

COATES ENERGY TRUST

ENERGY PLAZA II, SUITE 510

8610 N. NEW BRAUNFELS

SAN ANTONIO, TEXAS 78217

(210) 820-0113
FAX (210) 820-0160

P. O. BOX 171717

January 14, 2000

Mr. Glen E. Farmer
415 West Wall, Suite 705
Midland, Texas 79701-4417

Re: Oil and Gas Lease Proposal
NW/4 Section 2, T-20-S, R-38-E, N.M.P.M.
Lea County, New Mexico

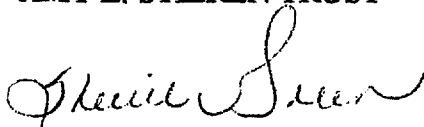
Dear Mr. Farmer

We are in receipt of your faxed message of January 14, 2000, in which you advised that Leonard Resource Investment Corp. agrees to the following basic terms set out in Coates' letter to you dated January 13, 2000.

Accordingly, for your review we have enclosed a copy of the Coates lease form. Please note that such form will need to be changed to reflect the agreed upon terms, the proper parties, and the correct references to the State of New Mexico instead of Texas, where applicable. If Leonard finds the basic terms of the attached lease form acceptable, please advise by 4:00 p.m. on January 22, 2000, and then Coates will prepare a completed lease form for final review. This is not, and is not intended to be, a binding agreement between the parties and none of the parties will have any liability to the other in the event a binding oil and gas lease is not executed for any reason.

Yours very truly,

COATES ENERGY TRUST; JENNY ROBERTS
SCHIMPF TRUST; CATHERINE G. ROBERTS
TRUST; BARRY COATES ROBERTS TRUST;
LISA STIEREN HARDEMAN TRUST; GEORGE L.
STIEREN TRUST; WENDY STIEREN WIRTH
TRUST; KELLY STIEREN DANIELL TRUST AND
AMY E. STIEREN TRUST


Sherrie Green, CPL
Land Manager

sg
Enclosure

NMOCD Case No. 12730

Coates Trust Exhibit No. 134

OIL AND GAS LEASE

THE STATE OF TEXAS §
 § KNOW ALL MEN BY THESE PRESENTS:
COUNTY OF §

THIS AGREEMENT is made and entered into this the ____ day of _____, 19____, by and between COATES ENERGY TRUST and _____, hereinafter collectively referred to as Lessor, whose mailing address is P. O. Box 171717, San Antonio, Texas 78217 and _____, hereinafter referred to as Lessee, whose address is _____.

GRANTING CLAUSE; LAND COVERED

1. Lessor, in consideration of TEN DOLLARS (\$10.00) in hand paid, of the royalties herein provided and of the agreements of Lessee herein contained, hereby LEASES and LETS unto Lessee for the purpose of (non-exclusive) investigating, exploring and prospecting; (exclusive) drilling for and producing oil and gas, the following described tract(s) of land in _____, County, _____ (hereinafter referred to as the "leased premises"), more particularly described as follows, to-wit:

(INSERT PROPERTY DESCRIPTION)

Lessor and Lessee agree that any defect in the description of the leased premises covered by this lease shall be corrected upon the request of either party, but at the sole cost and expense of Lessee, and that if a metes and bounds description of the lands covered by this lease is prepared by Lessee, then such metes and bounds description, together with a plat as hereafter prepared by a registered public surveyor shall take the place of the present description and that this lease is to be amended to include as a part of the description above a true and correct copy of said plat indicating the metes and bounds of the lands covered by this lease. (For the purpose of calculating any payments hereinafter provided for, the above described tract(s) shall be considered to comprise _____ acres, whether it actually comprises more or less.)

LEASE TERM

2. Subject to the other provisions herein contained, this lease shall be for a period of _____ (____) years from this date (called Primary Term), and for so long thereafter as oil or gas in paying quantities is produced from the leased premises or this lease is maintained in force by virtue of some other provision hereof, and so long as royalties are paid in full as provided hereinafter in this lease.

ROYALTIES

3. The royalties to be paid by Lessee are:

(a) On all oil and on all liquid hydrocarbons extracted from gas under the provisions of Subsection (b) below, one-fourth (1/4) of that which is produced and saved from the leased premises, the same to be delivered to Lessor into the storage tanks or into the pipeline to which the wells may be connected, or, at Lessor's option, such oil and liquid hydrocarbons shall be sold with Lessee's oil and liquid hydrocarbons at the same price received by Lessee (but in no event for less than the value thereof), or, at Lessor's further option, such products shall be delivered to Lessor at the wells into tanks or other receptacles to be furnished by Lessor. Lessor's options hereunder may be exercised from time to time, and the exercise or failure to exercise an option at any time shall not constitute a waiver of Lessor's right to exercise further options.

(b) On gas produced from the leased premises, including casinghead gas and residue gas at the tailgate of any plant through which gas produced from the leased premises may be processed, one-fourth (1/4) of the value of the gas (as defined herein) or at Lessor's sole option,

one-fourth (1/4) of the gas, in kind. In the event Lessor elects to take its gas in kind, Lessee shall transport and deliver without cost through its gathering or pipeline system such gas to interconnect with the gas gathering or transmission systems identified by Lessor, and such deliveries shall be made ratably, on a daily basis, and no gas imbalances will be permitted to accrue with respect to Lessor's in-kind gas. Prior to the use or sale of any gas produced from the leased premises, Lessee shall run such gas through a field-type separator or other comparable equipment ordinarily used in the industry for the purpose of separating, extracting and saving liquid and liquefiable hydrocarbons recoverable from the gas, and royalties shall be payable on the remaining gas under the provisions of this Subsection (b) and royalties on the extracted liquids shall be payable under the provisions of Subsection (a) above.

(c) On condensate and all other products separated, extracted or manufactured from gas produced from the leased premises by any extraction, absorption, pressuring or other plant belonging wholly or in part to Lessee or any affiliated, parent or subsidiary entity, one-fourth (1/4) of the value of all such condensate and other products so separated, extracted, or manufactured, or, at Lessor's option, one-fourth (1/4) of such condensate and other products in kind shall be delivered to Lessor at the plant outlet. In the event of the blending of any part of such condensate or other products with chemical additives for making any product therefrom, the royalty on such products, whether paid in kind or at value, shall be calculated at the plant outlet on the resulting blended product.

(d) On condensate and all other products separated, extracted or manufactured from gas produced from the leased premises by an extraction, absorption, pressuring or other plant belonging to a third party or parties, one-fourth (1/4) of the amount received by Lessee from the sale of condensate and other products separated, extracted or manufactured by said plant and credited to Lessee under the terms of Lessee's contract with such plant.

(e) Lessor reserves, and saves and excepts from this lease, all minerals other than oil, gas and associated by-products of oil and gas. If Lessee produces particular associated by-products of gas which are not specifically identified in this lease, the royalties to be paid by Lessee on such associated by-products of gas shall be one fourth (1/4) of the value of such associated by-products of gas. Sulphur extracted from hydrogen sulfide gas and carbon dioxide shall be included within the definition of "associated by-products of gas."

(f) While there is a gas well or wells on the leased premises, but gas is not being sold or used, Lessee may pay as royalty, commencing on or before ninety (90) days after the date on which each such gas well is shut-in, the sum of _____ DOLLARS (_____) for each acre of the leased premises ascribed to such gas well pursuant to the provisions of Section 5(c), and, if such payment is made or tendered, this lease shall continue in force and effect for the full ensuing year after such payment as to all of the leased premises ascribed to such gas well pursuant to the provisions of said Section 5(c) and for which such payment is made. The intermittent production of gas from any shut-in gas well during such year shall not render necessary any new or additional payments of shut-in gas well royalty with respect to such well, but Lessee shall account to Lessor for the royalty on any such gas actually produced in accordance with the other provisions of this Section 3, in addition to the shut-in royalty paid under this paragraph. This provision shall be recurring (the time for subsequent annual payments for each shut-in well to run from the date the first payment is made on such well); provided, however, that this provision shall not be effective to continue this lease in force and effect as to any shut-in well for a period of more than two (2) consecutive years after the date the first well is shut in or for shorter periods of time which from time to time aggregate two (2) years in all. Lessee shall notify Lessor promptly each time a gas well is shut in, furnishing Lessor with the reason for, and the specific date of, shutting the well in. Lessee shall also promptly notify Lessor of each date when a shut-in gas well is placed back on production. Any shut-in gas well royalty payment may be made by the check of Lessee mailed or delivered to Lessor at the address stated hereinabove, until a different address has been designated by Lessor. This provision as to the payment of shut-in gas royalty is a condition and not a covenant, and the failure to pay any shut-in gas royalty as herein provided shall effect an automatic termination of this lease as to the leased premises ascribed to said well.

(g) The "value" of any oil, gas, condensate or other products of gas (sometimes hereinafter collectively referred to as "hydrocarbons") for purposes of the calculation of royalty under this lease is the market value for like kind, quality and quantity of the hydrocarbons at the time and

place at which custody and risk of loss of the hydrocarbons are transferred to an unaffiliated purchaser or at the time and place of use by Lessee (but without deduction for marketing, gathering, and transportation of the hydrocarbons to the point of sale, delivery or use or any other post-production cost) and shall never be less than the total value received by Lessee or by any business entity owned in whole or in part by Lessee or any of its parent, subsidiary or affiliated entities by reason of the sale of such hydrocarbons and/or the dedication of reserves. The term "market value" herein shall not mean or be deemed modified by the definition of market value contained in the Texas Natural Resources Code §91.402. The "total value received" shall include, but not be limited to, the fair value of all consideration received by Lessee or by any affiliated, parent or subsidiary entity related to the marketing and/or dedication of hydrocarbons or reserves (such as take-or-pay payments, take-or-pay settlements and awards, dedication payments, advance payments, contract adjustments, gas exchange consideration, contract buy out/buy down payments or any other tied agreements and similar consideration). For the purposes of this Lease, "affiliated, parent or subsidiary entity" shall mean any business entity owned in whole or in part by Lessee or any of its parent, subsidiary or affiliated entities. Lessee shall be solely responsible for insuring that all such proceeds are received in accordance with all applicable laws and regulations. All royalties payable under Subsections (a), (b), (c), (d), (e) and (g) of this Section 3 shall be without deduction for any costs of marketing, gathering, transporting, separating, processing, dehydrating, compressing, construction, manufacturing or other post-production costs including any costs involved in making the oil or gas ready for sale or use. In the event Lessor does not elect to take Lessor's royalty gas in kind as provided for in this lease, Lessee shall act as Lessor's representative in negotiating and implementing sales arrangements for royalty gas in accordance with principles of good faith and fair dealing and the provisions of this lease. Further, Lessee shall not be authorized to enter into any contract which would result in Lessor receiving less than the royalty share of the value (as defined above) of the hydrocarbons produced from this lease at the time the hydrocarbons are produced. Irrespective of any contract for the sale of hydrocarbons from the subject lands which Lessee may enter into, Lessee's royalty obligation shall never be based upon a price which is less than the value of the hydrocarbons produced from the lease as defined above. It is expressly provided that Lessee and its affiliates as defined shall not have the right to dedicate the leased premises or gas reserves in and under the leased premises to the fulfillment of any public service obligation, and any dedication of gas required to fulfill Lessee's obligations under any gas purchase contract shall be specifically limited to only such gas as may be produced through the wellhead of gas wells on the leased premises during the period that this lease is being maintained in force and effect in accordance with its terms.

(h) Notwithstanding any provision of this lease to the contrary, Lessee expressly agrees that the royalties due Lessor on oil or gas produced from but sold off the leased premises, or products extracted from such production, and sold by Lessee, whether to an entity or entities associated or affiliated with Lessee or any business entity owned in whole or in part by Lessee or Lessee's parent, subsidiary or affiliated entities, or otherwise sold to a third party, are to be calculated and paid by Lessee on the greater of (a) the amount realized by Lessee, or any of Lessee's parent, subsidiary or affiliated entities, or (b) the prices paid in sales at the nearest market pooling point for the same monthly production period between unaffiliated buyers and sellers. "Market pooling point" shall be defined as independent market centers including but not limited to, by way of example only, the Houston Ship Channel, Henry Hub and other similar non-field or non-county pooling points. Lessor recognizes that sales at the nearest market pooling point require commingling of Lessor's production with that of other producers. Therefore, Lessor expressly agrees that Lessee may commingle Lessor's production, and Lessee shall not be required to trace individual sales of production back to the wellhead from the market pooling point. The market pooling point price for oil and condensate shall be determined by using the average of the "spot crude oil price assessments" as reported in Platt's Oilgram Price Report or equivalent publication such as NYMEX for the applicable grade of crude oil and for the trading period applicable to the month of delivery. The trading period is the period between pipeline nomination dates. The market pooling point price for gas (including all entrained liquids and hydrocarbons components) shall be determined by using the quoted index price per MMBTU as reported in the first issue for the month of production of the Inside F.E.R.C. Gas Marketing Report or equivalent publication such as NYMEX for the market pooling point as defined above nearest the field from which the gas was produced. Market pooling point for natural gas liquids shall be defined as including but not limited to, by way of example only, Mont Belvieu or similar non-field or non-county pooling points. All royalties payable under this section shall be without deduction for any costs of marketing, gathering, transporting, separating, processing, dehydrating, compressing, construction, manufacturing or other post-production costs

including any costs involved in making the oil or gas ready for sale or use. Lessee recognizes and acknowledges that the terms of this lease are unique to this transaction and are not applicable to any other relationship with Lessor, express or implied. If any publication used above ceases to be published or if a publication ceases to publish a specified price, then Lessor and Lessee shall agree upon a replacement publication.

(i) Lessor shall either take its royalty share of gas in kind or, in order to satisfy the market pooling point price set out in Section 3(h) above, be paid a royalty based upon the Ship Channel Pricing set out below. Lessor shall notify Lessee in writing of its election for a particular month on or prior to the 20th day of the preceding month. The failure to notify the Lessee timely of its election to take in kind shall be deemed to be an election by Lessor to be paid a royalty based upon the Ship Channel Pricing described below. If Lessor elects to take its royalty share of gas in kind, then the Lessor will take such gas at a central delivery point approved by Lessor which shall be designated by Lessee downstream of any well or wells drilled by Lessee (the CDP). Such CDP to be designated by Lessee will be the first non-affiliated interconnect with a pipeline which is transporting such gas. Lessor shall be responsible for such gas downstream of the CDP and shall arrange its own transportation and processing and shall pay all severance taxes and other taxes on such gas. If Lessor elects the Ship Channel Pricing for a month, then the price per MMBtu of the gas for royalty calculations will be the first of the month Houston Ship Channel/Beaumont, Texas Index (large package only) gas price for such month as published in Inside FERC under the heading Delivered Spot-Gas Prices (Ship Channel Large Package). If Lessee, or any affiliated company or entity owned in whole or part by Lessee, obtains amounts realized which are greater than the aforesaid prices, then the Lessor's royalty will be based on the higher amount realized by Lessee or any affiliated company or entity owned in whole or in part by Lessee. If the publication used above ceases to be published or ceases to publish a specified price, then Lessor and Lessee shall agree upon a replacement publication.

(j) The market pooling point price set out in Section 3(h) above shall be deemed satisfied for oil and condensate royalties if based upon NYMEX Pricing. Using NYMEX pricing, the price per barrel of oil/condensate for royalty calculations will be defined as the average of the daily settled prices reported by the New York Mercantile Exchange, for light sweet crude oil futures contract over the time period while the deliver month is the prompt month traded, less fifty (50) cents a barrel. If Lessee, or any affiliated company or entity owned in whole or part by Lessee, obtains amounts realized which are greater than the aforesaid price, then the Lessor's royalty will be based on the higher amount realized by Lessee or any affiliated company or entity owned in whole or in part by Lessee.

(k) The market pooling point price set out in Section 3(h) above shall be deemed satisfied for natural gas liquids royalties if such royalties are calculated using Mont Belvieu monthly prices as reported in Oil Price Information Service ("OPIS") for each product. The Non-Texas Eastern Transmission ("Non-TET") prices shall be used for propane (C₃) isobutane (IC₄), normal butane (NC₄). Purity prices shall be used for ethane (C₂). Non-TET prices shall be used for natural gasoline (C₅+). The value of the BTU shrinkage shall be the BTU shrinkage incurred by the plant attributable to the production from the leased premises (measured in MMBTUs) times the applicable gas price as determined under Section 3(i) above. If Lessee, or any affiliated company or entity owned in whole or part by Lessee, obtains amounts realized which are greater than the aforesaid price, then the Lessor's royalty will be based on the higher amount realized by Lessee or any affiliated company or entity owned in whole or in part by Lessee. If any publication used above ceases to be published or if a publication ceases to publish a specified price, then Lessor and Lessee shall agree upon a replacement publication.

(l) As a material consideration for the execution of this lease, Lessee is unconditionally obligated to Lessor to make and shall be liable for the payment of royalties pursuant to the terms of this lease irrespective of the failure or bankruptcy of any third party crude oil or gas purchaser, and irrespective of the execution by Lessor of a division order or any similar agreement in favor of any such third party purchaser. Accountings and payments to Lessor of royalties from the production of oil and gas from any well shall commence no later than ninety (90) days after the initial commencement of production. Thereafter, unless otherwise specifically provided herein, all accountings and payments for royalties shall be made on or before the 25th day of the second calendar month following the calendar month in which the production occurred. All accountings and payments for royalties payable hereunder shall be paid by Lessee, at Lessor's sole option, either (1)

by check directly to Lessor, or (2) by check or electronic transfer (as specified by Lessor) to the credit of Lessor in the Jefferson State Bank, P. O. Box 5190, San Antonio, Texas 78201-0190 (which bank and its successors are Lessor's agent and shall continue as a depository for all royalties payable hereunder unless instructed otherwise by Lessor). Should Lessee at any time fail to make royalty payments to Lessor in the full amount required by this lease in accordance with this provision, then this lease shall terminate as to such well and the leased premises ascribed to such well thirty (30) days after Lessor's delivery of written notice to Lessee of Lessee's failure to pay the royalties required hereunder; provided, however, that Lessee may avoid such termination by paying to Lessor all sums (including interest) then owed by Lessee to Lessor prior to the expiration of said thirty (30) day period. For purposes of this provision, payment of disputed royalties into an escrow account or Court registry shall not constitute a payment of royalties to Lessor. If such failure to pay the royalties required hereunder relates to a dispute over the method of computation and/or value of such royalties, then Lessor, at its sole and exclusive option, may elect to submit to Lessee the results of an audit conducted pursuant to subsection (o) hereunder, and if the accuracy of such audit is verified by the signature of a registered petroleum engineer or certified public accountant retained by Lessor, Lessee hereby agrees in advance to the accuracy of such audit, which accuracy shall be conclusively presumed, and of its obligation to pay such underpayment of royalties as audited by Lessor within the time frames set forth above in order to avoid lease termination as set forth herein. Lessee acknowledges and represents to Lessor that it understands the import of this remedy to Lessor, and that it has consulted with an attorney of its own choice to review the terms hereof, and it is willing to proceed and accept those terms. Lessee stipulates and by acceptance of this lease agrees that the filing of a lawsuit seeking declaratory relief or interpleading funds with a Court will not prevent termination of this lease and, Lessee further agrees, that it will not seek or enforce any award of attorneys' fees from Lessor in any such case. Unless otherwise herein expressly provided, and whether or not Lessor shall have given notice of termination of this lease as to any well and the leased premises ascribed to such well for non-payment, any royalties or other payments provided for in this lease which are suspended and not paid to Lessor within the time periods specified therefor shall accrue interest at the maximum rate of interest permitted by applicable law, compounded daily, from the due date until paid and, in addition to any other remedies available to Lessor at law, Lessor shall have a lien and perfected security interest on Lessee's leasehold estate and all property, including oil or gas which has been produced but not yet removed from the leased premises to secure payment of all amounts due to Lessor under the terms of this lease. Acceptance by Lessor of royalties which are insufficient or past due shall not act as a waiver or estoppel of Lessor's right to exercise any remedy provided herein including the right to receive or recover any and all interest due thereon under the provisions hereof unless the written acceptance or acknowledgment by Lessor to Lessee expressly so provides.

(m) Regardless of any statutes or other law to the contrary, the execution and delivery of a division order shall never be a requirement or condition precedent to distributing actual royalties to Lessor hereunder. Further, if Lessor should elect to execute a division order related to production attributable to this lease, the terms of any such division order may serve as a basis for royalty payments only to the extent the terms of the division order are consistent with the terms of this lease. Any terms of a division order which attempt to modify the terms of this lease including, but not limited to, the basis for calculation, payment or timing of royalty payments, shall be ineffective. In lieu of any such division order, Lessor may execute and deliver to Lessee or the purchaser of oil or gas, for the purposes of paying royalties attributable to this lease, a written statement which stipulates an amount being at least the interest of Lessor. Any amendment, ratification or other modification or revival of this lease may be accomplished only by an instrument executed by Lessor and Lessee, clearly entitled as a "ratification of lease", "amendment of lease", "modification of lease" or such other title as may be appropriate to describe the intended purpose of the instrument with reference made to the lease. Similarly, any payment to Lessor of an amount which is intended as a settlement, compromise or accord and satisfaction as to any amount owed hereunder shall operate as such only if accompanied by a document which clearly and conspicuously describes the intent and purpose and which is executed by Lessor.

(n) All payments made hereunder to Lessor from the proceeds derived from the sale of oil or gas production pursuant to this lease shall include, but not be limited to, the information required by Section 91.502 of the V.T.C.A. Natural Resources Code on the check stub or on an attachment to such payments. Provided, however, if royalty payments paid hereunder are made by electronic transfer, the information required by this subsection (n) will be provided directly to Lessor at the address set out above until a different address has been designated by Lessor in writing. The

information will include, but not be limited to, the date of check, name of owner to whom payment is being made, owner identification number, property identification number, property name to include county and state, month and year of sales for which payment is being made, type of interest (WI, RI, ORR), type of product, owner's decimal interest, gross volume at property level with volume indicator, gross volume at owner's interest with volume indicator, gross sales value at property level, gross sales value at owner's interest, state production & severance taxes at property level, state production & severance taxes at owner's interest, other deductions at property level, other deductions at owner's interest, net sales value at property level (after taxes & deductions), net sales value at owner's interest (after taxes & deductions), unit price, BTU adjustment factor, and any and all other information required by the state statute referenced above or necessary in order to calculate the payment of royalties in accordance with the terms and provisions of this lease. In situations where there are deductions made from royalty payments, these deductions must be shown as a separate figure on the check and not netted in the gross value figure. In situations where there is more than one payor, and each is paying Lessor a portion of his interest under this lease, each payor will reflect the total gross volume at the property level and not their share of the gross volume. The Lessor's decimal interest will be adjusted to reflect the portion of Lessor's interest being paid by each payor. If any adjustments are made in which Lessor is due additional royalty, then such royalty will be paid with interest at the same rate and in the same manner as specified in Section 3(l) above.

(o) Lessor shall have the right at all reasonable times to audit, inspect and/or review the books, accounts, contracts, records and raw data of Lessee and any business entity owned in whole or in part by Lessee or any of its parent, subsidiary or affiliated entities, if any, as well as interpreted data, if any, pertaining to the development, production, saving, transportation, sale and marketing of the oil and gas from the leased premises. Nothing contained herein shall relieve Lessee or its affiliates of its express fiduciary obligation to market Lessor's share of production for the maximum possible price.

DELAY RENTALS; REDUCTION IN RENTALS UPON SURRENDER OF LEASE

4. (a) If operations for drilling are not commenced on the leased premises on or before one (1) year from the date of this lease, this lease shall then terminate as to both parties unless on or before said date, Lessee shall pay or tender to Lessor at the address stated hereinabove, until a different address has been designated by Lessor, the sum of _____ DOLLARS (\$ _____) per acre (herein called rental) for the number of acres then covered by this lease which shall cover the privilege of deferring commencement of drilling operations for a period of twelve (12) months. Thereafter, upon the payment or tender in like manner annually the sum of _____ DOLLARS (\$ _____) per acre (herein called Rental) for the number of acres then covered by this lease and not previously surrendered as herein provided, the commencement of drilling operations may be further deferred for successive periods of twelve (12) months each during the Primary Term. Payment or tender of rental under this Section may be made by check of Lessee, mailed or delivered to the parties entitled thereto on or before such date of payment. The cash down payment is consideration for this lease according to its terms and shall not be allocated as a mere rental for a period.

(b) Anything contained in this lease to the contrary notwithstanding, it is expressly provided that a drilling well shall not have the effect of continuing this lease in force and effect without the payment of delay rentals as provided for herein except as to a tract of forty (40) acres upon which such drilling well is situated, nor shall a well producing oil and/or gas in commercial quantities (or a shut-in well with all shut-in payments having been timely made thereon) have the effect of continuing this lease in force and effect without payment of delay rentals as provided for herein except as to the particular tract on which such producing or shut-in well is situated and the number of acres allocated to such well as provided for in Section 5 (c). Accordingly, in order to continue this lease in force and effect during the primary term as to such of the leased premises on which is not situated a drilling well or a producing well or shut-in gas well and the number of acres ascribed thereto, as herein provided, Lessee shall be required to make timely payment of delay rentals as provided for herein.

(c) Lessee may at any time or times during the primary term of this lease and subject to the requirements of Paragraph 17(a) herein, execute and deliver to Lessor a recordable release or releases covering any portion or portions of the leased premises as to all depths and

thereby surrender this lease as to such portion or portions and be relieved of delay rental obligations as to the acreage surrendered. Upon receipt by Lessor of such release or releases, rentals thereafter payable hereunder shall be reduced in the proportion that the acreage covered hereby is reduced by said release or releases.

CESSATION OF PRODUCTION; CONTINUOUS DEVELOPMENT

5. (a) If, prior to production of oil or gas on the leased premises, Lessee should drill a dry hole or holes thereon, or if, after discovery and production of oil or gas, the production thereof should cease from any cause this lease shall not terminate if Lessee commences additional drilling or reworking operations within sixty (60) days thereafter or (if it be within the Primary Term) commences or resumes the payment or tender of rentals on or before the rental paying date next ensuing after the date of completion of a dry hole or cessation of production; provided, however, if the next ensuing rental payment date is less than sixty (60) days from date of completion of a dry hole or cessation of production (herein called "Said Dates"), the rental shall be considered timely paid, for the purposes of this lease, if actually paid within sixty (60) days of either of Said Dates. If at the expiration of the Primary Term oil or gas is not being produced on the leased premises but Lessee is then engaged in drilling or reworking operations thereon, or shall have completed a dry hole thereon within sixty (60) days prior to the end of the Primary Term, the lease shall remain in force so long as the same or any additional drilling or reworking operations are prosecuted with no cessation of more than sixty (60) consecutive days, and if they result in the production of oil or gas, so long thereafter as oil or gas is produced from the leased premises; provided, however, with respect to any particular well being drilled or reworked, it shall not be considered for the purposes of this lease that Lessee is drilling or reworking the same in good faith unless operations on said well are prosecuted with diligence and without cessation of more than thirty (30) consecutive days.

(b) Anything in this lease to the contrary notwithstanding, and without any intention to negate the implied covenant to reasonably develop the leased premises but cumulative thereof, after the discovery of oil or gas on the leased premises and while the production of oil or gas is relied upon to perpetuate this lease, Lessee shall, commencing with the expiration of the Primary Term hereof, reasonably develop the acreage retained hereunder with due diligence, as due diligence is hereafter defined, and in discharging this obligation, Lessee shall be required to drill at least one (1) well per the number of acres specified in subsection (c) of this Section 5, and further, Lessee shall also drill such other wells as a reasonably prudent operator would drill under the same or similar circumstances.

(c) "Due diligence" as used in the last preceding subsection in connection with reasonable development of the leased premises shall mean that Lessee, once production is obtained, shall proceed with reasonable development as provided for above in such manner that there shall not elapse more than ninety (90) consecutive days between the completion of one well and the commencement of operations for the drilling of the next well; and in the event under the conditions herein mentioned, more than ninety (90) days elapse between the completion of one well and the commencement of operations for the drilling of another well then this lease shall terminate as to all the acreage and depths included in this lease, except as to the following described well tracts to the depths specified herein: (1) forty (40) acres around each then commercially producing oil well and (2) _____ () acres around each then commercially producing gas well. Each tract so retained shall be in as nearly the form of a square as is practicable with the well at all points being located at a legal spacing distance within its boundaries and as near the center as practicable. Notwithstanding the above, in the event governmental authority having jurisdiction should hereafter prescribe a well density of a lesser number of acres than the number of acres specified above, then Lessee may retain around each such well only such number of acres so prescribed by governmental authority or in the alternative, if after one year has elapsed for the designation of a new field discovery and field rules have not been established for such field, then 40 acres shall be the density deemed prescribed for each well, irrespective of whether such well is classified as an oil well or gas well. Furthermore, within the limited areas herein specified, Lessee may retain only from the surface down to one hundred feet (100') below the deepest perforation from which a well is producing -- this lease as to all deeper depths (subject to further requirements hereof) will terminate and revert to Lessor. Upon the later of the expiration of said primary term, or at any applicable time thereafter under the provisions of this Section 5, Lessee shall furnish to Lessor a plat and field notes of the retained acreage, together with a release in recordable form properly executed covering all of the acreage and depths which Lessee is not entitled to retain hereunder. Said plat, field notes and release

are to be furnished to Lessor within 30 days after any such termination. At anytime thereafter and subject to subsection (a) of this Section 5, whenever Lessee has discontinued production from any deeper zone(s) in a well and Lessee attempts to produce such well at a shallower zone, this lease will terminate with respect to such deeper zone(s) and such other depths that are more than 100 feet below the deepest perforation from which that well is producing. If Lessee fails, for any reason, to furnish any release or releases required by this lease within 30 calendar days of the time required, or, if Lessor has determined in good faith that this lease has terminated with respect to any part or all of the leased premises, Lessor may, at Lessor's option, prepare, execute and file an affidavit, release or other recordable instrument to effect such release, and when recorded, such affidavit, release or instrument shall have the same force and effect as if executed by Lessee. For this purpose, Lessor, in preparing, executing and filing such affidavit, release or other instrument shall be deemed to be the agent of Lessee, but under no circumstances shall Lessor ever incur any liability to Lessee for acts under taken as Lessee's agent. Reference in this and the preceding subsection of this lease to an oil well or a gas well shall be taken to mean a well classified as an oil well or a gas well, as the case may be, by the Railroad Commission of Texas or other regulatory authority having jurisdiction.

(d) Notwithstanding the provisions of the foregoing subsection as to the acreage entitled to be retained, if a gas well (originally classified as such by the Railroad Commission of Texas or other governmental authority having jurisdiction and as to which Lessee has elected, after the Primary Term expires or thereafter, to retain the maximum acreage permitted a gas well) is later reclassified by the Railroad Commission of Texas or other governmental authority having jurisdiction as an oil well, then Lessee will within thirty (30) days, release the excess acreage retained around the gas well in order that the retained acreage as to such an oil well will conform to the "oil well" formula for retained acreage as set forth above.

(e) One or more oil wells physically located on a "gas well tract" designated before or after the completion of the said oil well or wells shall not entitle Lessee to retain the additional acreage provided for an oil well or wells so physically located on a designated "gas well tract" or a "gas well tract" which Lessee has the right to designate for a gas well. It is the intention of the Parties, Lessor and Lessee, that double credit shall not be taken by Lessee for both oil and gas wells where the "drillsites" for the oil well or wells may be physically located on the same acreage included in a designated "gas well tract," but that Lessee shall be entitled to retain at the conclusion of the stipulated required development period only that acreage allotted to and included in the "gas well tract" which Lessee has earned and is entitled to retain pursuant to this Section 5.

(f) Upon termination of this lease except as to each oil well and each gas well and the number of acres hereinabove specified in subsection (c) of this Section 5 around each such well, each separate well tract shall be treated as a separate lease tract subject to the provisions of this lease, and the continuation of this lease as to each such separate lease tract shall be determined by the provisions of this lease applied to each separate lease tract as if each such separate lease tract were separately leased under the provisions hereof. It is understood and agreed that when production under each separate lease tract terminates, without production having been re-established in accordance with subsection (a) of this Section 5, Lessee or its assigns is obligated to deliver to Lessor, within thirty (30) days from such termination, a release of the acreage and depths covered by such lease tract.

(g) Upon the termination of this lease as to a part (but not all) of the acreage described herein, Lessee shall have a continuing non-exclusive easement (but only to the extent that Lessor may legally permit such an easement) across the surface and subsurface of all of the leased premises for conducting permitted operations and producing and selling oil and gas from any wells drilled under the terms of this lease, but not otherwise.

(h) A well shall be deemed to be commenced under the terms of this lease on the date the drill bit enters the earth for the actual drilling of a validly permitted well with a rig capable of drilling to the permitted depth. A well shall be deemed to be completed under the provisions of this lease (i) three days after the well reaches total depth in the event no attempt is made to complete the well as a producer of oil and/or gas by the running of production casing (a dry hole) or (ii) thirty days after the date production casing is cemented in the well (as reflected by the cementing affidavit required to be filed with the Railroad Commission of Texas) in the event an attempt is made to complete the well as a producer of oil and/or gas.

(i) Subject to the terms of Section 14, Lessee agrees to plug, upon the sooner of sixty (60) days from the date such well ceases to produce in paying quantities, or in accordance with the rules and regulations of the Railroad Commission of Texas or other governmental authority having jurisdiction, all dry holes drilled by Lessee on the leased premises and all wells which have once produced but which have ceased producing.

OFFSET WELL OBLIGATION

6. (a) Lessee shall have a duty to fully protect the property it leases from Lessor from drainage. In the event a well or wells producing oil and/or gas in paying quantities should be brought in (either before or after the date of this lease) on lands adjacent to and draining the leased premises, Lessee shall immediately act to fully protect the leased premises from drainage. In fully protecting the premises from drainage Lessee expressly agrees either (a) to drill, complete and produce such offset well or wells as may be necessary or advisable in order to offset each draining well as to all depths and horizons covered hereby in which the draining well or wells are completed, or (b) to pay to Lessor an adequate sum of compensatory royalty. For purposes of this provision, it will be presumed that any well producing in paying quantities situated 700 feet or less from any boundary line of this lease is draining the lands covered hereby; provided, however, in no way does the 700 feet distance stipulation relieve Lessee of the obligation to protect the leased premises from drainage in cases where there is an offsetting well situated greater than 700 feet and draining the leased premises. With regard to option (b) herein, an "adequate sum" of compensatory royalty is a monthly payment which is no less than the amount of royalty which would be payable hereunder to Lessor if the offsetting well requiring payment of the compensatory royalty were situated on lands covered hereby and such lands were not included in a pooled unit. Said compensatory royalty will be considered royalty within the meaning of Section 3 hereof and will serve to hold this lease in force and effect but only as to a well tract as prescribed in Section 5(c) hereof, the area of which shall be determined on the basis of the assumption that the well is the type of well completed at a legal offsetting location on the lease at the same depth as the offsetting well which requires the payment of the compensatory royalty. It shall be assumed that Lessee has agreed to pay the compensatory royalty provided for in (b) above if Lessee has not commenced drilling operations for an offsetting well on the leased premises within sixty (60) days after the date of this lease or within sixty (60) days after the commencement of actual production for market from a draining well brought in (either before or after the date of this lease) on adjacent land, whichever is later; provided, however, that compensatory royalties shall be paid on all production beginning with first runs from the draining well.

(b) The foregoing obligations are recurring obligations and will arise upon the completion of each well on adjacent land. That is to say that Lessee's obligations to offset wells on adjacent lands shall be considered to arise with each draining well completed on the adjacent land and without regard to the existence or locations of wells on the lease at the time the draining well is completed.

(c) Lessee's duty to fully protect the leased premises from drainage as required under subsections (a) and (b) of this Section 6. shall also apply to any well or wells actually drilled on the leased premises and not owned in whole or in part by Lessee, its successors or assigns.

(d) Lessee binds and obligates itself, its successors and assigns, to sell gas ratably from wells owned or controlled by it, in whole or in part, and to make nominations, requests for allowables or other designations for gas production so that Lessor shall not be drained by production from wells on tracts in the vicinity of the leased premises.

(e) At Lessor's sole option and upon Lessee providing Lessor with full information regarding the other leases covering undivided interests in the leased acreage, Lessee's obligations to either drill or pay compensatory royalty as set out under subparagraph (a) of this Section 6 may be discharged if, for a well to be drilled to offset the draining well, Lessee (1) releases all leasehold interest covered by this lease from the surface down to all depths covered by this lease at the time of the release in a well tract in the same size specified in Section 5(c) herein, and (2) assigns to Lessor all remaining undivided leasehold interest from the surface down to all depths in a well tract in the same size specified in Section 5(c) herein.

ASSIGNMENTS AND CHANGES IN OWNERSHIP

7. (a) The rights and estate of any party hereto may be assigned from time to time in whole or in part and as to any mineral or horizon, provided, however, that, due to the special relationship of trust and confidence between Lessor and Lessee, any assignment, mortgage or other transfer of all or any interest in this Lease by Lessee without the prior written consent of Lessor, which may be withheld for any reason (or for no reason) at Lessor's sole discretion and option, shall be void, and any such unpermitted assignment of this Lease by the Lessee shall terminate this Lease, at Lessor's option. As an express condition to such approval as may be granted by Lessor, Lessee shall furnish to Lessor a true or certified copy of all such assignments and fully inform Lessor of the identity and address of any such assignee. The provisions of this Section 7 shall be applicable to any type of assignment, sublease, conveyance or transfer of all or a portion of this Lease or rights or interest thereunder. All of the covenants, obligations, and considerations of this Lease shall extend to and be binding upon the parties hereto, their respective permitted successors-in-title and assigns.

(b) No change or division in ownership by Lessor of the leased premises, rentals or royalties, however accomplished, shall operate to enlarge the obligations or diminish the rights of Lessee; and no change or division in such ownership shall be binding upon Lessee until thirty (30) days after Lessee shall have been furnished by certified United States mail at Lessee's principal place of business with a copy of recorded instrument or instruments evidencing same.

WARRANTY; LIENS

8. (a) This lease is executed without warranty of title, either express or implied. However, if Lessor owns an interest in the oil and gas in or under the leased premises less than the entire mineral fee estate, then the royalties and rentals to be paid Lessor shall be reduced proportionately as may be required by such lesser ownership. Failure of Lessee to reduce rental payable hereunder shall not impair the right of Lessee to reduce royalties. Lessor agrees that Lessee, at its option, may discharge any tax, mortgage or other lien upon the leased premises (the basis of which lien is any obligation of Lessor), and in the event Lessee does so, it shall be subrogated to such lien with the right to enforce same and apply rental and royalties accruing hereunder toward satisfying same. In the event of failure of Lessor's title, in whole or in part, Lessor's sole obligation shall be the return to Lessee of that portion of the bonus paid Lessor for the execution of this lease attributable to the acreage affected by such failure.

(b) The fiduciary representative of each party Lessor herein shall never, under any circumstances, incur any liability whatsoever to Lessee or a successor or assign of Lessee in his or her individual capacity.

(c) Lessee may not purchase or lease the rights of any party claiming any interest in conflict with Lessor's interest in the leased premises without the prior written consent of Lessor and any attempt by Lessee so to do, directly or indirectly, shall be construed as a breach of Lessee's obligations hereunder, constituting grounds for immediate default and cancellation of this lease. This provision shall apply only to the interest in the leased premises which are in conflict with the interest claimed by Lessor herein and shall not apply to undivided interest claimed and owned by other parties which are not in conflict with the interest claimed by Lessor herein.

TITLE EXAMINATION; ABSTRACTS OF TITLE

9. (a) It is understood and agreed that Lessor shall, upon the request of Lessee, furnish to Lessee such abstracts of title as Lessor presently has in its possession, for use by Lessee in examination of title, but the use of Lessor's abstracts for examination shall be confined to Lessor's offices during normal business hours. It is understood and provided, however, that Lessor shall not be liable for the correctness or accuracy of any such abstracts so provided to Lessee for examination. The cost and expense of any supplemental abstracts thereto necessary to reflect the title to the leased premises covered hereby, and the expense, if any, of the curative matter necessary to cure or correct defects in title prior to the date of this lease, shall be borne solely by Lessee. Lessee agrees to promptly furnish Lessor with a copy of any supplemental abstracts prepared covering the leased premises.

(b) If Lessee obtains a title opinion or opinions covering all or any part of the leased premises, Lessee shall furnish copies thereof to Lessor within ten (10) days after receipt of same.

ENVIRONMENTAL PROVISIONS; SURFACE OWNERSHIP

10. (a) Lessee shall install and maintain all equipment and conduct all operations in an environmentally sound manner, in accordance with all applicable regulations of the Railroad Commission of Texas, the Texas Natural Resources Conservation Commission, the Environmental Protection Agency and any other governmental authorities. Lessee shall not use, store or dispose of any hazardous materials on the leased premises, except to the extent such substances are contemporaneously required for actual oil or gas operations on the leased premises and any such substances shall be used, stored and disposed of in a safe manner, in compliance with all applicable governmental regulations. Lessee shall insure that all contractors comply with the terms of this subsection. In the event Lessee is notified of any environmentally harmful or dangerous conditions on the leased premises resulting from Lessee's operations, Lessee shall promptly take all actions required to clean up and correct such dangerous or harmful conditions, in accordance with applicable law and regulations and sound engineering practices. Lessor shall have no responsibility to inspect or oversee Lessee's operations or to identify or correct any potentially harmful, dangerous or damaging conditions, and Lessor shall have no right to control any details of Lessee's operations, nor to designate or control Lessee's contractors. Neither Lessee nor any contractors shall have any right of contribution or indemnity whether statutory or otherwise from Lessor for any matters relating to operations on the leased premises or conditions on the leased premises, regardless of whether such matters arise from Lessor's negligence. LESSEE INDEMNIFIES AND HOLDS LESSOR HARMLESS FROM ANY AND ALL COSTS, EXPENSES AND LIABILITIES INCLUDING LITIGATION COSTS AND ATTORNEYS' FEES LESSOR MIGHT INCUR RELATING TO ANY HARMFUL, DAMAGING OR DANGEROUS CONDITIONS CONNECTED WITH OPERATIONS HEREUNDER, REGARDLESS OF WHETHER SUCH MATTERS ARISE FROM LESSOR'S NEGLIGENCE. By commencing any such operations, Lessee shall acknowledge its consent to the terms of this Subsection. In the event any claim is made against Lessor based upon an alleged breach of this provision, upon request by Lessor, Lessee shall post a bond for the amount of the alleged damage, such bond to be maintained at Lessee's expense for the benefit of Lessor until such claim is fully resolved.

(b) This lease is expressly made giving due regard to the rights of the owner of the surface estate. Unless specifically set forth herein, the terms and provisions of this lease shall not affect those rights. Lessee herein agrees to indemnify and save harmless Lessor herein from any claims asserted against, or damages to the surface estate committed by Lessee hereunder, or Lessee's successors or assigns. Lessee further agrees to reimburse the owner of the surface estate for all damages done thereto and if requested, to furnish Lessor proof of the payment of such damages.

(c) The provisions of this Section 10 are specifically applicable not only to Lessee but also to Lessee's successors and assigns, and no assignment of this lease shall relieve Lessee of the obligations of Lessee under this section all of which Lessee assumes by the acceptance of this lease.

INFORMATION TO LESSOR

11. (a) Lessor shall at all times be entitled to full information covering all of Lessee's and/or its assign's operations on the leased premises, as well as any operations on adjoining tracts or within one-half (1/2) mile of the boundaries of the leased premises, whichever is greater, in which Lessee or its assigns has an interest. To this end, Lessor, through its representative or representatives duly designated from time to time in writing, shall have free access to all operations conducted by Lessee and/or its assigns upon the leased premises and, at all reasonable times, to all of Lessee's and/or its assign's records and data pertaining thereto. Further, Lessee shall furnish Lessor, pertaining to all wells drilled, re-entered, reworked or recompleted hereon, as well as on adjoining tracts or within one-half (1/2) mile of the boundaries of the leased premises, whichever is greater, in which Lessee or its assigns has an interest, the following: (i) notice of at least thirty-six (36) hours prior to commencement of drilling or reworking operations and notice of at least twenty-four (24) hours prior to the estimated time of logging, coring, or testing, (ii) during the drilling, reworking, completion or recompletion, and testing operations of any well, copies of any daily reports reflecting the operations being conducted, such records to be furnished to Lessor on a daily basis as they become available to Lessee, (iii) if requested in writing and within five (5) days following such request (and thereafter, concurrently with submission of such reports by Lessee to such governmental agency), copies of all reports and/or forms filed with the Railroad Commission of Texas or other

governmental agency having jurisdiction in connection with such operations, examples of such reports and/or forms include but are not limited to: Form W-1 and plat, Water Board letter, approved drilling permit, Form G-1, Form G-5, Form W-2, Form L-1, Form W-12, Form W-15, Form G-10, Form W-10, Form P-1, Form P-2, Form P-4, Form P-12, Form P-15, (iv) copies of all mud logs, open-hole logs, formation tests, drillstem tests, core analyses, or other types of formation analyses (including intermediate and composite log runs and tests) run in any such well, (v) copies of all records of any completion or recompletion operations, including copies of any cased-hole logs run, wireline surveys, perforation records, stimulation treatments, (vi) copies of all records of testing operations, including copies of all reservoir studies performed including but not limited to pressure buildups, pressure draw downs, and reservoir limits testing in any formation.

(b) If Lessee and/or Lessee's assigns acquires, has acquired, conducted or will conduct, participate in or underwrite any geophysical surveys on any part of the leased premises, then Lessee will furnish free of cost to Lessor all seismic data and associated survey information, including but not limited to, the following:

- (1) A surveyed ownership map and topographic map, in duplicate, illustrating all source and receiver locations of the entire seismic survey along with DOS compatible 3-1/2 inch diskette containing elevations and respective X Y coordinates for each source and receiver location in SEG P1 format. All source and receiver location surveyed points that are established with GPS shall be identified on the ownership maps, topographic maps, and SEG P1 files described herein.
- (2) For 3-D seismic surveys only, a surveyed ownership map and topographic map, in duplicate, illustrating all cell center locations of the entire 3-D seismic survey along with a DOS compatible 3-1/2 inch diskette containing elevations and X Y coordinates for each cell center location in SEG P1 format. All cell center location surveyed points that are established with GPS shall be identified on the ownership maps, topographic maps, and SEG P1 files described herein.
- (3) For 3-D seismic surveys only, all information related to well locations which fall within the entire 3-D seismic survey, including but not limited to, X Y coordinates. For either 2-D or 3-D seismic surveys, all well location information that is established with GPS shall be identified on the ownership maps, topographic maps, and SEG P1 files described herein.
- (4) For 3-D seismic surveys only, a fold Plot for the entire seismic survey, in duplicate, with sufficient survey information to determine the position of the leased premises on the plot.
- (5) For 2-D seismic surveys only, a linear graph of the fold for the entire seismic survey, in duplicate.
- (6) Copies of Observers Reports for the entire seismic survey.
- (7) For 2-D seismic surveys, a copy of the full fold data in Seg Y digital format and paperprint (or whatever data acquired if not full fold) through final processing, to include all processed versions, including but not limited to, pre-stack and post-stack, time and/or depth migrations and AVO, if produced, across the leased premises plus one-half (1/2) mile in all directions from the boundary lines of the leased premises. For 3-D seismic surveys, a copy of the full fold 3-D data volume (or whatever data acquired if not full fold) through final processing, to include all processed versions, including but not limited to, pre-stack and post-stack, time and/or depth migrations, AVO and coherency cube, if produced, across the leased premises plus one-half (1/2) mile in all directions from the boundary lines of the leased premises. Said data will be supplied on the medium and format requested by Lessor along with a header description and data loading sheet.

- (8) Any preliminary and/or reprocessed versions of the data.
- (9) Copies of the original field tapes and related information sufficient to allow Lessor to have the data reprocessed. Said copies will include a sufficient amount of data to enable the reprocessing of full fold data across the leased premises plus one-half (½) mile in all directions from the boundary lines of the leased premises. Said copies of the original field tapes will be supplied on the medium and format requested by Lessor.
- (10) Copies of all velocity surveys, check shot surveys, synthetic seismic traces derived from sonic logs and vertical seismic profiles (VSP surveys) conducted on the leased premises plus one-half (½) mile in all directions from the boundary lines of the leased premises.

Notwithstanding anything contained herein to the contrary, it is agreed that Lessee shall furnish Lessor the data required hereunder in a manner which conforms to industry standards to allow Lessor to load and work the data on a computer workstation. If the data is unloadable on the workstation utilized by Lessor, said data will be corrected or amended by Lessee immediately. Lessee and/or Lessee's assigns agree that any contract entered into with third parties (including the granting of a seismic permit) pertaining to geophysical surveys to be conducted on the leased premises will be made subject to the terms of this lease, including but not limited to, the furnishing of data to Lessor as outlined under this Section 11(b). In addition, if Lessee and/or Lessee's assigns conduct or participate in any geophysical surveys on the leased premises after the date of this lease, Lessee and/or Lessee's assigns agree that in no event shall any type of explosion or impulse from any such geophysical surveys be created nearer than one thousand feet (1,000') of any oil and gas installations or drilling, shut-in or producing wells and/or flow lines without the express written consent of Lessor.

(c) In the event Lessee makes application to the Texas Railroad Commission or is given notice of an application filed by another operator to the Railroad Commission, or other regulatory agency for regulatory relief relating to or affecting production from or exploration or development of the lands covered by this lease or any part thereof, Lessee shall immediately provide Lessor notice of such application together with full information regarding the application, the nature of the relief requested and the factual information supporting (or controverting) the position of Lessee. Lessee shall not object to and will (if requested) urge the regulatory body to afford Lessor party status in any such proceeding. Regardless of whether Lessor is afforded party status Lessee shall, on request, provide Lessor copies of all matters filed or served upon Lessee in any such proceeding concurrently with Lessee's filing or receipt of same.

(d) In addition to the foregoing information to be furnished to Lessor, Lessee covenants and agrees to notify Lessor whenever a well which has been drilled on the leased premises is plugged and abandoned, whether the same was a producing well or a dry hole, and to include with the notification a copy of the plugging report furnished the Railroad Commission of Texas.

(e) As a part of the consideration for this lease, Lessee agrees to run a mud log and an induction electric log from the bottom of the surface casing to the total depth of each well drilled hereon; to run gamma ray type logs and neutron-density porosity type logs of all prospective zones; to take sidewall cores and formation fluid tests; and to evaluate all indications of the possible presence of oil or gas. In addition, Lessee agrees to furnish sufficient notice to Lessor of all coring, testing and logging so that Lessor or a representative of Lessor may be present for the operation involved.

(f) Lessee shall furnish to Lessor copies of all contracts and agreements pertaining to the sale or disposition of production of oil and/or gas from the leased premises.

(g) All of the information described in subsections 11.(a) through (f) above is referred to herein as "information to Lessor." Information to Lessor shall be provided to Lessor as soon as it is available to Lessee by the most expeditious means possible. For example, but without limitation, all reports, such as drilling, completion, testing, re-working, Railroad Commission, logs, and other reports should be delivered immediately by facsimile or other instantaneous transfer. As for any information to Lessor which was in existence prior to the execution of this lease, for

example, but not by way of limitation, geophysical surveys and related seismic data described in subsection (b) above, this information to Lessor shall be provided upon delivery of the executed lease.

(h) Further, Lessee specifically agrees that upon the expiration of the Primary Term, and annually thereafter on the anniversary date of this lease, to furnish to Lessor a summary report covering a period of twelve (12) months ending with the date of the report, which said report shall include the following:

- (1) Lease number assigned by the Railroad Commission of Texas.
- (2) On the reporting date, the number of producing wells and their well number(s) or well designation(s).
- (3) On the reporting date, the number of wells not producing but not plugged, and their number(s) or designation(s).
- (4) The number of wells that were plugged during the previous twelve (12) months, and their well number(s) or well designation(s).

MINIMUM ROYALTY

12. (a) Whether a well has been drilled on the leased premises or not, Lessee shall, during each anniversary year of this lease (each twelve month period calculated from the date of this lease) during which period all payments by Lessee to Lessor as royalty or rental do not equal the sum of _____ DOLLARS (\$_____) per acre during the Primary Term of this lease and _____ DOLLARS (\$_____) per acre after the expiration of the Primary Term of this lease for each acre held under this lease by Lessee as of the beginning of any such anniversary year, pay to Lessor as and for Minimum Royalty a sum in dollars equal to the difference between the sums actually paid by Lessee to Lessor as either royalty or rental and the minimum amount stipulated above, any such sum to be due and owing within sixty (60) days following the end of any such anniversary year. Lessee shall accompany the payment of any additional sums so owing and that may be due with accounting certified as correct by Lessee, an officer of Lessee or the comptroller of Lessee, setting forth the total sum actually paid by Lessee to Lessor during the anniversary year in question and any sum that may be due to Lessor as and for the Minimum Royalty under the formula set forth above. Any such payment by Lessee to Lessor may be paid by Lessee under the same procedures as govern the payment of delay rentals as provided for under Section 4 of this lease. Once production is obtained and at the anniversary date of this lease each year, Lessee shall render an accounting to Lessor setting forth just what payments were made, of whatever kind, to Lessor under this lease.

(b) If Lessee fails to make and render to Lessor the accounting accompanied by any required payment of the balance due on the Minimum Royalty stipulated in the provision of this Section 12 within sixty (60) days following the close of any such anniversary year then Lessor, upon notice to Lessee in writing sent by certified United States mail with postage prepaid to Lessee's last known address filed with the Lessor or set forth in this lease, may elect to cancel this lease if said requirements as to accounting and payment of any additional sum as Minimum Royalty as may be required are not made within thirty (30) days after the receipt by Lessee of such notice in the United States mails as aforesaid.

FORCE MAJEURE

13. The covenants and agreements herein expressed or implied in this agreement shall be subject to all valid Federal and State laws, executive orders, rules or regulations, and this lease shall not be terminated, in whole or in part, nor Lessee held liable in damages for failure to comply therewith if compliance is prevented by, or if such failure is the result of such law, order, rule or regulation. And if after the Primary Term from such cause, Lessee is prevented from conducting drilling or reworking operations on or producing oil or gas from the leased premises, the time while Lessee is so prevented shall not be counted against Lessee, and this lease shall be extended for a period of time equal to that during which such Lessee is so prevented from conducting such drilling or reworking operations on, or producing oil or gas from such leased premises notwithstanding any other provision thereof. Lessee shall within a reasonable time (not to exceed thirty (30) days) after

receiving notice of any such Federal or State law, executive order, rule or regulation, contemplated under this Section 13, notify Lessor thereof and advise Lessor of the effect of such upon this lease. Provided, however, the provisions of this Section 13, shall in no way abridge the right of Lessor to receive or relieve Lessee of the obligation to pay the minimum sums per net mineral acres described and provided for in Section 12 above or in anyway affect Lessee's obligation to make any monetary payments timely to Lessor as required by the terms and provisions of this lease.

WELL TAKEOVER UPON ABANDONMENT

14. If at any time Lessee elects to abandon any well drilled on the leased premises as a dry hole or as uneconomic after commercial production has been obtained, Lessee shall give notice of that fact to Lessor. Within thirty (30) days, or if there is a drilling rig on location, within forty-eight (48) hours (excluding Saturdays, Sundays and legal holidays), after receipt of such notice, Lessor shall have the right to take over any such well for additional testing by any method at Lessor's sole cost and expense. Lessee shall also, immediately upon request, provide Lessor copies of all other leases or agreements relating to operations on the leased premises. After such testing if Lessor elects to have the well plugged and abandoned, the well shall be returned to Lessee or the operator thereof, but Lessor shall be responsible for any excess costs of plugging and abandoning caused by such testing operations. If Lessor elects to take over operation of the well, Lessee agrees to assign all working interest in the well and its allocated acres (including this lease as well as all of the other leases on the remaining mineral interests under the leased premises) surrounding same to Lessor upon such form of assignment as may be reasonably requested by Lessor. If Lessor requests an assignment from Lessee as herein set forth, Lessor agrees to pay Lessee a mutually agreeable sum for any long string casing and/or other equipment in the well, said sum to be arrived at by considering both the value of salvageable casing and other equipment and the estimated cost of plugging and abandoning the well.

NOTICE CLAUSE

15. Lessee agrees to designate in writing, mailed or delivered to Lessor, or give notice in person to Lessor, of the person or persons to be present from time to time on said premises as current operations are being conducted with whom Lessor may contact directly concerning Lessee's operations or other activity on the said premises. All notices required to be given under the terms of this lease shall be given to the following persons who are designated Lessor's and Lessee's respective agents:

TO LESSOR:

Coates Energy Trust
P. O. Box 171717
San Antonio, Texas 78217-1017
Telephone (210) 820-0113
Facsimile (210) 820-0160

Attention: Mr. Barry C. Roberts
Office (210) 820-0113
Home (210) 826-3103

TO LESSEE:

(Insert Name, Address & Telephone Number)

In regard to notice of surface use or damages, the surface owner affected by such operations shall be entitled to prior notice of such operations. Either party hereto may from time to time designate in writing a different address or agent for the giving of any notice hereunder.

INDEMNITY

16. LESSEE AGREES TO INDEMNIFY, PROTECT AND HOLD LESSOR (AND SURFACE OWNER, IF DIFFERENT FROM LESSOR) HARMLESS OF AND FROM ANY AND ALL CLAIMS, DEMANDS, COSTS, (INCLUDING BUT NOT LIMITED TO REASONABLE ATTORNEY'S FEES) EXPENSES, DAMAGES, LOSSES AND CAUSES OF ACTION OR SUITS FOR DAMAGES ARISING OUT OF INJURY TO PERSONS (INCLUDING DEATH) AND INJURY OR DAMAGE TO OR LOSS OF ANY PROPERTY OR IMPROVEMENTS CAUSED

BY LESSEE, ITS AGENTS, EMPLOYEES, SERVANTS, CONTRACTORS OR ANY PERSON ACTING UNDER ITS DIRECTION OR CONTRACT. Further, neither Lessor nor surface owner shall ever be liable for any claims, demands, costs, expenses, damages, losses and causes of action or suits for damages because of injury to persons or property arising out of acts or omissions of Lessee, its agents, employees, servants, contractors, or any person acting under its direction and control on the leased premises.

RELEASE OF LEASE

17. (a) Lessee, provided it is not then in breach of any obligation arising under the terms hereof, may at any time or from time to time execute in recordable form and deliver to Lessor a release or releases of the lease as to all or any part of the lands or strata covered thereby; and, upon Lessor's receipt of such release(s) Lessee shall thereafter be relieved from further responsibility as regards the released acreage and intervals. It is understood and agreed by Lessee, however, that it may not release the lease if it is in breach of any of the terms thereof or if it would thereby avoid any affirmative obligations arising under the terms of the lease relating to events and circumstances occurring prior to the date of the tendered release; and in such event any attempted release of the lease shall be ineffective. That is to say, if circumstances exist at the time of the tendered release which would require Lessee to provide information, drill an offset well or wells, pay compensatory or minimum royalties, abate or remove pollutants, or take some other action to protect the rights or interests of Lessor, Lessee shall be relieved of responsibility for such obligation only upon an express release by Lessor or upon its full satisfaction of all of the obligations imposed by this lease.

(b) In the event this lease terminates at the end of the primary term with no drilling having been commenced, or if during the primary term such lease terminates due to the non-payment of delay rental, Lessee or its assigns is obligated to deliver to Lessor, within thirty (30) days from such termination, a release of this lease as to all of the acreage and depths covered hereby.

(c) If Lessee fails, for any reason, to furnish any release or releases required by this lease within 30 calendar days of the time required, or, if Lessor has determined in good faith that this lease has terminated with respect to any part or all of the leased premises, Lessor may, at Lessor's option, prepare, execute and file an affidavit, release or other recordable instrument to effect such release, and when recorded, such affidavit, release or instrument shall have the same force and effect as if executed by Lessee. For this purpose, Lessor, in preparing, executing and filing such affidavit, release or other instrument shall be deemed to be the agent of Lessee, but under no circumstances shall Lessor ever incur any liability to Lessee for acts under taken as Lessee's agent.

MISCELLANEOUS

18. (a) Lessee agrees to measure accurately, on the premises, all gas produced from each well on said land separately, by means of an orifice meter of standard make and design commonly accepted in the industry to be installed in such a manner that Lessor may install and operate a similar meter as a check meter downstream from Lessee's meter. Lessee binds and obligates itself to furnish Lessor promptly upon request with copies of its meter readings on a monthly basis and to cooperate fully with Lessor in providing Lessor, its successors and assigns, all the information and access required under all of the terms and provisions of this lease. In making all gas accounting calculations affecting Lessor's gas royalty, it is recognized and agreed that the maximum pressure base to be used in measuring gas produced under the terms of this lease shall be 14.65 pounds per square inch absolute; that the standard base temperature shall be sixty (60) degrees fahrenheit, correction to be made for pressure according to Boyle's Law, and for specific gravity according to tests made by the Balance Method, or by the most approved method of measuring and testing in use by the industry at that time; that all gas shall be measured and accounted for before the same leaves the lease in accordance with the complete provisions of Gas Measurement Committee Report No. 3 of the American Gas Association, as revised and reprinted September, 1984, together with any subsequent amendments or revisions; that gross heating value of the gas for all royalty accounting shall be calculated according to the technical standards currently recommended by the Gas Processors Association on a dry gas basis; and gas chromatograph tests on well meters shall be made at least semi-annually and tests on all sales meters shall be made at least monthly utilizing standard methods in general use by the gas industry.

(b) Lessee shall have the right at any time during or within three (3) months after the expiration of this lease to remove all property and fixtures placed by Lessee on the leased premises, including the right to draw and remove all casing. When required by Lessor, Lessee will bury all pipelines below ordinary plow depth and no well shall be drilled within two hundred (200) feet of any residence or barn now on the leased premises without Lessor's consent.

(c) None of the covenants contained in this lease shall negate or in any way limit or serve in lieu of any implied covenant for the benefit of or otherwise available to Lessor, including, without limitation, the implied covenants to market, develop, protect against drainage, and manage and administer the lease; and nothing contained herein shall relieve Lessee or its affiliates of its express fiduciary obligation to market Lessor's share of production for the maximum possible price.

(d) Due to the difficulty in ascertaining damages for Lessee's breach, default or non-performance (collectively herein called "Default") of any covenant and/or obligation contained in this lease, the parties hereto agree that in the event of Lessee's Default, then Lessor may, in addition to its other remedies available at law or in equity, at Lessor's sole option immediately (i) terminate this lease, (ii) terminate this lease and collect from Lessee all monies due hereunder or (iii) collect from Lessee all monies due hereunder. Provided, however, if Lessor chooses to terminate the lease, Lessee shall continue to remain additionally liable for any damages which accrued prior to such lease termination; and further provided that, in the event of lease termination hereunder, if Lessee fails to vacate the leased premises, Lessee shall conclusively be presumed to be a trespasser in bad faith under applicable law. This provision shall not affect any other provision of this lease whereby lease termination is automatic by operation of law, including but not limited to the automatic termination of this lease due to the failure to timely pay delay rentals, drill, or conduct operations as herein provided.

(e) Texas law shall govern any actions brought with respect to this lease or relating thereto, and venue for any suit brought hereunder shall be in either Bexar County, Texas or the county in which the leased premises is located, such county to be chosen exclusively by Lessor. The applicable Texas statutes of limitation shall govern the filing of suits brought hereunder, however, all causes of action relating to, or arising out of this lease shall be tolled during the existence of this lease.

(f) If Lessor shall bring any legal proceeding to enforce any term or provision of this lease and shall be adjudged any substantial relief hereunder, Lessee shall be liable for Lessor's attorneys' fees in any such proceeding in a reasonable amount to be fixed by the court in which such action is brought and maintained.

(g) Lessee is under a duty and obligation to protect the interest and rights of Lessor before state, as well as federal, administrative authorities and agencies such as the Railroad Commission of Texas, the Federal Energy Regulatory Commission and any state or federal courts. Lessee's duty, in this regard, shall be the duty of a reasonable and prudent operator, dealing with its own, as well as Lessor's interests in mind. Notwithstanding such implied and expressed duty, Lessee and Lessor agree that Lessor or Lessor's representative shall have the concurrent rights and privileges with Lessee to pursue and/or defend against proceedings before any administrative agency without the joinder or consent of Lessee, but Lessor agrees to give Lessee prior notice of Lessor's purposes in seeking administrative relief, and Lessor agrees to first attempt to reconcile any such differences with Lessee prior to any hearings or proceedings, and Lessee agrees that Lessor shall have standing to pursue or defend any matter before such administrative agency. Nothing herein shall in any way be construed to diminish Lessee's implied duties and obligations to protect and preserve Lessor's rights before administrative agencies, but shall be supplemental of such duties.

(h) In light of the Lessee's greater access to information regarding the operations contemplated under this lease, Lessee shall treat Lessor fairly and with utmost good faith with respect to all matters arising under this lease. Further, Lessee hereby agrees to monitor the Deed and/or Official Public Records and the records of the Railroad Commission of Texas, or other governmental agency having jurisdiction, for information which may affect Lessor's interest in the lands covered hereby and to notify Lessor of any such information.

(i) Lessee agrees to notify Lessor immediately upon its discovery of any third party or parties who damage or threaten to damage the leasehold covered hereby. In addition, Lessee

agrees to seek administrative relief against such third party or parties and pursue litigation if necessary, for itself and on behalf of the Lessor, free of any costs to the Lessor. If Lessee seeks and either receives or is awarded damages, whether through settlement or litigation, Lessee shall tender Lessor's proportionate share to Lessor immediately upon receipt of any such damages.

(j) It is specifically provided, understood and agreed to by Lessor and Lessee that in the event Lessee, its successors or assigns shall extend more favorable terms to any party owning an interest in the mineral estate in said lands, or on lands contiguous thereto or within one (1) mile, whichever is greater, than those received by Lessor herein, then the bonus consideration per acre paid to Lessor in consideration of the granting of this lease, and/or the royalty fraction provided for herein, shall be increased by such an amount as to equal the highest bonus consideration and/or greatest royalty fraction (including any overriding royalty interest) extended to any other owner. Lessee shall promptly notify Lessor of any such occurrence and shall, within forty-five (45) days of the execution of any other lease for which it has tendered a higher bonus per net acre or which provides for a greater royalty fraction (including any overriding royalty interest), tender its check or draft to Lessor for such additional consideration as may be due or deliver to Lessor an amendment of lease providing for the increased royalty. It is agreed that Lessee's failure to timely tender such sums or lease amendment shall entitle Lessor to be paid liquidated damages by Lessee in the amount of \$10,000.00 plus attorney's fees in the event it is necessary to retain the services of an attorney for the collection of such liquidated damages in addition to compliance with this provision.

(k) No presumptions relative to the control of drafting of this lease shall apply against Lessor because both Lessor and Lessee have had the benefit of consultation with counsel of their own choosing and the right to negotiate this lease and they have negotiated and accepted these lease terms of their own free will.

(l) Time is of the essence of this lease and every provision hereof.

(m) This lease shall inure to the benefit of and be binding upon Lessor and Lessee, their respective heirs, permitted successors-in-title and assigns, where assignment by Lessee has been permitted and consented to by Lessor.

IN WITNESS WHEREOF, this instrument was executed on the day first above written.

COATES ENERGY TRUST and _____

By: _____
Barry Coates Roberts, Trustee

By: _____
George L. Stieren, Trustee

LESSOR

(LESSEE'S NAME)

By: _____

LESSEE

STATE OF TEXAS §
 §
COUNTY OF BEXAR §

 This instrument was acknowledged before me on the _____ day of _____,
1999, by BARRY COATES ROBERTS and GEORGE L. STIEREN, as Trustees of COATES
ENERGY TRUST and _____.

Notary Public, State of Texas

My Commission Expires:_____

Typed or printed name of Notary

STATE OF TEXAS §
 §
COUNTY OF _____ §

 This instrument was acknowledged before me on the _____ day of _____,
1999, by _____.

Notary Public, State of Texas

My Commission Expires:_____

Typed or printed name of Notary