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**RULES AND REGULATIONS
BOARD OF LAND COMMISSIONERS**

Chapter 18

Leasing of Oil and Gas

Section 1. Authority.

This chapter is adopted pursuant to the authority granted in W.S. 36-6-101(b).

Section 2. Definitions.

(a) “Beneficiaries” means the common schools and those state institutions designated by Congress as beneficiaries of lands granted to the State of Wyoming.

(b) “Board” means the Board of Land Commissioners.

(c) “Director” means The Director of the Office of State Lands and Investments.

(d) “Office” means the Office of State Lands and Investments.

(e) “Oil and Gas” means oil and gas, coalbed gas, other kindred hydrocarbons present in the earth and extracted in a gaseous or liquid state, and non-hydrocarbon gases and any by-products recovered from such gases. It does not mean coal, lignite, oil shale, or similar solid hydrocarbons.

(f) “State Lands” means all lands under the jurisdiction of the Board of Land Commissioners in which the Board owns some or all of the mineral estate.

Section 3. General Provisions.

(a) The Board may, without prior notice, withdraw specific lands from leasing for oil and gas when it appears reasonably necessary to protect the economic or environmental interests of the beneficiaries. Any party desiring to lease lands for oil and gas which have been withdrawn may request that a withdrawal be rescinded in whole or in part.

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(b) The Board may condition the issuance of any oil and gas lease upon specific stipulations for the protection of the public, the environment, the waters of the state, historical, archeological or paleontological materials, the wildlife resources, or any of the subsurface or surface resources of the state.

(c) The Board may deny an oil and gas lease to any person or legal entity which has failed to comply with any rules of the Board or any terms and conditions of any lease or other agreement with the Board.

(d) The Board may refuse to issue an oil and gas lease or approve an assignment of an interest in an existing oil and gas lease if issuing the lease or approving the assignment will diminish the interest of the beneficiaries.

(e) On lands in which the state owns less than the entire interest in the oil and gas estate, a lease will be issued by the Board covering the state's interest independent of the other co-owners.

(f) Oil and gas covered by an existing lease is not available for lease (top leasing) until the existing lease terminates, and the oil and gas is made available for leasing under Section 5 of this chapter.

(g) An application may be filed for a lease on lands not shown by the records of the Office to be owned by the state. The applicant must submit evidence through the Office to the Wyoming Attorney General showing that it is probable that the lands applied for, or any interest therein, have escheated to the State of Wyoming. Such applicant shall coordinate with and pay for all costs for the Office and the Attorney General pursuant to the filing of a petition under W.S. 9-5-203 seeking title for the state. After receiving a court order vesting title in the state, the applicant shall have the right to lease the escheated lands under the Board's current form of lease without bidding thereon at auction. If the lands are not found to have escheated to the state, applicant will not be entitled to any lease or cost reimbursement.

(h) Discovery of historical, archaeological, or paleontological deposits on state lands during the course of development shall be reported to the Office by the lessee prior to further disturbance, and operations may only re-commence as authorized by the Director. The Director shall notify the lessee regarding mitigation within five (5) working days after receiving the report.

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Section 4. Qualified Lessee.

To be qualified to receive or hold any interest in a state lease, corporations, limited partnerships and limited liability companies must be authorized to transact business in the State of Wyoming by the Secretary of State, and general partnerships shall provide the Office with a copy of their partnership papers.

Section 5. Leasing Procedures.

(a) All oil and gas leases on state lands will be first offered by competitive bidding. The Office shall set a time and place for the auction sale, describing each tract to be offered, noting the terms of the leases to be issued, noting the terms and conditions of sale, detailing the procedure to be followed in conducting the sale, and any other necessary information. Notice of the sale shall be given in such form and manner as the Board shall direct but shall at a minimum be published in a Wyoming newspaper of statewide distribution and provided individually to entities and persons having registered with the Office to receive auction listings.

(b) Leases which are not purchased at the initial auction sale may be offered at a subsequent auction at a lower royalty rate.

(c) After leases have been offered competitively under subsections (a) and (b) of this section, the Office shall place them on a list of leases available for lease to the first qualified applicant filing an application. The Office may remove leases from the list at any time. Applications may be filed with the Office during regular hours of any business day. The Office shall note the date of filing on all applications. Applications filed on the same day, whether presented by personal delivery or received through any mail service, shall be considered as filed simultaneously.

(d) Each application must be accompanied by the required filing fee as established by the Board in Chapter 17 of the Board's rules. The filing fee will not be refunded on any application. An application under this section must also be accompanied by a remittance for the advance rental for the first year at the rental per acre specified in Section 6 of this chapter.

(e) If two or more applications for the same interests in oil and gas are filed simultaneously, the applications are in conflict.

(i) An application which is in conflict as to only a part of the lands applied for, will be processed as to the lands not in conflict in the same manner as a separate application for such lands.

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(ii) The priority of applications which are in conflict as to all or any part of the lands applied for shall, as to the lands in conflict, be determined by sealed bid between the applicants in conflict.

(f) When an application is rejected in its entirety, advance rentals paid by the applicant will be refunded. When rejected in part, the unused portion of the advance rental payment will be refunded.

(g) An application for an oil and gas lease may be withdrawn, in whole or in part, at any time prior to issuance of the lease. The advance rental and all fees transmitted with the application applicable to the portion of the application withdrawn, will be forfeited for failure to fulfill the obligations of the lease offer. However, if a withdrawal was for the purpose of removing a conflict, rentals applicable to the portion withdrawn will be refunded if a lease for the portion withdrawn is issued to another applicant.

Section 6. Rentals.

(a) The annual rental payments on all non-producing oil and gas leases shall be one dollar (\$1)/acre per year for the five (5) year term, and for producing leases, two dollars (\$2)/acre per year for the remaining term of the lease.

(b) Failure to pay rentals on or before the lease anniversary date shall result in termination of the lease. Termination of a lease shall not relieve the lessee of any obligation incurred under the lease other than the obligation to pay rental or penalty.

(c) After initial submission of the increased annual rental required by the lease upon the discovery of oil and gas in paying quantities, lessees are exempt from submission of subsequent annual creditable lease annual rentals for so long as annual royalties paid meet or exceed the required annual rental amount. The annual rental shall be held for a credit on annual royalty in any year the annual royalty does not equal the required annual rental (minimum royalty) amount. Any credit amount used in making up the difference in royalty paid and the minimum lease royalty due must be paid within thirty (30) days following the next lease anniversary date to continue the lease. The Office shall notify lessees of any minimum royalty amount due after the lease anniversary for which a shortfall occurs.

Section 7. Royalties.

(a) Royalties for oil and gas and other kindred hydrocarbons, natural gasoline, sulfur, and non-hydrocarbon gases and any by-products recovered from such gases shall be based on the terms of the particular lease agreement, subject to all state royalty statutes and

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rules, and shall be based on the total consideration received for state production. The following royalty rates shall apply, unless a different rate is specifically authorized by the Board:

(i) Sixteen and two-thirds percent (16 2/3%), except that in cases where competitive bidding results in no offer to lease, a tract may be re-offered at the discretion of the Director at a subsequent competitive sale at a twelve and one-half percent (12½%) royalty rate;

(ii) Further, from a list established by the Director containing leases unleased after offerings at both sixteen and two-thirds percent (16 2/3%) and twelve and one-half percent (12½%) royalty rates, and located further than one mile from existing production, tracts may be leased non-competitively at a royalty of twelve and one-half percent (12½%) by applications personally delivered to the Office under the procedures described in Section 5 of this chapter;

(iii) At the Board's discretion, when deemed favorable in stimulating exploration on non-producing, primary term oil and gas leases, a specified "drilling window" of no greater than two (2) years may be requested and set for specific leases, allowing a lease royalty rate of ten percent (10%) where production in paying quantities is established during a "window" from a wildcat well as defined by the Rules of the Wyoming Oil and Gas Conservation Commission. Announcement of a "drilling window" will be made no less than thirty (30) days prior to commencement. Leases establishing paying quantity production within a "drilling window" shall receive the royalty rate reduction to ten percent (10%) for so long as paying quantity production exists for any well on the lease thereafter, except that in the event the producer receives an average price equal to or above twenty dollars (\$20) per barrel of oil from a well classified as an oil well or one dollar and fifty cents (\$1.50) per mmbtu of gas from a well classified as a gas well for six (6) consecutive months from lease production, the ten percent (10%) royalty rate shall cease, and the original lease royalty rate shall be effective for the remaining term of the lease;

(iv) After an oil and gas lease becomes an operating lease, the Board may reduce the royalty payable to the state, as to all or any of the lands or formations covered by the lease, if it determines that such a reduction is necessary to allow the lessee to undertake additional operations or to continue to operate with a reasonable expectation that the operations will be profitable. Royalty rate reduction to the statutory minimum of five percent (5%) may be granted for a limited time, specific to new well production, to allow for the recovery of drilling costs for deep zone exploration completions in excess of twelve thousand feet (12,000'). Royalty rate reductions may also be granted when lease basis income statements reflect that reasonable actual operations costs, when combined with the royalty rate, create a loss situation under arms-length sales. Such a reduction in the

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royalty payable to the state shall in all cases be conditioned upon the cancellation of all cost-free interests in excess of five percent (5%) and the reduction of all other cost-free interests in the same proportion as the state's royalty is reduced. The Board may also impose other conditions to the reduction in royalty.

Section 8. Lease Term.

(a) Oil and gas leases shall be for a primary term of five (5) years and as long thereafter as oil or gas may be produced in paying quantities.

(b) The Board may extend the term of an existing undeveloped and non-unitized oil and gas lease for a period not to exceed five (5) years, in one-year increments, if it determines that the lessee has been prevented from drilling because of governmental action or regulation, safety issues to include but not limited to proximity to mining operations, permitted surface activities or habitation, drilling target zone conditions, or other causes beyond the lessee's reasonable control. Rig availability, financing, geological or geophysical reviews, weather conditions, and product pricing shall not be considered as causes beyond the lessee's reasonable control but ordinary to the business. A single extension request may be considered based on weather where the attempt to prudently drill prior to the expiration of the lease primary term was negated by unseasonable weather conditions.

(i) Extensions shall be on the express condition that the lessee commence drilling operations on the leased lands within the extended term and drill the well diligently to completion as a dry hole, producing well, or after commencement of drilling operations loses the hole due to uncontrollable downhole conditions.

(ii) Unless specifically waived by the Board, lessees must agree to pay liquidated damages if the well is not commenced and completed or unavoidably lost in accordance with the terms of the lease extension. The lessee shall furnish a ten thousand dollar (\$10,000) cash bond in the form of a certified or cashier's check made payable to the Office or a ten thousand dollar (\$10,000) certificate of deposit in the name of the Office of State Lands and Investments as an amount approved by the Board to secure the payment of such liquidated damages, refundable upon lessee's fulfillment of lease drilling requirements or usable as necessary to meet the performance bond obligations of the lease and Section 13 of this chapter.

(iii) Notwithstanding subsection (b) above, the Board may extend the term of an existing undeveloped oil and gas lease for a period not to exceed five (5) years in one-year increments, for rig unavailability. These extensions shall only be granted where the lessee has filed with the Office of State Lands and Investments written

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correspondence dated within the year of the extension with all known financially, environmentally and operationally suitable drilling contractors operating in the Rocky Mountain Region showing the unavailability of drilling rigs through those contractors. Such correspondence must be filed on an annual basis along with an application for an extension of the lease term.

(c) The Director may approve oil and gas lease suspensions of operations, where suspensions are authorized by lease terms, appear to be in the best interest of orderly development of the leases, and can serve to prevent premature lease abandonment.

Section 9. Unit or Cooperative Plans and Agreements.

(a) All leases are issued subject to the right of the Director to require a cooperative plan or unit agreement if the Director determines that participation is necessary to protect the state's interest.

(b) Any person may request that state lands be included in a cooperative or unit plan for exploration, development, operation, and production of oil and gas through the following procedure:

(i) The proponent of the plan or agreement shall submit to the Office two (2) copies of a plat showing the area to be unitized, together with such geological and other information as may exist and be available, in support of the delineation of the area sought for unitization or cooperative development. The Office shall hold the information submitted confidential until released by the proponent.

(ii) The proponent shall submit to the Office:

(A) Two (2) copies of the preliminary draft of the agreement for approval as to form;

(B) A copy of the schedule of interest ownership by tract and, upon request, any operating agreement, accounting agreement, or other pertinent documents affecting the plan or agreement;

(C) The fee established by the Board in Chapter 17 of the Board's rules.

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(iii) If the form is acceptable to the Office, the unit or cooperative plan meets the requirements of W.S. 36-6-101 (d) and (k), and all leases sought for commitment are in good standing, the Director will approve the agreement. If approved, it will be duly executed using the Board's "Approval-Certification-Determination" form.

(iv) If the Director approves the agreement, the proponent of the agreement shall submit for execution as many counterpart joinder copies as are required for all parties in interest, including one copy to be delivered when fully executed to the Office and any final form of agreement if different from the draft submitted.

(c) When only part of the land under a non-producing lease is committed to a unit, the portion not committed shall be segregated.

(d) An oil and gas lease which has once been extended beyond its primary term under W.S. 36-6-101(e) will not be committed to a subsequent unit or cooperative agreement.

(e) The Board shall use its "Approval-Certification-Determination" form to join unit or cooperative plans.

(f) Board joinder in a unit or cooperative plan shall not alter the rental or royalty clauses of any state lease involved.

(g) Unless the Director specifically requires a lessee to participate, joinder by the Board shall not become effective until the lessee has also joined the unit.

Section 10. General Assignment Requirements.

(a) Pursuant to W.S. 36-6-101(c), the Director shall approve or disapprove any assignment or transfer of a lease or an interest therein. Assignments shall be submitted for approval in duplicate on the form provided by the Office. If an assignment transfers an interest in more than one lease, an extra duly executed copy of the assignment or a photostatic copy of the original assignment shall be furnished for each lease in which an interest is transferred. The required filing fee must be paid for each separate lease in which an interest is assigned.

(b) The Director shall approve an assignment which has been properly executed and appears to comply with the law and this chapter, unless he determines that:

(i) Approval would interfere with the development of the oil or gas;

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(ii) The assignable lease is delinquent in rental or royalty payment status;

(iii) Existing bonding is insufficient to cover lease premises activities;

(iv) Conditions exist that would otherwise be detrimental to the interests of the beneficiaries;

(v) The assignee is not a qualified lessee as provided in Section 4 of this chapter; or

(vi) The number of persons holding undivided interest in a lease exceed two (2) in number, unless a designation of agent or a power of attorney executed by all lessees is filed with the Office which designates one of the lessees as agent or attorney to receive all notices, pay all rentals, and is authorized to represent the lessees with the same effect as though the agent or attorney was the sole lessee. For the purposes of this paragraph, owners of overriding royalties, production payments or other cost-free interests are not considered lessees, but owners of carried working interest, net profit owners, and other persons who may be required to bear a share of the cost out of their share of the production are considered lessees.

(c) If the Director disapproves an assignment, he shall advise the assignee by letter of his decision, the reason for disapproval, and when possible, advise what action is necessary to secure approval.

(d) An assignment or transfer of a lease or any interest therein, including overriding royalties and other cost-free interests created out of the leasehold estate, must be in writing and executed and acknowledged in accordance with the requirements of the law applicable to conveyances of interest in real estate. The instrument must clearly set forth the serial number of the lease, accurately describe the lands affected, the interest being conveyed as a percentage of total leasehold, and be free of any ambiguity.

Section 11. Partial Assignments.

(a) Subject to the requirements of this chapter, a lessee may assign or transfer all or part of his interest in the released acreage as to either a divided or undivided interest therein, including cost-free interest such as overriding royalties and production payments.

(b) The Director shall approve assignments or reservations of an overriding royalty subject to the condition that the overriding royalty or a portion thereof may be

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cancelled or suspended by the Board if it finds that it creates a burden upon the lease which prevents or unreasonably interferes with development.

(c) Assignment of a divided interest, i.e., an assignment of the full leasehold or working interest in a lease as to all interest in all deposits, formations, or depths below a separate tract of the lands subject to the lease or as to one or more separate deposits, formations, or depths below all or a part of the land subject to the lease, segregates the assigned interest from the retained interest and creates new lease obligations as to the lands and the deposits, formations, or depths assigned.

(i) The rights and obligations of the lessees under the retained portion and the assigned portion of the original lease are separate and distinct as though two (2) separate leases, one (1) covering only the retained interest and the other the assigned interest, had originally been issued on the effective date of the original lease.

(ii) The Director may disapprove any assignment which has the effect of creating separate lease obligations covering the retained and the assigned interest even though it purports to assign less than all of the leasehold or working interest, unless both assignor and assignee agree to accept the separate obligations.

(d) Upon assignment as to only a part of the lease acreage, including assignment as to separate deposits, formations, or depths, the Office may issue a reissue lease with a new serial number covering the assigned lands for the unexpired primary term. In lieu of issuing a reissue lease, the Office may note the assignment upon its records with all lands covered by the original lease maintained under the original serial number, and with each separate tract or interest resulting from an assignment designated by a letter suffix to the original serial number. Each assignee holding a lease on a separate tract or interest may be required to furnish a bond under Section 13 of this chapter.

Section 12. Surface Integrity and Minimum Reclamation.

(a) Lessees shall use care and proper safeguards to prevent pollution of the soil or any water, including underground aquifers, by virtue of lessee's or lessee's designee's operation on state lands and shall capture and dispose of any operation's pollutants not permitted under Wyoming Department of Environmental Quality regulation, resulting from lessee's or lessee's designee's operations, and shall be responsible for any and all damages caused thereby related to lessee's operations.

(b) When any oil, gas, or disposal well on state lands becomes dormant as defined by Wyoming Oil and Gas Conservation Commission Rules at Chapter 3, Section 4, the lessee shall either properly plug and abandon it within one hundred eighty (180) days

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after first reaching that status or post an additional bond with the Office in the amount of two dollars (\$2.00) per foot of well depth. All wells must be properly plugged and abandoned, unless otherwise authorized by the Director, within one hundred eighty (180) days of the loss of lease. Lessee's bond will not be released until satisfactory abandonment, as approved by the Wyoming Oil and Gas Conservation Commission and the Office, has been completed.

(c) Upon completion of operations on state lands, all related disturbances on state lands must be reclaimed to leave the land in as near as practicable to the original condition of the land prior to operations. All topsoil must be salvaged before an area is disturbed by roads, buildings or other related activities. The salvaged topsoil must be stockpiled in such a way to protect it from wind and water erosion. If no topsoil exists for use in reclamation, with the Director's written approval, a cover soil that has been amended to sustain vegetation may be applied. If lessees can demonstrate that stripping and stockpiling of topsoil as precursor to their activities will be more detrimental to the topsoil as relates to reclamation, the Director may waive this requirement.

(d) New roads shall cross all drainages at right angles with culverts installed in a manner to avoid constricting the flow of surface water. All drainage or creek crossings must be constructed of erosion resistant material and constructed in a manner to prevent degradation of waters of the state from eroded sediment. No pits or impoundments shall remain after operations and reclamation activities, unless they have developed into viable wetlands as that term is defined by current federal regulation or if the pits or impoundments could potentially be of use to the state or to the surface lessee. All reclaimed areas must have slopes as approved by the Director and in conformance with existing State of Wyoming laws, rules, and regulations governing reclamation.

(e) All reclaimed areas must be reseeded, where possible, with an approved seed mixture.

Section 13. Bonds.

(a) A lessee is not required to post a bond until actual operations, including exploration activities, are to be commenced on the leased lands. Before commencing actual operations, the lessee shall submit a copy of Oil and Gas Conservation Commission Form 1, Application for Permit to Drill to the Office. Operations shall not commence until an adequate bond has been furnished and approved.

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(b) The bond shall be in an amount found by the Director sufficient to protect and indemnify the State of Wyoming and shall be in the form approved by the Wyoming Attorney General. Two (2) executed copies of the bond must be submitted to the Office. The bond shall bind the principal and its surety for:

(i) The payment of all moneys, rents, and royalties accruing to the Board;

(ii) Full compliance with all applicable statutes and terms and conditions of the Board's leases and rules and regulations;

(iii) The proper plugging and abandonment of all inactive, non-productive wells on the leases;

(iv) Reclamation of the surface; and

(v) For the payment of all disturbances to the surface and improvements thereon.

(c) The bond shall be one of the following:

(i) A corporate surety bond executed by the lessee and by a surety authorized to do business in the state;

(ii) A cash bond;

(iii) A certified cashier's check made payable to the Office of State Lands and Investments;

(iv) A certificate of deposit in the name of the Office of State Lands and Investments;

(v) Non-revocable letters of credit; or

(vi) AAA-rated debentures of sufficient market value to meet bonding minimums with a signed stock power made out to the Office of State Lands and Investments.

(d) In lieu of individual lease bonds, the lessee may request and the Director may allow the lessee to file a corporate surety bond in the sum of not less than one hundred thousand dollars (\$100,000) covering all of the lessee's state leases.

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(e) The lessee shall promptly advise the Office of any change in operations. The Office may at any time reduce or increase the amount of the bond as conditions may require. The Director may require a per well bond instead of allowing bonding per lease.

Section 14. Relinquishment.

(a) An oil and gas lease or any divided interest therein may be relinquished by the record title holder to the Board in the following manner:

(i) If no operations have been conducted under the lease and no surface disturbance or damage has occurred on the land to be relinquished, the lessee shall file with the Office a written statement on a form provided by the Office that he wishes to relinquish the lease or interest. The relinquishment shall become effective on the date and hour of receipt by the Office or at some later date if specified.

(ii) If operations have been conducted under the lease or surface disturbance or damage has occurred on land proposed to be relinquished, the lessee shall file with the Office a statement on a form provided by the Office that he wishes to relinquish the lease or interest. Relinquishment shall not become effective until the land and the wells thereon shall have been placed in acceptable condition and an inspection report has been completed by the State Oil & Gas Supervisor.

(iii) Once a relinquishment on state lands becomes effective, the lease may not be reinstated. The lands shall be made available for lease as provided in Section 5 of this chapter.

Section 15. Royalty Reporting.

(a) All lessees shall submit to the Office a completed monthly royalty reporting statement on a form provided by the Office for each lease (Forms M-1 and/or M-2). The lessee shall submit each lease statement within thirty (30) days of the last day of the month of sales for oil and condensate and sixty (60) days of the last day of the month of sales for gas and gas plant products. The lessee shall attach to the M-1 statement copies of original arms-length sales transaction documents showing the quantity, quality, and value of products sold, including all lease volume sales through affiliate companies.

(b) For participating leases within a unit, a participating area, or a cooperative plan, the unit operator, the participating area operator, or the cooperative plan (communitization) operator shall submit to the Office a completed monthly royalty reporting statement on a form provided by the Office for each unit, unit participating area,

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and cooperative plan embracing state leases (Form M-4). The respective operator shall attach to the M-4 statement copies of original arms-length sales transaction documents showing the quantity, quality, and value of products sold.

Section 16. Field Audits.

(a) The Wyoming Department of Audit, the Director, or the duly authorized representative of either shall have the right at reasonable times and intervals to audit the books and records of any oil and gas lessee or operator on state lands and to inspect the leased premises and conduct field audits for the purpose of determining compliance with this chapter or the terms of the lease.

(b) Any and all parties producing and selling state lands royalty interests shall retain their records for six (6) years from the date of sale reporting as due under this chapter for any production from or allocated to state lands for all periods ending after January 1, 2000.

(c) Absent state lessee or operator production sales reporting as required in this subsection, the state's oil and gas lessee shall only sell or deliver any leased substance to any person who agrees:

(i) To file reports with the Office stating the price, quantity, origin, and disposition of all production purchased from a state lease; and

(ii) To allow an audit as provided for in this section.

Section 17. Cancellation for Default.

(a) If any oil and gas lessee defaults in the performance or observance of any of this chapter or any of the terms, covenants, or conditions of the lease under which it is operating, the Board may serve notice of such failure or default either by personal service or by certified or registered mail upon the lessee. If the failure or default continues for a period of thirty (30) days after service of the notice, the Board may declare a forfeiture and cancel the lease, whereupon all rights and privileges obtained by the lessee under the lease shall terminate, and the Board may re-enter and take possession of the premises and surface and down hole equipment if there are outstanding obligations owed the State.

(a) This section shall not be construed to prevent the exercise by the Director or the Board of any other legal or equitable remedy which the state might otherwise have nor to relieve the lessee from any accrued obligation under the lease. Failure of the lessor to give notice of default in any particular case or waiver of a particular cause of forfeiture

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shall

not prevent the cancellation and forfeiture of the lease for any other cause of forfeiture or for the same default or cause if it continues or occurs at any other time.

Section 18. Multiple Use.

(a) The Board may issue separate leases for different minerals on the same tract of land. If all mineral leases under a tract of land are non-producing leases, each lessee has an equal right to conduct exploratory operations on the land, and each shall conduct such operations in a manner which does not prevent or unduly interfere with the operations of the other.

(b) The first lessee to commence actual production operations so that his lease becomes an operating lease shall have the right to continue operations without substantial interference from any other mineral lessee so long as the lease remains in effect. The lessee may not be deprived of this right in whole or in part without compensation equal to the value of the rights lost as per Subsection (d)(iii) of this section.

(c) If a lessee desires to commence operations on the same tract upon which one or more lessees are already conducting operations, and the lessees can agree that the operations can be conducted at the same time without materially reducing the amount or value of the resources which will be produced under each lease, and without unduly interfering with or raising the cost of operations of the prior lessee(s), unless he is adequately compensated therefor, the lessees may agree upon a plan of operations and assessment of costs under which the operations may be carried out concurrently. Any such agreement shall be submitted to and be subject to the approval of the Board.

(d) If, under the circumstances set out in Subsection (c) of this section, the lessees either agree that the operations cannot be carried out concurrently or cannot agree upon a plan of operations and assessment of costs, the Director may resolve the conflict.

(i) If the Director determines that the operations can be carried out concurrently without materially reducing the quantity or value of the oil and gas which will be produced, and either that the costs of operation of any prior lessee(s) will not be increased significantly, or that if they are, such costs are capable of determination and if paid by the subsequent lessee will not constitute an unreasonable burden on the operation, he shall enter his decision approving a plan of operation and assessment of cost under which operations may be carried out concurrently.

(ii) If the Director determines that the proposed operations cannot be carried out concurrently and that the value which will be realized by the beneficiaries from

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the existing operation is such that the proposed operation should be deferred, he shall enter

his decision deferring the development obligations under the lease of the proposing lessee. The lease will be placed in operating status and remain in effect subject to the requirement that annual rentals will be paid and to the condition that if development is deferred more than five (5) years, the lease may be amended to conform to the lease form in effect upon commencement of production operations for the class of subsurface resource to be produced.

(iii) If the Director determines that the proposed operations cannot be carried out concurrently and that the benefit which would be realized by the beneficiaries from initiating the proposed operation so far exceeds that which would be realized from the existing operation that it is clearly more beneficial to the beneficiaries that the existing operation be terminated or deferred and the proposed operation commenced, he shall enter his decision terminating the existing operation and allowing the commencement of the proposed operation, conditioned upon the payment by the lessee proposing the operation to the lessee whose operations are terminated of an amount equal to the value of the rights lost by that lessee determined in the same manner as if the right were being condemned in eminent domain proceedings.

(iv) A lease upon which operations are terminated as above provided shall, upon payment to the lessee of the value of the right lost, be assigned to the lessee making the payment, who shall be entitled to hold it subject to the same terms and conditions applicable to a lease upon which operations were deferred under Paragraph (ii) of this section.

(v) If the proposing lessee disagrees with the Director's or the Board's determination, he may refuse to commence the proposed operation. His refusal to do so shall not constitute a violation of the covenants for lease development, unless the amounts he would be required to pay to the prior lessee constitute such an insubstantial addition to the cost of operation that a reasonable, prudent lessee would assume them.