

LEONARD RESOURCE INVESTMENT CORPORATION

**P. O. BOX 3422
MIDLAND, TEXAS 79702**

OIL AND GAS INVESTMENTS

(915) 682-3712 OFFICE
(915) 682-8652 FAX

June 26, 2000

Coates Energy Trust
P.O. Box 171717
San Antonio, Texas 78217

Attn: Ms. Sherrie Green
Land Manager

RE: Oil & Gas Lease Proposal
Township 20 South, Range 38 East
Section 2: Lots 3, 4 and S/2 NW/4
Lea County, New Mexico

Gentlemen:

Beginning in June of 1999, through Mr. Glen Farmer here in Midland, we entered into lengthy negotiations with Sherrie Green for an oil and gas lease covering the undivided one-quarter (1/4) mineral interest owned by the Coates Energy Trust, et al, in the captioned 160 acre tract of land.

Under cover letter dated January 13, 2000, Ms. Green provided us with a counter proposal and a copy of the Coates lease form for review. After careful consideration of both the counter proposal and your lease form, we are unable to accept either.

The trade involves too much money and royalty burden for a two-year term with 90 day continuous development, particularly in a stratigraphic play where every 40 acre location seems to be a wildcat, daily production rates are low and payouts are lengthy. The Coates lease form would require an immense amount of administration to ensure compliance with provisions such as No. 3, Royalties. We are a small independent company administering a very complex surface and mineral ownership for a reasonably aggressive drilling and development program in this area, and simply do not have the staff necessary to administer the type of lease you propose.

We do have a majority of the minerals under the NW/4 of Section 2 under lease, and would like to acquire a lease covering the Coates' undivided 1/4 interest. We would be willing

Wrote 7/17/2000

to pay \$250.00 per acre for a 30 month paid-up lease bearing a 25% royalty, but using the more typical form of lease we enclose for your review.

If those terms and the form of lease we propose are unacceptable, then we will be happy to submit an AFE for your consideration once we are ready to drill on your acreage, so that you may join with your 25% interest in drilling a proposed test well.

We look forward to hearing from you.

Very truly yours,

LEONARD RESOURCE INVESTMENT
CORPORATION

A handwritten signature in black ink, appearing to read "Dan M. Leonard", with a stylized flourish at the end.

Dan M. Leonard, President

DML/cel
Enclosures

OIL & GAS LEASE

THIS AGREEMENT, made this _____ day of _____, 2000, between **Coates Energy Trust**, herein called Lessor (whether one or more) and **Leonard Resource Investment Corporation** of P. O. Box 3422, Midland, Texas 79702, Lessee.

1. Lessor, in consideration of Ten and Other Dollars in hand paid, receipt of which is hereby acknowledged, and of the agreements of the lessee herein contained, hereby grants, leases and lets exclusively unto Lessee for the purpose of investigating, exploring, prospecting, drilling and operating for and producing oil and gas, injecting gas, waters, other fluids, and air into subsurface strats, laying pipe lines, storing oil, building tanks, roadways, telephone lines and other structures and things thereon to produce, save, take care of, treat, process, store and transport said minerals, the following described land in Lea County, New Mexico, hereinafter referred to as "said land" or "the land", to-wit:

Township 20 South, Range 38 East
Section 2: Lots 3, 4 and S/2 NW/4

Said land is estimated to comprise 160 acres, whether it actually comprises more or less.

2. Subject to the other provisions herein contained, this lease shall remain in force for a term of thirty (30) months from this date, (called "primary term") and as long thereafter as oil or gas is produced from said land or from land with which said land is pooled.

3. The royalties to be paid by Lessee are: a) on oil, and other liquid hydrocarbons saved at the well, 1/4th of that produced and saved from said land, same to be delivered at the wells or to the credit of Lessor in the pipeline to which the wells may be connected; b) on gas, casinghead gas or other gaseous substance produced from said land and used off the premises or used in the manufacture of gasoline or other products, the market value at the well of 1/4th of the gas used, provided that on gas sold on or off the premises, the royalties shall be 1/4th of the amount realized from such sale; c) and at any time when this lease is not validated by other provisions hereof and there is a gas and/or condensate well on said land, or land pooled therewith, but gas or condensate is not being sold or used and such well is shut-in, either before or after production therefrom then on or before 90 days after said well is shut-in, and thereafter at annual intervals, Lessee may pay or tender an advance shut-in royalty equal to \$1.00 per net acre of Lessor's gas acreage then held under this lease by the party making such payment or tender, and so long as shut-in royalty is paid or tendered, this lease shall not terminate and it shall be considered under all clauses hereof that gas is being produced from the leased premises in paying quantities. Each payment shall be paid or tendered to the party or parties who at the time of such payment would be entitled to receive the royalties which would be paid under this lease if the well were in fact producing. The payment or tender of royalties and shut-in royalties may be made by check or draft. Any timely payment or tender of shut-in royalty which is made in a bona fide attempt to make proper payment, but which is erroneous in whole or in part as to parties or amounts, shall nevertheless be sufficient to prevent termination of this lease in the same manner as though a proper payment had been made if Lessee shall correct such error within thirty (30) days after Lessee has received written notice thereof by certified mail from the party or parties entitled to receive payment together with such written instruments (or certified copies thereof) as are necessary to enable Lessee to make proper payment. The amount realized from the sale of gas on or off the premises shall be the price established by the gas sales contract entered into in good faith by Lessee and gas purchaser for such term and under such conditions as are customary in the industry. "Price" shall mean the net amount received by Lessee after giving effect to applicable regulatory orders and after application of any applicable price adjustments specified in such contract or regulatory orders. In the event Lessee compresses, treats, purifies, or dehydrates such gas (whether on or off the leased premises) or transports gas off the leased premises, Lessee in computing royalty hereunder may deduct from such price a reasonable charge for each of the functions performed.

4. This is a paid-up lease and Lessee shall not be obligated during the primary term hereof to commence any operations of whatsoever character or to make any payments hereunder in order to maintain this lease in force during the primary term; however, this provision is not intended to relieve Lessee of the obligation to pay royalties on actual production pursuant to the provisions of Paragraph 3 hereof.

5. Lessee is hereby granted the right and power, from time to time, to pool or combine this lease, the land covered by it or any part or horizon thereof with any other land, leases, mineral estates or parts thereof for the production of oil or gas. Units pooled hereunder shall not exceed the standard proration unit fixed by law or by the Oil Conservation Division of the Energy and Minerals Department of the State of New Mexico or by any other lawful authority for the pool or area in which said land is situated, plus a tolerance of ten percent. Lessee shall file written unit designations in the county in which the premises are located and such units may be designated from time to time and either before or after the completion of wells. Drilling operations on or production from any part of any such unit shall be considered for all purposes, except the payment of royalty, as operations conducted upon or production from the land described in this lease. There shall be allocated to the land covered by this lease included in any such unit that portion of the total

production of pooled minerals from wells in the unit, after deducting any used in lease or unit operations, which the net oil or gas acreage in the land covered by this lease included in the unit bears to the total number of surface acres in the unit. The production so allocated shall be considered for all purposes, including the payment or delivery of royalty, to be the entire production of pooled minerals from the portion of said land covered hereby and included in said unit in the same manner as though production from said land under the terms of this lease. Any pooled unit designated by lessee, as provided herein, may be dissolved by lessee by recording an appropriate instrument in the County where the land is situated at any time after completion of a dry hole or the cessation of production on said unit.

6. If at the expiration of the primary term there is no well upon said land capable of producing oil or gas, but Lessee has commenced operations for drilling or reworking thereon, this lease shall remain in force so long as operations are prosecuted with no cessation of more than 60 consecutive days, whether such operations be on the same well or on a different or additional well or wells, and if they result in the production of oil or gas, so long thereafter as oil or gas is produced from said land. If, after the expiration of the primary term, all wells upon said land should become incapable of producing from any cause, this lease shall not terminate if Lessee commences operations for additional drilling or for re-working within 60 days thereafter. If any drilling, additional drilling, or re-working operations hereunder result in production, then this lease shall remain in full force so long thereafter as oil or gas is produced hereunder.

7. Lessee shall have the free use of oil, gas and water from said land, except water from Lessor's wells and tanks, for all operations hereunder, and the royalty shall be computed after deducting any so used. Lessee shall have the right at any time during or after the expiration of this lease to remove all property and fixtures placed by Lessee on said land, including the right to draw and remove all casing. When required by Lessor, Lessee will bury all pipelines on cultivated lands below ordinary plow depth, and no well shall be drilled within two hundred feet (200ft.) or any residence or barn now on said land without Lessor's consent.

8. The right of either party hereunder may be assigned in whole or in part and the provisions hereof shall extend to the heirs, executors, administrators, successors and assigns; but no change in the ownership of the land or in the ownership of, or rights to receive, royalties or shut-in royalties, however accomplished shall operate to enlarge the obligations or diminish the rights of Lessee: and no such change or division shall be binding upon Lessee for any purpose until 30 days after Lessee has been furnished by certified mail at Lessee's principal place of business with acceptable instruments or certified copies thereof constituting the chain of title from the original Lessor. If any such change in ownership occurs through the death of the owner, Lessee may, at its option, pay or tender royalties or shut-in royalties in the name of the deceased or to his estate or to his heirs, executor or administrator until such time as Lessee has been furnished with evidence satisfactory to Lessee as to the persons entitled to such sums. An assignment of this lease in whole or in part shall, to the extent of such assignment, relieve and discharge Lessee of any obligations hereunder and, if Lessee or assignee of part or parts hereof shall fail or make default in the payment of the proportionate part of royalty or shut-in royalty due from such Lessee or assignee or fail to comply with any of the provisions of this lease, such default shall not affect this lease insofar as it covers a part of said lands upon which Lessee or any assignee thereof shall properly comply or make such payments.

9. Should Lessee be prevented from complying with any express or implied covenant of this lease, or from conducting drilling or re-working operations hereunder, or from producing oil or gas hereunder by reason of scarcity or inability to obtain or use equipment or materials, or by operation of force majeure, or by any Federal or state law or order, rule or regulation of governmental authority, then while so prevented, Lessee's duty shall be suspended and Lessee shall not be liable for failure to comply therewith; and this lease shall be extended while and so long as Lessee is prevented by any such cause from conducting drilling or re-working operations or from producing oil or gas hereunder; and the time while Lessee is so prevented shall not be counted against Lessee, anything in this lease to the contrary notwithstanding.

10. Lessor hereby warrants and agrees to defend the title to said land and agrees that Lessee at its option may discharge any tax, mortgage or other lien upon said land, and in the event Lessee does so it shall be subrogated to such lien with the right to enforce same and to apply royalties and shut-in royalties payable hereunder toward satisfying same. Without impairment of Lessee's rights under the warranty, if this lease covers a less interest in the oil or gas in all or any part of said land the entire and undivided fee simple estate (whether Lessor's interest is herein specified or not) then the royalties, shut-in royalty, and other payments, if any, accruing from any part as to which this lease covers less than such full interest, shall be paid only in the proportion which the interest therein, if any, covered by this lease, bears to the whole and undivided fee simple estate therein. Should any one or more of the parties named above as Lessors fail to execute this lease, it shall nevertheless be binding upon the party or parties executing the same.

11. Lessee, its or his successors, heirs and assigns, shall have the right at any time to surrender this lease, in whole or in part, to Lessor or his heirs, successors and assigns by delivering or mailing a release thereof to the Lessor, or by placing a release thereof of record in the county in which said land is situated; thereupon Lessee shall be relieved from all obligations, expressed or implied, of this agreement as to acreage so surrendered, and thereafter the shut-in royalty payable hereunder shall be reduced in the proportion that the acreage covered hereby is reduced by said release or releases.

12. Continuous Development (a) If Lessee is at the expiration of the primary term engaged in actual drilling operations, this lease shall remain in full force and effect as to all lands covered hereby for so long as such operations continue to completion or abandonment and for so long thereafter as continuous development is conducted, being defined as no more than 180 days elapsing between the completion or abandonment of one well and the commencement of actual drilling operations of another well; or (b) If at the end of the primary term, Lessee is not conducting actual drilling operations, but Lessee has completed a well on the leased premises prior to the expiration of the primary term either as

a well capable of producing oil and/or gas in paying quantities or as a dry hole, this lease shall remain in full force and effect for so long as actual drilling operations on an additional well are commenced within 180 days following the expiration of the primary term, and this lease shall continue in force for so long thereafter as continuous development is conducted, being defined as no more than 180 days elapsing between completion or abandonment of one well and the commencement of actual drilling on the next succeeding well. (c) At such time as Lessee (1) fails to commence said continuous development, or (2) once commenced, fails to continue same, this lease shall terminate as to all land not then included within a proration unit assigned to a well then producing oil or gas in paying quantities, and said proration unit shall be limited in depth from the surface down to and including 100 feet below the base of the deepest formation penetrated by drilling. (d) The term "proration unit" as used herein shall be the number of acres which are allocated to a well under the regulations of the New Mexico Oil Conservation Division (NMOCD), (or other governmental body having jurisdiction over producing tracts) for production of oil or gas under special Field Rules applicable to the area involved herein so as to enable the well to a full allowable; provided, however, if no Special Field Rules have been adopted by said commission, then such proration unit shall be deemed to be 40 acres as to oil wells and 160 acres as to gas wells.

IN WITNESS WHEREOF, this instrument is executed on the date first above written shall be extended while and so

COATES ENERGY TRUST

BY: _____

ACKNOWLEDGMENTS

THE STATE OF _____ }
COUNTY OF _____ }

This instrument was acknowledged before me on this _____ day of _____, 2000, by _____, as _____ of _____.

Notary Public in and for the State of Texas
Notary's printed name: _____

My commission expires: _____