MINUTES OF THE JANUARY 22, 2009 UNATEGO AREA LANDOWNERS ASSOCIATION JANUARY MONTHLY MEETING

Anna Hein opened the meeting with organizational chores dealing with membership applications, dues, deeds, and a brief mention of Association by-laws which will keep us moving in an orderly fashion. While not required at this very moment, the collection of deeds will prevent a legal log jam when we go to contract.

Using attorney Scott Kurkoski's 12 elements of a good gas lease, Dick Downey examined Lenape Energy's original lease (Lenape One). This is the lease they offered in acquiring their first 5,000 acres in the Otego. A rewrite of this lease, followed by two separate addendums, sweetened the terms, but essentially kept Lenape interests intact.

Mr. Kurkoski suggests that the landowners interests are best served when a gas company drills, produces gas, pays royalties, or moves on. Landowners don't want encumbrances on their land over long periods of time without adequate payment. With that in mind, Downey reviewed Lenape One.

1) A good lease has a short primary term, preferably 5 years.

Lenape One is essentially a 10 year lease, posing as a 5 year. Article #6 of Lenape One states, "Lessee (Lenape), its successors or assignees may, AT ITS OPTION, extend the primary term of the lease an additional 5 years by paying an amount equal to the initial payment. All other terms remain the same."

This is a ten year lease!

2) People familiar with the gas industry know that the real money is in the royalties. Royalties should be a negotiated item, hopefully better than the 12 1/2% MINIMUM set by law. Aside from the percentage, the benchmark price makes a difference, well head or point-of-sale. Furthermore, the terms of the agreement should be clear.

Lenape One bases its MINIMAL 12 1/2% royalties on the lower well head price, but then states "subject to reduction for costs associated with marketing and transportation." The words "marketing and transportation" are an invitation for creative accounting.

Downey read from Article #4 of XTOs contract with the Hancock/Deposit landowners, the Association that negotiated 15% royalties and a $2,411

per acre sign on bonus. While the royalty is paid on the well head price, minus proportionate share of production, severance, and excise taxes (all easily verifiable), the lease clearly states what can't be deducted. The gas company cannot deduct "the costs of producing, gathering, storing, treating, dehydrating, transporting, or otherwise making the gas produced ready for sale or use." The lease further states that the sale must be an arm's length contract (no subsidiaries buying at a sweetheart price) and adds other landowner protective measures. That's a good lease with clearly stated terms.

3) Water right should be clearly explained and tightly contained.

Water is a valuable asset and a possible source of income. Article #10 of Lenape One states "Lessee (Lenape) shall have the rights to use, FREE OF COST, gas, oil, water produced from the premises for its operations thereon, except water from the wells of the lessor (the landowner).

Lenape would leave you your well, but goodbye pond, goodbye wetland, goodbye money.

4) Costs for environmental damage must be covered by the drillers. The lease must cover indemnification for claims and any defense of those claims through additional insurance paid by the driller.

Lenape One had no coverage for the landowner. Lenape One had one environmental SENTENCE in the lease. That SENTENCE stated, "The lessee (Lenape) shall pay for damages caused by its operation to growing crops, trees, and fences located on the premises."

THAT'S IT! No before, during, and after testing of water. No mention of insurance for the company. No mention of liability insurance for you. No mention of accident insurance. This is an industrial operation on your property. If you signed Lenape One, you were out there naked.

5) There should be a shut-in royalty with term limits.

Circumstances arise where the gas drillers have to shut down a well for economic reasons. Market prices go down, gas fields grow old and more costly to extract as well as other circumstances. Landowners are partners with the gas companies; landowners have to allow for shut-in situations.

HOWEVER, Lenape One is forever. There is no expiration date for a shut-in situation. Article #4 of the Lenape lease states, " If at any time during or after the primary term there is a well CAPABLE OF PRODUCING GAS but such a well is shut in ----- --------- NEVERTHELESS it shall be considered that gas is being produced in payable quantities within the

meaning of this lease." "Paying quantities" is the magic word of gas leases. It the well is producing in "paying quantities" a driller can stay on your property. And in case this isn't clear, Article #4 of Lenape One has a wrap-up sentence. "As long as any well is shut -in, it shall be considered for the purposes of maintaining this lease in force that gas is being produced in paying quantities, and that this lease shall continue in effect both before and after the primary term."

Conceivably, a landowner could have a perfectly good well on his property for 9 years and receive no money. The penalty according to Lenape One - $1 per acre per year. If they are late paying the shut-in penalty - 8% interest, BUT no possibility of cancelation.

The lease reviewed by the Steering Committee and sent back to Mr. Kukoski for his final rewrite has a two year shut-in and a $50 per acre per year penalty. That's a good lease.

Downey further explained the necessity of the Pugh Clause. The Pugh Clause essentially tells the gas driller, "use my property or lose it." If after the primary term all or part of a landowner's property is not producing gas in payable quantities, the mineral rights to the unproductive portion of that property reverts back to the landowner. If there is a 100 acres property and only 25 acres is in a pooled unit after the 5 year primary term, the mineral rights to the 75 unproductive acres reverts back to the landowner. The landowners can then negotiate with another gas driller for the rights to those acres.

Not so with Lenape One. If they are productive on any portion of your property, the remaining acreage can be rolled over to a secondary term. Without a Pugh Clause you have a bad lease.

6) No storage, no compressors, no injection of waste, no pipelines from outside the unit without more money.

Right up front in Article #1 of Lenape One the landowner signs away all of these sources of extra income for a dollar (the one dollar the landman hands you) and a dream (the minimum royalty allowed by law and the sign-on bonus). Article #1 states that the landowner "hereby grants, leases, and lets exclusively unto the lessee" - - -EVERYTHING - - - as spelled out in sentence that runs over 120 words.

In case the right to store gas isn't clear in Article #1, it is restated in Article #8 where Lenape tells the landowner what they will pay him or her - $2 per acre per year.

There is a problem with stored gas. It compromises the well. What is their

gas? What is the landowner's gas? Furthermore the last sentence in Article #3 states, "No royalty shall be due on stored gas produced from the premises OR ON GAS PRODUCED FROM A STORAGE FORMATION OR FORMATIONS THEREUNDER. Without consent (the right to consent is given up in Article #1) the landowner could lose the potential for royalties in formations below the stored formation. This is not a good lease.

7) Operations must be carefully defined.

In Article #15 of Lenape One the conditions for extending a lease that has a shut-in situation or has a dry hole are spelled out in an open ended manner. The key word is "operations." Operations can mean just about everything remotely related to gas field practices. Article #15 states, "the term operations in this lease shall include BUT NOT BE LIMITED TO " - - - the sentence then proceeds to describe just about every phase of gas production. But remember, if by chance something is forgotten, that circumstance can be covered by the words "but not limited to." So, as the term of a lease draws near a company can "get busy" and extend a lease because of "operations."

A good lease encourages a company to drill, produce gas, pay royalties, or move on. A bad lease lets them linger without production.

8) Assignment only with landowners' consent.

The lease is a tangible asset for a gas company. From time to time even the wealthiest company finds itself short of cash and has to dispose of assets. This was the case with Chesapeake when it transferred 1,300 leases in Broome County to Statoilhydro of Norway for $283,000,000 on November 3rd. This is normal in business.

While both parties in a gas lease can assign rights to the lease to another party, it is prudent for the landowner to retain the right to approve the new "tenant." The new "tenant" must be financially able to drill, produce gas, and pay the royalties. A good lease retains the right to examine that capability.

There is no mention of landowner consent in Lenape One.

9) Surface use must be carefully spelled out in the Development Plan.

The gas company and the landowner are partners. The company needs reasonable parameters to operate. Downey said a delegation from the Association visited Lenape Energy sites in Clyde, NY. There seemed to be good cooperation between the landowner and the company. Access

roads were redirected and contoured to the landowners benefit. Relationships seemed cordial.

10) A spud fee must compensate for the noise and inconvenience of placing a well on a landowners property.

There was no spud fee in Lenape One.

11) Damages must be fully compensated.

Compensation for damages was barely mention in Lenape One. Downey said he found only one sentence in this regard, the Environmental Sentence referred to in Item # 3.

12) Audit rights are extremely important.

There is no mention of audit right in Lenape One. In the lease prepared for the Association, the Steering Committee found at least three articles granting landowners access to gas measurement reports, revenue reports and access to all reports demanded by state and federal authorities. Transparency is key to trust.

Downey noted that the Steering Committee, and earlier the Lease Committee, had read leases from Lenape (Lenape One & Two, followed by Addendums), Whitmar, Excelo, Penn General, and Nornew. While all were different, they all were the same. They protected the gas driller while taking advantage of the individual landowner.

Downey then outlined the Lease Process.

1) Steering committee reviews/comments on attorneys' draft least. Done.

2) Attorney reviews comments, consults w/ Steering Committee. In process.

3) Lease presented to membership by attorneys. After review, membership votes.

4) If approved, attorneys send bid letters to about 100 companies.

5) Gas drilling companies respond and negotiations begin.

6) Steering Committee reviews negotiated lease - make recommendations to members.

7) Membership receives final version of the lease, then votes.

8) Legal "housekeeping" chores are done at this point, i.e. confidentiality signatures, retainer agreements, conflict waivers, etc. Social Security numbers and copies of deeds must be supplied prior to closing.

9) Proceed to a closing between the Association and the gas drilling company.

10) Gas drilling company does a title search of all Association properties.

11) Upon completion, usually 60 days, landowners receive sign-on bonus minus one-time fee of $20 per acre.

Downey introduced and thanked Richard Averett, the Association Web-master. Averett's acceptance of this position has made it easier to communicate with Association members. The web-site is:

www.otegogas.webs.com

There was about a 30 minute Q&A. All questions not immediately answered will be addressed by the next meeting.

Minutes Respectfully Submitted,

Richard Downey