>45</sup> Under the preferential right to purchase (PRP), sometimes called a “right of refusal,”<sup>46</sup> “preemptive right,”<sup>47</sup> or “preemptive option,”<sup>48</sup> an owner is required, “when and *if* he decides to sell, to offer the property first to the person entitled to

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subject to the AMI had terminated and a new lease covering the same lands was taken by the same parties who had purchased the terminated lease from a party to the AMI covenant).

<sup>40</sup> *Id.* at 27-4.

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> Bledsoe, *supra* note 16, at 2-9.

<sup>44</sup> *Id.*

<sup>45</sup> For a more extensive discussion on preferential rights to purchase, see Timothy C. Dowd, “Preferential Rights to Purchase in Oil and Gas Transactions,” 49 *Rocky Mt. Min. L. Inst.* 5-1 (2003).

<sup>46</sup> *Citgo Petroleum Corp. v. Occidental Chem. Corp.*, No. 01-5022, 2002 WL 89921, at \*1 (10th Cir. Jan. 24, 2002); *Tenneco Inc. v. Enterprise Prods. Co.*, 925 S.W. 2d 640, 642 (Tex. 1996).

<sup>47</sup> *Missouri State Highway Comm'n v. Stone*, 311 S.W. 2d 588, 589 (Mo. Ct. App. 1958); *Draper v. Gochman*, 400 S.W. 2d 545, 548 (Tex. 1966).

<sup>48</sup> See *Tadros v. Middlebury Med. Ctr., Inc.*, 820 A.2d 230, 240 (Conn. 2003).

the [preferential right] on terms identical to those the owner has received from another...<sup>49</sup>

A PRP differs from an option. A holder of an option has a present power of acceptance and can even compel an unwilling owner to sell, while the holder of the PRP has no power of acceptance and may not exercise his right until the owner enters into a contract to sell.<sup>50</sup> A PRP is often referred to as a conditional option.<sup>51</sup>

The most common form of a PRP is found in the AAPL Form 610 Model Form Operating Agreement.<sup>52</sup>

Article VIII.F of the 1989 Model Form JOA provides that any time a party:

“desires to sell all or any part of its interest in the Contract Area, it shall promptly give written notice to the other parties, with full information concerning its proposed disposition, which shall include the name and address of the prospective transferee (who much be ready, willing and able to purchase), the purchase price, a legal description sufficient to identify the property, and all other terms of the offer. The other parties shall then have an optional right, for a period of (10) days after the notice is delivered, to purchase for the stated consideration on the same terms and conditions the interest which the other party proposes to sell...”

A PRP generally serves two goals. First, the PRP affords each party the opportunity to increase its ownership position and economic stake in the geographical area of common interest, which may have increased in value by virtue of the parties' oil and gas operations.<sup>53</sup> Second, the PRP gives the parties some measure of control over the identity of their co-owners by allowing the holders of the preferential right to preempt the introduction of an undesirable third party as a co-owner of the unit.<sup>54</sup>

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<sup>49</sup> *Ollie v. Rainbolt*, 669 P.2d 275, 279 (Okla. 1983); see also *Tenneco Inc. v. Enterprise Prods. Co.*, 925 S.W.2d 640, 642 (Tex. 1996)

<sup>50</sup> See *Nelson v. Reisner*, 331 P.2d 17, 20 (Cal. 1958); *Producers Oil Co. v. Gore*, 610 P.2d 772, 73-74 (Okla. 1980).

<sup>51</sup> See *Estate of Johnson v. Carr*, 706 S.W.2d 388, 390 (Ark. 1986); *Kamas State Bank v. Bougeois*, 380 P.2d 931, 932 (Utah 1963).

<sup>52</sup> Even though the PRP provision has been part of the A.A.P.L. form since 1956, typically, the provision is deleted.

<sup>53</sup> Timothy C. Dowd, “Preferential Rights to Purchase in Oil and Gas Transactions,” 49 *Rocky Mt. Min. L. Inst.* 5-1, 5-4 (2003).

<sup>54</sup> *Id.*

## **[B] Events that Trigger a Sale**

### **[1] What Constitutes a Sale**

During the process of due diligence, an essential issue in a preferential purchase right is what constitutes a “sale.” Typically, the term “sale” is not defined in the underlying agreement. The primary disputes over preferential rights concern what types of transactions actually constitute a sale, which triggers the holder’s PRP right.

The determination of what is a sale in a complex commercial transaction is more difficult. In one line of authority, the courts have placed emphasis on the presence of an arm’s length transfer which, if completed, would put the property beyond the reach of the preference right holder.<sup>55</sup> This line of authority holds a “sale” occurs when a transaction occurs in which the disposition of the property, while not falling within the technical definition of a sale, has the same practical effect as a sale.<sup>56</sup> These courts hold that if a transaction accomplishes what a direct sale would accomplish, then the PRP is applicable.<sup>57</sup> In a second line of authority, courts have held that if sophisticated parties intended to include all possible dispositions as sales, the drafters could have included the many possible dispositions in the PRP.<sup>58</sup>

### **[2] Mergers, Sales of Stock, Subsidiaries and Affiliates**

Closely aligned to the question of what constitutes a sale, is the issue of mergers and stock transfers. Generally, even where the PRP provision does not contain an exclusion, courts have held that the sale of a corporation’s stock does not trigger the preferential right.<sup>59</sup> As a corporation is a separate entity from its stockholders, the courts have generally held that the assets were not sold, but, rather the ownership of the corporate entity holding the asset was transferred.<sup>60</sup>

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<sup>55</sup>See *Fina Oil & Chem. Co. v. Amoco Prod. Co.*, 673 So.2d 668, 672 (La. Ct. App. 1996); *Williams Gas Processing – Wamsutter Co. v. Union Pacific Resources Co.*, 25 P.3d 1064, 1072-73 (Wyo. 2001).

<sup>56</sup>See *Anderson v. Armour & Co.*, 473 P.2d 84, 89 (Kan. 1970); *Cherokee Water Co. v. Forderhause*, 641 S.W.2d 522, 525 (Tex. 1982); *contra Tenneco Inc. v. Enterprise Prods. Co.*, 925 S.W.2d 640 (Tex. 1996).

<sup>57</sup>See *Gorum v. Optimist Club of Glenmora*, 771 So.2d 690, 695 (La. Ct. App. 2000), *Galveston Terminals, Inc. v. Tenneco Oil Co.*, 904 S.W.2d 787, 791 (Tex. Ct. App. 1995), *set aside without reference to the merits*, 922 S.W.2d 549 (Tex. 1996); (*but, see Tenneco*, 925 S.W.2d at 646, where the Texas Supreme Court rejected and disapproved the reasoning in *Galveston Terminals*).

<sup>58</sup>See *Citgo Petroleum Corp. v. Occidental Chem. Corp.*, 29 Fed. Appx. 525, 2002 WL 89921 (10th Cir. 2002); *Fina Oil*, 673 So.2d at 675.

<sup>59</sup>*Kaiser v. Bowlen*, 200 P.3d 1098 (Colo. App. 2008).

<sup>60</sup>See *Gamble v. Cornell Oil Co.*, 154 F.Supp. 581, 588 (W.D. Okla. 1957), *aff’d*, 260 F.2d 860 (10th Cir. 1958); *Tenneco*, 925 S.W.2d at 646.

One technique of a stock transfer to avoid the activation of a PRP clause was used in *Tenneco Inc. v. Enterprise Products Co.*<sup>61</sup> In *Tenneco*, the parties were subject to an operating agreement which governed operations of a natural gas liquids fractionation plant. In the first of three transfers, Tenneco Oil transferred its ownership share in the plant to Tenneco Natural Gas Liquids, a wholly owned subsidiary. Tenneco Oil sold its Tenneco Natural Gas Liquids' stock to Enron Gas Processing in the second transfer. After the second transfer, Tenneco Natural Gas Liquids' name was changed to Enron Natural Gas Liquids Corporation. In the third transfer, Enron Gas Processing sold Enron Natural Gas Liquids' stock to Enron Liquids Pipeline Operating Limited Partnership.<sup>62</sup> Enterprise sued Tenneco Oil and Enron Gas Processing, asserting that the second and third transfers violated Enterprise's PRP.<sup>63</sup> The Tenneco and Enron defendants defended, in essence, on the basis that the second and third transfers were only stock sales and did not trigger the PRP.<sup>64</sup> Enterprise countered saying that no matter how the parties structured the transaction, it was, in substance, a transfer of an ownership interest which invoked the right of first refusal.<sup>65</sup> In support of its position, Enterprise cited the Texas Court of Appeals decision of *Galveston Terminals, Inc. v. Tenneco Oil Co.*,<sup>66</sup> wherein the court held that the trial court erred by not examining the stock transferor's intent.<sup>67</sup> In *Galveston Terminals*, the Court of Appeals held that to determine the parties' intent, the "three-step" transfers should be viewed as a single transaction.<sup>68</sup> The *Galveston Terminals* court held that the transferor, Tenneco, failed to prove, as a matter of law, that its stock sale was not actually an asset sale.<sup>69</sup>

The *Tenneco v. Enterprise* court expressly rejected the court's reasoning in *Galveston Terminals*.<sup>70</sup> The Texas Supreme Court stated that "sound corporate jurisprudence requires that courts narrowly construe rights of first refusal and other provisions that effectively restrict the free transfer of stock."<sup>71</sup> The court further stated:

Viewing several separate transactions as a single transaction to invoke the right of first refusal compromises the law's unfavorable estimation of such restrictive provisions. . . .

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<sup>61</sup>925 S.W.2d 640 (Tex. 1996).

<sup>62</sup>*Id.* at 642.

<sup>63</sup>*Id.*

<sup>64</sup>*Id.* at 644.

<sup>65</sup>*Id.* at 646.

<sup>66</sup>904 S.W.2d 787 (Tex. Ct. App. 1995), *set aside without reference to the merits*, 922 S.W.2d 549 (Tex. 1996).

<sup>67</sup>*Id.* at 791.

<sup>68</sup>*Id.*

<sup>69</sup>*Id.* at 792.

<sup>70</sup>925 S.W.2d at 646.

<sup>71</sup>*Id.*

Moreover, the plain language of the Restated Operating Agreement provides that only a transfer of an ownership interest triggers the preferential right to purchase; it says nothing about a change in stockholders. The Enterprise Parties could have included a change-of-control provision in the agreements that would trigger the preferential right to purchase. None of the agreements among the parties contained such a provision. We have long held that courts will not rewrite agreements to insert provisions parties could have included or to imply restraints for which they have not bargained.<sup>72</sup>

In its argument, Enterprise also asserted: 1) that, initially, Tenneco had offered the properties as an asset sale before transferring them in a stock sale approach, 2) a press release characterized the transaction as a sale of Tenneco's natural gas liquids business, and 3) both Tenneco and Enron treated the transaction as an asset sale rather than a stock sale for tax purposes.<sup>73</sup> The Supreme Court stated that the parties' early structuring, press releases and tax treatments were immaterial.<sup>74</sup>

The drafters of the PRP provision in the Model Form Agreement made the PRP inapplicable where any party wishes:

to dispose of its interests by merger, reorganization, consolidation or by sale of all or substantially all of its Oil and Gas assets to any party, or by transfer of its interests to a subsidiary or parent company or to a subsidiary of a parent company, or to any company in which such party owns a majority of the stock.<sup>75</sup>

As a result of the specific exclusion, the transfer of stock by the shareholder of a corporate entity subject to the operating agreement is not a transfer of the party's interest in the contract area.<sup>76</sup>

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<sup>72</sup>*Id.*; see also *Citgo Petroleum Corp. v. Occidental Chem. Corp.* 29 Fed. Appx. 525, 2002 WL 89921 at \*3-6 (10th Cir., Jan. 24, 2002) (construing Louisiana law); *contra Williams Gas Proc.-Wamsutter Co. v. Union Pacific Resources Co.*, 25 P.3d 1064, 1072 (Wyo. 2001), wherein the court held that the transfer of an asset into a subsidiary, of which the stock was sold to a third party, was a transparent action to do indirectly what could not be done directly. The court expressly declined to follow the reasoning of *Tenneco v. Enterprise*.

<sup>73</sup>*Tenneco*, 925 S.W.2d at 645.

<sup>74</sup>*Id.* at 646; see also *Questa Energy Corp. v. Vantage Point Energy, Inc.*, 887 S.W.2d 217, 221 (Tex. Ct. App. 1994).

<sup>75</sup>A.A.P.L. Form 610 – 1989 Model Form Operating Agreement, Art. VIII.F.

<sup>76</sup>See *Fina Oil & Chem. Co. v. Amoco Prod. Co.*, 673 So.2d 668, 672 (La. Ct. App. 1996).

### [3] Package Sales

The most common means of selling producing oil and gas properties is through a multi-property or “package” sale wherein multiple properties, typically in one geographical area, are sold to a willing buyer. It is common for one or more PRP burdened properties to be included in a package which includes many properties which are not subject to a preferential right held by a party.

The PRP provisions, including those in the A.A.P.L. Model Forms, typically do not address the issue where no specific offer is made for the burdened property and no particular portion of the purchase price is allocated to it.

In the context of a PRP provision burdening one property included in a package of several properties, the majority of courts hold:

- a) a seller does not nullify a preference right by selling the burdened property as part of a package sale;<sup>77</sup>
- b) a PRP is not activated by the inclusion of a burdened property with unburdened property;<sup>78</sup>
- c) the preference right holder’s remedy is in the form of injunctive relief;<sup>79</sup> and
- d) if the property has already been conveyed, the purchaser may be ordered to reconvey the option-encumbered property back to the owner.<sup>80</sup>

The general rule is that a seller may not defeat a PRP simply by selling the burdened property with other properties he may own.<sup>81</sup> The often-quoted case of *Guaclides v. Kruse*<sup>82</sup> states: “To allow the owner of the whole to by-pass the optionee merely by attaching additional land to the part under option would

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<sup>77</sup>*Fordoché, Inc. v. Texaco, Inc.*, 463 F.3d 388 (5th Cir. 2006) (applying Louisiana law); *Unlimited Equip. Lines, Inc. v. Graphic Arts*, 889 S.W.2d 926, 935 (Mo. Ct. App. 1994); *Ollie v. Rainbolt*, 669 P.2d 275, 280 (Okla. 1983); *Navasota Resources, L.P. v. First Source Texas, Inc.*, 249 S.W.3d 526 (Tex. App. 2008); *contra Crow-Spieker #23 v. Helms Constr. & Dev. Co.*, 731 P.2d 348, 350 (Nev. 1987).

<sup>78</sup>*Myers v. Lovetinsky*, 189 N.W.2d 571, 576 (Iowa 1971); *Guaclides v. Kruse*, 170 A.2d 488, 494 (N.J. Super. Ct. App. Div.), cert. den’d, 174 A.2d 658 (1961); *Ollie*, 669 P.2d at 279-80; *contra Berry-Iverson Co. of N.D., Inc. v. Johnson*, 242 N.W.2d 126, 134 (N.D. 1976).

<sup>79</sup>*Gyurkey v. Babler*, 651 P.2d 928, 934 (Idaho 1982); *Ollie*, 669 P.2d at 280.

<sup>80</sup>*Ollie*, 669 P.2d at 280; *Chapman v. Mutual Life Ins. Co. of N.Y.*, 800 P.2d 1147, 1152 (Wyo. 1990).

<sup>81</sup>*Unlimited Equip. Lines, Inc. v. Graphic Arts*, 889 S.W.2d 926, 935 (Mo. Ct. App. 1994); *Ollie*, 669 P.2d at 280; *McMillan v. Dooley*, 144 S.W.3d 159 (Tex. App. 2004).

<sup>82</sup>170 A.2d 488 (N.J. Super. Ct. App. Div.), cert. den’d, 174 A.2d 658 (1961).

render nugatory a substantial right which the optionee had bargained for and obtained.”<sup>83</sup>

The majority of cases involving the applicability of a PRP in the context of a package sale are limited to real estate, stock sales or equipment sales. There are limited cases involving package sales of oil and gas properties. In *McMillan v. Dooley*, the court decided that the general rule is the same and that a purchaser cannot be forced to purchase the entire package to preserve his rights.<sup>84</sup>

One unpublished case involving oil and gas properties upheld the general rule and held that a purchaser cannot be forced to purchase the entire package. In *Brown v. Samson Resources Co.*,<sup>85</sup> the parties were subject to a 1956 Model Form Agreement containing a PRP. The purchase and sale agreement between Huber, the seller, and Coda, the buyer, accounted for the existence of preferential right holders, by attaching a schedule listing allocated values for the individual leasehold interests.<sup>86</sup> Pursuant to the PRP, Huber notified Brown and Samson of their option to purchase an interest in two wells included in a unit under a single operating agreement.<sup>87</sup> After determining the case on other grounds, the court in dicta, cited the Oklahoma case of *Ollie v. Rainbolt*,<sup>88</sup> stating: “We know from *Ollie* Samson cannot be forced to choose between purchasing all the interests, whether subject to their preferential right or not, included in the Coda agreement, and forfeiting its preferential right to purchase in the Cummings and Lance wells.”<sup>89</sup>

Based upon the *Brown* and *McMillan* cases, there is no reason to believe that the courts will not continue to construe PRP provisions in the context of an oil and gas package sale any differently from real estate or other transactions. A seller and purchaser would be prudent in assuming that the preferential right rules apply to package sales.

### **[C] Mechanics of Complying With Preferential Right to Purchase**

The procedure and requirements for giving notice and responding to notices under PRPs will depend on the language in the relevant preferential right. The 1989 A.A.P.L. Model Form requires a notice setting forth the a) name and address of the prospective buyer, b) the purchase price, c) a legal description

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<sup>83</sup>*Id.* at 495.

<sup>84</sup> 144 S.W.3d 159 (Tex. App. 2004); see also *Navasota Resources, L.P. v. First Source Texas, Inc.*, 249 S.W.3d 526 (Tex. App. 2008) (Navasota had to comply only with the terms of sale relating to the working interest being conveyed and not the additional terms of sale).

<sup>85</sup>Nos. 99-6344, 99-6345, 2000 WL 1234851 (10th Cir. August 31, 2000).

<sup>86</sup>*Id.* at 1.

<sup>87</sup>*Id.*

<sup>88</sup>669 P.2d 275 (Okla. 1983).

<sup>89</sup>*Brown v. Samson Resources Co.*, 2000 U.S. App. Lexis 22389, 2000 WL 1234851 at 5 (10th Cir. August 31, 2000); see *McMillan* 144 S.W.3d 159.

sufficient to identify the property, and d) all other terms of the offer. One commentator has stated that it would be difficult to justify anything less than providing a copy of the entire purchase agreement to the preferential right holder.<sup>90</sup>

The right of the holder is activated and converted into an option when the owner evidences his intent to sell.<sup>91</sup> The obligation is on the seller to give the holder notice of the proposed sale and offer the holder an opportunity to exercise the right.<sup>92</sup> The duty is not satisfied by giving the holder an opportunity merely to make an offer<sup>93</sup> or by giving the holder an opportunity to buy the burdened property at a greater price than which he subsequently sells.<sup>94</sup> The addition of terms and conditions unrelated to the purchase of the burdened property is not a satisfactory performance of the contractual obligation, and does not constitute a bona fide offer under the PRP.<sup>95</sup> Further, the contract made by the seller and third party to be submitted to the holder must be made in good faith.

Where the PRP is based upon the holder's right to accept the same terms and conditions offered by a third party, the outstanding offer becomes, in essence, the seller's offer to the holder.<sup>96</sup>

Once the offer under a PRP is made, it is a basic principle of contract law that, in order to create a contract, an acceptance must be unconditional, identical to the offer, and must not modify, delete or introduce any new terms.<sup>97</sup> Any proposal by the holder to change the terms is a rejection of the offer and the holder's proposal becomes a counter-offer.<sup>98</sup> Once the right holder gives notice of his acceptance, a sales contract is created,<sup>99</sup> even if the third party offer is

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<sup>90</sup>Cross, *supra* note 22, at 203.

<sup>91</sup>See *Peters v. Smuggler-Durant Min. Corp.*, 910 P.2d 34, 38 (Colo. App. 1995), *aff'd*, 930 P.2d 575 (Colo. 1997); *Navasota Resources, L.P. v. First Source Texas*, 249 S.W.3d 526, 533 (Tex. App. 2008); *Fasken Land and Minerals, Ltd. v. Occidental Permian Ltd.*, 225 S.W.3d 577, 591 (Tex. App. 2005).

<sup>92</sup>*Navasota*, 249 S.W.3d at 532; *No. Central Oil Corp. v. Louisiana Land & Expl. Co.*, 22 S.W.3d 572, 581 (Tex. Ct. App. 2000).

<sup>93</sup>See *Jurgenson v. Morris*, 185 N.Y.S. 386, 388 (N.Y. App. Div. 1920); *Superior Portland Cement, Inc. v. Pacific Coast Cement Co.*, 205 P.2d 597, 623 (Wash. 1949).

<sup>94</sup>See *Fordoche, Inc. v. Texaco, Inc.*, 463 F.3d 388 (5th Cir. 2006) (applying Louisiana law); *Nelson v. Reisner*, 331 P.2d 17, 22 (Cal. 1958); *San Diego Watercrafts, Inc. v. Wells Fargo Bank, N.A.*, 125 Cal. Rptr.2d 499, 505 (Cal. Ct. App. 2002).

<sup>95</sup>*Samson Resources Co. v. Amerada Hess Corp.*, 41 P.3d 1055, 1059 (Okla. Ct. App. 2001); see also *Ollie*, 669 P.2d at 280; *City of Brownsville v. Golden Spread Elec. Co-op., Inc.*, 192 S.W.3d 876, 880 (Tex. App. 2006).

<sup>96</sup>*Ollie*, 669 P.2d at 280; *Samson*, 41 P.3d at 1059; *Navasota*, 249 S.W.3d at 533.

<sup>97</sup>*Ollie*, 669 P.2d at 280; *Samson*, 41 P.3d at 1059; *Navasota*, 249 S.W.3d at 533; *City of Brownsville*, 192 S.W.3d at 880.

<sup>98</sup>See *Ollie* 669 P.2d at 281; *Samson*, 41 P.3d at 1059-60 (the court held the holder's election to purchase only certain wells in an operating agreement contract area unit was a rejection of the seller's offer); *City of Brownsville*, 192 S.W.3d at 880.

<sup>99</sup>*Abraham Inv. Co. v. Payne Ranch, Inc.*, 968 S.W.2d 518, 525 (Tex. Ct. App. 1998).

withdrawn.<sup>100</sup> Acceptance must be done in a timely manner or it will be deemed to have lapsed.<sup>101</sup>

The A.A.P.L. Model Form and other typical preferential right provisions require that the right holder be given all terms of the offer. This presents a problem on the part of the seller. Since there are usually numerous issues (and revisions) that arise from the time of agreement to the date of closing of the sale transaction, a preference holder could challenge a sale on the grounds that not all the terms were disclosed.<sup>102</sup> One commentator has suggested the seller secure a written waiver from the holder.<sup>103</sup> The waiver should be broadly drafted to cover a sale from the seller to a specific buyer so long as it closes before a specific date.<sup>104</sup>

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<sup>100</sup>Henderson v. Nitschke, 470 S.W.2d 410, 413 (Tex. Ct. App. 1971), writ ref'd n.r.e.

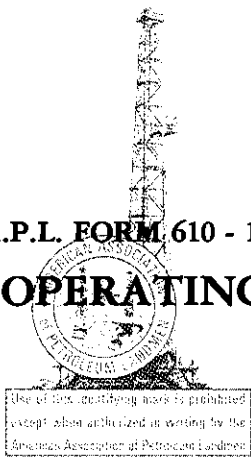
<sup>101</sup>Dyrdal v. Golden Nuggets, Inc., 689 N.W.2d 779, 785; Koch Industries, Inc. v. Sun Co. Inc. 918 F.2d 1203, 1209 (5<sup>th</sup> Cir. 1990) (interpreting Texas Law).

<sup>102</sup>Cross, *supra* note 30, at 205.

<sup>103</sup>*Id.*

<sup>104</sup>*Id.*

A.A.P.L. FORM 610 - 1989  
**MODEL FORM OPERATING AGREEMENT**



**OPERATING AGREEMENT**

**DATED**

\_\_\_\_\_, 20 \_\_\_\_\_,

**OPERATOR** \_\_\_\_\_

**CONTRACT AREA** \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

**COUNTY OR PARISH OF** \_\_\_\_\_, **STATE OF** \_\_\_\_\_

**COPYRIGHT 1989 — ALL RIGHTS RESERVED  
AMERICAN ASSOCIATION OF PETROLEUM  
LANDMEN, 4100 FOSSIL CREEK BLVD.  
FORT WORTH, TEXAS, 76137, APPROVED FORM.**

**A.A.P.L. NO. 610 - 1989**

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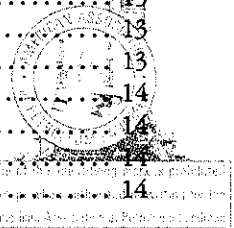
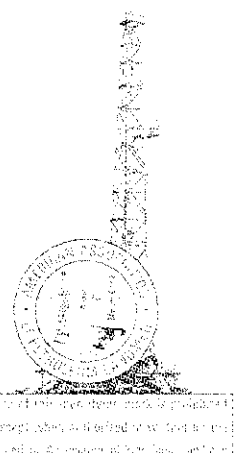


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OPERATING AGREEMENT

THIS AGREEMENT, entered into by and between \_\_\_\_\_, hereinafter designated and referred to as "Operator," and the signatory party or parties other than Operator, sometimes hereinafter referred to individually as "Non-Operator," and collectively as "Non-Operators."

WITNESSETH:

WHEREAS, the parties to this agreement are owners of Oil and Gas Leases and/or Oil and Gas Interests in the land identified in Exhibit "A," and the parties hereto have reached an agreement to explore and develop these Leases and/or Oil and Gas Interests for the production of Oil and Gas to the extent and as hereinafter provided,

NOW, THEREFORE, it is agreed as follows:

ARTICLE I. DEFINITIONS

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

A. The term "AFE" shall mean an Authority for Expenditure prepared by a party to this agreement for the purpose of estimating the costs to be incurred in conducting an operation hereunder.

B. The term "Completion" or "Complete" shall mean a single operation intended to complete a well as a producer of Oil and Gas in one or more Zones, including, but not limited to, the setting of production casing, perforating, well stimulation and production testing conducted in such operation.

C. The term "Contract Area" shall mean all of the lands, Oil and Gas Leases and/or Oil and Gas Interests intended to be developed and operated for Oil and Gas purposes under this agreement. Such lands, Oil and Gas Leases and Oil and Gas Interests are described in Exhibit "A."

D. The term "Deepen" shall mean a single operation whereby a well is drilled to an objective Zone below the deepest Zone in which the well was previously drilled, or below the Deepest Zone proposed in the associated AFE, whichever is the lesser.

E. The terms "Drilling Party" and "Consenting Party" shall mean a party who agrees to join in and pay its share of the cost of any operation conducted under the provisions of this agreement.

F. 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 Contract Area unless fixed by express agreement of the Drilling Parties.

G. The term "Drillsite" shall mean the Oil and Gas Lease or Oil and Gas Interest on which a proposed well is to be located.

H. The term "Initial Well" shall mean the well required to be drilled by the parties hereto as provided in Article VI.A.

I. The term "Non-Consent Well" shall mean a well in which less than all parties have conducted an operation as provided in Article VI.B.2.

J. The terms "Non-Drilling Party" and "Non-Consenting Party" shall mean a party who elects not to participate in a proposed operation.

K. The term "Oil and Gas" shall mean oil, gas, casinghead gas, gas condensate, and/or all other liquid or gaseous hydrocarbons and other marketable substances produced therewith, unless an intent to limit the inclusiveness of this term is specifically stated.

L. The term "Oil and Gas Interests" or "Interests" shall mean unleased fee and mineral interests in Oil and Gas in tracts of land lying within the Contract Area which are owned by parties to this agreement.

M. The terms "Oil and Gas Lease," "Lease" and "Leasehold" shall mean the oil and gas leases or interests therein covering tracts of land lying within the Contract Area which are owned by the parties to this agreement.

N. The term "Plug Back" shall mean a single operation whereby a deeper Zone is abandoned in order to attempt a Completion in a shallower Zone.

O. The term "Recompletion" or "Recomplete" shall mean an operation whereby a Completion in one Zone is abandoned in order to attempt a Completion in a different Zone within the existing wellbore.

P. The term "Rework" shall mean an operation conducted in the wellbore of a well after it is Completed to secure, restore, or improve production in a Zone which is currently open to production in the wellbore. Such operations include, but are not limited to, well stimulation operations but exclude any routine repair or maintenance work or drilling, Sidetracking, Deepening, Completing, Recompleting, or Plugging Back of a well.

Q. The term "Sidetrack" shall mean the directional control and intentional deviation of a well from vertical so as to change the bottom hole location unless done to straighten the hole or to drill around junk in the hole to overcome other mechanical difficulties.

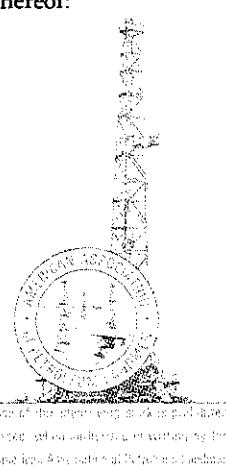
R. The term "Zone" shall mean a stratum of earth containing or thought to contain a common accumulation of Oil and Gas separately producible from any other common accumulation of Oil and Gas.

Unless the context otherwise clearly indicates, words used in the singular include the plural, the word "person" includes natural and artificial persons, the plural includes the singular, and any gender includes the masculine, feminine, and neuter.

ARTICLE II. EXHIBITS

The following exhibits, as indicated below and attached hereto, are incorporated in and made a part hereof:

- A. Exhibit "A," shall include the following information: (1) Description of lands subject to this agreement, (2) Restrictions, if any, as to depths, formations, or substances, (3) Parties to agreement with addresses and telephone numbers for notice purposes, (4) Percentages or fractional interests of parties to this agreement, (5) Oil and Gas Leases and/or Oil and Gas Interests subject to this agreement, (6) Burdens on production. B. Exhibit "B," Form of Lease. C. Exhibit "C," Accounting Procedure. D. Exhibit "D," Insurance. E. Exhibit "E," Gas Balancing Agreement. F. Exhibit "F," Non-Discrimination and Certification of Non-Segregated Facilities. G. Exhibit "G," Tax Partnership. H. Other: \_\_\_\_\_



1 If any provision of any exhibit, except Exhibits "E," "F" and "G," is inconsistent with any provision contained in  
2 the body of this agreement, the provisions in the body of this agreement shall prevail.

3 **ARTICLE III.**  
4 **INTERESTS OF PARTIES**

5 **A. Oil and Gas Interests:**

6 If any party owns an Oil and Gas Interest in the Contract Area, that Interest shall be treated for all purposes of this  
7 agreement and during the term hereof as if it were covered by the form of Oil and Gas Lease attached hereto as Exhibit "B,"  
8 and the owner thereof shall be deemed to own both royalty interest in such lease and the interest of the lessee thereunder.

9 **B. Interests of Parties in Costs and Production:**

10 Unless changed by other provisions, all costs and liabilities incurred in operations under this agreement shall be borne  
11 and paid, and all equipment and materials acquired in operations on the Contract Area shall be owned, by the parties as their  
12 interests are set forth in Exhibit "A." In the same manner, the parties shall also own all production of Oil and Gas from the  
13 Contract Area subject, however, to the payment of royalties and other burdens on production as described hereafter.

14 Regardless of which party has contributed any Oil and Gas Lease or Oil and Gas Interest on which royalty or other  
15 burdens may be payable and except as otherwise expressly provided in this agreement, each party shall pay or deliver, or  
16 cause to be paid or delivered, all burdens on its share of the production from the Contract Area up to, but not in excess of,  
17 \_\_\_\_\_ and shall indemnify, defend and hold the other parties free from any liability therefor.

18 Except as otherwise expressly provided in this agreement, if any party has contributed hereto any Lease or Interest which is  
19 burdened with any royalty, overriding royalty, production payment or other burden on production in excess of the amounts  
20 stipulated above, such party so burdened shall assume and alone bear all such excess obligations and shall indemnify, defend  
21 and hold the other parties hereto harmless from any and all claims attributable to such excess burden. However, so long as  
22 the Drilling Unit for the productive Zone(s) is identical with the Contract Area, each party shall pay or deliver, or cause to  
23 be paid or delivered, all burdens on production from the Contract Area due under the terms of the Oil and Gas Lease(s)  
24 which such party has contributed to this agreement, and shall indemnify, defend and hold the other parties free from any  
25 liability therefor.

26 No party shall ever be responsible, on a price basis higher than the price received by such party, to any other party's  
27 lessor or royalty owner, and if such other party's lessor or royalty owner should demand and receive settlement on a higher  
28 price basis, the party contributing the affected Lease shall bear the additional royalty burden attributable to such higher price.

29 Nothing contained in this Article III.B. shall be deemed an assignment or cross-assignment of interests covered hereby,  
30 and in the event two or more parties contribute to this agreement jointly owned Leases, the parties' undivided interests in  
31 said Leaseholds shall be deemed separate leasehold interests for the purposes of this agreement.

32 **C. Subsequently Created Interests:**

33 If any party has contributed hereto a Lease or Interest that is burdened with an assignment of production given as security  
34 for the payment of money, or if, after the date of this agreement, any party creates an overriding royalty, production  
35 payment, net profits interest, assignment of production or other burden payable out of production attributable to its working  
36 interest hereunder, such burden shall be deemed a "Subsequently Created Interest." Further, if any party has contributed  
37 hereto a Lease or Interest burdened with an overriding royalty, production payment, net profits interest, or other burden  
38 payable out of production created prior to the date of this agreement, and such burden is not shown on Exhibit "A," such  
39 burden also shall be deemed a Subsequently Created Interest to the extent such burden causes the burdens on such party's  
40 Lease or Interest to exceed the amount stipulated in Article III.B. above.

41 The party whose interest is burdened with the Subsequently Created Interest (the "Burdened Party") shall assume and  
42 alone bear, pay and discharge the Subsequently Created Interest and shall indemnify, defend and hold harmless the other  
43 parties from and against any liability therefor. Further, if the Burdened Party fails to pay, when due, its share of expenses  
44 chargeable hereunder, all provisions of Article VII.B. shall be enforceable against the Subsequently Created Interest in the  
45 same manner as they are enforceable against the working interest of the Burdened Party. If the Burdened Party is required  
46 under this agreement to assign or relinquish to any other party, or parties, all or a portion of its working interest and/or the  
47 production attributable thereto, said other party, or parties, shall receive said assignment and/or production free and clear of  
48 said Subsequently Created Interest, and the Burdened Party shall indemnify, defend and hold harmless said other party, or  
49 parties, from any and all claims and demands for payment asserted by owners of the Subsequently Created Interest.

50 **ARTICLE IV.**  
51 **TITLES**

52 **A. Title Examination:**

53 Title examination shall be made on the Drillsite of any proposed well prior to commencement of drilling operations and,  
54 if a majority in interest of the Drilling Parties so request or Operator so elects, title examination shall be made on the entire  
55 Drilling Unit, or maximum anticipated Drilling Unit, of the well. The opinion will include the ownership of the working  
56 interest, minerals, royalty, overriding royalty and production payments under the applicable Leases. Each party contributing  
57 Leases and/or Oil and Gas Interests to be included in the Drillsite or Drilling Unit, if appropriate, shall furnish to Operator  
58 all abstracts (including federal lease status reports), title opinions, title papers and curative material in its possession free of  
59 charge. All such information not in the possession of or made available to Operator by the parties, but necessary for the  
60 examination of the title, shall be obtained by Operator. Operator shall cause title to be examined by attorneys on its staff or  
61 by outside attorneys. Copies of all title opinions shall be furnished to each Drilling Party. Costs incurred by Operator in  
62 procuring abstracts, fees paid outside attorneys for title examination (including preliminary, supplemental, shut-in royalty  
63 opinions and division order title opinions) and other direct charges as provided in Exhibit "C" shall be borne by the Drilling  
64 Parties in the proportion that the interest of each Drilling Party bears to the total interest of all Drilling Parties as such  
65 interests appear in Exhibit "A." Operator shall make no charge for services rendered by its staff attorneys or other personnel  
66 in the performance of the above functions.

67 Each party shall be responsible for securing curative matter and pooling amendments or agreements required in  
68 connection with Leases or Oil and Gas Interests contributed by such party. Operator shall be responsible for the preparation  
69 and recording of pooling designations or declarations and communitization agreements as well as the conduct of hearings  
70 before governmental agencies for the securing of spacing or pooling orders or any other orders necessary or appropriate to  
71 the conduct of operations hereunder. This shall not prevent any party from appearing on its own behalf at such hearings.  
72 Costs incurred by Operator, including fees paid to outside attorneys, which are associated with hearings before governmental  
73 agencies, and which costs are necessary and proper for the activities contemplated under this agreement, shall be direct  
74 charges to the joint account and shall not be covered by the administrative overhead charges as provided in Exhibit "C."

1 Operator shall make no charge for services rendered by its staff attorneys or other personnel in the performance of the above  
2 functions.

3 No well shall be drilled on the Contract Area until after (1) the title to the Drillsite or Drilling Unit, if appropriate, has  
4 been examined as above provided, and (2) the title has been approved by the examining attorney or title has been accepted by  
5 all of the Drilling Parties in such well.

6 **B. Loss or Failure of Title:**

7 1. Failure of Title: Should any Oil and Gas Interest or Oil and Gas Lease be lost through failure of title, which results in a  
8 reduction of interest from that shown on Exhibit "A," the party credited with contributing the affected Lease or Interest  
9 (including, if applicable, a successor in interest to such party) shall have ninety (90) days from final determination of title  
10 failure to acquire a new lease or other instrument curing the entirety of the title failure, which acquisition will not be subject  
11 to Article VIII.B., and failing to do so, this agreement, nevertheless, shall continue in force as to all remaining Oil and Gas  
12 Leases and Interests; and,

13 (a) The party credited with contributing the Oil and Gas Lease or Interest affected by the title failure (including, if  
14 applicable, a successor in interest to such party) shall bear alone the entire loss and it shall not be entitled to recover from  
15 Operator or the other parties any development or operating costs which it may have previously paid or incurred, but there  
16 shall be no additional liability on its part to the other parties hereto by reason of such title failure;

17 (b) There shall be no retroactive adjustment of expenses incurred or revenues received from the operation of the  
18 Lease or Interest which has failed, but the interests of the parties contained on Exhibit "A" shall be revised on an acreage  
19 basis, as of the time it is determined finally that title failure has occurred, so that the interest of the party whose Lease or  
20 Interest is affected by the title failure will thereafter be reduced in the Contract Area by the amount of the Lease or Interest failed;

21 (c) If the proportionate interest of the other parties hereto in any producing well previously drilled on the Contract  
22 Area is increased by reason of the title failure, the party who bore the costs incurred in connection with such well attributable  
23 to the Lease or Interest which has failed shall receive the proceeds attributable to the increase in such interest (less costs and  
24 burdens attributable thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well  
25 attributable to such failed Lease or Interest;

26 (d) Should any person not a party to this agreement, who is determined to be the owner of any Lease or Interest  
27 which has failed, pay in any manner any part of the cost of operation, development, or equipment, such amount shall be paid  
28 to the party or parties who bore the costs which are so refunded;

29 (e) Any liability to account to a person not a party to this agreement for prior production of Oil and Gas which arises  
30 by reason of title failure shall be borne severally by each party (including a predecessor to a current party) who received  
31 production for which such accounting is required based on the amount of such production received, and each such party shall  
32 severally indemnify, defend and hold harmless all other parties hereto for any such liability to account;

33 (f) No charge shall be made to the joint account for legal expenses, fees or salaries in connection with the defense of  
34 the Lease or Interest claimed to have failed, but if the party contributing such Lease or Interest hereto elects to defend its title  
35 it shall bear all expenses in connection therewith; and

36 (g) If any party is given credit on Exhibit "A" to a Lease or Interest which is limited solely to ownership of an  
37 interest in the wellbore of any well or wells and the production therefrom, such party's absence of interest in the remainder  
38 of the Contract Area shall be considered a Failure of Title as to such remaining Contract Area unless that absence of interest  
39 is reflected on Exhibit "A."

40 2. Loss by Non-Payment or Erroneous Payment of Amount Due: If, through mistake or oversight, any rental, shut-in well  
41 payment, minimum royalty or royalty payment, or other payment necessary to maintain all or a portion of an Oil and Gas  
42 Lease or Interest is not paid or is erroneously paid, and as a result a Lease or Interest terminates, there shall be no monetary  
43 liability against the party who failed to make such payment. Unless the party who failed to make the required payment  
44 secures a new Lease or Interest covering the same interest within ninety (90) days from the discovery of the failure to make  
45 proper payment, which acquisition will not be subject to Article VIII.B., the interests of the parties reflected on Exhibit "A"  
46 shall be revised on an acreage basis, effective as of the date of termination of the Lease or Interest involved, and the party  
47 who failed to make proper payment will no longer be credited with an interest in the Contract Area on account of ownership  
48 of the Lease or Interest which has terminated. If the party who failed to make the required payment shall not have been fully  
49 reimbursed, at the time of the loss, from the proceeds of the sale of Oil and Gas attributable to the lost Lease or Interest,  
50 calculated on an acreage basis, for the development and operating costs previously paid on account of such Lease or Interest,  
51 it shall be reimbursed for unrecovered actual costs previously paid by it (but not for its share of the cost of any dry hole  
52 previously drilled or wells previously abandoned) from so much of the following as is necessary to effect reimbursement:

53 (a) Proceeds of Oil and Gas produced prior to termination of the Lease or Interest, less operating expenses and lease  
54 burdens chargeable hereunder to the person who failed to make payment, previously accrued to the credit of the lost Lease or  
55 Interest, on an acreage basis, up to the amount of unrecovered costs;

56 (b) Proceeds of Oil and Gas, less operating expenses and lease burdens chargeable hereunder to the person who failed  
57 to make payment, up to the amount of unrecovered costs attributable to that portion of Oil and Gas thereafter produced and  
58 marketed (excluding production from any wells thereafter drilled) which, in the absence of such Lease or Interest termination,  
59 would be attributable to the lost Lease or Interest on an acreage basis and which as a result of such Lease or Interest  
60 termination is credited to other parties, the proceeds of said portion of the Oil and Gas to be contributed by the other parties  
61 in proportion to their respective interests reflected on Exhibit "A"; and,

62 (c) Any monies, up to the amount of unrecovered costs, that may be paid by any party who is, or becomes, the owner  
63 of the Lease or Interest lost, for the privilege of participating in the Contract Area or becoming a party to this agreement.

64 3. Other Losses: All losses of Leases or Interests committed to this agreement, other than those set forth in Articles  
65 IV.B.1. and IV.B.2. above, shall be joint losses and shall be borne by all parties in proportion to their interests shown on  
66 Exhibit "A." This shall include but not be limited to the loss of any Lease or Interest through failure to develop or because  
67 express or implied covenants have not been performed (other than performance which requires only the payment of money),  
68 and the loss of any Lease by expiration at the end of its primary term if it is not renewed or extended. There shall be no  
69 readjustment of interests in the remaining portion of the Contract Area on account of any joint loss.

70 4. Curing Title: In the event of a Failure of Title under Article IV.B.1. or a loss of title under Article IV.B.2. above, any  
71 Lease or Interest acquired by any party hereto (other than the party whose interest has failed or was lost) during the ninety  
72 (90) day period provided by Article IV.B.1. and Article IV.B.2. above covering all or a portion of the interest that has failed  
73 or was lost shall be offered at cost to the party whose interest has failed or was lost, and the provisions of Article VIII.B.  
74 shall not apply to such acquisition.

**ARTICLE V.  
OPERATOR**

**A. Designation and Responsibilities of Operator:**

\_\_\_\_\_ shall be the Operator of the Contract Area, and shall conduct and direct and have full control of all operations on the Contract Area as permitted and required by, and within the limits of this agreement. In its performance of services hereunder for the Non-Operators, Operator shall be an independent contractor not subject to the control or direction of the Non-Operators except as to the type of operation to be undertaken in accordance with the election procedures contained in this agreement. Operator shall not be deemed, or hold itself out as, the agent of the Non-Operators with authority to bind them to any obligation or liability assumed or incurred by Operator as to any third party. Operator shall conduct its activities under this agreement as a reasonable prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulation, but in no event shall it have any liability as Operator to the other parties for losses sustained or liabilities incurred except such as may result from gross negligence or willful misconduct.

**B. Resignation or Removal of Operator and Selection of Successor:**

1. Resignation or Removal of Operator: Operator may resign at any time by giving written notice thereof to Non-Operators. If Operator terminates its legal existence, no longer owns an interest hereunder in the Contract Area, or is no longer capable of serving as Operator, Operator shall be deemed to have resigned without any action by Non-Operators, except the selection of a successor. Operator may be removed only for good cause by the affirmative vote of Non-Operators owning a majority interest based on ownership as shown on Exhibit "A" remaining after excluding the voting interest of Operator; such vote shall not be deemed effective until a written notice has been delivered to the Operator by a Non-Operator detailing the alleged default and Operator has failed to cure the default within thirty (30) days from its receipt of the notice or, if the default concerns an operation then being conducted, within forty-eight (48) hours of its receipt of the notice. For purposes hereof, "good cause" shall mean not only gross negligence or willful misconduct but also the material breach of or inability to meet the standards of operation contained in Article V.A. or material failure or inability to perform its obligations under this agreement.

Subject to Article VII.D.1., such resignation or removal shall not become effective until 7:00 o'clock A.M. on the first day of the calendar month following the expiration of ninety (90) days after the giving of notice of resignation by Operator or action by the Non-Operators to remove Operator, unless a successor Operator has been selected and assumes the duties of Operator at an earlier date. Operator, after effective date of resignation or removal, shall be bound by the terms hereof as a Non-Operator. A change of a corporate name or structure of Operator or transfer of Operator's interest to any single subsidiary, parent or successor corporation shall not be the basis for removal of Operator.

2. Selection of Successor Operator: Upon the resignation or removal of Operator under any provision of this agreement, a successor Operator shall be selected by the parties. The successor Operator shall be selected from the parties owning an interest in the Contract Area at the time such successor Operator is selected. The successor Operator shall be selected by the affirmative vote of two (2) or more parties owning a majority interest based on ownership as shown on Exhibit "A"; provided, however, if an Operator which has been removed or is deemed to have resigned fails to vote or votes only to succeed itself, the successor Operator shall be selected by the affirmative vote of the party or parties owning a majority interest based on ownership as shown on Exhibit "A" remaining after excluding the voting interest of the Operator that was removed or resigned. The former Operator shall promptly deliver to the successor Operator all records and data relating to the operations conducted by the former Operator to the extent such records and data are not already in the possession of the successor operator. Any cost of obtaining or copying the former Operator's records and data shall be charged to the joint account.

3. Effect of Bankruptcy: If Operator becomes insolvent, bankrupt or is placed in receivership, it shall be deemed to have resigned without any action by Non-Operators, except the selection of a successor. If a petition for relief under the federal bankruptcy laws is filed by or against Operator, and the removal of Operator is prevented by the federal bankruptcy court, all Non-Operators and Operator shall comprise an interim operating committee to serve until Operator has elected to reject or assume this agreement pursuant to the Bankruptcy Code, and an election to reject this agreement by Operator as a debtor in possession, or by a trustee in bankruptcy, shall be deemed a resignation as Operator without any action by Non-Operators, except the selection of a successor. During the period of time the operating committee controls operations, all actions shall require the approval of two (2) or more parties owning a majority interest based on ownership as shown on Exhibit "A." In the event there are only two (2) parties to this agreement, during the period of time the operating committee controls operations, a third party acceptable to Operator, Non-Operator and the federal bankruptcy court shall be selected as a member of the operating committee, and all actions shall require the approval of two (2) members of the operating committee without regard for their interest in the Contract Area based on Exhibit "A."

**C. Employees and Contractors:**

The number of employees or contractors used by Operator in conducting operations hereunder, their selection, and the hours of labor and the compensation for services performed shall be determined by Operator, and all such employees or contractors shall be the employees or contractors of Operator.

**D. Rights and Duties of Operator:**

1. Competitive Rates and Use of Affiliates: All wells drilled on the Contract Area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. If it so desires, Operator may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the area 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 are customary and usual in the area in contracts of independent contractors who are doing work of a similar nature. All work performed or materials supplied by affiliates or related parties of Operator shall be performed or supplied at competitive rates, pursuant to written agreement, and in accordance with customs and standards prevailing in the industry.

2. Discharge of Joint Account Obligations: Except as herein otherwise specifically provided, Operator shall promptly pay and discharge expenses incurred in the development and operation of the Contract Area pursuant to this agreement and shall charge each of the parties hereto with their respective proportionate shares upon the expense basis provided in Exhibit "C." Operator shall keep an accurate record of the joint account hereunder, showing expenses incurred and charges and credits made and received.

3. Protection from Liens: Operator shall pay, or cause to be paid, as and when they become due and payable, all accounts of contractors and suppliers and wages and salaries for services rendered or performed, and for materials supplied on, to or in respect of the Contract Area or any operations for the joint account thereof, and shall keep the Contract Area free from

1 liens and encumbrances resulting therefrom except for those resulting from a bona fide dispute as to services rendered or  
2 materials supplied.

3 4. Custody of Funds: Operator shall hold for the account of the Non-Operators any funds of the Non-Operators advanced  
4 or paid to the Operator, either for the conduct of operations hereunder or as a result of the sale of production from the  
5 Contract Area, and such funds shall remain the funds of the Non-Operators on whose account they are advanced or paid until  
6 used for their intended purpose or otherwise delivered to the Non-Operators or applied toward the payment of debts as  
7 provided in Article VII.B. Nothing in this paragraph shall be construed to establish a fiduciary relationship between Operator  
8 and Non-Operators for any purpose other than to account for Non-Operator funds as herein specifically provided. Nothing in  
9 this paragraph shall require the maintenance by Operator of separate accounts for the funds of Non-Operators unless the  
10 parties otherwise specifically agree.

11 5. Access to Contract Area and Records: Operator shall, except as otherwise provided herein, permit each Non-Operator  
12 or its duly authorized representative, at the Non-Operator's sole risk and cost, full and free access at all reasonable times to  
13 all operations of every kind and character being conducted for the joint account on the Contract Area and to the records of  
14 operations conducted thereon or production therefrom, including Operator's books and records relating thereto. Such access  
15 rights shall not be exercised in a manner interfering with Operator's conduct of an operation hereunder and shall not obligate  
16 Operator to furnish any geologic or geophysical data of an interpretive nature unless the cost of preparation of such  
17 interpretive data was charged to the joint account. Operator will furnish to each Non-Operator upon request copies of any  
18 and all reports and information obtained by Operator in connection with production and related items, including, without  
19 limitation, meter and chart reports, production purchaser statements, run tickets and monthly gauge reports, but excluding  
20 purchase contracts and pricing information to the extent not applicable to the production of the Non-Operator seeking the  
21 information. Any audit of Operator's records relating to amounts expended and the appropriateness of such expenditures  
22 shall be conducted in accordance with the audit protocol specified in Exhibit "C."

23 6. Filing and Furnishing Governmental Reports: Operator will file, and upon written request promptly furnish copies to  
24 each requesting Non-Operator not in default of its payment obligations, all operational notices, reports or applications  
25 required to be filed by local, State, Federal or Indian agencies or authorities having jurisdiction over operations hereunder.  
26 Each Non-Operator shall provide to Operator on a timely basis all information necessary to Operator to make such filings.

27 7. Drilling and Testing Operations: The following provisions shall apply to each well drilled hereunder, including but not  
28 limited to the Initial Well:

29 (a) Operator will promptly advise Non-Operators of the date on which the well is spudded, or the date on which  
30 drilling operations are commenced.

31 (b) Operator will send to Non-Operators such reports, test results and notices regarding the progress of operations on the well  
32 as the Non-Operators shall reasonably request, including, but not limited to, daily drilling reports, completion reports, and well logs.

33 (c) Operator shall adequately test all Zones encountered which may reasonably be expected to be capable of producing  
34 Oil and Gas in paying quantities as a result of examination of the electric log or any other logs or cores or tests conducted  
35 hereunder.

36 8. Cost Estimates. Upon request of any Consenting Party, Operator shall furnish estimates of current and cumulative costs  
37 incurred for the joint account at reasonable intervals during the conduct of any operation pursuant to this agreement.  
38 Operator shall not be held liable for errors in such estimates so long as the estimates are made in good faith.

39 9. Insurance: At all times while operations are conducted hereunder, Operator shall comply with the workers  
40 compensation law of the state where the operations are being conducted; provided, however, that Operator may be a self-  
41 insurer for liability under said compensation laws in which event the only charge that shall be made to the joint account shall  
42 be as provided in Exhibit "C." Operator shall also carry or provide insurance for the benefit of the joint account of the parties  
43 as outlined in Exhibit "D" attached hereto and made a part hereof. Operator shall require all contractors engaged in work on  
44 or for the Contract Area to comply with the workers compensation law of the state where the operations are being conducted  
45 and to maintain such other insurance as Operator may require.

46 In the event automobile liability insurance is specified in said Exhibit "D," or subsequently receives the approval of the  
47 parties, no direct charge shall be made by Operator for premiums paid for such insurance for Operator's automotive  
48 equipment.

49 **ARTICLE VI.**  
50 **DRILLING AND DEVELOPMENT**

51 **A. Initial Well:**

52 On or before the \_\_\_\_\_ day of \_\_\_\_\_, 20 \_\_\_\_\_, Operator shall commence the drilling of the Initial  
53 Well at the following location:

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60 and shall thereafter continue the drilling of the well with due diligence to

61  
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67 The drilling of the Initial Well and the participation therein by all parties is obligatory, subject to Article VI.C.1. as to participation  
68 in Completion operations and Article VI.F. as to termination of operations and Article XI as to occurrence of force majeure.

69 **B. Subsequent Operations:**

70 1. Proposed Operations: If any party hereto should desire to drill any well on the Contract Area other than the Initial Well, or  
71 if any party should desire to Rework, Sidetrack, Deepen, Recomplete or Plug Back a dry hole or a well no longer capable of  
72 producing in paying quantities in which such party has not otherwise relinquished its interest in the proposed objective Zone under  
73 this agreement, the party desiring to drill, Rework, Sidetrack, Deepen, Recomplete or Plug Back such a well shall give written  
74 notice of the proposed operation to the parties who have not otherwise relinquished their interest in such objective Zone

1 under this agreement and to all other parties in the case of a proposal for Sidetracking or Deepening, specifying the work to be  
 2 performed, the location, proposed depth, objective Zone and the estimated cost of the operation. The parties to whom such a  
 3 notice is delivered shall have thirty (30) days after receipt of the notice within which to notify the party proposing to do the work  
 4 whether they elect to participate in the cost of the proposed operation. If a drilling rig is on location, notice of a proposal to  
 5 Rework, Sidetrack, Recomplete, Plug Back or Deepen may be given by telephone and the response period shall be limited to forty-  
 6 eight (48) hours, exclusive of Saturday, Sunday and legal holidays. Failure of a party to whom such notice is delivered to reply  
 7 within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.  
 8 Any proposal by a party to conduct an operation conflicting with the operation initially proposed shall be delivered to all parties  
 9 within the time and in the manner provided in Article VI.B.6.

10 If all parties to whom such notice is delivered elect to participate in such a proposed operation, the parties shall be  
 11 contractually committed to participate therein provided such operations are commenced within the time period hereafter set  
 12 forth, and Operator shall, no later than ninety (90) days after expiration of the notice period of thirty (30) days (or as  
 13 promptly as practicable after the expiration of the forty-eight (48) hour period when a drilling rig is on location, as the case  
 14 may be), actually commence the proposed operation and thereafter complete it with due diligence at the risk and expense of  
 15 the parties participating therein; provided, however, said commencement date may be extended upon written notice of same  
 16 by Operator to the other parties, for a period of up to thirty (30) additional days if, in the sole opinion of Operator, such  
 17 additional time is reasonably necessary to obtain permits from governmental authorities, surface rights (including rights-of-  
 18 way) or appropriate drilling equipment, or to complete title examination or curative matter required for title approval or  
 19 acceptance. If the actual operation has not been commenced within the time provided (including any extension thereof as  
 20 specifically permitted herein or in the force majeure provisions of Article XI) and if any party hereto still desires to conduct  
 21 said operation, written notice proposing same must be resubmitted to the other parties in accordance herewith as if no prior  
 22 proposal had been made. Those parties that did not participate in the drilling of a well for which a proposal to Deepen or  
 23 Sidetrack is made hereunder shall, if such parties desire to participate in the proposed Deepening or Sidetracking operation,  
 24 reimburse the Drilling Parties in accordance with Article VI.B.4. in the event of a Deepening operation and in accordance  
 25 with Article VI.B.5. in the event of a Sidetracking operation.

## 26 2. Operations by Less Than All Parties:

27 (a) Determination of Participation. If any party to whom such notice is delivered as provided in Article VI.B.1. or  
 28 VI.C.1. (Option No. 2) elects not to participate in the proposed operation, then, in order to be entitled to the benefits of this  
 29 Article, the party or parties giving the notice and such other parties as shall elect to participate in the operation shall, no  
 30 later than ninety (90) days after the expiration of the notice period of thirty (30) days (or as promptly as practicable after the  
 31 expiration of the forty-eight (48) hour period when a drilling rig is on location, as the case may be) actually commence the  
 32 proposed operation and complete it with due diligence. Operator shall perform all work for the account of the Consenting  
 33 Parties; provided, however, if no drilling rig or other equipment is on location, and if Operator is a Non-Consenting Party,  
 34 the Consenting Parties shall either: (i) request Operator to perform the work required by such proposed operation for the  
 35 account of the Consenting Parties, or (ii) designate one of the Consenting Parties as Operator to perform such work. The  
 36 rights and duties granted to and imposed upon the Operator under this agreement are granted to and imposed upon the party  
 37 designated as Operator for an operation in which the original Operator is a Non-Consenting Party. Consenting Parties, when  
 38 conducting operations on the Contract Area pursuant to this Article VI.B.2., shall comply with all terms and conditions of this  
 39 agreement.

40 If less than all parties approve any proposed operation, the proposing party, immediately after the expiration of the  
 41 applicable notice period, shall advise all Parties of the total interest of the parties approving such operation and its  
 42 recommendation as to whether the Consenting Parties should proceed with the operation as proposed. Each Consenting Party,  
 43 within forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) after delivery of such notice, shall advise the  
 44 proposing party of its desire to (i) limit participation to such party's interest as shown on Exhibit "A" or (ii) carry only its  
 45 proportionate part (determined by dividing such party's interest in the Contract Area by the interests of all Consenting Parties in  
 46 the Contract Area) of Non-Consenting Parties' interests, or (iii) carry its proportionate part (determined as provided in (ii)) of  
 47 Non-Consenting Parties' interests together with all or a portion of its proportionate part of any Non-Consenting Parties'  
 48 interests that any Consenting Party did not elect to take. Any interest of Non-Consenting Parties that is not carried by a  
 49 Consenting Party shall be deemed to be carried by the party proposing the operation if such party does not withdraw its  
 50 proposal. Failure to advise the proposing party within the time required shall be deemed an election under (i). In the event a  
 51 drilling rig is on location, notice may be given by telephone, and the time permitted for such a response shall not exceed a  
 52 total of forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays). The proposing party, at its election, may  
 53 withdraw such proposal if there is less than 100% participation and shall notify all parties of such decision within ten (10)  
 54 days, or within twenty-four (24) hours if a drilling rig is on location, following expiration of the applicable response period.  
 55 If 100% subscription to the proposed operation is obtained, the proposing party shall promptly notify the Consenting Parties  
 56 of their proportionate interests in the operation and the party serving as Operator shall commence such operation within the  
 57 period provided in Article VI.B.1., subject to the same extension right as provided therein.

58 (b) Relinquishment of Interest for Non-Participation. The entire cost and risk of conducting such operations shall be  
 59 borne by the Consenting Parties in the proportions they have elected to bear same under the terms of the preceding  
 60 paragraph. Consenting Parties shall keep the leasehold estates involved in such operations free and clear of all liens and  
 61 encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such an operation results  
 62 in a dry hole, then subject to Articles VI.B.6. and VI.E.3., the Consenting Parties shall plug and abandon the well and restore  
 63 the surface location at their sole cost, risk and expense; provided, however, that those Non-Consenting Parties that  
 64 participated in the drilling, Deepening or Sidetracking of the well shall remain liable for, and shall pay, their proportionate  
 65 shares of the cost of plugging and abandoning the well and restoring the surface location insofar only as those costs were not  
 66 increased by the subsequent operations of the Consenting Parties. If any well drilled, Reworked, Sidetracked, Deepened,  
 67 Recompleted or Plugged Back under the provisions of this Article results in a well capable of producing Oil and/or Gas in  
 68 paying quantities, the Consenting Parties shall Complete and equip the well to produce at their sole cost and risk, and the  
 69 well shall then be turned over to Operator (if the Operator did not conduct the operation) and shall be operated by it at the  
 70 expense and for the account of the Consenting Parties. Upon commencement of operations for the drilling, Reworking,  
 71 Sidetracking, Recompleting, Deepening or Plugging Back of any such well by Consenting Parties in accordance with the  
 72 provisions of this Article, each Non-Consenting Party shall be deemed to have relinquished to Consenting Parties and the  
 73 Consenting Parties shall own and be entitled to receive, in proportion to their respective interests, all of such Non-  
 74 Consenting Party's interest in the well and share of production therefrom or, in the case of a Reworking, Sidetracking,

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1 Deepening, Recompleting or Plugging Back, or a Completion pursuant to Article VI.C.1. Option No. 2, all of such Non-  
2 Consenting Party's interest in the production obtained from the operation in which the Non-Consenting Party did not elect  
3 to participate. Such relinquishment shall be effective until the proceeds of the sale of such share, calculated at the well, or  
4 market value thereof if such share is not sold (after deducting applicable ad valorem, production, severance, and excise taxes,  
5 royalty, overriding royalty and other interests not excepted by Article III.C. payable out of or measured by the production  
6 from such well accruing with respect to such interest until it reverts), shall equal the total of the following:

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

14 (ii) \_\_\_\_\_ % of (a) that portion of the costs and expenses of drilling, Reworking, Sidetracking, Deepening,  
15 Plugging Back, testing, Completing, and Recompleting, after deducting any cash contributions received under Article VIII.C.,  
16 and of (b) that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections),  
17 which would have been chargeable to such Non-Consenting Party if it had participated therein.

18 Notwithstanding anything to the contrary in this Article VI.B., if the well does not reach the deepest objective Zone  
19 described in the notice proposing the well for reasons other than the encountering of granite or practically impenetrable  
20 substance or other condition in the hole rendering further operations impracticable, Operator shall give notice thereof to each  
21 Non-Consenting Party who submitted or voted for an alternative proposal under Article VI.B.6. to drill the well to a  
22 shallower Zone than the deepest objective Zone proposed in the notice under which the well was drilled, and each such Non-  
23 Consenting Party shall have the option to participate in the initial proposed Completion of the well by paying its share of the  
24 cost of drilling the well to its actual depth, calculated in the manner provided in Article VI.B.4. (a). If any such Non-  
25 Consenting Party does not elect to participate in the first Completion proposed for such well, the relinquishment provisions  
26 of this Article VI.B.2. (b) shall apply to such party's interest.

27 (c) Reworking, Recompleting or Plugging Back. An election not to participate in the drilling, Sidetracking or  
28 Deepening of a well shall be deemed an election not to participate in any Reworking or Plugging Back operation proposed in  
29 such a well, or portion thereof, to which the initial non-consent election applied that is conducted at any time prior to full  
30 recovery by the Consenting Parties of the Non-Consenting Party's recoupment amount. Similarly, an election not to  
31 participate in the Completing or Recompleting of a well shall be deemed an election not to participate in any Reworking  
32 operation proposed in such a well, or portion thereof, to which the initial non-consent election applied that is conducted at  
33 any time prior to full recovery by the Consenting Parties of the Non-Consenting Party's recoupment amount. Any such  
34 Reworking, Recompleting or Plugging Back operation conducted during the recoupment period shall be deemed part of the  
35 cost of operation of said well and there shall be added to the sums to be recouped by the Consenting Parties \_\_\_\_\_ % of  
36 that portion of the costs of the Reworking, Recompleting or Plugging Back operation which would have been chargeable to  
37 such Non-Consenting Party had it participated therein. If such a Reworking, Recompleting or Plugging Back operation is  
38 proposed during such recoupment period, the provisions of this Article VI.B. shall be applicable as between said Consenting  
39 Parties in said well.

40 (d) Recoupment Matters. During the period of time Consenting Parties are entitled to receive Non-Consenting Party's  
41 share of production, or the proceeds therefrom, Consenting Parties shall be responsible for the payment of all ad valorem,  
42 production, severance, excise, gathering and other taxes, and all royalty, overriding royalty and other burdens applicable to  
43 Non-Consenting Party's share of production not excepted by Article III.C.

44 In the case of any Reworking, Sidetracking, Plugging Back, Recompleting or Deepening operation, the Consenting  
45 Parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all  
46 such equipment shall remain unchanged; and upon abandonment of a well after such Reworking, Sidetracking, Plugging Back,  
47 Recompleting or Deepening, the Consenting Parties shall account for all such equipment to the owners thereof, with each  
48 party receiving its proportionate part in kind or in value, less cost of salvage.

49 Within ninety (90) days after the completion of any operation under this Article, the party conducting the operations  
50 for the Consenting Parties shall furnish each Non-Consenting Party with an inventory of the equipment in and connected to  
51 the well, and an itemized statement of the cost of drilling, Sidetracking, Deepening, Plugging Back, testing, Completing,  
52 Recompleting, and equipping the well for production; or, at its option, the operating party, in lieu of an itemized statement  
53 of such costs of operation, may submit a detailed statement of monthly billings. Each month thereafter, during the time the  
54 Consenting Parties are being reimbursed as provided above, the party conducting the operations for the Consenting Parties  
55 shall furnish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the operation of  
56 the well, together with a statement of the quantity of Oil and Gas produced from it and the amount of proceeds realized from  
57 the sale of the well's working interest production during the preceding month. In determining the quantity of Oil and Gas  
58 produced during any month, Consenting Parties shall use industry accepted methods such as but not limited to metering or  
59 periodic well tests. Any amount realized from the sale or other disposition of equipment newly acquired in connection with  
60 any such operation which would have been owned by a Non-Consenting Party had it participated therein shall be credited  
61 against the total unreturned costs of the work done and of the equipment purchased in determining when the interest of such  
62 Non-Consenting Party shall revert to it as above provided; and if there is a credit balance, it shall be paid to such Non-  
63 Consenting Party.

64 If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest the amounts provided  
65 for above, the relinquished interests of such Non-Consenting Party shall automatically revert to it as of 7:00 a.m. on the day  
66 following the day on which such recoupment occurs, and, from and after such reversion, such Non-Consenting Party shall  
67 own the same interest in such well, the material and equipment in or pertaining thereto, and the production therefrom as  
68 such Non-Consenting Party would have been entitled to had it participated in the drilling, Sidetracking, Reworking,  
69 Deepening, Recompleting or Plugging Back of said well. Thereafter, such Non-Consenting Party shall be charged with and  
70 shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this  
71 agreement and Exhibit "C" attached hereto.

72 3. Stand-By Costs: When a well which has been drilled or Deepened has reached its authorized depth and all tests have  
73 been completed and the results thereof furnished to the parties, or when operations on the well have been otherwise  
74 terminated pursuant to Article VI.F., stand-by costs incurred pending response to a party's notice proposing a Reworking,

1 Sidetracking, Deepening, Recompleting, Plugging Back or Completing operation in such a well (including the period required  
2 under Article VI.B.6. to resolve competing proposals) shall be charged and borne as part of the drilling or Deepening  
3 operation just completed. Stand-by costs subsequent to all parties responding, or expiration of the response time permitted,  
4 whichever first occurs, and prior to agreement as to the participating interests of all Consenting Parties pursuant to the terms  
5 of the second grammatical paragraph of Article VI.B.2. (a), shall be charged to and borne as part of the proposed operation,  
6 but if the proposal is subsequently withdrawn because of insufficient participation, such stand-by costs shall be allocated  
7 between the Consenting Parties in the proportion each Consenting Party's interest as shown on Exhibit "A" bears to the total  
8 interest as shown on Exhibit "A" of all Consenting Parties.

9 In the event that notice for a Sidetracking operation is given while the drilling rig to be utilized is on location, any party  
10 may request and receive up to five (5) additional days after expiration of the forty-eight hour response period specified in  
11 Article VI.B.1. within which to respond by paying for all stand-by costs and other costs incurred during such extended  
12 response period; Operator may require such party to pay the estimated stand-by time in advance as a condition to extending  
13 the response period. If more than one party elects to take such additional time to respond to the notice, standby costs shall be  
14 allocated between the parties taking additional time to respond on a day-to-day basis in the proportion each electing party's  
15 interest as shown on Exhibit "A" bears to the total interest as shown on Exhibit "A" of all the electing parties.

16 4. Deepening: If less than all the parties elect to participate in a drilling, Sidetracking, or Deepening operation proposed  
17 pursuant to Article VI.B.1., the interest relinquished by the Non-Consenting Parties to the Consenting Parties under Article  
18 VI.B.2. shall relate only and be limited to the lesser of (i) the total depth actually drilled or (ii) the objective depth or Zone  
19 of which the parties were given notice under Article VI.B.1. ("Initial Objective"). Such well shall not be Deepened beyond the  
20 Initial Objective without first complying with this Article to afford the Non-Consenting Parties the opportunity to participate  
21 in the Deepening operation.

22 In the event any Consenting Party desires to drill or Deepen a Non-Consent Well to a depth below the Initial Objective,  
23 such party shall give notice thereof, complying with the requirements of Article VI.B.1., to all parties (including Non-  
24 Consenting Parties). Thereupon, Articles VI.B.1. and 2. shall apply and all parties receiving such notice shall have the right to  
25 participate or not participate in the Deepening of such well pursuant to said Articles VI.B.1. and 2. If a Deepening operation  
26 is approved pursuant to such provisions, and if any Non-Consenting Party elects to participate in the Deepening operation,  
27 such Non-Consenting party shall pay or make reimbursement (as the case may be) of the following costs and expenses:

28 (a) If the proposal to Deepen is made prior to the Completion of such well as a well capable of producing in paying  
29 quantities, such Non-Consenting Party shall pay (or reimburse Consenting Parties for, as the case may be) that share of costs  
30 and expenses incurred in connection with the drilling of said well from the surface to the Initial Objective which Non-  
31 Consenting Party would have paid had such Non-Consenting Party agreed to participate therein, plus the Non-Consenting  
32 Party's share of the cost of Deepening and of participating in any further operations on the well in accordance with the other  
33 provisions of this Agreement; provided, however, all costs for testing and Completion or attempted Completion of the well  
34 incurred by Consenting Parties prior to the point of actual operations to Deepen beyond the Initial Objective shall be for the  
35 sole account of Consenting Parties.

36 (b) If the proposal is made for a Non-Consent Well that has been previously Completed as a well capable of producing  
37 in paying quantities, but is no longer capable of producing in paying quantities, such Non-Consenting Party shall pay (or  
38 reimburse Consenting Parties for, as the case may be) its proportionate share of all costs of drilling, Completing, and  
39 equipping said well from the surface to the Initial Objective, calculated in the manner provided in paragraph (a) above, less  
40 those costs recouped by the Consenting Parties from the sale of production from the well. The Non-Consenting Party shall  
41 also pay its proportionate share of all costs of re-entering said well. The Non-Consenting Parties' proportionate part (based  
42 on the percentage of such well Non-Consenting Party would have owned had it previously participated in such Non-Consent  
43 Well) of the costs of salvable materials and equipment remaining in the hole and salvable surface equipment used in  
44 connection with such well shall be determined in accordance with Exhibit "C." If the Consenting Parties have recouped the  
45 cost of drilling, Completing, and equipping the well at the time such Deepening operation is conducted, then a Non-  
46 Consenting Party may participate in the Deepening of the well with no payment for costs incurred prior to re-entering the  
47 well for Deepening.

48 The foregoing shall not imply a right of any Consenting Party to propose any Deepening for a Non-Consent Well prior  
49 to the drilling of such well to its Initial Objective without the consent of the other Consenting Parties as provided in Article  
50 VI.F.

51 5. Sidetracking: Any party having the right to participate in a proposed Sidetracking operation that does not own an  
52 interest in the affected wellbore at the time of the notice shall, upon electing to participate, tender to the wellbore owners its  
53 proportionate share (equal to its interest in the Sidetracking operation) of the value of that portion of the existing wellbore  
54 to be utilized as follows:

55 (a) If the proposal is for Sidetracking an existing dry hole, reimbursement shall be on the basis of the actual costs  
56 incurred in the initial drilling of the well down to the depth at which the Sidetracking operation is initiated.

57 (b) If the proposal is for Sidetracking a well which has previously produced, reimbursement shall be on the basis of  
58 such party's proportionate share of drilling and equipping costs incurred in the initial drilling of the well down to the depth  
59 at which the Sidetracking operation is conducted, calculated in the manner described in Article VI.B.4(b) above. Such party's  
60 proportionate share of the cost of the well's salvable materials and equipment down to the depth at which the Sidetracking  
61 operation is initiated shall be determined in accordance with the provisions of Exhibit "C."

62 6. Order of Preference of Operations. Except as otherwise specifically provided in this agreement, if any party desires to  
63 propose the conduct of an operation that conflicts with a proposal that has been made by a party under this Article VI, such  
64 party shall have fifteen (15) days from delivery of the initial proposal, in the case of a proposal to drill a well or to perform  
65 an operation on a well where no drilling rig is on location, or twenty-four (24) hours, exclusive of Saturday, Sunday and legal  
66 holidays, from delivery of the initial proposal, if a drilling rig is on location for the well on which such operation is to be  
67 conducted, to deliver to all parties entitled to participate in the proposed operation such party's alternative proposal, such  
68 alternate proposal to contain the same information required to be included in the initial proposal. Each party receiving such  
69 proposals shall elect by delivery of notice to Operator within five (5) days after expiration of the proposal period, or within  
70 twenty-four (24) hours (exclusive of Saturday, Sunday and legal holidays) if a drilling rig is on location for the well that is the  
71 subject of the proposals, to participate in one of the competing proposals. Any party not electing within the time required  
72 shall be deemed not to have voted. The proposal receiving the vote of parties owning the largest aggregate percentage  
73 interest of the parties voting shall have priority over all other competing proposals; in the case of a tie vote, the

1 initial proposal shall prevail. Operator shall deliver notice of such result to all parties entitled to participate in the operation  
2 within five (5) days after expiration of the election period (or within twenty-four (24) hours, exclusive of Saturday, Sunday  
3 and legal holidays, if a drilling rig is on location). Each party shall then have two (2) days (or twenty-four (24) hours if a rig  
4 is on location) from receipt of such notice to elect by delivery of notice to Operator to participate in such operation or to  
5 relinquish interest in the affected well pursuant to the provisions of Article VI.B.2.; failure by a party to deliver notice within  
6 such period shall be deemed an election not to participate in the prevailing proposal.

7 **7. Conformity to Spacing Pattern.** Notwithstanding the provisions of this Article VI.B.2., it is agreed that no wells shall be  
8 proposed to be drilled to or Completed in or produced from a Zone from which a well located elsewhere on the Contract  
9 Area is producing, unless such well conforms to the then-existing well spacing pattern for such Zone.

10 **8. Paying Wells.** No party shall conduct any Reworking, Deepening, Plugging Back, Completion, Recompletion, or  
11 Sidetracking operation under this agreement with respect to any well then capable of producing in paying quantities except  
12 with the consent of all parties that have not relinquished interests in the well at the time of such operation.

13 **C. Completion of Wells; Reworking and Plugging Back:**

14 **1. Completion:** Without the consent of all parties, no well shall be drilled, Deepened or Sidetracked, except any well  
15 drilled, Deepened or Sidetracked pursuant to the provisions of Article VI.B.2. of this agreement. Consent to the drilling,  
16 Deepening or Sidetracking shall include:

17  **Option No. 1:** All necessary expenditures for the drilling, Deepening or Sidetracking, testing, Completing and  
18 equipping of the well, including necessary tankage and/or surface facilities.

19  **Option No. 2:** All necessary expenditures for the drilling, Deepening or Sidetracking and testing of the well. When  
20 such well has reached its authorized depth, and all logs, cores and other tests have been completed, and the results  
21 thereof furnished to the parties, Operator shall give immediate notice to the Non-Operators having the right to  
22 participate in a Completion attempt whether or not Operator recommends attempting to Complete the well,  
23 together with Operator's AFE for Completion costs if not previously provided. The parties receiving such notice  
24 shall have forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) in which to elect by delivery of  
25 notice to Operator to participate in a recommended Completion attempt or to make a Completion proposal with an  
26 accompanying AFE. Operator shall deliver any such Completion proposal, or any Completion proposal conflicting  
27 with Operator's proposal, to the other parties entitled to participate in such Completion in accordance with the  
28 procedures specified in Article VI.B.6. Election to participate in a Completion attempt shall include consent to all  
29 necessary expenditures for the Completing and equipping of such well, including necessary tankage and/or surface  
30 facilities but excluding any stimulation operation not contained on the Completion AFE. Failure of any party  
31 receiving such notice to reply within the period above fixed shall constitute an election by that party not to  
32 participate in the cost of the Completion attempt; provided, that Article VI.B.6. shall control in the case of  
33 conflicting Completion proposals. If one or more, but less than all of the parties, elect to attempt a Completion, the  
34 provisions of Article VI.B.2. hereof (the phrase "Reworking, Sidetracking, Deepening, Recompleting or Plugging  
35 Back" as contained in Article VI.B.2. shall be deemed to include "Completing") shall apply to the operations  
36 thereafter conducted by less than all parties; provided, however, that Article VI.B.2 shall apply separately to each  
37 separate Completion or Recompletion attempt undertaken hereunder, and an election to become a Non-Consenting  
38 Party as to one Completion or Recompletion attempt shall not prevent a party from becoming a Consenting Party  
39 in subsequent Completion or Recompletion attempts regardless whether the Consenting Parties as to earlier  
40 Completions or Recompletions have recouped their costs pursuant to Article VI.B.2.; provided further, that any  
41 recoupment of costs by a Consenting Party shall be made solely from the production attributable to the Zone in  
42 which the Completion attempt is made. Election by a previous Non-Consenting Party to participate in a subsequent  
43 Completion or Recompletion attempt shall require such party to pay its proportionate share of the cost of salvable  
44 materials and equipment installed in the well pursuant to the previous Completion or Recompletion attempt,  
45 insofar and only insofar as such materials and equipment benefit the Zone in which such party participates in a  
46 Completion attempt.

47 **2. Rework, Recomplete or Plug Back:** No well shall be Reworked, Recompleted or Plugged Back except a well Reworked,  
48 Recompleted, or Plugged Back pursuant to the provisions of Article VI.B.2. of this agreement. Consent to the Reworking,  
49 Recompleting or Plugging Back of a well shall include all necessary expenditures in conducting such operations and  
50 Completing and equipping of said well, including necessary tankage and/or surface facilities.

51 **D. Other Operations:**

52 Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of \_\_\_\_\_  
53 \_\_\_\_\_ Dollars (\$ \_\_\_\_\_ ) except in connection with the  
54 drilling, Sidetracking, Reworking, Deepening, Completing, Recompleting or Plugging Back of a well that has been previously  
55 authorized by or pursuant to this agreement; provided, however, that, in case of explosion, fire, flood or other sudden  
56 emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion  
57 are required to deal with the emergency to safeguard life and property but Operator, as promptly as possible, shall report the  
58 emergency to the other parties. If Operator prepares an AFE for its own use, Operator shall furnish any Non-Operator so  
59 requesting an information copy thereof for any single project costing in excess of \_\_\_\_\_ Dollars  
60 ( \$ \_\_\_\_\_ ). Any party who has not relinquished its interest in a well shall have the right to propose that  
61 Operator perform repair work or undertake the installation of artificial lift equipment or ancillary production facilities such as  
62 salt water disposal wells or to conduct additional work with respect to a well drilled hereunder or other similar project (but  
63 not including the installation of gathering lines or other transportation or marketing facilities, the installation of which shall  
64 be governed by separate agreement between the parties) reasonably estimated to require an expenditure in excess of the  
65 amount first set forth above in this Article VI.D. (except in connection with an operation required to be proposed under  
66 Articles VI.B.1. or VI.C.1. Option No. 2, which shall be governed exclusively by those Articles). Operator shall deliver such  
67 proposal to all parties entitled to participate therein. If within thirty (30) days thereof Operator secures the written consent  
68 of any party or parties owning at least \_\_\_\_\_ % of the interests of the parties entitled to participate in such operation,  
69 each party having the right to participate in such project shall be bound by the terms of such proposal and shall be obligated  
70 to pay its proportionate share of the costs of the proposed project as if it had consented to such project pursuant to the terms  
71 of the proposal.

72 **E. Abandonment of Wells:**

73 **1. Abandonment of Dry Holes:** Except for any well drilled or Deepened pursuant to Article VI.B.2., any well which has  
74 been drilled or Deepened under the terms of this agreement and is proposed to be completed as a dry hole shall not be

1 plugged and abandoned without the consent of all parties. Should Operator, after diligent effort, be unable to contact any  
 2 party, or should any party fail to reply within forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) after  
 3 delivery of notice of the proposal to plug and abandon such well, such party shall be deemed to have consented to the  
 4 proposed abandonment. All such wells shall be plugged and abandoned in accordance with applicable regulations and at the  
 5 cost, risk and expense of the parties who participated in the cost of drilling or Deepening such well. Any party who objects to  
 6 plugging and abandoning such well by notice delivered to Operator within forty-eight (48) hours (exclusive of Saturday,  
 7 Sunday and legal holidays) after delivery of notice of the proposed plugging shall take over the well as of the end of such  
 8 forty-eight (48) hour notice period and conduct further operations in search of Oil and/or Gas subject to the provisions of  
 9 Article VI.B.; failure of such party to provide proof reasonably satisfactory to Operator of its financial capability to conduct  
 10 such operations or to take over the well within such period or thereafter to conduct operations on such well or plug and  
 11 abandon such well shall entitle Operator to retain or take possession of the well and plug and abandon the well. The party  
 12 taking over the well shall indemnify Operator (if Operator is an abandoning party) and the other abandoning parties against  
 13 liability for any further operations conducted on such well except for the costs of plugging and abandoning the well and  
 14 restoring the surface, for which the abandoning parties shall remain proportionately liable.

15 2. Abandonment of Wells That Have Produced: Except for any well in which a Non-Consent operation has been  
 16 conducted hereunder for which the Consenting Parties have not been fully reimbursed as herein provided, any well which has  
 17 been completed as a producer shall not be plugged and abandoned without the consent of all parties. If all parties consent to  
 18 such abandonment, the well shall be plugged and abandoned in accordance with applicable regulations and at the cost, risk  
 19 and expense of all the parties hereto. Failure of a party to reply within sixty (60) days of delivery of notice of proposed  
 20 abandonment shall be deemed an election to consent to the proposal. If, within sixty (60) days after delivery of notice of the  
 21 proposed abandonment of any well, all parties do not agree to the abandonment of such well, those wishing to continue its  
 22 operation from the Zone then open to production shall be obligated to take over the well as of the expiration of the  
 23 applicable notice period and shall indemnify Operator (if Operator is an abandoning party) and the other abandoning parties  
 24 against liability for any further operations on the well conducted by such parties. Failure of such party or parties to provide  
 25 proof reasonably satisfactory to Operator of their financial capability to conduct such operations or to take over the well  
 26 within the required period or thereafter to conduct operations on such well shall entitle Operator to retain or take possession  
 27 of such well and plug and abandon the well.

28 Parties taking over a well as provided herein shall tender to each of the other parties its proportionate share of the value of  
 29 the well's salvable material and equipment, determined in accordance with the provisions of Exhibit "C," less the estimated cost  
 30 of salvaging and the estimated cost of plugging and abandoning and restoring the surface; provided, however, that in the event  
 31 the estimated plugging and abandoning and surface restoration costs and the estimated cost of salvaging are higher than the  
 32 value of the well's salvable material and equipment, each of the abandoning parties shall tender to the parties continuing  
 33 operations their proportionate shares of the estimated excess cost. Each abandoning party shall assign to the non-abandoning  
 34 parties, without warranty, express or implied, as to title or as to quantity, or fitness for use of the equipment and material, all  
 35 of its interest in the wellbore of the well and related equipment, together with its interest in the Leasehold insofar and only  
 36 insofar as such Leasehold covers the right to obtain production from that wellbore in the Zone then open to production. If the  
 37 interest of the abandoning party is or includes an Oil and Gas Interest, such party shall execute and deliver to the non-  
 38 abandoning party or parties an oil and gas lease, limited to the wellbore and the Zone then open to production, for a term of  
 39 one (1) year and so long thereafter as Oil and/or Gas is produced from the Zone covered thereby, such lease to be on the form  
 40 attached as Exhibit "B." The assignments or leases so limited shall encompass the Drilling Unit upon which the well is located.  
 41 The payments by, and the assignments or leases to, the assignees shall be in a ratio based upon the relationship of their  
 42 respective percentage of participation in the Contract Area to the aggregate of the percentages of participation in the Contract  
 43 Area of all assignees. There shall be no readjustment of interests in the remaining portions of the Contract Area.

44 Thereafter, abandoning parties shall have no further responsibility, liability, or interest in the operation of or production  
 45 from the well in the Zone then open other than the royalties retained in any lease made under the terms of this Article. Upon  
 46 request, Operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and  
 47 charges contemplated by this agreement, plus any additional cost and charges which may arise as the result of the separate  
 48 ownership of the assigned well. Upon proposed abandonment of the producing Zone assigned or leased, the assignor or lessor  
 49 shall then have the option to repurchase its prior interest in the well (using the same valuation formula) and participate in  
 50 further operations therein subject to the provisions hereof.

51 3. Abandonment of Non-Consent Operations: The provisions of Article VI.E.1. or VI.E.2. above shall be applicable as  
 52 between Consenting Parties in the event of the proposed abandonment of any well excepted from said Articles; provided,  
 53 however, no well shall be permanently plugged and abandoned unless and until all parties having the right to conduct further  
 54 operations therein have been notified of the proposed abandonment and afforded the opportunity to elect to take over the well  
 55 in accordance with the provisions of this Article VI.E.; and provided further, that Non-Consenting Parties who own an interest  
 56 in a portion of the well shall pay their proportionate shares of abandonment and surface restoration costs for such well as  
 57 provided in Article VI.B.2.(b).

58 **F. Termination of Operations:**

59 Upon the commencement of an operation for the drilling, Reworking, Sidetracking, Plugging Back, Deepening, testing,  
 60 Completion or plugging of a well, including but not limited to the Initial Well, such operation shall not be terminated without  
 61 consent of parties bearing \_\_\_\_\_ % of the costs of such operation; provided, however, that in the event granite or other  
 62 practically impenetrable substance or condition in the hole is encountered which renders further operations impractical,  
 63 Operator may discontinue operations and give notice of such condition in the manner provided in Article VI.B.1. and the  
 64 provisions of Article VI.B. or VI.E. shall thereafter apply to such operation, as appropriate.

65 **G. Taking Production in Kind:**

66  Option No. 1: Gas Balancing Agreement Attached

67 Each party shall take in kind or separately dispose of its proportionate share of all Oil and Gas produced from the  
 68 Contract Area, exclusive of production which may be used in development and producing operations and in preparing and  
 69 treating Oil and Gas for marketing purposes and production unavoidably lost. Any extra expenditure incurred in the taking  
 70 in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party. Any  
 71 party taking its share of production in kind shall be required to pay for only its proportionate share of such part of  
 72 Operator's surface facilities which it uses.

73 Each party shall execute such division orders and contracts as may be necessary for the sale of its interest in  
 74 production from the Contract Area, and, except as provided in Article VII.B., shall be entitled to receive payment

1 directly from the purchaser thereof for its share of all production.

2 If any party fails to make the arrangements necessary to take in kind or separately dispose of its proportionate  
3 share of the Oil produced from the Contract Area, Operator shall have the right, subject to the revocation at will by  
4 the party owning it, but not the obligation, to purchase such Oil or sell it to others at any time and from time to  
5 time, for the account of the non-taking party. Any such purchase or sale by Operator may be terminated by  
6 Operator upon at least ten (10) days written notice to the owner of said production and shall be subject always to  
7 the right of the owner of the production upon at least ten (10) days written notice to Operator to exercise at any  
8 time its right to take in kind, or separately dispose of, its share of all Oil not previously delivered to a purchaser.  
9 Any purchase or sale by Operator of any other party's share of Oil shall be only for such reasonable periods of time  
10 as are consistent with the minimum needs of the industry under the particular circumstances, but in no event for a  
11 period in excess of one (1) year.

12 Any such sale by Operator shall be in a manner commercially reasonable under the circumstances but Operator  
13 shall have no duty to share any existing market or to obtain a price equal to that received under any existing  
14 market. The sale or delivery by Operator of a non-taking party's share of Oil under the terms of any existing  
15 contract of Operator shall not give the non-taking party any interest in or make the non-taking party a party to said  
16 contract. No purchase shall be made by Operator without first giving the non-taking party at least ten (10) days  
17 written notice of such intended purchase and the price to be paid or the pricing basis to be used.

18 All parties shall give timely written notice to Operator of their Gas marketing arrangements for the following  
19 month, excluding price, and shall notify Operator immediately in the event of a change in such arrangements.  
20 Operator shall maintain records of all marketing arrangements, and of volumes actually sold or transported, which  
21 records shall be made available to Non-Operators upon reasonable request.

22 In the event one or more parties' separate disposition of its share of the Gas causes split-stream deliveries to separate  
23 pipelines and/or deliveries which on a day-to-day basis for any reason are not exactly equal to a party's respective proportion-  
24 ate share of total Gas sales to be allocated to it, the balancing or accounting between the parties shall be in accordance with  
25 any Gas balancing agreement between the parties hereto, whether such an agreement is attached as Exhibit "E" or is a  
26 separate agreement. Operator shall give notice to all parties of the first sales of Gas from any well under this agreement.

27  **Option No. 2: No Gas Balancing Agreement:**

28 Each party shall take in kind or separately dispose of its proportionate share of all Oil and Gas produced from  
29 the Contract Area, exclusive of production which may be used in development and producing operations and in  
30 preparing and treating Oil and Gas for marketing purposes and production unavoidably lost. Any extra expenditure  
31 incurred in the taking in kind or separate disposition by any party of its proportionate share of the production shall  
32 be borne by such party. Any party taking its share of production in kind shall be required to pay for only its  
33 proportionate share of such part of Operator's surface facilities which it uses.

34 Each party shall execute such division orders and contracts as may be necessary for the sale of its interest in  
35 production from the Contract Area, and, except as provided in Article VII.B., shall be entitled to receive payment  
36 directly from the purchaser thereof for its share of all production.

37 If any party fails to make the arrangements necessary to take in kind or separately dispose of its proportionate  
38 share of the Oil and/or Gas produced from the Contract Area, Operator shall have the right, subject to the  
39 revocation at will by the party owning it, but not the obligation, to purchase such Oil and/or Gas or sell it to others  
40 at any time and from time to time, for the account of the non-taking party. Any such purchase or sale by Operator  
41 may be terminated by Operator upon at least ten (10) days written notice to the owner of said production and shall  
42 be subject always to the right of the owner of the production upon at least ten (10) days written notice to Operator  
43 to exercise its right to take in kind, or separately dispose of, its share of all Oil and/or Gas not previously delivered  
44 to a purchaser; provided, however, that the effective date of any such revocation may be deferred at Operator's  
45 election for a period not to exceed ninety (90) days if Operator has committed such production to a purchase  
46 contract having a term extending beyond such ten (10) -day period. Any purchase or sale by Operator of any other  
47 party's share of Oil and/or Gas shall be only for such reasonable periods of time as are consistent with the  
48 minimum needs of the industry under the particular circumstances, but in no event for a period in excess of one (1)  
49 year.

50 Any such sale by Operator shall be in a manner commercially reasonable under the circumstances, but Operator  
51 shall have no duty to share any existing market or transportation arrangement or to obtain a price or transportation  
52 fee equal to that received under any existing market or transportation arrangement. The sale or delivery by  
53 Operator of a non-taking party's share of production under the terms of any existing contract of Operator shall not  
54 give the non-taking party any interest in or make the non-taking party a party to said contract. No purchase of Oil  
55 and Gas and no sale of Gas shall be made by Operator without first giving the non-taking party ten days written  
56 notice of such intended purchase or sale and the price to be paid or the pricing basis to be used. Operator shall give  
57 notice to all parties of the first sale of Gas from any well under this Agreement.

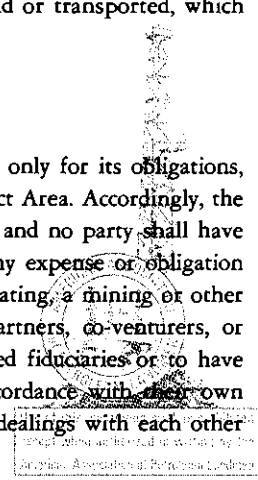
58 All parties shall give timely written notice to Operator of their Gas marketing arrangements for the following  
59 month, excluding price, and shall notify Operator immediately in the event of a change in such arrangements.  
60 Operator shall maintain records of all marketing arrangements, and of volumes actually sold or transported, which  
61 records shall be made available to Non-Operators upon reasonable request.

62 **ARTICLE VII.**

63 **EXPENDITURES AND LIABILITY OF PARTIES**

64 **A. Liability of Parties:**

65 The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations,  
66 and shall be liable only for its proportionate share of the costs of developing and operating the Contract Area. Accordingly, the  
67 liens granted among the parties in Article VII.B. are given to secure only the debts of each severally, and no party shall have  
68 any liability to third parties hereunder to satisfy the default of any other party in the payment of any expense or obligation  
69 hereunder. It is not the intention of the parties to create, nor shall this agreement be construed as creating a mining or other  
70 partnership, joint venture, agency relationship or association, or to render the parties liable as partners, co-venturers, or  
71 principals. In their relations with each other under this agreement, the parties shall not be considered fiduciaries or to have  
72 established a confidential relationship but rather shall be free to act on an arm's-length basis in accordance with their own  
73 respective self-interest, subject, however, to the obligation of the parties to act in good faith in their dealings with each other  
74 with respect to activities hereunder.



1 **B. Liens and Security Interests:**

2 Each party grants to the other parties hereto a lien upon any interest it now owns or hereafter acquires in Oil and Gas  
3 Leases and Oil and Gas Interests in the Contract Area, and a security interest and/or purchase money security interest in any  
4 interest it now owns or hereafter acquires in the personal property and fixtures on or used or obtained for use in connection  
5 therewith, to secure performance of all of its obligations under this agreement including but not limited to payment of expense,  
6 interest and fees, the proper disbursement of all monies paid hereunder, the assignment or relinquishment of interest in Oil  
7 and Gas Leases as required hereunder, and the proper performance of operations hereunder. Such lien and security interest  
8 granted by each party hereto shall include such party's leasehold interests, working interests, operating rights, and royalty and  
9 overriding royalty interests in the Contract Area now owned or hereafter acquired and in lands pooled or unitized therewith or  
10 otherwise becoming subject to this agreement, the Oil and Gas when extracted therefrom and equipment situated thereon or  
11 used or obtained for use in connection therewith (including, without limitation, all wells, tools, and tubular goods), and accounts  
12 (including, without limitation, accounts arising from gas imbalances or from the sale of Oil and/or Gas at the wellhead),  
13 contract rights, inventory and general intangibles relating thereto or arising therefrom, and all proceeds and products of the  
14 foregoing.

15 To perfect the lien and security agreement provided herein, each party hereto shall execute and acknowledge the recording  
16 supplement and/or any financing statement prepared and submitted by any party hereto in conjunction herewith or at any time  
17 following execution hereof, and Operator is authorized to file this agreement or the recording supplement executed herewith as  
18 a lien or mortgage in the applicable real estate records and as a financing statement with the proper officer under the Uniform  
19 Commercial Code in the state in which the Contract Area is situated and such other states as Operator shall deem appropriate  
20 to perfect the security interest granted hereunder. Any party may file this agreement, the recording supplement executed  
21 herewith, or such other documents as it deems necessary as a lien or mortgage in the applicable real estate records and/or a  
22 financing statement with the proper officer under the Uniform Commercial Code.

23 Each party represents and warrants to the other parties hereto that the lien and security interest granted by such party to  
24 the other parties shall be a first and prior lien, and each party hereby agrees to maintain the priority of said lien and security  
25 interest against all persons acquiring an interest in Oil and Gas Leases and Interests covered by this agreement by, through or  
26 under such party. All parties acquiring an interest in Oil and Gas Leases and Oil and Gas Interests covered by this agreement,  
27 whether by assignment, merger, mortgage, operation of law, or otherwise, shall be deemed to have taken subject  
28 to the lien and security interest granted by this Article VII.B. as to all obligations attributable to such interest hereunder  
29 whether or not such obligations arise before or after such interest is acquired.

30 To the extent that parties have a security interest under the Uniform Commercial Code of the state in which the  
31 Contract Area is situated, they shall be entitled to exercise the rights and remedies of a secured party under the Code.  
32 The bringing of a suit and the obtaining of judgment by a party for the secured indebtedness shall not be deemed an  
33 election of remedies or otherwise affect the lien rights or security interest as security for the payment thereof. In  
34 addition, upon default by any party in the payment of its share of expenses, interests or fees, or upon the improper use  
35 of funds by the Operator, the other parties shall have the right, without prejudice to other rights or remedies, to collect  
36 from the purchaser the proceeds from the sale of such defaulting party's share of Oil and Gas until the amount owed by  
37 such party, plus interest as provided in "Exhibit C," has been received, and shall have the right to offset the amount  
38 owed against the proceeds from the sale of such defaulting party's share of Oil and Gas. All purchasers of production  
39 may rely on a notification of default from the non-defaulting party or parties stating the amount due as a result of the  
40 default, and all parties waive any recourse available against purchasers for releasing production proceeds as provided in  
41 this paragraph.

42 If any party fails to pay its share of cost within one hundred twenty (120) days after rendition of a statement therefor by  
43 Operator, the non-defaulting parties, including Operator, shall, upon request by Operator, pay the unpaid amount in the  
44 proportion that the interest of each such party bears to the interest of all such parties. The amount paid by each party so  
45 paying its share of the unpaid amount shall be secured by the liens and security rights described in Article VII.B., and each  
46 paying party may independently pursue any remedy available hereunder or otherwise.

47 If any party does not perform all of its obligations hereunder, and the failure to perform subjects such party to foreclosure  
48 or execution proceedings pursuant to the provisions of this agreement, to the extent allowed by governing law, the defaulting  
49 party waives any available right of redemption from and after the date of judgment, any required valuation or appraisalment  
50 of the mortgaged or secured property prior to sale, any available right to stay execution or to require a marshalling of assets  
51 and any required bond in the event a receiver is appointed. In addition, to the extent permitted by applicable law, each party  
52 hereby grants to the other parties a power of sale as to any property that is subject to the lien and security rights granted  
53 hereunder, such power to be exercised in the manner provided by applicable law or otherwise in a commercially reasonable  
54 manner and upon reasonable notice.

55 Each party agrees that the other parties shall be entitled to utilize the provisions of Oil and Gas lien law or other lien  
56 law of any state in which the Contract Area is situated to enforce the obligations of each party hereunder. Without limiting  
57 the generality of the foregoing, to the extent permitted by applicable law, Non-Operators agree that Operator may invoke or  
58 utilize the mechanics' or materialmen's lien law of the state in which the Contract Area is situated in order to secure the  
59 payment to Operator of any sum due hereunder for services performed or materials supplied by Operator.

60 **C. Advances:**

61 Operator, at its election, shall have the right from time to time to demand and receive from one or more of the other  
62 parties payment in advance of their respective shares of the estimated amount of the expense to be incurred in operations  
63 hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an  
64 itemized statement of such estimated expense, together with an invoice for its share thereof. Each such statement and invoice  
65 for the payment in advance of estimated expense shall be submitted on or before the 20th day of the next preceding month.  
66 Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and  
67 invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest as  
68 provided in Exhibit "C" until paid. Proper adjustment shall be made monthly between advances and actual expense to the end  
69 that each party shall bear and pay its proportionate share of actual expenses incurred, and no more.

70 **D. Defaults and Remedies:**

71 If any party fails to discharge any financial obligation under this agreement, including without limitation the failure to  
72 make any advance under the preceding Article VII.C. or any other provision of this agreement, within the period required for  
73 such payment hereunder, then in addition to the remedies provided in Article VII.B. or elsewhere in this agreement, the  
74 remedies specified below shall be applicable. For purposes of this Article VII.D., all notices and elections shall be delivered

1 only by Operator, except that Operator shall deliver any such notice and election requested by a non-defaulting Non-Operator,  
2 and when Operator is the party in default, the applicable notices and elections can be delivered by any Non-Operator.  
3 Election of any one or more of the following remedies shall not preclude the subsequent use of any other remedy specified  
4 below or otherwise available to a non-defaulting party.

5 1. Suspension of Rights: Any party may deliver to the party in default a Notice of Default, which shall specify the default,  
6 specify the action to be taken to cure the default, and specify that failure to take such action will result in the exercise of one  
7 or more of the remedies provided in this Article. If the default is not cured within thirty (30) days of the delivery of such  
8 Notice of Default, all of the rights of the defaulting party granted by this agreement may upon notice be suspended until the  
9 default is cured, without prejudice to the right of the non-defaulting party or parties to continue to enforce the obligations of  
10 the defaulting party previously accrued or thereafter accruing under this agreement. If Operator is the party in default, the  
11 Non-Operators shall have in addition the right, by vote of Non-Operators owning a majority in interest in the Contract Area  
12 after excluding the voting interest of Operator, to appoint a new Operator effective immediately. The rights of a defaulting  
13 party that may be suspended hereunder at the election of the non-defaulting parties shall include, without limitation, the right  
14 to receive information as to any operation conducted hereunder during the period of such default, the right to elect to  
15 participate in an operation proposed under Article VI.B. of this agreement, the right to participate in an operation being  
16 conducted under this agreement even if the party has previously elected to participate in such operation, and the right to  
17 receive proceeds of production from any well subject to this agreement.

18 2. Suit for Damages: Non-defaulting parties or Operator for the benefit of non-defaulting parties may sue (at joint  
19 account expense) to collect the amounts in default, plus interest accruing on the amounts recovered from the date of default  
20 until the date of collection at the rate specified in Exhibit "C" attached hereto. Nothing herein shall prevent any party from  
21 suing any defaulting party to collect consequential damages accruing to such party as a result of the default.

22 3. Deemed Non-Consent: The non-defaulting party may deliver a written Notice of Non-Consent Election to the  
23 defaulting party at any time after the expiration of the thirty-day cure period following delivery of the Notice of Default, in  
24 which event if the billing is for the drilling of a new well or the Plugging Back, Sidetracking, Reworking or Deepening of a  
25 well which is to be or has been plugged as a dry hole, or for the Completion or Recompletion of any well, the defaulting  
26 party will be conclusively deemed to have elected not to participate in the operation and to be a Non-Consenting Party with  
27 respect thereto under Article VI.B. or VI.C., as the case may be, to the extent of the costs unpaid by such party,  
28 notwithstanding any election to participate theretofore made. If election is made to proceed under this provision, then the  
29 non-defaulting parties may not elect to sue for the unpaid amount pursuant to Article VII.D.2.

30 Until the delivery of such Notice of Non-Consent Election to the defaulting party, such party shall have the right to cure  
31 its default by paying its unpaid share of costs plus interest at the rate set forth in Exhibit "C," provided, however, such  
32 payment shall not prejudice the rights of the non-defaulting parties to pursue remedies for damages incurred by the non-  
33 defaulting parties as a result of the default. Any interest relinquished pursuant to this Article VII.D.3. shall be offered to the  
34 non-defaulting parties in proportion to their interests, and the non-defaulting parties electing to participate in the ownership  
35 of such interest shall be required to contribute their shares of the defaulted amount upon their election to participate therein.

36 4. Advance Payment: If a default is not cured within thirty (30) days of the delivery of a Notice of Default, Operator, or  
37 Non-Operators if Operator is the defaulting party, may thereafter require advance payment from the defaulting  
38 party of such defaulting party's anticipated share of any item of expense for which Operator, or Non-Operators, as the case may  
39 be, would be entitled to reimbursement under any provision of this agreement, whether or not such expense was the subject of  
40 the previous default. Such right includes, but is not limited to, the right to require advance payment for the estimated costs of  
41 drilling a well or Completion of a well as to which an election to participate in drilling or Completion has been made. If the  
42 defaulting party fails to pay the required advance payment, the non-defaulting parties may pursue any of the remedies provided  
43 in this Article VII.D. or any other default remedy provided elsewhere in this agreement. Any excess of funds advanced remaining  
44 when the operation is completed and all costs have been paid shall be promptly returned to the advancing party.

45 5. Costs and Attorneys' Fees. In the event any party is required to bring legal proceedings to enforce any financial  
46 obligation of a party hereunder, the prevailing party in such action shall be entitled to recover all court costs, costs of  
47 collection, and a reasonable attorney's fee, which the lien provided for herein shall also secure.

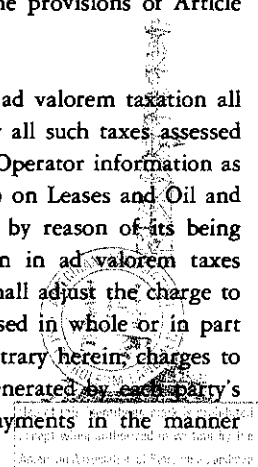
48 **E. Rentals, Shut-in Well Payments and Minimum Royalties:**

49 Rentals, shut-in well payments and minimum royalties which may be required under the terms of any lease shall be paid  
50 by the party or parties who subjected such lease to this agreement at its or their expense. In the event two or more parties  
51 own and have contributed interests in the same lease to this agreement, such parties may designate one of such parties to  
52 make said payments for and on behalf of all such parties. Any party may request, and shall be entitled to receive, proper  
53 evidence of all such payments. In the event of failure to make proper payment of any rental, shut-in well payment or  
54 minimum royalty through mistake or oversight where such payment is required to continue the lease in force, any loss which  
55 results from such non-payment shall be borne in accordance with the provisions of Article IV.B.2.

56 Operator shall notify Non-Operators of the anticipated completion of a shut-in well, or the shutting in or return to  
57 production of a producing well, at least five (5) days (excluding Saturday, Sunday and legal holidays) prior to taking such  
58 action, or at the earliest opportunity permitted by circumstances, but assumes no liability for failure to do so. In the event of  
59 failure by Operator to so notify Non-Operators, the loss of any lease contributed hereto by Non-Operators for failure to make  
60 timely payments of any shut-in well payment shall be borne jointly by the parties hereto under the provisions of Article  
61 IV.B.3.

62 **F. Taxes:**

63 Beginning with the first calendar year after the effective date hereof, Operator shall render for ad valorem taxation all  
64 property subject to this agreement which by law should be rendered for such taxes, and it shall pay all such taxes assessed  
65 thereon before they become delinquent. Prior to the rendition date, each Non-Operator shall furnish Operator information as  
66 to burdens (to include, but not be limited to, royalties, overriding royalties and production payments) on Leases and Oil and  
67 Gas Interests contributed by such Non-Operator. If the assessed valuation of any Lease is reduced by reason of its being  
68 subject to outstanding excess royalties, overriding royalties or production payments, the reduction in ad valorem taxes  
69 resulting therefrom shall inure to the benefit of the owner or owners of such Lease, and Operator shall adjust the charge to  
70 such owner or owners so as to reflect the benefit of such reduction. If the ad valorem taxes are based in whole or in part  
71 upon separate valuations of each party's working interest, then notwithstanding anything to the contrary herein, charges to  
72 the joint account shall be made and paid by the parties hereto in accordance with the tax value generated by each party's  
73 working interest. Operator shall bill the other parties for their proportionate shares of all tax payments in the manner  
74 provided in Exhibit "C."



1 If Operator considers any tax assessment improper, Operator may, at its discretion, protest within the time and manner  
2 prescribed by law, and prosecute the protest to a final determination, unless all parties agree to abandon the protest prior to final  
3 determination. During the pendency of administrative or judicial proceedings, Operator may elect to pay, under protest, all such taxes  
4 and any interest and penalty. When any such protested assessment shall have been finally determined, Operator shall pay the tax for  
5 the joint account, together with any interest and penalty accrued, and the total cost shall then be assessed against the parties, and be  
6 paid by them, as provided in Exhibit "C."

7 Each party shall pay or cause to be paid all production, severance, excise, gathering and other taxes imposed upon or with respect  
8 to the production or handling of such party's share of Oil and Gas produced under the terms of this agreement.

9 **ARTICLE VIII.**

10 **ACQUISITION, MAINTENANCE OR TRANSFER OF INTEREST**

11 **A. Surrender of Leases:**

12 The Leases covered by this agreement, insofar as they embrace acreage in the Contract Area, shall not be surrendered in whole  
13 or in part unless all parties consent thereto.

14 However, should any party desire to surrender its interest in any Lease or in any portion thereof, such party shall give written  
15 notice of the proposed surrender to all parties, and the parties to whom such notice is delivered shall have thirty (30) days after  
16 delivery of the notice within which to notify the party proposing the surrender whether they elect to consent thereto. Failure of a  
17 party to whom such notice is delivered to reply within said 30-day period shall constitute a consent to the surrender of the Leases  
18 described in the notice. If all parties do not agree or consent thereto, the party desiring to surrender shall assign, without express or  
19 implied warranty of title, all of its interest in such Lease, or portion thereof, and any well, material and equipment which may be  
20 located thereon and any rights in production thereafter secured, to the parties not consenting to such surrender. If the interest of the  
21 assigning party is or includes an Oil and Gas Interest, the assigning party shall execute and deliver to the party or parties not  
22 consenting to such surrender an oil and gas lease covering such Oil and Gas Interest for a term of one (1) year and so long  
23 thereafter as Oil and/or Gas is produced from the land covered thereby, such lease to be on the form attached hereto as Exhibit "B."  
24 Upon such assignment or lease, the assigning party shall be relieved from all obligations thereafter accruing, but not theretofore  
25 accrued, with respect to the interest assigned or leased and the operation of any well attributable thereto, and the assigning party  
26 shall have no further interest in the assigned or leased premises and its equipment and production other than the royalties retained  
27 in any lease made under the terms of this Article. The party assignee or lessee shall pay to the party assignor or lessor the  
28 reasonable salvage value of the latter's interest in any well's salvable materials and equipment attributable to the assigned or leased  
29 acreage. The value of all salvable materials and equipment shall be determined in accordance with the provisions of Exhibit "C," less  
30 the estimated cost of salvaging and the estimated cost of plugging and abandoning and restoring the surface. If such value is less  
31 than such costs, then the party assignor or lessor shall pay to the party assignee or lessee the amount of such deficit. If the  
32 assignment or lease is in favor of more than one party, the interest shall be shared by such parties in the proportions that the  
33 interest of each bears to the total interest of all such parties. If the interest of the parties to whom the assignment is to be made  
34 varies according to depth, then the interest assigned shall similarly reflect such variances.

35 Any assignment, lease or surrender made under this provision shall not reduce or change the assignor's, lessor's or surrendering  
36 party's interest as it was immediately before the assignment, lease or surrender in the balance of the Contract Area; and the acreage  
37 assigned, leased or surrendered, and subsequent operations thereon, shall not thereafter be subject to the terms and provisions of this  
38 agreement but shall be deemed subject to an Operating Agreement in the form of this agreement.

39 **B. Renewal or Extension of Leases:**

40 If any party secures a renewal or replacement of an Oil and Gas Lease or Interest subject to this agreement, then all other parties  
41 shall be notified promptly upon such acquisition or, in the case of a replacement Lease taken before expiration of an existing Lease,  
42 promptly upon expiration of the existing Lease. The parties notified shall have the right for a period of thirty (30) days following  
43 delivery of such notice in which to elect to participate in the ownership of the renewal or replacement Lease, insofar as such Lease  
44 affects lands within the Contract Area, by paying to the party who acquired it their proportionate shares of the acquisition cost  
45 allocated to that part of such Lease within the Contract Area, which shall be in proportion to the interests held at that time by the  
46 parties in the Contract Area. Each party who participates in the purchase of a renewal or replacement Lease shall be given an  
47 assignment of its proportionate interest therein by the acquiring party.

48 If some, but less than all, of the parties elect to participate in the purchase of a renewal or replacement Lease, it shall be owned  
49 by the parties who elect to participate therein, in a ratio based upon the relationship of their respective percentage of participation in  
50 the Contract Area to the aggregate of the percentages of participation in the Contract Area of all parties participating in the  
51 purchase of such renewal or replacement Lease. The acquisition of a renewal or replacement Lease by any or all of the parties hereto  
52 shall not cause a readjustment of the interests of the parties stated in Exhibit "A," but any renewal or replacement Lease in which  
53 less than all parties elect to participate shall not be subject to this agreement but shall be deemed subject to a separate Operating  
54 Agreement in the form of this agreement.

55 If the interests of the parties in the Contract Area vary according to depth, then their right to participate proportionately in  
56 renewal or replacement Leases and their right to receive an assignment of interest shall also reflect such depth variances.

57 The provisions of this Article shall apply to renewal or replacement Leases whether they are for the entire interest covered by  
58 the expiring Lease or cover only a portion of its area or an interest therein. Any renewal or replacement Lease taken before the  
59 expiration of its predecessor Lease, or taken or contracted for or becoming effective within six (6) months after the expiration of the  
60 existing Lease, shall be subject to this provision so long as this agreement is in effect at the time of such acquisition or at the time  
61 the renewal or replacement Lease becomes effective; but any Lease taken or contracted for more than six (6) months after the  
62 expiration of an existing Lease shall not be deemed a renewal or replacement Lease and shall not be subject to the provisions of this  
63 agreement.

64 The provisions in this Article shall also be applicable to extensions of Oil and Gas Leases.

65 **C. Acreage or Cash Contributions:**

66 While this agreement is in force, if any party contracts for a contribution of cash towards the drilling of a well or any other  
67 operation on the Contract Area, such contribution shall be paid to the party who conducted the drilling or other operation and shall  
68 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  
69 the contribution is made shall promptly tender an assignment of the acreage, without warranty of title, to the Drilling Parties in the  
70 proportions said Drilling Parties shared the cost of drilling the well. Such acreage shall become a separate Contract Area and, to the  
71 extent possible, be governed by provisions identical to this agreement. Each party shall promptly notify all other parties of any  
72 acreage or cash contributions it may obtain in support of any well or any other operation on the Contract Area. The above  
73 provisions shall also be applicable to optional rights to earn acreage outside the Contract Area which are in support of well drilled  
74 inside the Contract Area.

1 If any party contracts for any consideration relating to disposition of such party's share of substances produced hereunder,  
2 such consideration shall not be deemed a contribution as contemplated in this Article VIII.C.

3 **D. Assignment; Maintenance of Uniform Interest:**

4 For the purpose of maintaining uniformity of ownership in the Contract Area in the Oil and Gas Leases, Oil and Gas  
5 Interests, wells, equipment and production covered by this agreement no party shall sell, encumber, transfer or make other  
6 disposition of its interest in the Oil and Gas Leases and Oil and Gas Interests embraced within the Contract Area or in wells,  
7 equipment and production unless such disposition covers either:

- 8 1. the entire interest of the party in all Oil and Gas Leases, Oil and Gas Interests, wells, equipment and production; or
- 9 2. an equal undivided percent of the party's present interest in all Oil and Gas Leases, Oil and Gas Interests, wells,  
10 equipment and production in the Contract Area.

11 Every sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement  
12 and shall be made without prejudice to the right of the other parties, and any transferee of an ownership interest in any Oil and  
13 Gas Lease or Interest shall be deemed a party to this agreement as to the interest conveyed from and after the effective date of  
14 the transfer of ownership; provided, however, that the other parties shall not be required to recognize any such sale,  
15 encumbrance, transfer or other disposition for any purpose hereunder until thirty (30) days after they have received a copy of the  
16 instrument of transfer or other satisfactory evidence thereof in writing from the transferor or transferee. No assignment or other  
17 disposition of interest by a party shall relieve such party of obligations previously incurred by such party hereunder with respect  
18 to the interest transferred, including without limitation the obligation of a party to pay all costs attributable to an operation  
19 conducted hereunder in which such party has agreed to participate prior to making such assignment, and the lien and security  
20 interest granted by Article VII.B. shall continue to burden the interest transferred to secure payment of any such obligations.

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

28 **E. Waiver of Rights to Partition:**

29 If permitted by the laws of the state or states in which the property covered hereby is located, each party hereto owning an  
30 undivided interest in the Contract Area waives any and all rights it may have to partition and have set aside to it in severalty its  
31 undivided interest therein.

32 **F. Preferential Right to Purchase:**

33  (Optional; Check if applicable.)

34 Should any party desire to sell all or any part of its interests under this agreement, or its rights and interests in the Contract  
35 Area, it shall promptly give written notice to the other parties, with full information concerning its proposed disposition, which  
36 shall include the name and address of the prospective transferee (who must be ready, willing and able to purchase), the purchase  
37 price, a legal description sufficient to identify the property, and all other terms of the offer. The other parties shall then have an  
38 optional prior right, for a period of ten (10) days after the notice is delivered, to purchase for the stated consideration on the  
39 same terms and conditions the interest which the other party proposes to sell; and, if this optional right is exercised, the  
40 purchasing parties shall share the purchased interest in the proportions that the interest of each bears to the total interest of all  
41 purchasing parties. However, there shall be no preferential right to purchase in those cases where any party wishes to mortgage  
42 its interests, or to transfer title to its interests to its mortgagee in lieu of or pursuant to foreclosure of a mortgage of its interests,  
43 or to dispose of its interests by merger, reorganization, consolidation, or by sale of all or substantially all of its Oil and Gas assets  
44 to any party, or by transfer of its interests to a subsidiary or parent company or to a subsidiary of a parent company, or to any  
45 company in which such party owns a majority of the stock.

46 **ARTICLE IX.**

47 **INTERNAL REVENUE CODE ELECTION**

48 If, for federal income tax purposes, this agreement and the operations hereunder are regarded as a partnership, and if the  
49 parties have not otherwise agreed to form a tax partnership pursuant to Exhibit "G" or other agreement between them, each  
50 party thereby affected elects to be excluded from the application of all of the provisions of Subchapter "K," Chapter 1, Subtitle  
51 "A," of the Internal Revenue Code of 1986, as amended ("Code"), as permitted and authorized by Section 761 of the Code and  
52 the regulations promulgated thereunder. Operator is authorized and directed to execute on behalf of each party hereby affected  
53 such evidence of this election as may be required by the Secretary of the Treasury of the United States or the Federal Internal  
54 Revenue Service, including specifically, but not by way of limitation, all of the returns, statements, and the data required by  
55 Treasury Regulations §1.761. Should there be any requirement that each party hereby affected give further evidence of this  
56 election, each such party shall execute such documents and furnish such other evidence as may be required by the Federal Internal  
57 Revenue Service or as may be necessary to evidence this election. No such party shall give any notices or take any other action  
58 inconsistent with the election made hereby. If any present or future income tax laws of the state or states in which the Contract  
59 Area is located or any future income tax laws of the United States contain provisions similar to those in Subchapter "K," Chapter  
60 1, Subtitle "A," of the Code, under which an election similar to that provided by Section 761 of the Code is permitted, each party  
61 hereby affected shall make such election as may be permitted or required by such laws. In making the foregoing election, each  
62 such party states that the income derived by such party from operations hereunder can be adequately determined without the  
63 computation of partnership taxable income.

64 **ARTICLE X.**

65 **CLAIMS AND LAWSUITS**

66 Operator may settle any single uninsured third party damage claim or suit arising from operations hereunder if the expenditure  
67 does not exceed \_\_\_\_\_ Dollars (\$ \_\_\_\_\_ ) and if the payment is in complete settlement  
68 of such claim or suit. If the amount required for settlement exceeds the above amount, the parties hereto shall assume and take over  
69 the further handling of the claim or suit, unless such authority is delegated to Operator. All costs and expenses of handling, settling,  
70 or otherwise discharging such claim or suit shall be at the joint expense of the parties participating in the operation from which the  
71 claim or suit arises. If a claim is made against any party or if any party is sued on account of any matter arising from operations  
72 hereunder over which such individual has no control because of the rights given Operator by this agreement, such party shall  
73 immediately notify all other parties, and the claim or suite shall be treated as any other claim or suit involving operations hereunder.

ARTICLE XI.  
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 indemnify or make money payments or furnish security, 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 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 or other act of nature, explosion, governmental action, governmental delay, restraint or inaction, 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.

The affected party shall use all reasonable diligence to remove the force majeure situation as quickly as practicable. 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.

ARTICLE XII.  
NOTICES

All notices authorized or required between the parties by any of the provisions of this agreement, unless otherwise specifically provided, shall be in writing and delivered in person or by United States mail, courier service, telegram, telex, telecopier or any other form of facsimile, postage or charges prepaid, and addressed to such parties at the addresses listed on Exhibit "A." All telephone or oral notices permitted by this agreement shall be confirmed immediately thereafter by written notice. The originating notice given under any provision hereof shall be deemed delivered only when received by the party to whom such notice is directed, and the time for such party to deliver any notice in response thereto shall run from the date the originating notice is received. "Receipt" for purposes of this agreement with respect to written notice delivered hereunder shall be actual delivery of the notice to the address of the party to be notified specified in accordance with this agreement, or to the telecopy, facsimile or telex machine of such party. The second or any responsive notice shall be deemed delivered when deposited in the United States mail or at the office of the courier or telegraph service, or upon transmittal by telex, telecopy or facsimile, or when personally delivered to the party to be notified, provided, that when response is required within 24 or 48 hours, such response shall be given orally or by telephone, telex, telecopy or other facsimile within such period. 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. If a party is not available to receive notice orally or by telephone when a party attempts to deliver a notice required to be delivered within 24 or 48 hours, the notice may be delivered in writing by any other method specified herein and shall be deemed delivered in the same manner provided above for any responsive notice.

ARTICLE XIII.  
TERM OF AGREEMENT

This agreement shall remain in full force and effect as to the Oil and Gas Leases and/or Oil and Gas Interests subject hereto for the period of time selected below; provided, however, no party hereto shall ever be construed as having any right, title or interest in or to any Lease or Oil and Gas Interest contributed by any other party beyond the term of this agreement.

- Option No. 1: So long as any of the Oil and Gas Leases subject to this agreement remain or are continued in force as to any part of the Contract Area, whether by production, extension, renewal or otherwise.
- Option No. 2: In the event the well described in Article VI.A., or any subsequent well drilled under any provision of this agreement, results in the Completion of a well as a well capable of production of Oil and/or Gas in paying quantities, this agreement shall continue in force so long as any such well is capable of production, and for an additional period of \_\_\_\_\_ days thereafter; provided, however, if, prior to the expiration of such additional period, one or more of the parties hereto are engaged in drilling, Reworking, Deepening, Sidetracking, Plugging Back, testing or attempting to Complete or Re-complete a well or wells hereunder, this agreement shall continue in force until such operations have been completed and if production results therefrom, this agreement shall continue in force as provided herein. In the event the well described in Article VI.A., or any subsequent well drilled hereunder, results in a dry hole, and no other well is capable of producing Oil and/or Gas from the Contract Area, this agreement shall terminate unless drilling, Deepening, Sidetracking, Completing, Re-completing, Plugging Back or Reworking operations are commenced within \_\_\_\_\_ days from the date of abandonment of said well. "Abandonment" for such purposes shall mean either (i) a decision by all parties not to conduct any further operations on the well or (ii) the elapse of 180 days from the conduct of any operations on the well, whichever first occurs.

The termination of this agreement shall not relieve any party hereto from any expense, liability or other obligation or any remedy therefor which has accrued or attached prior to the date of such termination.

Upon termination of this agreement and the satisfaction of all obligations hereunder, in the event a memorandum of this Operating Agreement has been filed of record, Operator is authorized to file of record in all necessary recording offices a notice of termination, and each party hereto agrees to execute such a notice of termination as to Operator's interest, upon request of Operator, if Operator has satisfied all its financial obligations.

ARTICLE XIV.  
COMPLIANCE WITH LAWS AND REGULATIONS

A. Laws, Regulations and Orders:

This agreement shall be subject to the applicable laws of the state in which the Contract Area is located, to the valid rules, regulations, and orders of any duly constituted regulatory body of said state; and to all other applicable federal, state, and local laws, ordinances, rules, regulations and orders.

B. Governing Law:

This agreement and all matters pertaining hereto, including but not limited to matters of performance, non-performance, breach, remedies, procedures, rights, duties, and interpretation or construction, shall be governed and determined by the law of the state in which the Contract Area is located. If the Contract Area is in two or more states, the law of the state of \_\_\_\_\_ shall govern.

C. Regulatory Agencies:

Nothing herein contained shall grant, or be construed to grant, Operator the right or authority to waive or release any rights, privileges, or obligations which Non-Operators may have under federal or state laws or under rules, regulations or

1 orders promulgated under such laws in reference to oil, gas and mineral operations, including the location, operation, or  
2 production of wells, on tracts offsetting or adjacent to the Contract Area.

3 With respect to the operations hereunder, Non-Operators agree to release Operator from any and all losses, damages,  
4 injuries, claims and causes of action arising out of, incident to or resulting directly or indirectly from Operator's interpretation  
5 or application of rules, rulings, regulations or orders of the Department of Energy or Federal Energy Regulatory Commission  
6 or predecessor or successor agencies to the extent such interpretation or application was made in good faith and does not  
7 constitute gross negligence. Each Non-Operator further agrees to reimburse Operator for such Non-Operator's share of  
8 production or any refund, fine, levy or other governmental sanction that Operator may be required to pay as a result of such  
9 an incorrect interpretation or application, together with interest and penalties thereon owing by Operator as a result of such  
10 incorrect interpretation or application.

11 **ARTICLE XV.**  
12 **MISCELLANEOUS**

13 **A. Execution:**

14 This agreement shall be binding upon each Non-Operator when this agreement or a counterpart thereof has been  
15 executed by such Non-Operator and Operator notwithstanding that this agreement is not then or thereafter executed by all of  
16 the parties to which it is tendered or which are listed on Exhibit "A" as owning an interest in the Contract Area or which  
17 own, in fact, an interest in the Contract Area. Operator may, however, by written notice to all Non-Operators who have  
18 become bound by this agreement as aforesaid, given at any time prior to the actual spud date of the Initial Well but in no  
19 event later than five days prior to the date specified in Article VI.A. for commencement of the Initial Well, terminate this  
20 agreement if Operator in its sole discretion determines that there is insufficient participation to justify commencement of  
21 drilling operations. In the event of such a termination by Operator, all further obligations of the parties hereunder shall cease  
22 as of such termination. In the event any Non-Operator has advanced or prepaid any share of drilling or other costs  
23 hereunder, all sums so advanced shall be returned to such Non-Operator without interest. In the event Operator proceeds  
24 with drilling operations for the Initial Well without the execution hereof by all persons listed on Exhibit "A" as having a  
25 current working interest in such well, Operator shall indemnify Non-Operators with respect to all costs incurred for the  
26 Initial Well which would have been charged to such person under this agreement if such person had executed the same and  
27 Operator shall receive all revenues which would have been received by such person under this agreement if such person had  
28 executed the same.

29 **B. Successors and Assigns:**

30 This agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective heirs,  
31 devisees, legal representatives, successors and assigns, and the terms hereof shall be deemed to run with the Leases or  
32 Interests included within the Contract Area.

33 **C. Counterparts:**

34 This instrument may be executed in any number of counterparts, each of which shall be considered an original for all  
35 purposes.

36 **D. Severability:**

37 For the purposes of assuming or rejecting this agreement as an executory contract pursuant to federal bankruptcy laws,  
38 this agreement shall not be severable, but rather must be assumed or rejected in its entirety, and the failure of any party to  
39 this agreement to comply with all of its financial obligations provided herein shall be a material default.

40 **ARTICLE XVI.**  
41 **OTHER PROVISIONS**



1 IN WITNESS WHEREOF, this agreement shall be effective as of the \_\_\_\_\_ day of \_\_\_\_\_ ,

2 20 \_\_\_\_\_ .

3 ATTEST OR WITNESS:

OPERATOR

4 \_\_\_\_\_

5 \_\_\_\_\_ By \_\_\_\_\_

6 \_\_\_\_\_  
7 Type or print name

8 Title \_\_\_\_\_

9 Date \_\_\_\_\_

10 Tax ID or S.S. No. \_\_\_\_\_

11

12 NON-OPERATORS

13

14 \_\_\_\_\_

15 \_\_\_\_\_ By \_\_\_\_\_

16 \_\_\_\_\_  
17 Type or print name

18 Title \_\_\_\_\_

19 Date \_\_\_\_\_

20 Tax ID or S.S. No. \_\_\_\_\_

21

22 \_\_\_\_\_

23 \_\_\_\_\_ By \_\_\_\_\_

24 \_\_\_\_\_  
25 Type or print name

26 Title \_\_\_\_\_

27 Date \_\_\_\_\_

28 Tax ID or S.S. No. \_\_\_\_\_

29

30 \_\_\_\_\_ By \_\_\_\_\_

31 \_\_\_\_\_  
32 Type or print name

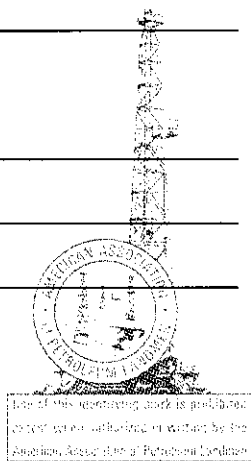
33 Title \_\_\_\_\_

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ACKNOWLEDGMENTS

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Note: The following forms of acknowledgment are the short forms approved by the Uniform Law on Notarial Acts. The validity and effect of these forms in any state will depend upon the statutes of that state.

Individual acknowledgment:

State of \_\_\_\_\_ )

\_\_\_\_\_ ) ss.

County of \_\_\_\_\_ )

This instrument was acknowledged before me on \_\_\_\_\_ by \_\_\_\_\_.

(Seal, if any) \_\_\_\_\_

Title (and Rank) \_\_\_\_\_

My commission expires: \_\_\_\_\_

Acknowledgment in representative capacity:

State of \_\_\_\_\_ )

\_\_\_\_\_ ) ss.

County of \_\_\_\_\_ )

This instrument was acknowledged before me on \_\_\_\_\_ by \_\_\_\_\_ as \_\_\_\_\_

\_\_\_\_\_ of \_\_\_\_\_.

(Seal, if any) \_\_\_\_\_

Title (and Rank) \_\_\_\_\_

My commission expires: \_\_\_\_\_

