

ACTION: Consideration of Oil and Gas Lease Form Revision

AUTHORITY: W.S. 36-6-101

ALTERNATIVES:

- Approve lease form
- Reject lease form

ANALYSIS:

Functionally, the State's oil and gas lease form was last revised in March of 1982. In the intervening 30 years, much has changed in the leasing, drilling and production of oil and gas. From the advent of coal bed natural gas development to the proliferation of horizontal drilling, many provisions in the current state oil and gas lease form are not adequate to protect the interests of the state trust land beneficiaries and, in certain instances, actually work to the detriment of those beneficiaries.

Following roundtable discussions with the oil and gas industry and other related interests in 2010 and several opportunities to comment on various renditions of a revised lease form, staff of the Office of State Lands and Investments has arrived at the point of presenting the lease revision to the Board for its consideration and approval. The most recent comment opportunity started in mid-April of this year and resulted in the Petroleum Association of Wyoming Proposed State Land Lease Amendments Committee Comments dated May 11, 2011, which are attached for your consideration. Please note that the Comment form contains three columns. The "Proposed Lease Language" and "PAW Comment" fields were filled out and provided by the Petroleum Association of Wyoming and have not been altered or edited – the comments are as they were presented to the Office. The third column, entitled "State Response," provides the Office's response to the offered comment.

Apart from the "clean copy" of the proposed oil and gas lease, staff has also attached a "marked up" version of the lease form for ease of reference. The red underlined language represents all of the new language in the lease. The red underlined yellow highlighted language represents those portions of the new lease that were changed pursuant to comments submitted by the Petroleum Association of Wyoming. Notable in their absence in the lease form revision are the previously offered Pugh Clause and royalty rate increase. After considerable discussion with industry and others, those two (2) items were tabled, despite their potential to enhance returns to the state trust land beneficiaries, in the interest of securing timely Board consideration and support for the other necessary terms that are being moved forward in the current lease revision.

General Overview of Pertinent Changes

Changes begin with Section 1 on page 1 of the lease to add language to assure that surface entry and use is subject to applicable non-mineral rule chapter requirements, specifically the Office's requirement to obtain a Surface Use Lease if non-state interests are being served by the placement of equipment and facilities on the state lease.

In Section 2, a definition of "paying quantities" has been added, where no definition previously existed in the lease form to clarify the term of the lease. The addition of this "continuance of operations" requirement, standard in most leases but not currently contained in State lease, enforces timeliness in operations and ensures that value is actually being received for production on the lease.

Starting on page 2, in the Oil and Gas Lease Terms portion of the lease, Section 1 (a) places the Board, in its capacity as Lessor, in the position to have maximum control

over bonding and protection of the lease. A show cause provision was added at the behest of industry to ensure that the lessee would have some recourse to request bond reduction or alteration.

The royalty section provides the most significant changes in the form. The language adds specificity regarding disallowed costs in computing royalty valuation. The draft language provides a definition of “market value,” which was not previously in the lease, together with an expanded interest provision, which comports with existing W.S. 30-5-303. The lease also provides explicit guidance as to what uses of production *on lease* will be permitted, which was not previously clear to all parties and the subject of considerable dispute with industry. The language also addresses the issue of accountability for and timeliness to remedy adjacent drilling and production that potentially affects State lease lands. Finally, the royalty provision expressly states that the Wyoming Royalty Payment Act applies to the lease.

Section 1 (f) adds additional language clarifying the production measurement standards and requirements for state land leases and specificity in terms of the reports and documents that must accompany all royalty report filings.

Section 1 (g) provides for a uniform “pay” date for natural gas and oil in the lease, which matches current practice and rules.

Section 1 (i) develops an additional lessee obligation to provide sharing arrangement production volumes and sales details as needed to confirm royalty volumes and potentially review valuation disparities.

Section 1 (j) requires accountability for production of all potential hydrocarbons and salable non-hydrocarbons.

Section 1(k) relates to suspension of operations, now a widely relied upon lease clause, and is changed to provide additional language for suspensions related to de-watering and other, functional pre-production activities.

Section 1(l) is altered to provide express directives to fully reclaim drill sites – a matter that remains insufficiently covered in the Board’s current lease form.

Section 1 (n) is changed to expressly reserve to the Board the ability to approve or reject an assignment of lease interest(s).

Section 1 (o) is written to assure that if casing is cemented in the well bore, the lessee has no right to remove this casing. This protects the state against well bore damage potential in the event that the operator would want to pull the casing.

The described changes are meant to protect the interests of the state trust land beneficiaries, while not unduly burdening state land lessees. Given the repeated and extended opportunities for comment from industry and the public, the offered lease revision represents, in the view of the Office, a balanced and fair contract. The state interest is served through clarity in terms of the allowable deductions against the state’s royalty and what constitutes “market value,” and the industry interest is furthered with the certainty that is now afforded it. Finally, the revised lease has been bolstered with numerous “show cause” and “reasonability” determinations to assure that the lessee has full opportunity to “have its day in court and make its case” in the event the lessee disagrees with a determination under the lease.

DIRECTOR’S RECOMMENDATION:

The Director recommends approval of the revised State oil and gas lease form.

BOARD ACTION: The Board tabled Board Matter E-20 subject to resolution of issues.

STATE OF WYOMING OIL AND GAS LEASE

This indenture of lease is entered into by and between the State of Wyoming, acting by and through its Board of Land Commissioners as **LESSOR**, and administered by the Office of State Lands and Investments, and _____ as **LESSEE**.

Section 1. PURPOSE. LESSOR, in consideration of the rents and royalties to be paid and the covenants and agreements to be kept and performed by LESSEE, does hereby grant and lease to LESSEE, the exclusive right to drill for, mine, extract, remove, and dispose of all the oil, gas and associated hydrocarbon substances and gaseous substances and elements produced therewith, including sulfur, hydrogen sulfide, sulfur dioxide, nitrogen, carbon dioxide and helium, which may be produced from the following described land, to wit:

County: _____ Total Acres: _____ Advance Rental: \$ _____
(\$1.00 per acre or fraction thereof)

Together with the right of ingress and egress and the right to use so much of the surface of said lands as is necessary to construct and maintain thereupon all works, buildings, plants, waterways, roads, communication lines, pipe lines, reservoirs, tanks, pumping stations, or other facilities necessary to the proper conduct of operations hereunder in conformance with all applicable rules and regulations of the Board of Land Commissioners in effect during the term of this lease. Equipment and facilities placed on this leasehold which benefit non-State interests must obtain a Special Use Lease pursuant to Chapter 5 of the Rules of the Board of Land Commissioners.

Section 2. TERM OF LEASE. Subject to the terms and conditions herein, this lease shall become effective on the day and year set out below and shall remain in effect for a primary term of five (5) years and for so long thereafter as leased substances may be produced from the lands in paying quantities. "Paying quantities" is defined as gross income from lease operations, less royalties and taxes, exceeding the costs of operating the lease. This lease may also be extended beyond its primary term in the absence of production of leased substances as may be provided by the statutes of the State of Wyoming and the regulations of the Board of Land Commissioners adopted pursuant thereto. Provided, however, if drilling, completion, testing or reworking operations are being diligently conducted, either during the primary term or during any extension thereof, this lease shall continue in full force and effect so long as such operations are being conducted and so long thereafter as oil or gas may be produced in paying quantities. This lease may be relinquished or terminated at an earlier date as herein provided.

Section 3. If LESSOR owns an interest in oil and gas in said land less than the entire fee simple estate, then the royalties and rentals to be paid LESSOR shall be reduced proportionately.

Section 4. LESSEE expressly represents that, if an individual, LESSEE is a citizen of the United States, or has declared an intention to become a citizen, and is over 19 years of age, and if a corporation, is duly qualified to transact business in Wyoming.

Section 5. This lease is issued under the authority conferred by Title 36, as to the State and School Lands, and Title 11, as to Farm Loan lands, and shall be subject to, and operations by LESSEE hereunder shall be conducted in compliance with the specific lease terms set out on the reverse of this lease, and with all applicable state statutory requirements and the rules and regulations issued thereunder, including those providing for the leasing of State or Farm Loan Lands for oil and gas; the conservation of oil and gas; and the regulation of security transactions.

Section 6. HEIRS AND SUCCESSORS IN INTEREST. It is covenanted and agreed that each obligation hereunder shall extend to and be binding upon, and every benefit thereof shall inure to the heirs, executors, administrators, successors of, or assigns of the respective parties hereto.

Section 7. SOVEREIGN IMMUNITY. The State of Wyoming and LESSOR do not waive sovereign immunity by entering into this lease, and specifically retain immunity and all defenses available to them as sovereigns pursuant to WYO. STAT. § 1-39-104 (a) and all other laws of the State of Wyoming.

IN WITNESS WHEREOF, this lease has been executed by LESSOR and LESSEE to become effective on the _____ day of _____, A.D.

LESSOR, STATE OF WYOMING, Acting by and through its Board of Land Commissioners.

LESSEE:
BY: _____

Signature _____

Address: _____

Director, Office of State Lands and Investments

City _____ State _____ Zip _____

Subject to Stipulation No(s) _____

OIL AND GAS TERMS

Section 1. LESSEE AGREES:

(a) BOND. To furnish a bond with an approved corporate surety company authorized to transact business in the State of Wyoming, or such other surety as may be reasonably acceptable to LESSOR, in an amount fixed by LESSOR, to secure the payment for any damages to the surface of the land, including livestock, crops, water wells, reservoirs, or improvements, caused by LESSEE'S operations on the land, and to assure compliance with all the terms and provisions of this lease, including rent and royalties owed, the laws of the State of Wyoming, and the rules and regulations promulgated thereunder. LESSEE shall provide such bonds prior to the development of the lands contained in this lease. Such bonds may be increased in such reasonable amounts as LESSOR may decide upon commencement of drilling and other operations, and after discovery of oil or gas, in which case lessee has sixty (60) days to post any additional bond or show cause reasonably acceptable to LESSOR that a bond increase should not be required or this lease may be terminated. This bonding requirement does not affect any obligations pursuant to the Split Estate Act. WYO. STAT. §§ 30-5-401 - 409.

(b) PAYMENTS. To make all payments accruing hereunder to the State of Wyoming - Office of State Lands and Investments, 122 West 25th Street, Cheyenne, Wyoming 82002-0600.

(c) RENTALS/MINIMUM ANNUAL ROYALTY. (i) Prior to the discovery of oil or gas in paying quantities, to pay LESSOR in advance, beginning with the effective date hereof, an annual delay rental of \$1.00 per acre or fraction thereof. If the delay rental is not paid on or before the date it becomes due, notice of default will be sent to LESSEE, and an administrative handling assessment of \$1.00 per acre for the missing payment will be assessed. LESSEE agrees that if the rental and any administrative handling assessment are not paid within thirty (30) days after the notice of default has been received, the lease shall terminate.

(ii) After the discovery of oil or gas in paying quantities, to pay LESSOR in advance beginning with the first day of the lease year succeeding the lease year in which actual discovery was made, a minimum annual rental of \$2.00 per acre or fraction thereof, unless changed by agreement. To maintain the lease, any deficient lease minimum annual rental shall be paid within thirty (30) days after the receipt of the deficiency notice from the Office of State Lands & Investments sent by certified U.S. Mail to LESSEE'S last known address. Such rental so paid for any one year shall be credited on the royalty for that year.

(d) ROYALTIES. Unless otherwise stipulated and agreed in writing, the royalties to be paid by LESSEE are:

(i) On oil, one-sixth ($1/6^{\text{th}}$) of the market value (as defined (d) (v) herein below) of that produced, saved, and sold from said land, the same to be delivered at the wells or to the credit of LESSOR into the pipe line to which the wells may be connected. LESSOR'S royalty is not subject to costs incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, pumping and lifting, recycling, gathering, separating, treating, dehydrating, removing contaminants, transporting the oil to storage tanks, storing as well as any marketing costs and taxes of any kind. The reasonable, actual, unreimbursed costs of transportation of oil and condensate beyond the storage tanks shall be deductible; however such costs are subject to audit at the discretion of LESSOR.

(ii) On gas, including casinghead gas or other hydrocarbon substances, produced from said land saved and sold or used off the premises or processed for the extraction of natural gasoline, natural gas liquids or other products therefrom, one-sixth ($1/6^{\text{th}}$) of the market value, (as defined (d) (v) herein below) of the gas, natural gasoline, natural gas liquids, or other hydrocarbon and non-hydrocarbon elements and compounds, including, but not limited to, inert gases, sulfur and helium so sold or used. LESSOR'S royalty is not subject to costs incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, lifting, recycling, gathering, single or multiple stage compression, separating, treating, dehydrating, removing contaminants, amine treating, glycol, methanol and chemical injection, or transporting the gas to the market pipeline, as well as any marketing costs and taxes of any kind. The reasonable, actual, unreimbursed costs of transportation in the market pipeline shall be deductible; however such costs are subject to audit at the discretion of LESSOR. Market pipeline transportation is defined and accepted as movement from the furthestmost downstream entry/suction point from which thereafter immediate physical delivery can be made to residential, commercial and industrial end-users for consumption without further treating or compressing upon such entry thereto.

(iii) On all other hydrocarbons of value and gaseous substances and elements produced or extracted, including, but not limited to, propane, butane, sulfur, nitrogen, carbon dioxide, and helium one-sixth ($1/6^{\text{th}}$) of the market value of that produced, saved, and sold from said land subject to (d) (iv) herein below.

(iv) For royalty purposes on gas and natural gasoline the value shall be as reasonably approved by LESSOR, and in the determination of the value of natural gasoline the reasonable, actual, unreimbursed cost of extraction shall be considered as a deductible item; provided, however, that the allowance for the cost of extraction may exceed two-thirds ($2/3^{\text{rds}}$) of the amount or value only on approval of the LESSOR and in no event shall the arms-length price for gas, or natural gasoline, be less than that received by the United States of America for its royalties from the same field, or, if no such royalties exist from the same field, then from any adjacent or geographically and geologically associated field.

(v) "Market value" is defined as the sales price received by lessee for production in merchantable condition, including all premiums and consideration in whatever form and at whatever time, unless such production is sold pursuant to a non-arm's length transaction or at a price not consistent with the prices received for like quality production for sales of merchantable production in the same general area or market hub. In such case, "market value" shall be defined as the highest arm's-length price, including all premiums and consideration in whatever form, regardless of time and place, for like quality production in merchantable condition at the closest recognized market point or hub.

(vi) Natural gas and oil actually used for operating purposes upon the land and, except as to the ultimate sale thereof, gas or liquid hydrocarbons returned to the sand for stimulating the production of oil or secondary recovery purposes shall be royalty free. "Operating purposes upon the land" is defined as fuel used to run a pumping unit(s), operate initial separation equipment at the well for separation of oil, water and gas, and run tank heaters, not to exceed two percent (2%) of wellhead volume unless a greater amount is agreed to by LESSOR, but specifically excludes any use beyond separation and storage tank heating to include all procedures and processes specifically deemed as the cost of production under the laws of the State of Wyoming.

(vii) If LESSEE receives any compensation for any function, process or liability related to production from this lease without the right given herein to deduct the costs related to such compensation, such compensation amount shall be added to the market value for such production type and royalty must be computed and paid thereon at the lease royalty rate.

(viii) Interest shall accrue and be payable on all royalty obligations for production in paying quantities unpaid at the required date under this lease at the rate of eighteen percent (18%) per annum from the date such obligation shall arise. Payment for royalty obligations is due by no later than the end of the month immediately following the month of production and sales for oil and lease condensate. Payment for royalty obligations is due by no later than the end of the second month following the month of production and sales for gas, plant inlet condensate and natural gas liquids/natural gasoline. The accrual and payment of interest does not constitute waiver or satisfaction of any penalty that may apply under the rules and regulations of the Board of Land Commissioners in effect during the term of this lease.

(ix) If during any period of non-production from this lease, any production is sold from offsetting acreage from any well closer than four-hundred sixty feet (460') in any direction from the lease line, the right to continue this lease will be satisfied only by the payment of compensatory royalty, in the amount of one-half (1/2) the volume of the offset well at market value, at the lease royalty rate; or; by evidence of regulatory agency permission for an exception location at a point closer than four-hundred sixty feet (460') from any boundary of this lease. Further, offset production may not continue for greater than one-hundred eighty (180) days in paying quantities, as sold from the offset well, without lessee beginning the drilling of a lease offset hereon; or, providing geological, reservoir characteristic, logistical and/or financial information as necessary to satisfy LESSOR that the drilling of any specific offset on this lease will be un-economical or otherwise not feasible pursuant to the recovery of drilling, testing, completing, equipping and producing costs associated with this lease over the life of the lease and the estimated recoverable reserves associated with this lease. It is agreed that failure to comply with this requirement will be cause for termination of this lease unless LESSEE can demonstrate to the reasonable satisfaction of LESSOR that no drainage could occur from an off-lease offset well.

(x) The Wyoming Royalty Payment Act, WYO. STAT. §§ 30-5-301 through -305 shall apply to this lease; however, where there is a conflict between the Wyoming Royalty Payment Act and the terms of this lease, the lease language shall control.

(e) DISPOSITION OF ROYALTY OIL AND GAS. To deliver to LESSOR, or to such individual, firm or corporation as LESSOR may designate, all royalty oil, gas, or other kindred hydrocarbons, free of charge on the premises where produced, or, at the option of LESSOR, and in lieu of said royalties in kind, LESSEE agrees to pay LESSOR the market value of all royalty oil, gas, or other kindred hydrocarbons produced and spilled, lost, stolen, flared and vented, or, saved and sold, unless otherwise approved by LESSOR in writing.

When LESSOR elects to take its royalty oil, gas, or other hydrocarbons in kind such oil, gas, or other kindred hydrocarbons shall be good merchantable oil, gas, or other kindred hydrocarbons. LESSEE shall, if necessary, furnish storage for royalty oil free of charge for thirty (30) days after the end of the calendar month in which the oil is produced upon the leased premises, or at such place as LESSOR and LESSEE may mutually agree upon, provided, that LESSEE shall not be held liable for loss or destruction of royalty oil so stored from causes beyond its control. The free storage of oil, as herein provided, shall apply only as long as the said oil is the property of LESSOR.

(f) MEASUREMENTS OF PRODUCTION. LESSEE or its operator or any purchaser from this lease shall meter, gauge, measure and correct for temperature, all production from the lands leased hereunder and pooled or unitized with this lease in conformance with the methods and time intervals accepted as standard industry practice and the rules and regulations adopted by the Board of Land Commissioners, and report said production to LESSOR in accordance therewith.

To keep books, records, charts, invoices and reports pertaining to the production from the land herein leased as well as those pertaining to the production from offset wells operated by LESSEE, his operator, or sub-lessee on other lands, which shall be opened at all times for the inspection of any duly authorized agent of LESSOR.

To furnish LESSOR with copies of all pertinent original transporter and/or pipe line and processor statements/reports showing the day, if appropriate, month, year, amount, gravities, temperatures and pricing of all oil run and monthly reports showing the day, if appropriate, month, year, amount (volume), gas BTU; and, price of all gas natural gas liquids and/or and natural gas gasoline and other products produced and allocated to, and sold from the land herein leased, and the amount of gas and/or natural gas liquids or oil/condensate returned to the underlying producing zones/ horizons, for production purposes.

To furnish LESSOR with copies of original sales reports showing the month, year, amount, gravity, BTU, temperature and price per unit of sales and by product, for all products sold from the lease or from interest within which this lease shares by any form of unit or pooling arrangement. Further LESSEE agrees to furnish all other pertinent volume and valuation information in the form prescribed by LESSOR.

(g) MONTHLY PAYMENTS AND STATEMENTS. Unless the time of payment is otherwise extended by the Office of State Lands and Investments to make payment on or before the last day of the calendar month succeeding the month of production and removal and sale of oil from the leased land and any land with which this lease is pooled or unitized; and, to make payment on or before the last day of the second calendar month succeeding the month of production and removal and sale of gas from the leased land and any land with which this lease is pooled or unitized; and to furnish monthly operator and payer production and royalty statements therewith showing in detail the quantity and quality of the production (per well if required where practical), including reports reflecting no production, from the land hereby leased, and the quantity and quality of the production (per well where practical) from offset wells upon cornering or contiguous land operated by LESSEE, its operator or sub-lessee and such other information as may be called for in the form or report prescribed by LESSOR. Failure to timely submit LESSOR-required reports and reporting documents, including reports reflecting no production, as called for within a practical time period as directed, shall result in a penalty assessment against LESSEE of \$100 per lease, per month, or fraction thereof, missing or delinquent. Non-submission, and continued incorrect/untimely/improper reporting may result in lease cancellation upon expiration of the thirty (30) days of receipt of LESSOR'S written notice to LESSEE requiring a show cause for the delinquency, or, provision of the reporting required, where such good cause for the delinquency or delinquencies is not satisfactorily shown by LESSEE during the thirty (30) day period.

(h) WELLS TO BE DRILLED. To drill and operate effectively all wells necessary to reasonably offset wells upon, and production from, adjoining lands. To drill such additional wells at such times or places as are necessary and essential to the proper development and commercial production of the oil and gas content of said land.

(i) LOG OF WELLS AND REPORTS. To keep a log, in the form approved by LESSOR, of each well drilled by LESSEE on the lands herein leased, showing the strata and character of the formations, water sands and mineral deposits penetrated by the drill, amount of casing, size and where set, and such other information as LESSOR may require, which log or copy thereof shall be furnished to LESSOR. To furnish copies of any and all reports affecting this lease as filed with the appropriate oil and gas regulatory agency or the authorized officer under any joinder in federal unitization/communitization or any non-federal pooling arrangements or communitization.

To file progress reports, in the form prescribed by LESSOR, at the end of each thirty (30) day period while each well is being drilled.

To file annually, or at such times as LESSOR may require, maps/plats showing the development of the structure and the location of all wells, pipe lines and other works used in connection with the operations of LESSEE, its operator(s) and any transporters or purchasers upon said land.

To make such other reports pertaining to the production and operations by LESSEE on said land, and report such other information as may be possessed by LESSEE on the wells, production or operations of others on lands on the same geologic structure that may be of importance in effecting proper development and operation of the lands herein leased, as may be called for by LESSOR. The Office of State Lands and Investments may waive such reports as conditions may warrant.

(j)PRODUCTION. To operate the wells upon the land herein leased in a competent and efficient manner in an endeavor to recover and deliver for sale all the oil, gas, natural gas liquids/natural gasoline and salable non-hydrocarbons economically possible from said land and to prevent the under drainage of the oil and gas thereunder by wells operated by LESSEE or others on cornering or contiguous lands to those leased herein.

All plans or methods for the purpose of stimulating or increasing production on lands herein leased other than those in common use shall first be presented to LESSOR for approval before being put into actual operation.

No production agreements or decisions limiting, restricting, prorating, shutting-in or temporarily abandoning any well on this lease, or otherwise affecting the natural production from said land shall be entered into by LESSEE, nor shall LESSEE limit, restrict, shut-in or temporarily abandon any well on this lease, nor prorate the natural production from said land in any way or in any event, except with the consent in writing of LESSOR having first been obtained.

(k)SUSPENSION OF OPERATIONS. Should any well drilled upon lands covered by this lease obtain production of oil, gas, or other hydrocarbons in paying quantities and LESSEE is unable to establish a satisfactory market for the oil, gas or hydrocarbons produced from said well, or, should any well drilled upon lands covered by this lease require de-watering or stimulating, LESSEE may apply for and LESSOR may grant permission for the suspension of production operations from the well and/or the lease until such times as a satisfactory market for the product from said well or lease can be developed. Such grants of suspension shall be approved by LESSOR for periods of no greater than one year without LESSEE'S additional petition therefor. During the time any such suspension of operations is in effect, LESSEE shall continue to pay the annual royalty (rental) of \$2.00 per acre or fraction thereof for the first such suspension, and thereafter, as directed by LESSOR upon approval of each suspension, and this lease shall remain in effect as though oil or gas was being produced from said lands.

(l)DILIGENCE-PREVENTION OF WASTE. To exercise reasonable diligence in drilling, producing, and operating all wells on the land covered hereby, unless consent to suspend operations temporarily is granted by LESSOR; to carry on all operations hereunder in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil and gas, or the entrance of water to the oil or gas bearing sands or strata to the destruction or injury of such deposits, the preservation and conservation of the property for future productive operations and to the health and safety of workmen and employees; to plug securely in an approved manner any well before abandoning it and to reclaim the well site and any disturbances associated therewith that will not be further used in operations on the lease,, and not to abandon any such well without permission of LESSOR, and not to drill any well within two hundred feet (200') of any of the outer boundaries of the land covered hereby, unless to protect against drainage by wells drilled on lands adjoining less than two hundred feet (200') from the property lines thereof; to conduct all operations subject to the inspection of LESSOR; to carry out at LESSEE'S expense all reasonable orders and requirements of LESSOR relative to the prevention of waste and preservation of the property and the health and safety of workmen; and, to complete all required reclamation activities including, but not limited to, the re-contouring, replanting and reseeding of drilling sites and other areas disturbed by drilling or other operations; and, upon failure of LESSEE to do so, LESSOR shall have the right, together with other recourse herein provided, to enter on the property to repair damage or prevent waste at LESSEE'S expense; to abide by and conform to valid applicable regulations prescribed to reimburse the owner of the surface, if other than LESSOR, or lessee of grazing rights thereof, for actual damages thereto and injury to improvements thereon, provided, that LESSEE shall not be held responsible for acts of providence or actions beyond its control. Failure to extinguish such obligations will cause a call for LESSEE and operator bonds and result in further action to recover any loss to LESSOR should such bonding amounts not cover the expenses/costs incurred.

(m)TAXES AND WAGES-FREEDOM OF PURCHASE. To pay, when due all taxes lawfully assessed and levied under the laws of the State of Wyoming upon improvements, oil and gas produced from the land hereunder, or other rights, property or assets of LESSEE, to accord all workmen and employees complete freedom of purchase, and to pay all wages due workmen and employees in conformance with the laws of the State of Wyoming.

(n)ASSIGNMENTS OF LEASE-PRODUCTION AGREEMENTS. Not to assign this lease or any interest therein, nor sublet any portion of the leased premises, except with the consent in writing of LESSOR first had and obtained. LESSOR reserves the right to refuse approval of any assignment of any interest in this lease, including over-riding royalty interests should LESSOR determine such assignment would be to the detriment of proper and timely lease development. Approval will not be unreasonably withheld.

(o)DELIVER PREMISES IN CASE OF FORFEITURE. To deliver up the leased premises, with all permanent improvements thereon, including downhole cemented casing, in good order and condition in case of forfeiture of this lease, but this shall not be construed to prevent the removal, alteration or renewal of equipment and improvements in the ordinary course of continuing operations. Failure to deliver up the leased premises in good order and condition satisfactory to LESSOR will cause a call for LESSEE and operator bonds and result in further action to recover any loss to LESSOR.

Section 2. THE LESSOR EXPRESSLY RESERVES:

(a) The right to lease, sell, or otherwise dispose of the surface of the land embraced within this lease under existing laws or laws hereafter enacted, and in accordance with the rules of the Board of Land Commissions insofar as the surface is not necessary for the use of LESSEE in the conduct of operations hereunder.

(b)The right to lease, sell, or otherwise dispose of other mineral or subsurface resources not covered by the lease, in accordance with the applicable laws and the rules of the Board of Land Commissioners.

(c)From the operation of this lease, the surface lands heretofore granted for rights-of-way and easements and reserves the right to grant such other rights-of-way and easements as provided by the statutes of the State of Wyoming, as long as such rights-of-way and easements do not conflict with the operations for oil and gas on the land herein leased.

(d)The right to refuse to commit the leased lands to a unit plan of development if LESSOR finds such action would impair LESSOR'S reserved right to take its royalty gas in kind and to purchase all other gas allocated to the leased lands as provided in Section 3(e) below.

(e)The right to alter or modify the quantity and rate of production to the end that waste may be eliminated or that production may conform to LESSEE'S fair share of allowable production under any system of State or National curtailment and proration authorized by law.

(f) In addition to its right to take its royalty gas in kind, LESSOR reserves the right and option to purchase all other gas produced for sale or use off the leased lands. This option shall be exercised only if LESSOR finds that LESSEE has

received and is willing to accept a bona fide offer from a purchaser who intends to sell or transport the gas into interstate commerce and that one or more intrastate purchasers (i.e., purchasers who will use, consume, or sell the gas for use or consumption entirely within the State of Wyoming) are willing and able to purchase the gas upon terms reasonably comparable to and at least as favorable to LESSEE as those offered by the interstate purchaser. LESSOR shall waive this option and permit an interstate sale if it finds that no intrastate purchaser is willing and able to purchase the gas upon terms which are reasonably comparable to and at least as favorable to LESSEE. As a condition to such waiver, a satisfactory agreement may be entered into by which the production of its royalty gas may be deferred until it can be produced and sold for consumption and use entirely within the State of Wyoming.

Section 3. APPRAISAL OF IMPROVEMENTS. LESSEE shall have the right subject to the provisions of Title 36, as to State and State School Lands, and Title 11, as to State Loan and Investments Board Lands, to remove any improvements owned by LESSEE, except downhole cemented casing, within a reasonable time after the termination of this lease. LESSEE agrees that any such improvements not removed within one hundred-eighty (180) days after termination of this lease may be disposed of at LESSOR'S option and is forfeited by LESSEE without recourse.

Section 4. FORFEITURE CLAUSE. LESSOR shall have the power and authority to cancel leases procured by fraud, deceit, or misrepresentations, or for the use of the lands for unlawful or illegal purposes, or for the violation of the covenants of the lease, and/or the rules and regulations of the Board of Land Commissioners and all effective applicable statutes. Upon proper proof thereof, in the event that LESSEE shall default in the performance or observance of any of the terms, covenants, and stipulations hereof, or of the general rules and regulations promulgated by the Board of Land Commissioners and in force on the date hereof, LESSOR shall serve notice of such failure or default either by personal service or by certified or registered mail upon LESSEE, and if such failure or default continues for a period of thirty (30) days after the service of such notice, then and in that event LESSOR may, at its option, declare a forfeiture and cancel this lease, whereupon all rights and privileges, obtained by LESSEE hereunder shall terminate and cease and LESSOR may re-enter and take possession of said premises or any part thereof. These provisions shall not be construed to prevent the exercise by LESSOR any legal or equitable remedy which LESSOR might otherwise have. A waiver of any particular cause or forfeiture shall not prevent the cancellation and forfeiture of this lease by any other cause of forfeiture, or for the same cause occurring at any other time.

Section 5. RELINQUISHMENT AND SURRENDER. This lease may be relinquished and surrendered to LESSOR as to all or any legal subdivision of said lands as follows:

(a) If no operations have been conducted under the lease on the land to be relinquished, LESSEE shall file with the State Land Board and State Loan and Investment Board, a written relinquishment or surrender, duly signed and acknowledged and stating therein that no operations have been conducted on the land. The relinquishment so filed shall become effective on the date and hour of receipt thereof in the office of the Director or at some later date, if such be so specified by LESSEE therein. If the said relinquishment fails to state that no operations have been conducted, the effective date of relinquishment shall be the date the relinquishment is approved by LESSOR.

(b) If operations have been conducted under the lease on land proposed to be relinquished, LESSEE shall give sixty (60) days notice and shall file with the Director a written relinquishment or surrender duly acknowledged and stating therein that operations have been conducted on the land. The relinquishment shall not become effective until the land and the wells thereon shall have been placed in condition acceptable to LESSOR and shall have been approved by the State Oil and Gas Supervisor. Bonding under this lease shall not be released to any party until such time as a field inspection has established that reclamation is satisfactory and complete.

All rentals and any minimum annual royalties becoming due prior to a surrender or relinquishment becoming effective, shall be payable by LESSEE unless payment thereof shall be waived by LESSOR. A relinquishment having become effective, there shall be no recourse by LESSEE and the lease as to the relinquished lands may not be reinstated.

Section 6. Governing Law and Jurisdiction. The construction, interpretation and enforcement of this lease shall be governed by the laws of the State of Wyoming. The Courts of the State of Wyoming shall have jurisdiction over this lease and the parties, and the venue shall be the First Judicial District, Laramie County, Wyoming.

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STATE OF WYOMING OIL AND GAS LEASE

**Revised 5/16/2011 to include comments
of PAW where accepted – Final Draft**

This indenture of lease is entered into by and between the State of Wyoming, acting by and through its Board of Land Commissioners as **LESSOR**, and administered by the Office of State Lands and Investments, and as **LESSEE**.

Section 1. PURPOSE. **LESSOR**, in consideration of the rents and royalties to be paid and the covenants and agreements to be kept and performed by LESSEE, does hereby grant and lease to **LESSEE**, the exclusive right to drill for, mine, extract, remove, and dispose of all the oil, gas and associated hydrocarbon substances and gaseous substances and elements produced therewith, including **sulfur**, hydrogen sulfide, **sulfur** dioxide, nitrogen, carbon dioxide and helium, which may be produced from the following described land, to wit:

County: _____ Total Acres: _____ Advance Rental: \$ _____
(\$1.00 per acre or fraction thereof)

Together with the right of ingress and egress and the right to use so much of the surface of said lands as is necessary to construct and maintain thereupon all works, buildings, plants, waterways, roads, communication lines, pipe lines, reservoirs, tanks, pumping stations, or other facilities necessary to the proper conduct of operations hereunder, in conformance with all applicable rules and regulations of the Board of Land Commissioners in effect during the term of this lease. Equipment and facilities placed on this leasehold which benefit non-State interests must obtain a Special Use Lease pursuant to Chapter 5 of the Rules of the Board of Land Commissioners.

Section 2. TERM OF LEASE. Subject to the terms and conditions herein, this lease shall become effective on the day and year set out below and shall remain in effect for a primary term of five (5) years and for so long thereafter as leased substances may be produced from the lands in paying quantities. "Paying quantities" is defined as gross income from lease operations, less royalties and taxes, exceeding the costs of operating the lease. This lease may also be extended beyond its primary term in the absence of production of leased substances as may be provided by the statutes of the State of Wyoming and the regulations of the Board of Land Commissioners adopted pursuant thereto. Provided, however, if drilling, completion, testing or reworking operations are being diligently conducted, either during the primary term or during any extension thereof, this lease shall continue in full force and effect so long as such operations are being conducted and so long thereafter as oil or gas may be produced in paying quantities. This lease may be relinquished or terminated at an earlier date as herein provided.

Section 3. If **LESSOR** owns an interest in oil and gas in said land less than the entire fee simple estate, then the royalties and rentals to be paid **LESSOR** shall be reduced proportionately.

Section 4. **LESSEE** expressly represents that, if an individual, **LESSEE** is a citizen of the United States, or has declared an intention to become a citizen, and is over 19 years of age, and if a corporation, is duly qualified to transact business in Wyoming.

Section 5. This lease is issued under the authority conferred by Title 36, as to the State and School Lands, and Title 11, as to Farm Loan lands, and shall be subject to, and operations by **LESSEE** hereunder shall be conducted in compliance with the specific lease terms set out on the reverse of this lease, and with all applicable state statutory requirements and the rules and regulations issued thereunder, including those providing for the leasing of State or Farm Loan Lands for oil and gas; the conservation of oil and gas; and the regulation of security transactions.

Section 6. HEIRS AND SUCCESSORS IN INTEREST. It is covenanted and agreed that each obligation hereunder shall extend to and be binding upon, and every benefit thereof shall inure to the heirs, executors, administrators, successors of, or assigns of the respective parties hereto.

Section 7. SOVEREIGN IMMUNITY. The State of Wyoming and **LESSOR** do not waive sovereign immunity by entering into this lease, and specifically retain immunity and all defenses available to them as sovereigns pursuant to WYO. STAT. § 1-39-104 (a) and all other laws of the State of Wyoming.

IN WITNESS WHEREOF, this lease has been executed by LESSOR and LESSEE to become effective on the ____ day of _____, A.D.

LESSOR, STATE OF WYOMING, Acting by and through its Board of Land Commissioners.

LESSEE:
BY: _____

Signature _____

Address: _____

Director, Office of State Lands and Investments

City _____ State _____ Zip _____

Subject to Stipulation No(s).

OIL AND GAS TERMS

Section 1. LESSEE AGREES:

(a) BOND. To furnish a bond with an approved corporate surety company authorized to transact business in the State of Wyoming, or such other surety as may be reasonably acceptable to LESSOR, in an amount fixed by LESSOR, to secure the payment for any damages to the surface of the land, including livestock, crops, water wells, reservoirs, or improvements, caused by LESSEE'S operations on the land, and to assure compliance with all the terms and provisions of this lease, including rent and royalties owed, the laws of the State of Wyoming, and the rules and regulations promulgated thereunder. LESSEE shall provide such bonds prior to the development of the lands contained in this lease. Such bonds may be increased in such reasonable amounts as LESSOR may decide upon commencement of drilling and other operations, and after discovery of oil or gas, in which case lessee has sixty (60) days to post any additional bond or show cause reasonably acceptable to LESSOR that a bond increase should not be required or this lease may be terminated. This bonding requirement does not affect any obligations pursuant to the Split Estate Act. WYO. STAT. §§ 30-5-401 - 409.

(b) PAYMENTS. To make all payments accruing hereunder to the State of Wyoming - Office of State Lands and Investments, 122 West 25th Street, Cheyenne, Wyoming 82002-0600.

(c) RENTALS/MINIMUM ANNUAL ROYALTY. (i) Prior to the discovery of oil or gas in paying quantities, to pay LESSOR in advance, beginning with the effective date hereof, an annual delay rental of \$1.00 per acre or fraction thereof. If the delay rental is not paid on or before the date it becomes due, notice of default will be sent to LESSEE, and an administrative handling assessment of \$1.00 per acre for the missing payment will be assessed. LESSEE agrees that if the rental and any administrative handling assessment are not paid within thirty (30) days after the notice of default has been received, the lease shall terminate.

(ii) After the discovery of oil or gas in paying quantities, to pay LESSOR in advance beginning with the first day of the lease year succeeding the lease year in which actual discovery was made, a minimum annual rental of \$2.00 per acre or fraction thereof, unless changed by agreement. To maintain the lease, any deficient lease minimum annual rental shall be paid within thirty (30) days after the receipt of the deficiency notice from the Office of State Lands & Investments sent by certified U.S. Mail to LESSEE'S last known address. Such rental so paid for any one year shall be credited on the royalty for that year.

(d) ROYALTIES. Unless otherwise stipulated and agreed in writing, the royalties to be paid by LESSEE are:

(i) On oil, one-sixth (1/6th) of the market value (as defined (d) (v) herein below) of that produced, saved, and sold from said land, the same to be delivered at the wells or to the credit of LESSOR into the pipe line to which the wells may be connected. LESSOR'S royalty is not subject to costs incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, pumping and lifting, recycling, gathering, separating, treating, dehydrating, removing contaminants, transporting the oil to storage tanks, storing as well as any marketing costs and taxes of any kind. The reasonable, actual, unreimbursed costs of transportation of oil and condensate beyond the storage tanks shall be deductible, however such costs are subject to audit at the discretion of LESSOR.

(ii) On gas, including casinghead gas or other hydrocarbon substances, produced from said land saved and sold or used off the premises or processed for the extraction of natural gasoline, natural gas liquids or other products therefrom, one-sixth (1/6th) of the market value, (as defined (d) (v) herein below) of the gas, natural gasoline, natural gas liquids, or other hydrocarbon and non-hydrocarbon elements and compounds, including, but not limited to, inert gases, sulfur and helium so sold or used. LESSOR'S royalty is not subject to costs incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, lifting, recycling, gathering, single or multiple stage compression, separating, treating, dehydrating, removing contaminants, amine treating, glycol, methanol and chemical injection, or transporting the gas to the market pipeline, as well as any marketing costs and taxes of any kind. The reasonable, actual, unreimbursed costs of transportation in the market pipeline shall be deductible; however such costs are subject to audit at the discretion of LESSOR. Market pipeline transportation is defined and accepted as movement from the furthestmost downstream entry/suction point from which thereafter immediate physical delivery can be made to residential, commercial and industrial end-users for consumption without further treating or compressing upon such entry thereto.

(iii) On all other hydrocarbons of value and gaseous substances and elements produced or extracted, including, but not limited to, propane, butane, sulfur, nitrogen, carbon dioxide, and helium one-sixth (1/6th) of the market value of that produced, saved, and sold from said land subject to (d) (iv) herein below.

(iv) For royalty purposes on gas and natural gasoline the value shall be as reasonably approved by LESSOR, and in the determination of the value of natural gasoline the fair reasonable, actual, unreimbursed cost of extraction shall be considered as a deductible item; provided, however, that the allowance for the cost of extraction may exceed two-thirds (2/3rd) of the amount or value only on approval of the LESSOR and in no event shall the arms-length price for gas, or natural gasoline, be less than that received by the United States of America for its royalties from the same field, or, if no such royalties exist from the same field, then from any adjacent or geographically and geologically associated field.

(v) "Market value" is defined as the sales price received by lessee for production in merchantable condition, including all premiums and consideration in whatever form and at whatever time, unless such production is sold pursuant to a non-arm's length transaction or at a price not consistent with the prices received for like quality production for sales of merchantable production in the same general area or market hub. In such case, "market value" shall be defined as the highest arm's-length price, including all premiums and consideration in whatever form, regardless of time and place, for like quality production in merchantable condition at the closest recognized market point or hub.

(vi) Natural gas and oil actually used for operating purposes upon the land and, except as to the ultimate sale thereof, gas or liquid hydrocarbons returned to the sand for stimulating the production of oil or secondary recovery purposes shall be royalty free. "Operating purposes upon the land" is defined as fuel used to run a pumping unit(s), operate initial separation equipment at the well for separation of oil, water and gas, and run tank heaters, not to exceed two percent (2%) of wellhead volume unless a greater amount is agreed to by LESSOR, but specifically excludes any use beyond separation and storage tank heating to include all procedures and processes specifically deemed as the cost of production under the laws of the State of Wyoming.

(vii) If LESSEE receives any compensation for any function, process or liability related to production from this lease without the right given herein to deduct the costs related to such compensation, such compensation amount shall be added to the market value for such production type and royalty must be computed and paid thereon at the lease royalty rate.

(viii) Interest shall accrue and be payable on all royalty obligations for production in paying quantities unpaid at the required date under this lease at the rate of eighteen percent (18%) per annum from the date such obligation shall arise. Payment for royalty obligations is due by no later than the end of the month immediately following the month of production and sales for oil and lease condensate. Payment for royalty obligations is due by no later than the end of the second month following the month of production and sales for gas, plant inlet condensate and natural gas liquids/natural gasoline. The accrual and payment of interest does not constitute waiver or satisfaction of any penalty that may apply under the rules and regulations of the Board of Land Commissioners in effect during the term of this lease.

(ix) If during any period of non-production from this lease, any production is sold from offsetting acreage from any well closer than four-hundred sixty feet (460') in any direction from the lease line, the right to continue this lease will be satisfied only by the payment of compensatory royalty, in the amount of one-half (1/2) the volume of the offset well at market value, at the lease royalty rate; or, by evidence of regulatory agency permission for an exception location at a point closer than four-hundred sixty feet (460') from any boundary of this lease. Further, offset production may not continue for greater than one-hundred eighty (180) days in paying quantities, as sold from the offset well, without lessee beginning the drilling of a lease offset hereon; or, providing geological, reservoir characteristic, logistical and/or financial information as necessary to satisfy LESSOR that the drilling of any specific offset on this lease will be un-economical or otherwise not feasible pursuant to the recovery of drilling, testing, completing, equipping and producing costs associated with this lease over the life of the lease and the estimated recoverable reserves associated with this lease. It is agreed that failure to comply with this requirement will be cause for termination of this lease unless LESSEE can demonstrate to the reasonable satisfaction of LESSOR that no drainage could occur from such an off-lease offset well.

(x) The Wyoming Royalty Payment Act, WYO. STAT. §§ 30-5-301 through -305 shall apply to this lease; however, where there is a conflict between the Wyoming Royalty Payment Act and the terms of this lease, the lease language shall control.

(e) DISPOSITION OF ROYALTY OIL AND GAS. To deliver to LESSOR, or to such individual, firm or corporation as LESSOR may designate, all royalty oil, gas, or other kindred hydrocarbons, free of charge on the premises where produced, or, at the option of LESSOR, and in lieu of said royalties in kind, LESSEE agrees to pay LESSOR the market value of all royalty oil, gas, or other kindred hydrocarbons produced and ~~wasted, spilled, lost, stolen, flared and vented, or, saved~~ and sold, unless otherwise approved by LESSOR in writing.

When LESSOR elects to take its royalty oil, gas, or other hydrocarbons in kind such oil, gas, or other kindred hydrocarbons shall be good merchantable oil, gas, or other kindred hydrocarbons. LESSEE shall, if necessary, furnish storage for royalty oil free of charge for thirty (30) days after the end of the calendar month in which the oil is produced upon the leased premises, or at such place as LESSOR and LESSEE may mutually agree upon, provided, that LESSEE shall not be held liable for loss or destruction of royalty oil so stored from causes beyond ~~his~~ its control. The free storage of oil, as herein provided, shall apply only as long as the said oil is the property of LESSOR.

(f) MEASUREMENTS OF PRODUCTION. ~~To~~ LESSEE or its operator or any purchaser from this lease shall meter, gauge, measure and correct for temperature, all production from the lands leased hereunder and pooled or unitized with this lease in conformance with the methods and time intervals accepted as standard industry practice and the rules and regulations adopted by the Board of Land Commissioners, and report said production to LESSOR in accordance therewith.

To keep books, records, charts, invoices and reports pertaining to the production from the land herein leased as well as those pertaining to the production from offset wells operated by LESSEE, his operator, or sub-lessee on other lands, which shall be opened at all times for the inspection of any duly authorized agent of LESSOR.

To furnish LESSOR with copies of all pertinent original transporter and/or pipe line and processor statements/reports showing the day, if appropriate, month, year, amount, gravities, temperatures and pricing of all oil run and monthly reports showing the day, if appropriate, month, year, amount (volume), gas BTU; and, price of all gas natural gas liquids and/or and natural gas gasoline and other products produced and allocated to, and sold from the land herein leased, and the amount of gas and/or natural gas liquids or oil/condensate returned to the ~~land~~ underlying producing zones/ horizons, for production purposes.

To furnish LESSOR with copies of original sales reports showing the month, year, amount, gravity, BTU, temperature and price per unit of sales and by product, for all products sold from the lease or from interest within which this lease shares by any form of unit or pooling arrangement. Further LESSEE agrees to furnish all other pertinent volume and valuation information in the form prescribed by LESSOR.

(g) MONTHLY PAYMENTS AND STATEMENTS. Unless the time of payment is otherwise extended by the Office of State Lands and Investments to make payment on or before the last day of the calendar month succeeding the month of production and removal and sale of oil from the leased land and any land with which this lease is pooled or unitized; and, to make payment on or before the last day of the second calendar month succeeding the month of production and removal and sale of gas from the leased land and any land with which this lease is pooled or unitized; and to furnish monthly operator and payer production and royalty statements therewith showing in detail the quantity and quality of the production (per well if required where practical), including reports reflecting no production, from the land hereby leased, and the quantity and quality of the production (per well where practical) from offset wells upon cornering or contiguous land operated by LESSEE, his operator or sub-lessee and such other information as may be called for in the form or report prescribed by LESSOR. Failure to timely submit LESSOR-required reports and reporting documents, including reports reflecting no production, as called for within a practical time period as directed, shall result in a penalty assessment against LESSEE of \$100 per lease, ~~per report~~, per month, or fraction thereof, missing or delinquent. Non-submission, and continued incorrect/untimely/improper reporting may result in lease cancellation upon expiration of the thirty (30) days of receipt of LESSOR'S written notice to LESSEE requiring a show cause for the delinquency, or, provision of the reporting required, where such good cause for the delinquency or delinquencies is not satisfactorily shown by LESSEE during the thirty (30) day period.

(h) WELLS TO BE DRILLED. To drill and operate effectively all wells necessary to reasonably offset wells upon, and production from, adjoining lands. ~~as directed in Section 1 (d) (ix) hereof.~~ To drill such additional wells at such times or places as are necessary and essential to the proper development and commercial production of the oil and gas content of said land.

(i) LOG OF WELLS AND REPORTS. To keep a log, in the form approved by LESSOR, of each well drilled by LESSEE on the lands herein leased, showing the strata and character of the formations, water sands and mineral deposits penetrated by the drill, amount of casing, size and where set, and such other information as LESSOR may require, which log or copy thereof shall be furnished to LESSOR. To furnish copies of any and all reports affecting this lease as filed with the appropriate oil and gas regulatory agency or the authorized officer under any joinder in federal unitization/communitization or any non-federal pooling arrangements or communitization.

To file progress reports, in the form prescribed by LESSOR, at the end of each thirty (30) day period while each well is

being drilled.

To file annually, or at such times as **LESSOR** may require, maps/plats showing the development of the structure and the location of all wells, pipe lines and other works used in connection with the operations of **LESSEE, its operator(s) and any transporters or purchasers** upon said land.

To make such other reports pertaining to the production and operations by **LESSEE** on said land, and report such other information as may be possessed by **LESSEE** on the wells, production or operations of others on lands on the same geologic structure that may be of importance in effecting proper development and operation of the lands herein leased, as may be called for by **LESSOR**. The Office of State Lands and Investments may waive such reports as conditions may warrant.

(j)PRODUCTION. To operate the wells upon the land herein leased in a competent and efficient manner in an endeavor to recover and deliver for sale all the oil, and gas, natural gas liquids/natural gasoline and salable non-hydrocarbons economically possible from said land and to prevent the under drainage of the oil and gas thereunder by wells operated by **LESSEE** or others on cornering or contiguous lands to those leased herein as directed in Section 1 (d) (ix) hereof.

All plans or methods for the purpose of stimulating or increasing production on lands herein leased other than those in common use shall first be presented to **LESSOR** for approval before being put into actual operation.

No production agreements or decisions limiting, restricting, prorating, shutting-in or temporarily abandoning any well on this lease, or otherwise affecting the natural production from said land shall be entered into by **LESSEE**, nor shall **LESSEE** limit, restrict, shut-in or temporarily abandon any well on this lease, nor prorate the natural production from said land in any way or in any event, except with the consent in writing of **LESSOR** having first been obtained.

(k)SUSPENSION OF OPERATIONS. Should any well drilled upon lands covered by this lease obtain production of oil, gas, or other hydrocarbons in paying quantities and **LESSEE** is unable to establish a satisfactory market for the oil, gas or hydrocarbons produced from said well, or, should any well drilled upon lands covered by this lease require de-watering or stimulating, LESSEE may apply for and **LESSOR** may grant permission for the suspension of production operations from the well and/or the lease until such times as a satisfactory market for the product from said well or lease can be developed. Such grants of suspension shall be approved by LESSOR for periods of no greater than one year without LESSEE'S additional petition therefor. During the time any such suspension of operations is in effect, **LESSEE** shall continue to pay the annual royalty (rental) of \$2.00 per acre or fraction thereof for the first such suspension, and thereafter, as directed by LESSOR upon approval of each suspension, and this lease shall remain in effect as though oil or gas was being produced from said lands.

(l)DILIGENCE-PREVENTION OF WASTE. To exercise reasonable diligence in drilling, producing, and operating all wells on the land covered hereby, unless consent to suspend operations temporarily is granted by **LESSOR**; to carry on all operations hereunder in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil and gas, or the entrance of water to the oil or gas bearing sands or strata to the destruction or injury of such deposits, the preservation and conservation of the property for future productive operations and to the health and safety of workmen and employees; to plug securely in an approved manner any well before abandoning it and to reclaim the well site and any disturbances associated therewith that will not be further used in operations on the lease, and not to abandon any such well without permission of **LESSOR**, and not to drill any well within two hundred feet (200') of any of the outer boundaries of the land covered hereby, unless to protect against drainage by wells drilled on lands adjoining less than two hundred feet (200') from the property lines thereof; to conduct all operations subject to the inspection of **LESSOR**; to carry out at **LESSEE'S** expense all reasonable orders and requirements of **LESSOR** relative to the prevention of waste and preservation of the property and the health and safety of workmen; and, to complete all required reclamation activities including, but not limited to,the re-contouring, replanting and reseeding of drilling sites and other areas disturbed by drilling or other operations; and, upon failure of LESSEE to do so, LESSOR shall have the right, together with other recourse herein provided, to enter on the property to repair damage or prevent waste at **LESSEE'S** expense; to abide by and conform to valid applicable regulations prescribed to reimburse the owner of the surface, if other than **LESSOR**, or lessee of grazing rights thereof, for actual damages thereto and injury to improvements thereon, provided, that **LESSEE** shall not be held responsible for acts of providence or actions beyond his its control. Failure to extinguish such obligations will cause a call for LESSEE and operator bonds and result in further action to recover any loss to LESSOR should such bonding amounts not cover the expenses/costs incurred.

(m)TAXES AND WAGES-FREEDOM OF PURCHASE. To pay, when due all taxes lawfully assessed and levied under the laws of the State of Wyoming upon improvements, oil and gas produced from the land hereunder, or other rights, property or assets of **LESSEE**, to accord all workmen and employees complete freedom of purchase, and to pay all wages due workmen and employees in conformance with the laws of the State of Wyoming.

(n)ASSIGNMENTS OF LEASE-PRODUCTION AGREEMENTS. Not to assign this lease or any interest therein, nor sublet any portion of the leased premises, except with the consent in writing of **LESSOR** first had and obtained. **LESSOR** reserves the right to refuse approval of any assignment of any interest in this lease, including over-riding royalty interests should LESSOR determine such assignment would be to the detriment of proper and timely lease development. Approval will not be unreasonably withheld.

(o)DELIVER PREMISES IN CASE OF FORFEITURE. To deliver up the leased premises, with all permanent improvements thereon, including downhole cemented casing, in good order and condition in case of forfeiture of this lease, but this shall not be construed to prevent the removal, alteration or renewal of equipment and improvements in the ordinary course of continuing operations. Failure to deliver up the leased premises in good order and condition satisfactory to LESSOR will cause a call for LESSEE and operator bonds and result in further action to recover any loss to LESSOR.

Section 2. THE LESSOR EXPRESSLY RESERVES:

(a) The right to lease, sell, or otherwise dispose of the surface of the land embraced within this lease under existing laws or laws hereafter enacted, and in accordance with the rules of the Board of Land Commissions insofar as the surface is not necessary for the use of **LESSEE** in the conduct of operations hereunder.

(b)The right to lease, sell, or otherwise dispose of other mineral or subsurface resources not covered by the lease, in accordance with the applicable laws and the rules of the Board of Land Commissioners.

(c)From the operation of this lease, the surface lands heretofore granted for rights-of-way and easements and reserves the right to grant such other rights-of-way and easements as provided by the statutes of the State of Wyoming, as long as such rights-of-way and easements do not conflict with the operations for oil and gas on the land herein leased.

(d)The right to refuse to commit the leased lands to a unit plan of development if the Board LESSOR finds such action would impair **LESSOR'S** reserved right to take its royalty gas in kind and to purchase all other gas allocated to the leased lands a provided in Section 3(e) below.

(e)The right to alter or modify the quantity and rate of production to the end that waste may be eliminated or that production may conform to **LESSEE'S** fair share of allowable production under any system of State or National curtailment and proration authorized by law.

(f) In addition to its right to take its royalty gas in kind, **LESSOR** reserves the right and option to purchase all other gas

produced for sale or use off the leased lands. This option shall be exercised only if ~~the Board~~ LESSOR finds that LESSEE has received and is willing to accept a bona fide offer from a purchaser who intends to sell or transport the gas into interstate commerce and that one or more intrastate purchasers (i.e., purchasers who will use, consume, or sell the gas for use or consumption entirely within the State of Wyoming) are willing and able to purchase the gas upon terms reasonably comparable to and at least as favorable to LESSEE as those offered by the interstate purchaser. ~~The Board~~ LESSOR shall waive this option and permit an interstate sale if it finds that no intrastate purchaser is willing and able to purchase the gas upon terms which are reasonably comparable to and at least as favorable to LESSEE. As a condition to such waiver, a satisfactory agreement may be entered into by which the production of its royalty gas may be deferred until it can be produced and sold for consumption and use entirely within the State of Wyoming.

Section 3. APPRAISAL OF IMPROVEMENTS. LESSEE shall have the right subject to the provisions of Title 36, as to State and State School Lands, and Title 11, as to State Loan and Investments Board Lands, ~~W.S. 1977~~, to remove any improvements owned by LESSEE, except downhole cemented casing, within a reasonable time after the termination of this lease. LESSEE agrees that any such improvements not removed within one hundred-eighty (180) days after termination of this lease may be disposed of at LESSOR'S option and is forfeited by LESSEE without recourse.

Section 4. FORFEITURE CLAUSE. ~~The Board~~ LESSOR shall have the power and authority to cancel leases procured by fraud, deceit, or misrepresentations, or for the use of the lands for unlawful or illegal purposes, or for the violation of the covenants of the lease, and/or the rules and regulations of the Board of Land Commissioners and all effective applicable statutes. Upon proper proof thereof, in the event that LESSEE shall default in the performance or observance of any of the terms, covenants, and stipulations hereof, or of the general rules and regulations promulgated by the Board of Land Commissioners and in force on the date hereof, LESSOR shall serve notice of such failure or default either by personal service or by certified or registered mail upon LESSEE, and if such failure or default continues for a period of thirty (30) days after the service of such notice, then and in that event LESSOR may, at its option, declare a forfeiture and cancel this lease, whereupon all rights and privileges, obtained by LESSEE hereunder shall terminate and cease and LESSOR may re-enter and take possession of said premises or any part thereof. These provisions shall not be construed to prevent the exercise by LESSOR any legal or equitable remedy which LESSOR might otherwise have. A waiver of any particular cause or forfeiture shall not prevent the cancellation and forfeiture of this lease by any other cause of forfeiture, or for the same cause occurring at any other time.

Section 5. RELINQUISHMENT AND SURRENDER. This lease may be relinquished and surrendered to LESSOR as to all or any legal subdivision of said lands as follows:

(a) If no operations have been conducted under the lease on the land to be relinquished, LESSEE shall file with the State Land Board and State Loan and Investment Board, a written relinquishment or surrender, duly signed and acknowledged and stating therein that no operations have been conducted on the land. The relinquishment so filed shall become effective on the date and hour of receipt thereof in the office of the Director or at some later date, if such be so specified by LESSEE therein. If the said relinquishment fails to state that no operations have been conducted, the effective date of relinquishment shall be the date the relinquishment is approved by ~~the Board~~ LESSOR.

(b) If operations have been conducted under the lease on land proposed to be relinquished, LESSEE shall give sixty (60) days notice and shall file with the Director a written relinquishment or surrender duly acknowledged and stating therein that operations have been conducted on the land. The relinquishment shall not become effective until the land and the wells thereon shall have been placed in condition acceptable to LESSOR and shall have been approved by the State Oil and Gas Supervisor. Bonding under this lease shall not be released to any party until such time as a field inspection has established that reclamation is satisfactory and complete.

All rentals and any minimum annual royalties becoming due prior to a surrender or relinquishment becoming effective, shall be payable by LESSEE unless payment thereof shall be waived by LESSOR. A relinquishment having become effective, there shall be no recourse by LESSEE and the lease as to the relinquished lands may not be reinstated.

Section 6. Governing Law and Jurisdiction. The construction, interpretation and enforcement of this lease shall be governed by the laws of the State of Wyoming. The Courts of the State of Wyoming shall have jurisdiction over this lease and the parties, and the venue shall be the First Judicial District, Laramie County, Wyoming.

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**Petroleum Association of Wyoming
Proposed State Land Lease Amendments
Committee Comments
5. 11.11**

Proposed Lease Language	PAW Comments	State Response
<p>Section 2. TERM OF LEASE. <u>Subject to the terms and conditions herein, t</u>his lease shall become effective on the day and year set out below and shall remain in effect for a primary term of five (5) years and for so long thereafter as leased substances may be produced from the lands in paying quantities. <u>“Paying quantities” is defined as gross income from lease operations, less royalties and taxes, exceeding the costs of operating the lease.</u> This lease may also be extended beyond its primary term in the absence of production of leased substances as may be provided by the statutes of the State of Wyoming and the regulations of the Board of Land Commissioners adopted pursuant thereto. Provided, however, if drilling, completion, testing or reworking operations are being diligently conducted, either during the primary term or during any extension thereof, this lease shall continue in full force and effect so long as such operations are being conducted and so long thereafter as oil or gas may be produced in paying quantities. This lease may be relinquished or terminated at an earlier date as herein provided.</p>	<p>1. Use “Paying quantities means revenues from the well or wells on the leased premises or lands pooled therewith, exceed operating expenses whether or not the costs of drilling, completing, equipping and operating may never be recovered.” Definition is paraphrased from Champion Ventures, Inc. v. Wayne H. Dunn, Jr., P.2d 724 (Wyo. 1977).</p>	<p>1. While the language offered provides useful guidance, no change is necessary. The term “paying quantities” is clear as written without any need for a specific reference to pooling or federal paying well determinations.</p>
<p>Together with the right of ingress and egress and the right to use so much of the surface of said lands as is necessary to construct and maintain thereupon all works, building, plants, waterways, roads, communication lines, pipe lines, reservoirs, tanks, pumping stations, or other facilities</p>	<p>1. Delete [or hereinafter] Can’t change the rules of the game in the middle of the game. Too much risk. It will lower bonuses paid for leases. 2. Define how Special Use Lease Status works with pooled lands or unitized lands. This is contrary to State and industry practice and is</p>	<p>1. Lessees must comply with all applicable statutory and regulatory requirements. Without taking any further position on the offered comment, we have removed the phrase “now or hereinafter in effect during the term of the lease”.</p>

<p>necessary to the proper conduct of operations there under <u>in conformance with all applicable rules and regulations of the Board of Land Commissioners now or hereinafter in effect during the term of this lease. Equipment and facilities placement on this leasehold which benefits unitized, pooled or non-State interests are subject to the Board's requirement for Special Use Lease status.</u></p>	<p>inconsistent with pooling and unitization doctrine. This is a change to the standard practice for State Lands</p> <p>3. .Special Use Leasing under Chapter 5 (d) of the OSLI Rules states: “‘Special use’ means any use of state land other than for grazing, agriculture, the extraction of minerals, or uses authorized under easements granted...” It appears language in this section is in direct conflict with the OSLI’s own Rules and Regulations</p>	<p>2. A special use on a State oil and gas lease works the same no matter the status of the leasehold and notwithstanding production sharing arrangements, be they units, pools, communitization agreements or straight leases. Where any storage, production separating equipment, conditioning or marketing-related equipment (i.e., multi-well T-Paks, compressors, injection facilities, etc.) is placed on State land surface and serves <u>non-State lease</u> production, a Special Use Lease is necessary to accommodate the <u>non-State lease</u> production. Lessees are not and have never been charged the surface use lease rate for State production.</p> <p>3. We do not recognize any conflict between the rule and the proposed lease language. Reference to “extraction of minerals” relates specifically to production-related equipment that offers benefits to the State trust land beneficiaries. Where the state realizes a direct benefit from the extraction of minerals (i.e., a royalty), the exclusions in Chapter 5(d) apply. Where the beneficiaries will not realize this sort of direct benefit from extraction, the cited rules are triggered to ensure that the use of the state surface is fully compensated and results in tangible and actual value being realized by the beneficiaries. Again, the concern is that large and potentially damaging equipment could be placed on State land, which is primarily</p>
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		<p>meant to serve <u>non-State</u> production. As such, the agency issues surface use leases on a routine basis for such uses and charges only the rate applicable to non-State lease production.</p>
<p>Section 5. This lease is issued under the authority conferred by Title 36, <u>W.S. 1977</u> as to the State and School Lands, and Title 11, <u>W.S. 1977</u> as to Farm Loan lands, and shall be subject to, and operations by LESSEE hereunder shall be conducted in compliance with the specific lease terms set out on the reverse of this lease, and with all applicable state statutory requirements and the <u>rules and regulations</u> issued thereunder, including those providing for the leasing of State or Farm Loan Lands for oil and gas; the conservation of oil and gas; and the regulation of security transactions <u>which may no or hereinafter be in effect</u>.</p>	<p>1. ‘which may or now’ add the “w”.</p>	<p>1. The comment is appreciated and addressed with the agency’s removal of the phrase: “which may no(w) or hereinafter be in effect”.</p>
<p>(a) BOND. To furnish a bond with an approved corporate surety company authorized to transact business in the State of Wyoming, or such other surety as may be acceptable to the lessor, <u>in an amount fixed by lessor, to secure the payment for any damages to the surface of the land, including livestock, crops, water wells, reservoirs, or improvements caused by lessee’s operations on the land, and to assure compliance with all the terms and provisions of this lease, including rent and royalties owed, the laws of the State of Wyoming, and the rules and regulations promulgated thereunder. Lessee shall provide such bond prior to the development of the lands contained in this lease. Such bond may be increased in such reasonable amounts as lessor may decide upon commencement of drilling and other operations, and after discovery of oil or gas, in which case lessee has sixty (60) days to post any additional bond or show cause acceptable to Lessor that a bond increase should not occur,</u></p>	<p>1. Think about the impact of “terminating” a producing lease. Need an additional or different resolution. 2. Reiterate alternative resolutions. Latest form added “or show cause acceptable to Lessor that a bond increase should not occur” or lease will terminate. Allows arbitrary lease termination. 3. 9th line “will” should be replaced with “shall”. 4. This should only apply where the State owns both the surface and the minerals and should be capped at the fair market value of the land. The split estate act covers all other situations. Chapter 18, Section 13: Provides bonds must cover: “Payment of all moneys, rents, and royalties; full compliance with all applicable statutes and terms and conditions of the Board’s <u>leas</u>es and rules and regulations; proper plugging and abandonment of all</p>	<p>1. and 2. The State has three choices when it comes to the posting of appropriate bond: (1) accept the reasoning offered by the lessee, which will not and never has been unreasonably denied in such matters; (2) if the lessee does not comply with agency directives, pull the bond that has been posted and plug and abandon the wells and restore the surface; and, (3) pursue any cost shortages not covered by bonding funds, re-sell the lease with any open well bores and sell whatever is not properly removed from the leasehold by the former lessee in the allotted time. If terminating the lease could create reservoir, downhole or other issues in the formation, the agency’s first preference would be to maintain operations through</p>

<p>or this lease will terminate. This bonding requirement does not affect any obligations pursuant to the Split Estate Act, WYO. STAT. §§ 30-5-401 - 409. Lessee may have additional bonding requirements pursuant to that Act. the penal sum as required by the current rules of the State Board of Land Commissioners, conditioned upon the payment of all rentals and royalties accruing to the lessor under the terms hereof, and upon the full compliance of all other terms and conditions of this lease and the rules and regulations relating thereto, and also conditioned on the payment of all damages to the surface and improvements thereon where the lease covers lands the surface of which has been sold or otherwise leased. Such bond or bonds furnished prior to the development of the lands contained in this lease may be increased in such reasonable amounts as the lessor may decide upon commencement of drilling operations and after the discovery of oil or gas.</p>	<p>inactive, non-productible wells, restoration of the surface; payment of all damages to the surface and improvements.” Definition does not include: livestock, crops water wells, reservoirs; however, Section 12 Surface Integrity and Minimum Reclamation does provide for proper safeguards to prevent pollution of the soil or any water, including aquifers... proper disposal of pollutants.</p>	<p>contractor/lessee use. With the show cause provision that has been inserted, the lessee and lessor have adequate tools to ensure that termination is truly a last resort. In sum, the agency has contemplated the impact of terminating a lease and made provisions for and actually employed additional and different forms of resolution for bond-related disputes.</p> <ol style="list-style-type: none"> 3. The language has been changed to “may be terminated” and, additionally, superfluous language has been removed regarding lessee obligations in a split estate status on State minerals. 4. These terms, as included, are lease terms, not rules. The agency is aware of its rules and is expanding the reference in the current lease beyond improvements to the surface to include specific liabilities potentially occurring on a parcel subject to multiple and sometimes conflicting activities on the property.
<p>(c)RENTALS/MINIMUM ANNUAL ROYALTY. Prior to the discovery of oil or gas in paying quantities to pay the lessor in advance, beginning with the effective date hereof, an annual <u>delay</u> rental of \$1.00 per acre or fraction thereof. <u>If the delay rental is not paid on or before the date it becomes due, notice of default will be sent to lessee, and an administrative handling assessment of \$1.00 per acre for the missing payment will be assessed. Lessee agrees that if the rental and any administrative handling assessment are not paid within thirty (30) days after the notice of default has been received, the lease will terminate automatically.</u></p>	<ol style="list-style-type: none"> 1. It has been questioned, but not yet answered, whether OSLI or the Board can automatically terminate a lease, as asserted in the draft lease, Section 1(c) and elsewhere, given Board Rules requiring lease cancellation proceedings, Chapter 1, Section 8. Also, with regard to the administrative handling assessment imposed by Section 1(c), Wyoming Statutes 16-4-204 (and Board Rules Chapter 17) require that all administrative fees be set by rule. 2. In the 6th line “will” should be replaced with “shall”. 	<ol style="list-style-type: none"> 1. This comment is appreciated. However, these terms are in the current lease form and will remain as terms in the lease going forward. The lease is a contract with known terms to the purchaser. Specifically with regard to rentals, the Board requires a \$1.00 per acre rental charge in its rules (reference Ch. 18, Section 6(a)). In terms of failure to pay rental amounts, the Board’s rules explicitly require lease termination (reference Ch. 18, Section 6(b)). The

After the discovery of oil or gas in paying quantities to pay ~~the~~ lessor in advance beginning with the first day of the lease year succeeding the lease year in which actual discovery was made, a ~~minimum~~ annual royalty (rental) of \$2.00 per acre or fraction thereof, unless changed by agreement or otherwise stipulated for the continuance of this lease. To maintain the lease, any deficient lease year minimum annual royalty shall be paid within ninety (90) days after the rental anniversary date of the lease as long as it is in effect. ~~Such rental so paid for any one year shall be credited on the royalty for that year.~~

~~Annual rentals on all leases shall be payable in advance for the first year and each year thereafter. No notice of rental due shall be sent to the lessee. If the rental is not paid on or before the date it becomes due, notice of default will be sent to the lessee, and a penalty of \$0.50 per acre for late payment will be assessed.~~

~~The lessee is not legally obligated to pay either the rental or the penalty, but if the rental and penalty are not paid within thirty (30) days after the notice of default has been received, the lease will terminate automatically by operation of law. Termination of the lease shall not relieve the lessee of any obligation incurred under the lease other than the obligation to pay rental or penalty. The lessee shall not be entitled to a credit on royalty due for any penalty paid for late payments of rental on an operating lease.~~

3. In the 9th line following “agreement and delete balance of sentence.
4. The Office of State Lands and Investments traditionally tells LESSEE not to send the minimum royalty payment until they forward a bill. The new language may cause a conflict with this practice.
5. Why is “Such rental so paid for any one year shall be credited on the royalty for that year” deleted?
6. Section 6 (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 rents for so long as annual royalties paid meet or exceed the required annual rental amount.” Why this is not acknowledge or addressed in lease form, is not apparent?

reference to Chapter 17 of the Board’s rules is noted; however the specific fees in Chapter 17 were established pursuant to W.S. 36-3-110, which spells out specific administrative fees for which the agency must establish fees. Delay rental is not mentioned in the exhaustive list of fees, which the director must adopt by rule pursuant to W.S. 36-3-110. Other agency rulemaking statutes, specifically W.S. 36-2-107, provide permissive rulemaking authority. The reference to W.S. 16-4-204 has no relation to the issue of delay rentals or other fees as that statute is specifically tied to the charging of fees related to public records requests, which are not at issue in conjunction with the delay rentals referenced in the comment. Pursuant to W.S. 36-6-101(c), however, the Board may issue mineral leases and, among other things, fix annual minimum rentals. With the terms of the lease being considered through formal Board action, the agency has determined that the provision is legally and otherwise supportable. Further, the cited lease provision actually inserts a degree of flexibility into the process to allow the lessee to cure the default prior to lease termination as opposed to an abrupt termination that would otherwise be required.

2. The reference to “will” and “automatically” are stricken from the lease draft and replaced with “shall” as

		<p>requested.</p> <p>3. The language in the 9th line following the word “agreement” has been removed as requested.</p> <p>4. The referenced practice is currently in place and will continue going forward. The lease language is intended to provide additional assurance to industry that leases will not be immediately terminated and, instead, the lessee will be given ample time to remedy the default.</p> <p>5. This comment is appreciated and language related to the creditability of the yearly annual production royalty against that particular year royalty has been added back to the form as it was inadvertently removed.</p> <p>6. The process of dealing with operating rentals is set through Board rules and the lease language in no way alters or detracts from the provisions contained in Ch. 18, Section 6(c) of those rules. The lease only serves to clarify the required action upon notice of deficiency from the agency.</p>
<p>(d)ROYALTIES. <u>Unless otherwise stipulated and agreed in writing,</u> the royalties to be paid by lessee are:</p>	<p>1. What is the legal basis or precedent for the compensatory royalty language in Section 1(d)? This provision comes perilously close to State Lands usurping the expertise and jurisdiction of the Wyoming Oil and Gas Conservation Commission to determine well locations and protect correlative rights.</p>	<p>1. The compensatory royalty language has been inserted to ensure that the state’s lessee protects the state’s interest. However, based on this comment, provisions have been added to reiterate the agency’s deference to the expertise and jurisdiction of the Wyoming Oil and Gas Conservation Commission. The language has also been bolstered with additional “show cause” language, allowing the lessee full opportunity to</p>

<p><u>Unless otherwise stipulated and agreed in writing, the royalties to be paid by lessee are:</u></p> <p><u>(i) On oil, one-sixth of the market value (as defined in (d)(v) herein below) of that produced, saved, and sold from said land, the same to be delivered at the wells or to the credit of lessor into the pipe line to which the wells may be connected. Lessee is solely responsible for the costs associated with putting the leased substances into a marketable condition and moving them to a marketing point. Thus, lessor's royalty is not subject to costs incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, pumping and lifting, recycling, gathering, separating, treating, dehydrating, removing contaminants, transporting the oil to storage tanks, storing as well as any marketing costs and taxes of any kind</u></p>	<ol style="list-style-type: none"> 1. "marketable condition" is being used and is not defined in the lease agreement. The state attempts to describe some of the costs that are not allowed but by using the term "marketable condition" it <u>will</u> result in litigation as this term has been grounds for litigation in several other states and with federal royalties. This term should be deleted and the state should simply identify the non-allowable deductions in the lease agreement. 2. What is the source of the definitions provided for "market value", "arms-length" and other defined terms. Unless these definitions have been adopted by statute or otherwise legally interpreted (through case law or settlements), they invite dispute. Rather than provide clarity, the draft lease language creates greater uncertainty regarding the valuation point for oil and gas royalty calculation purposes. 3. The language in Section 1(d)(i) that prohibits deduction from royalty payments the costs of "storing as well as any marketing costs and taxes of any kind" is over-broad and confusing. The WRPA includes as costs of production those costs incurred for "storing or transporting the oil to the storage tanks or the gas into the market pipeline" and does not include "as well as any marketing costs and taxes of any kind." The OS LI proposed lease form should stay consistent with §30-5-404; therefore, it should include "'Costs of production' does not included the reasonable and actual direct costs associated with the transporting the oil from storage tanks to market or the gas from the point 	<p>demonstrate its reasons to not drill an offset well.</p> <ol style="list-style-type: none"> 1. The terms "marketable condition" and "marketing point" are removed for clarity. Additionally, the non-deductible costs have been set forth in the contract language for oil and gas. Finally, additional language is added to provide assurance that the reasonable and actual costs of transportation will be allowed, as has been the past practice of the agency. 2. The definitions were crafted to provide clarity. The agency appreciates the comment, but ultimately believes that the provided definitions are appropriate and necessary. 3. The lease is purposefully crafted to exclude those deductions that are currently not allowed, including taxes and marketing costs. The reference to market pipeline is offered to accommodate industry and concerns that were previously voiced in past efforts to amend the lease form. 4. Severance, ad valorem, income and excise taxes are not, and never have been deductible. However, industry does receive a tax deduction related to the amount of royalties paid at both the State and federal level under Wyoming Revenue codes. 5. The State has always allowed the reasonable, actual costs of crude/condensate transportation, but with the caveat that "flashing"
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	<p>of entry into the market pipeline or the processing of gas in a processing plant;”</p> <ol style="list-style-type: none"> 4. The order of the language in the proposed lease changes the order and context of this wording thus creating ambiguity. More important, I believe severance taxes typically have been deemed to be a deductible cost. The proposed lease would expressly prohibit the deduction of all taxes from royalty payments. 5. Question: Oil – If price for oil has a deduct for transportation, we need to be able to pay based on what we get. Please clarify that this deduction can be passed on. 6. Replace with the Statutory language in the Royalty Payment Act. 7. For oil, introduces "marketable condition" as a limiting factor for deductions. Lessees are not be allowed a gathering deduction under this language. 	<p>condensate reduced from measurement at the lease tankage must be included initially at the wellhead volume for valuation.</p> <ol style="list-style-type: none"> 6. The agency appreciates the comment and reference to the Royalty Payment Act. However, in the estimation of the agency, the language is clear and supportable as written given the past experience of the agency. While certain provisions in the Royalty Payment Act will necessarily be included in the lease revision, other terms in the lease contract are more tailored to the circumstance of the agency to specifically address long-standing disagreements that have emanated from the existing lease terms. 7. To date, there has not been an allowance or other deduction for field gathering of oil or gas.
<p>(ii) On gas, including casinghead gas or other hydrocarbon substances, produced from said land saved and sold or used off the premises or <u>in the manufacture or processed for the extraction of natural gasoline, natural gas liquids or other products therefrom, the market value at the well of one sixth of the gas so sold or used, provided that on gas sold at the wells, the royalty shall be one sixth of the amount realized from such sale, one-sixth of the market value (as defined in (d)(v) herein below) of the gas, natural gasoline, natural gas liquids, or other hydrocarbon and non-hydrocarbon elements and compounds, including, but not limited to, inert gases, sulfur and helium so sold or used. Lessee is solely responsible for the costs associated with putting the leased substances into a marketable condition and moving them to a marketing point. Thus, lessor's royalty is not subject to costs</u></p>	<ol style="list-style-type: none"> 1. “marketable condition” is being used and is not defined in the lease agreement. The state attempts to describe some of the costs that are not allowed but by using the term “marketable condition” it <u>will</u> result in litigation as this term has been grounds for litigation in several other states and with federal royalties. This term should be deleted and the state should simply identify the non-allowable deductions in the lease agreement. 2. What is the source of the definitions provided for “market value”, “arms-length” and other defined terms. Unless these definitions have been adopted by statute or otherwise legally interpreted (through case law or settlements), they invite dispute. Rather than provide clarity, 	<ol style="list-style-type: none"> 1. The terms “marketable condition” and “marketing point” are removed for clarity. Additionally, the non-deductible costs have been set forth in the contract language for oil and gas. Finally, additional language is added to provide assurance that the reasonable and actual costs of transportation will be allowed, as has been the past practice of the agency. 2. The definitions were crafted to provide clarity. The agency appreciates the comment, but ultimately believes that the provided definitions are appropriate and necessary. 3. The lease is purposefully crafted to

<p><u>incurred for exploration, development, primary or enhanced recovery and abandonment operations, including, but not limited to, lease acquisition, drilling, testing and completion, lifting, recycling, gathering, single or multiple stage compression, separating, treating, dehydrating, removing contaminants, amine treating, glycol and methanol and chemical injection, or transporting the gas to the market pipeline, as well as any marketing costs and taxes of any kind.</u></p>	<p>the draft lease language creates greater uncertainty regarding the valuation point for oil and gas royalty calculation purposes.</p> <ol style="list-style-type: none"> 3. The language in Section 1(d)(ii) that prohibits deduction from royalty payments the costs of “storing as well as any marketing costs and taxes of any kind” is over-broad and confusing. The WRPA includes as costs of production those costs incurred for “storing or transporting the oil to the storage tanks or the gas into the market pipeline” and does not include “as well as any marketing costs and taxes of any kind.” The OSLI proposed lease form should stay consistent with §30-5-404; therefore, it should include “‘Costs of production’ does not include the reasonable and actual direct costs associated with the transporting the oil from storage tanks to market or the gas from the point of entry into the market pipeline or the processing of gas in a processing plant;” 4. Need to protect the right to use gas and oil on location royalty free, should only pay on product left after processing – shrunk gas volumes and ngl’s we get under processing contract. 5. No post production costs is a significant expense that can effectively add an additional 1-2% to the royalty 6. Use the Statutory language in the Royalty Payment Act and explain how Weighted Average Sales Price (WASP) works and does this mean all of LESSEE’s gas or just the gas from the State lease? 	<p>exclude those deductions that are currently not allowed, including taxes and marketing costs. The reference to market pipeline is offered to accommodate industry and concerns that were previously voiced in past efforts to amend the lease form.</p> <ol style="list-style-type: none"> 4. The right of use on lease exists pursuant to producing the product at the mouth of the well. To this end, the agency has provided explicit direction through its definition of “operating purposes upon the land” to guide its lessees going forward. 5. No post-production costs, except reasonable actual transportation in a marketing pipeline, (i.e., delivering to a refinery) and reasonable actual processing in a plant, without reimbursement or other reciprocity dealing beyond the initial custody transfer point is ever allowed. Even then, if the sale price is effectively at the wellhead, there should be no deduction for any movement unless the contract can be produced that reflects this pricing scheme and no reciprocity in dealing is involved. 6. The agency appreciates the comment and reference to the Royalty Payment Act. However, in the estimation of the agency, the language is clear and supportable as written given the past experience of the agency. While certain provisions in the Royalty Payment Act will necessarily be included in the lease revision, other
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	<ol style="list-style-type: none"> 4. The phrase “shall be as approved by the lessor” in Section 1(d)(iv) creates an opportunity for over-broad discretion by the Board. There have been arguments in the past that in certain circumstances, this language overrides more specific lease language establishing certain royalty percentages. 5. Lessor to approve of “value” – No! How does that work? Requires clarification and further comments. 6. The new lease language requires processing allowances exceeding 50% to be approved in advance by Wyoming. The historical standard utilized is a 662/3% which is the MMS Standard. 7. If the State wants this provision, then why not agree to adopt all royalty payment provisions within federal leases. 8. Confusing, requires clarification and further opportunity to comment. 9. It is not clear how new market value definition would be administered by the State of Wyoming or Lessees for transactions negotiate “at a price not consistent with the prices received for like quality production,” leading to lease administration uncertainty from both the perspective of lessor and lessee. 	<p>accommodation of the concern, however, the original reference to “two-thirds (2/3rds) of the amount or value” of natural gas liquids will be reinstated in the lease.</p> <ol style="list-style-type: none"> 2. The agency appreciates this clerical correction comment and the suggested change has been made. 3. To address this comment, language has been added to clarify the agency’s intent with regard to such price determinations. 4. The cited approval process is currently and has historically been in the existing lease form. Further, the language has no bearing on royalty rate percentages, and instead only relates to reasonable valuation in a less than transparent environment. 5. The cited approval process is currently and has historically been in the existing lease form. How the value “approval” process works is that the lessor examines value and if that value is not generally consistent with the values being received for like production, then additional assurance as to the appropriateness of the value, will be sought through audit review. 6. This language was changed to reinstate the original two-thirds (2/3rds) processing allowance language into the lease as requested. 7. The agency has been careful to tailor the lease form to state needs and considerations. As such, a wholesale adoption of the federal lease will not be
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		<p>recommended to the Board.</p> <p>8. The language is clear to the agency and has been refined in efforts to add clarity.</p> <p>9. The price caveat means that the office will review its weighted average price for all production sold of a like type from the geographic basin and if the price questioned is below that number (by a factor 10% or greater), further examination will be completed through an audit to ensure that appropriate value is being received by the trust beneficiaries. Further, concerns related to the definition of market value have been addressed through additional clarifying language.</p>
<p>(v) <u>“Market value” is defined as the sales price received by lessee for production in merchantable condition, including all premiums and consideration in whatever form and at whatever time, unless such production is sold pursuant to a non-arm’s length transaction or at a price not consistent with the prices received for like quality production. In such case, “market value” shall be defined as the highest arm’s-length price, including all premiums and consideration in whatever form, regardless of time and place, for like quality production in merchantable condition at a recognized market.</u></p>	<ol style="list-style-type: none"> 1. The language is “not consistent with prices received for like quality production” sets no standard at all. The language establishing “market value” for a non-arm’s length sale would apparently establish a standard as the highest price received in any world market. There is no basis in law or policy for this proposed valuation. 2. Use the Statutory language in the Royalty Payment Act and explain how WASP works and does this mean all of LESSEE’s gas or just the gas from the State lease? Additionally a transport reimbursement is a double dip-LESSEE cannot deduct the cost of transport from tanks to sales point but will have to pay additional royalty if purchaser reimburses the cost to transport. 	<ol style="list-style-type: none"> 1. The definition has been refined to further clarify the “market value” for a non-arm’s-length sale and to specifically narrow the comparable sales area that will be used for determinations under this subsection to “the same general area or market hub.” 2. The agency appreciates the comment and reference to the Royalty Payment Act. However, in the estimation of the agency, the language is clear and supportable as written given the past experience of the agency. While certain provisions in the Royalty Payment Act will necessarily be included in the lease revision, other terms in the lease contract are more tailored to the circumstance of the agency to specifically address long-standing disagreements that have

		<p>emanated from the existing lease terms. WASP means the weighted average price the State receives across the board for like gas. Further, Section 1 (d) (vi) has been edited to once again reflect the language related to operating purposes and secondary recovery and define “operating purposes upon the land.”</p>
<p>(vi) Natural gas and oil actually used for operating purposes upon the land and, except as to the ultimate sale thereof, gas or liquid hydrocarbons returned to the sand for stimulating the production of oil or secondary recovery purposes to effect recovery of downhole effluent at the mouth of the well(i.e., <u>reinjection to maintain reservoir pressure or create natural production drive enhancement and/or fueling a pumping unit</u>) shall be royalty free. <u>Any use other than this is not deductible for royalty calculation purposes.</u></p>	<ol style="list-style-type: none"> 1. Paying comp royalties under this provision will require obtaining volumes from the State, and monitoring 3rd party wells from State information; much of this information is 60-90 days in arrears. If the intent is to mirror the federal lease comp royalty provision, the State should at least allow that lessee can prove why drilling a well is not economic. 2. The wording implies that the State can dictate if a well is to be drilled without regard to lessee’s economic parameters. Lease termination for failure to comply is too onerous. An operator may have multiple millions of dollars invested in drilling a lease with even greater value in proven reserves on the books as a result of its’ investment efforts and be subject to losing all for failure to comply with this provision. 3. The deletion of the original language “for operating purposes upon the land...or secondary recovery purposes” is not supported by statute nor the OSLI’s rules and regulations. This language should be reinserted. It is totally unreasonable not to have natural gas and oil that is used for lease operations royalty free. While “Costs of Production” include compressing and other uses of natural gas and oil as a charge that cannot be assessed against the Lessor’s royalty, it does not preclude natural gas and oil used for 	<ol style="list-style-type: none"> 1. The agency believes that this comment is actually related to Section 1(d)(ix) and not the subsection cited at left. Assuming so, language has been added to reflect a show cause process not to drill, in addition to other protective language. If the State makes a demand under this provision of the lease, it will be incumbent upon us to monitor and provide the offset production information, which can be checked by our lessee against the Oil and Gas Conservation Commission information. 2. The agency believes that this comment is actually related to Section 1(d)(ix) and not the subsection cited at left. Assuming so, show cause language has been added regarding the economics of drilling the State offset. As such, monetization of acreage and reserves should not be hindered unless the show cause or drilling requirements are not met. 3. The referenced deleted language has been reinserted. Further, a definition of “lease operating purposes” and “operations upon the land” has been provided. The agency is willing to

	<p>lease operating purposes from being royalty free. Such use is for the benefit of the Lessor.</p>	<p>concede that measured gas used to fire a separator belonging to the State's lessee and not some affiliated or other third party, is potentially a use as operations upon the land. But separation of effluent would be the limit, and no uses pursuant to processes used to move the production off-lease/marketing would be allowed.</p>
<p><u>(vii) If lessee receives any compensation for any function, process or liability related to production from this lease without the right given herein to deduct the costs related to such compensation, such compensation amount shall be added to the market value for such production type and royalty must be computed and paid thereon at the lease royalty rate.</u></p>	<ol style="list-style-type: none"> 1. Clarification is needed on "to effect recovery of downhole effluent"? How is the lease use gas going to be measured/segregated for reporting purposes? 2. Transport reimbursement is a double dip- LESSEE cannot deduct the cost of transport from tanks to sales point but will have to pay additional royalty if purchaser reimburses the cost to transport. 	<ol style="list-style-type: none"> 1. The agency believes that this comment is actually related to Section 1(d)(vi) and not the subsection referenced at left. Assuming so, appropriate accounting for lease production, to include gas would start with a wellhead meter and if production was used downstream of the wellhead, it would need to be metered. There is a reference for operation levels and gas consumed in firing a separator or engine on a pump-jack. Language has been added to allow on-lease production to be used for firing a separator. 2. The cost of reasonable, actual transportation beyond the storage tanks is deductible, but if it is reimbursed, then the royalty will be due on the receipt amount as a total number.
<p><u>(viii) Interest shall accrue and be payable on all royalty obligations under this lease at the rate of eighteen percent (18%) per annum. Interest shall accrue and be payable without necessity of demand from the date each such obligation shall arise. The accrual and payment of interest does not constitute waiver or satisfaction of any penalty that</u></p>	<ol style="list-style-type: none"> 1. Industry does not pay interest until accessed by the agency. Even though some agencies have provided the ability for a company to report and pay interest upfront, companies have opted to not report and pay and wait until they are invoiced by the agency. Most companies claimed hardship when the 	<ol style="list-style-type: none"> 1. This language will not be changed, as, in the agency's view, the system will provide an up-front accounting of any interest due monthly and if from audit, that amount will also be calculated. 2. The first payment for royalty is due on the current 30 days for oil and 60 days

<p><u>may apply under the rules and regulations of the Board of Land Commissioners now or hereinafter in effect during the term of this lease.</u></p>	<p>ONRR/MMS attempted to require companies to report and pay interest on their reports and the ONRR/MMS calculates and assesses interest on most if not all companies. The language <i>"Interest shall accrue and be payable without necessity of demand from the date each such obligation shall arise."</i> needs to be deleted as industry would not be able to comply.</p> <ol style="list-style-type: none"> 2. Need clarification on when first payment is due, within how many months after well is completed and when is it considered late on a monthly basis? 3. What if a lessee also owns the gathering system; further, that lessee charges some other WIO/lessee to gather the other lessee's gas. It would seem that this provision would have the gatherer pay royalty on the fee paid by the other lessee. 4. Move this section to Section 1 (g) Page 2. 5. The interest charge is very high at 18%. Also, it does not cover interest on overpayments. 	<p>for gas after the end of the first sale month. Clarifying language has been added in this regard to Section 1(d)(viii).</p> <ol style="list-style-type: none"> 3. Regardless of who owns and charges what for gathering, the cost is not and has not historically been deductible. If the lessee, through another company owns the gathering laterals and charges other state lease working interests for that service, it has no bearing on the state's royalties. Gathering, in itself, cannot be taken as a deduction and payment for such gathering is not a part of operations which are in essence reimbursed to the charging party. Payment of royalty is not expected for collection on a service charge when the service provider is the state's lessee. 4. The agency appreciates the comment, but the section will remain as currently placed. 5. The interest charge is consistent with the Wyoming Royalty Payment Act. Interest is not paid, nor is such a payment required of lessee, on overpayments. However, in calculating interest due, if the State receives an overpayment during the calculated period, the overpayment will be directly offset against calculated interest.
<p><u>(ix) If during any period of non-production from this lease, any production is sold from offsetting acreage from any well closer than six-hundred sixty feet (660') in any direction from</u></p>	<ol style="list-style-type: none"> 1. Clarification is needed on when first payment is due, within how many months after well is completed and when is it considered late on a 	<ol style="list-style-type: none"> 1. The agency believes that this comment is actually related to Section 1(d)(viii) and not the subsection referenced at left.

<p><u>the lease line, the right to continue this lease will be satisfied only by the payment of compensatory royalty in the amount of one-half (1/2) the volume of the offset well at market value, at the lease royalty rate. Further, offset production may not continue greater than one-hundred eighty (180) days in paying quantities as sold from the offset well without lessee beginning the drilling of a lease offset hereon; or, providing geological, reservoir and financial information satisfactory to Lessor that the drilling of any specific offset on this lease will be un-economical pursuant to recovery of the drilling, completing, testing, equipping and producing costs associated with this lease over the life of the lease and the estimated ultimate recoverable reserves associated with the leasehold. It is agreed that failure to comply with this requirement will be cause for termination of this lease unless lessee can demonstrate to the satisfaction of lessor that no drainage could occur from such offset well or any offsetting well at distances greater than six-hundred sixty feet in any direction from this lease line boundary.</u></p>	<p>monthly basis?</p> <ol style="list-style-type: none"> 2. In the 2nd line from the end, place a period after “well” and delete the balance of the sentence. 3. Is this a surface location or a bottom hole location for directional wells. Horizontal wells where the lateral enters the target horizon. There needs to be clarification of the specifics. 4. The Wyoming Oil and Gas Conservation Commission is charged with preventing waste and protecting correlative rights and; therefore, it establishes drilling and spacing units and setbacks for natural gas and oil wells in order to accomplish its goals. In that regard, the OSLI should not be establishing a “blanket” well density for compensatory royalty and should tailor this provision to reflect the statutory authority of the WOGCC. In that regard such language should be amended to: <u>“If during any period of non-production from this lease, any production is sold from a well in an offsetting an approved WOGCC spacing or drilling unit as established under Chapter 3 of the WOGCC rules and regulations, the right to continue this lease...”</u> 5. Some operators have requested and received approval from the Wyoming Oil and Gas Conservation Commission to drill wells anywhere within a section with entry into the formation no closer than 330’ with perforations no closer than 660’. Under the proposed amendments to the lease form, where operators are allowed to drill any Niobrara or Frontier well on Federal or Fee acreage adjacent to a State of Wyoming tract under the new lease form, they would have an immediate obligation 	<p>Assuming so, the first payment for royalty is due on the current 30 days for oil and 60 days for gas after the end of the first sale month. If not paid within these timeframes, it is considered late. Specific language has been added to further clarify these timeframes.</p> <ol style="list-style-type: none"> 2. The agency agrees with this comment and the change has been made. 3. If the reference is to drainage concerns, the answer to the question that has been posed is the bottom-hole location or the further most point in a horizontal leg offsetting the State acreage. 4. The language is not intended to interfere in any manner with the rules and regulations of the Oil and Gas Conservation Commission related to spacing. The provision simply establishes an offset distance from a state lease that is considered close enough to require show cause that there is no drainage. Note that a show cause allowance has been inserted, in addition to an express statement of deference to the Oil and Gas Conservation Commission’s regulatory process. 5. As stated above, the provision simply establishes an offset distance from a state lease that is considered close enough to require show cause that there
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	<p>to drill an offset well or be required to pay compensatory royalty. Termination of the lease could result from not drilling an offset well on the State tract.</p>	<p>is no drainage. Note that a show cause allowance has been inserted, in addition to an express statement of deference to the Oil and Gas Conservation Commission’s regulatory process.</p>
<p><u>(x) The Wyoming Royalty Payment Act, WYO. STAT. §§ 30-5-301 through -305 shall apply and govern the interpretation of this lease to the extent those statutes are not in conflict with any of the provisions of this lease.</u></p>	<ol style="list-style-type: none"> 1. Does this provision refer to “lost” production? We must make sure it does not apply to Shut-in production. 2. Royalty valuation will continue to be problematic with the new lease agreement. Gas post production costs will be an issue with Wyoming’s new lease agreement since current process is deducting transportation cost between wellhead and main transmission pipe. The new lease language appears to prohibit transport cost upstream of the main transmission pipe. 3. This section should be amended to: The Wyoming Royalty Payment Act, Wyo. Stat. §§ 30-5-301 through -305 and Chapter 18 of the OSLI Rules and Regulations shall apply and govern the interpretation of this lease. If the express provisions of the oil and gas lease are in conflict, then those provisions should go through rule making versus adopted under a “lease revision.” 	<ol style="list-style-type: none"> 1. The agency believes that this comment is actually related to Section 1(e) and not the subsection referenced at left. Assuming so, shut-in production is a process that, when allowed by the agency, will not relate to lost production. Lost production, in the view of the agency, relates to a significant difference reported as well head volume versus a sale volume for which there is no explanation of the differential in those volumes. 2. The State is not knowingly allowing any “transportation” deduction between the wellhead and the main transmission pipe. Such a deduction has not been allowed in the past and will not be allowed going forward. 3. The Board of Land Commissioners is permitted to issue mineral leases pursuant to W.S. 36-6-101(c), with no apparent requirement to undertake rulemaking to accomplish this end. Implicit in this statutory allowance is the power to revise those lease terms as the Board deems necessary. However, based on the comment, the language has been modified to clarify the agency’s intent with regard to the Wyoming Royalty Payment Act.

<p>(e) DISPOSITION OF ROYALTY OIL AND GAS. To deliver to the lessor, or to such individual, firm or corporation as the lessor may designate, all royalty oil, gas, or other kindred hydrocarbons, free of charge on the premises where produced, or, at the option of the lessor, and in lieu of said royalties in kind, the lessee agrees to pay the lessor the field market price or value of all royalty oil, gas, or other kindred hydrocarbons produced and <u>wasted, or saved and sold, unless otherwise stipulated.</u></p> <p>When the lessor elects to take its royalty oil, gas, or other hydrocarbons in kind such as oil, gas, or other kindred hydrocarbons shall be good merchantable oil, gas, or other kindred hydrocarbons. The Lessee shall, if necessary, furnish storage for royalty oil free of charge for thirty (30) days after the end of the calendar month in which the oil is produced, upon the leased premises, or at the such place as the lessor and the lessee may mutually agree upon, provided, that the lessee shall not be held liable for loss or destruction of royalty oil so stored from causes beyond his control.</p> <p>The free storage of oil, as herein provided, shall apply only as long as the said oil is the property of the lessor.</p>	<ol style="list-style-type: none"> 1. What is the definition of “wasted”? Here again, the opening “unless otherwise stipulated” arguably is outside legal authority, is vague and creates an unlevel play field for state lessees. 2. What is the interplay between this language and the language in d) i) and ii) about the lessee having to transport the product to a "marketing point" free of transportation costs to Lessor? For example, if gas is sold at the lease to a third party, does State Lands intend to collect royalty (from Lessee, not Buyer) on the transportation expense incurred by the Buyer to take the gas to a "marketing point"? 	<ol style="list-style-type: none"> 1. In the view of the agency and based on its understanding of industry practice, “wasted” means product which is flared or vented without approval of the Board to do so on a royalty free basis regardless of any other agency’s allowance of disposition of production other than through sales. The reference to “unless otherwise stipulated” relates to the Board’s permissive grant of royalty-free disposition. However, pursuant to this comment, clarifying language has also been added to the lease. 2. The agency’s intent is to reiterate that gathering costs and compression are not allowable deductions, and if a sale is truly at the wellhead, then no cost deductions should be taken against the production.
<p>(f) MEASUREMENTS OF PRODUCTION. To <u>meter, gauge, measure and correct for temperature</u> all production from said lands in conformance with <u>the methods and time intervals accepted as standard industry practice and</u> the rules and regulations adopted by the Board of Land Commissioners and report said production to the lessor in accordance therewith.</p> <p>To keep books, records, <u>charts, invoices</u> and reports pertaining to the production from the land herein leased as</p>	<ol style="list-style-type: none"> 1. Wyoming places an unrealistic burden to provide this supporting information on a monthly basis. Every time the terms "<i>To furnish lessor</i>" are used, it should be changed to "<i>To furnish lessor upon request</i>". 2. It is already unrealistic to provide all this information in the original form received each month, but even more so if it has to be provided in the format prescribed by lessor. At a minimum the newly added sentence "<i>Further</i> 	<ol style="list-style-type: none"> 1. The agency already requires support media under the current lease form and pursuant to Board rules. The required support documents have traditionally been the copies of information that lessees and operators receive or distribute based on monthly production in their normal course of business. 2. As referenced above, support media will continue to be required as directed in the

<p>well as those pertaining to the production from offset wells operated by the lessee, his operator, or sub-lessee on other lands, which shall be opened at all times for the inspection of any duly authorized agent of the lessor.</p> <p>To furnish the lessor with <u>all pertinent original transporter and/or pipe line and processor statements/reports</u> showing the day, month, year, amount, gravities, and temperatures <u>and pricing</u> of all oil run and with monthly reports showing the day, month, year, amount (<u>volume</u>), <u>gas BTU</u>; and, price of all gas <u>natural gas liquids and/or</u> and natural gas gasoline and other products produced and sold from the land herein leased, and the amount of gas <u>and/or natural gas liquids or oil/condensate</u> returned to the sand <u>for production purposes</u>. <u>To furnish lessor with original sales reports showing the month, year, amount, gravity, BTU, temperature and price per unit of sales and by product, for all products sold from the lease or from interest within which this lease shares by any form of unit or pooling arrangement. Further lessee agrees to furnish all other volume and valuation information in the form prescribed by lessor.</u></p>	<p><i>lessee agrees to furnish all other volume and valuation information in the form prescribed by lessor"</i> needs to be deleted.</p> <ol style="list-style-type: none"> 3. Why would the State want "day" information on the monthly reports. Monthly reports are based on end of month volume measurement. If they are looking specifically for metered or SCADA info during an audit, then we would be able to produce that. The additional requirement to provide daily sales data would be a huge burden on industry. 4. What if there is a conflict between methods and time intervals established as standard industry practice by the American Gas Association and or the American Petroleum Institute. 5. The additional requirement to provide daily sales data would be a huge burden on the oil and gas industry. 6. Much of the data requested in this Section on a monthly or daily basis is data that is normally provided during an audit. The entire last 2 paragraphs need to be reworked. 7. Please explain the word "sand" at the end of the 2nd to last paragraph. 8. How is WASP going to be handled in this section? 9. Wyoming places an unrealistic burden to provide this supporting information on a monthly basis. The data requirements are unduly burdensome on LESSEES. Additionally many of those same documents are not used by the State on a monthly basis and are then re-requested during audits of royalty." 	<p>current lease form and as proposed in the draft lease contract.</p> <ol style="list-style-type: none"> 3. The "day" information is currently requested in the State's lease. 4. The agency does not know if this is intended as a hypothetical question – and if so, it cannot be answered. If the commenting party knows of pertinent reasons to resolve the question, those reasons will have to be supplied in order for the agency to appropriately respond to the comment. 5. The information is currently and has historically been required as a function of both lease and rule for many years. 6. Pursuant to the comment, the lease language has been modified to add clarity. 7. "Sand" is a term that was used in the old "Producer 88" form, which the State's current lease parrots in terms of the cited language. The agency's intent was to reference the producing horizon/zone and the language has been amended accordingly. 8. Any weighted average prices employed at any point in determining lease volume valuation will relate to the State's receipted weighted average price received for like production (in terms of type and condition) moving through the same general sales point (i.e., at Glenrock for CBM and plant volume sales based on total State volumetrics). 9. The agency does, in fact, make use of the supplied information to examine the
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		<p>veracity of lease royalty payments. The media received to date has actually served to reduce the need for a number of audits and audit team visits.</p>
<p>(g) MONTHLY PAYMENTS AND STATEMENTS. Unless the time of payment is otherwise extended by the Office of State Lands and Investments to make payment on or before the twentieth (20th) last day of the calendar month succeeding the month of production and removal and sale of oil and gas from said <u>the leased land</u>; and, to <u>make payment on or before the last day of the second calendar month succeeding the month of production and removal and sale of gas, and to furnish sworn monthly operator and payer production and royalty statements</u> therewith showing in detail the quantity and quality of the production (per well if required where practical) from the land hereby leased, and the quantity and quality of the production (per well where practical) from offset wells upon cornering or contiguous land operated by the lessee, his operator or sub-lessee and such other information as may be called for in the form or report prescribed by lessor. <u>Failure to submit timely the lessor-required reports and reporting documents will result in a penalty assessment against lessee of \$100 per lease, per report, per month or fraction thereof. Non-submission, and continued incorrect/untimely/improper reporting will result in lease cancellation upon written notice of lessor given.</u></p>	<ol style="list-style-type: none"> 1. Because of how industry reports their royalties to the state, the proposed penalty provision could result in an unrealistic amount of penalties. Some type of cap like "not to exceed \$5,000 per month" needs to be added to ensure the penalties assessed are appropriate. 2. Delete "Failure to submit timely the lessor required reports and reporting documents will result in a penalty assessment against lessee of \$100 per lease, per report, per month or fraction thereof. Non-submission, and continued incorrect/untimely/improper reporting will result in the lease cancellation upon written notice of lessor given." Covered under the Wyoming Royalty Payment Act referenced in (d)(x) above. 3. Current payments are made 60 days after production for oil and gas. The new form requires oil payment to be within 30 days and gas payment within 60 days. Both oil and gas should be required to be paid within 60 days. It would be very difficult and burdensome for operators' processes and systems to make this change. 4. The last statement in section (g) states "and such other information as may be called for in the form of report prescribed by Lessor." This statement is too open ended and allows for request for data and reports that are not 	<ol style="list-style-type: none"> 1. The penalty provision is drawn from the Wyoming Royalty Payment Act and has been crafted to also reflect the recent precedent set forth in <u>Morris v. CMS Oil and Gas</u>, which can be found at 227 P.3d 325. 2. The agency generally agrees that the language is covered by the Wyoming Royalty Payment Act. However, industry has, in repeated instances, questioned the agency's assessment of these penalties, specifically challenging how the penalty was calculated. In the wake of <u>Morris v. CMS Oil and Gas</u>, which can be found at 227 P.3d 325, the agency sought to be absolutely clear in how it intends to assess the penalties under this section of the lease. 3. The agency appreciates the comment and the desire to unify the timeframes set forth in the lease. However, the procedure will not be changed through this lease revision from what has been the policy of the agency for many years. Oil and lease condensate have always been due on a 30 days after the month of production and sales basis. The change is merely to reflect that the agency is now moving to the use of the term "calendar month" as relates to the relationship between production, sales and reporting.

	<p>generated or used in various transactions. We would like to see the phrase “where practical” added to the statement. The expectation is that this phrase will allow for different ways that companies do business and how they document sales, especially in terms of sales to affiliated companies. That phrase is used in other statements within this section as well.</p> <ol style="list-style-type: none"> 5. Language was added that allows termination of lease for failure to furnish incorrect/untimely/improper reports. Not acceptable 6. There should be no lease termination for royalty payment issues since there are other remedies available to the State. 	<ol style="list-style-type: none"> 4. Certain amendatory language has been supplied to help alleviate the concerns raised in the comment. The agency has been and will continue to be more than willing to ensure that the information that is called for under this lease section is not requested in a frivolous manner or form that is impractical for the lessee to supply. 5. A show cause provision has been added to the lease, in addition to the amending of the phrase “will result in lease cancellation” to now read “may result in cancellation.” However, absent the ability to terminate the lease, forcing compliance with this section has proven difficult. Even in the face of escalating penalty assessments, only threatened termination has been sufficient to affect lessee compliance in some very recent cases. As such, the agency believes that the ability to terminate the lease must be retained in the lease contract going forward. 6. While termination is admittedly a severe remedy, it is necessary. The agency agrees that there are other remedies available to the state, and those will be employed to attempt to affect lessee compliance. To this end, a show cause provision has been added to the lease, in addition to the amending of the phrase “will result in lease cancellation” to now read “may result in cancellation.” However, absent the ability to terminate the lease, forcing compliance with this
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		<p>section has proven difficult. Even in the face of escalating penalty assessments, only threatened termination has been sufficient to affect lessee compliance in some very recent cases. As such, the agency believes that the ability to terminate the lease must be retained in the lease contract going forward.</p>
<p>(h) WELLS TO BE DRILLED. To drill and operate effectively all wells necessary to reasonably offset wells upon, and production from, adjoining lands <u>as directed in Section 1 (d) (ix) hereof</u>. To drill such additional wells at such times or places as are necessary and essential to the proper development and commercial production of the oil and gas content of said land.</p>	<p>1. NO! Development must be at the discretion of the Lessee.</p>	<p>1. This language has historically been contained in the lease form and will continue to be included going forward. Certainly, the discretion of the lessee to develop must be retained, but the state must be able to ensure full development of the leasehold. Given the agency's historical treatment of lessees under this provision and with the addition of show cause provisions throughout the document, the concerns raised in the comment should be alleviated.</p>
<p>(j) PRODUCTION. To operate the wells upon the land herein leased in a competent and efficient manner in an endeavor to recover <u>and deliver for sale</u> all the oil, <u>and</u> gas, <u>natural gas liquids/natural gasoline and salable production-associated non-hydrocarbons</u> economically possible from said land and to prevent the under drainage of the oil and gas thereunder by wells operated by the lessee or others on cornering or contiguous lands to those leased herein <u>as directed in Section 1 (d) (ix) hereof</u>. All plans or methods for the purpose of stimulating or increasing production on lands herein leased other than those in common use shall first be presented to the lessor for approval before being put into actual operation.</p>	<p>1. Has sufficient thought been given to the likelihood that imposing requirements to develop non-hydrocarbons of value (Section 1(j)) may chill interest in state oil and gas leases? 2. In the last sentence it should read "having first been obtained" Also why this requirement for well suspensions if the lease is committed to a producing, secondary or tertiary unit and the State is receiving royalty and the balance of the wells are active.</p>	<p>1. There is no requirement under the lease to develop or produce any hydrocarbon or non-hydrocarbon where there is not a practical economic reason to do so, (i.e., produce at a paying quantity). 2. The comment is appreciated and the suggested change has been made.</p>

<p>No production agreements <u>or decisions</u> limiting, restricting, prorating, <u>shutting-in or temporarily abandoning any well on this lease</u>, or otherwise affecting the natural production from said land shall be entered into by the lessee, nor shall the lessee limit, restrict, or prorate, <u>shut-in or temporarily abandon any well on this lease, nor prorate</u> the natural production from said land in any way or in any event, except with the consent in writing of the lessor first had an obtained.</p>		
<p>(k)SUSPENSION OF OPERATIONS. Should any well drilled upon lands covered by this lease obtain production of oil, gas, or other hydrocarbons in paying quantities and if the lessee is unable to establish a satisfactory market for the oil, gas or hydrocarbons produced from said well, <u>or, should any well drilled upon lands covered by this lease require de-watering or stimulating</u>, the lessee may apply for and the lessor may grant permission for the suspension of production operations <u>from the well and/or the lease</u> until such times as a satisfactory market for the product from said well <u>or lease</u> can be developed. <u>Such grants of suspension shall be approved by lessor for periods of no greater than one year without lessee's additional petition therefor.</u> During the time any such suspension of operations is in effect, the lessee shall continue to pay the annual <u>royalty</u> (rental) of \$ 2 <u>3</u>.00 per acre or fraction thereof provided by (c) above <u>for the first such suspension, and thereafter, as directed by lessor upon approval of suspension,</u> and this lease shall remain in effect as though oil or gas was being produced from said lands.</p>	<ol style="list-style-type: none"> 1. Language needs to be added and clarified on how a suspension will affect the lessee and more importantly how it will affect the term of the lease. 2. The payment amount is inconsistent with Section 1 (a) leave the amount at \$2.00. 3. Requires operators to secure a suspension of operations for stimulation and/or dewatering. I do not understand this requirement when Section 2 (Term of Lease) states that the lease is in full force and effect whendrilling, completion, testing or reworking operations are being diligently conducted..... 	<ol style="list-style-type: none"> 1. The requested language is addressed in the rules of the Board of Land Commissioners. The lease directly indicates what will occur during a period of suspension. 2. The comment is appreciated and the suggested change has been made. 3. De-watering is not considered for purposes of holding the lease. Producing, drilling, completing, testing and re-working are considered for these purposes. This lease provision is the agency's attempt to add clarity to its suspension requirements and processes.
<p>(n)ASSIGNMENTS OF LEASE-PRODUCTION AGREEMENTS. Not to assign this lease or any interest therein, nor sublet any portion of the leased premises, except with the consent in writing of the lessor first had and</p>	<ol style="list-style-type: none"> 1. Replace "believe" with can "demonstrate". 2. This provides the State with discretion that ultimately dictates how a company conducts its business. From an industry standpoint if 	<ol style="list-style-type: none"> 1. The comment is appreciated. The agency will replace the word "believe" with "determine." 2. To be sure, no reasonable conveyance will be disallowed by the agency.

<p>obtained. <u>Lessor reserves the right to refuse approval of any assignment of any interest in this lease, including over-riding royalty interests should lessor believe such assignment would be to the detriment of proper and timely lease development.</u></p> <p>All overriding royalties to be valid, must have the approval of the Board or by the Office of State Lands and Investments when authority to do so has been delegated by the Board and will be recorded with the lease. The Board reserves the right of disapproval of such overriding royalties when in its opinion they become excessive and hence are detrimental to the proper development of the leased lands.</p>	<p>consent is required it is also typically stated that it will not be unreasonably withheld.</p> <p>3. The denial of an assignment of any nature should be subject to a hearing for the assignor and assignee to present the case for approval.</p>	<p>However, based on this and other comments, language has been added to explicitly indicate that consent will not be unreasonably withheld. Further, with the change noted in comment 1. above, lessor must “determine” that the assignment would be to the detriment of lease development.</p> <p>3. No reasonable conveyance will be disallowed by the agency. However, based on this and other comment, language has been added to explicitly indicate that consent will not be unreasonably withheld. Further, with the change noted in comment 1. above, lessor must “determine” that the assignment would be to the detriment of lease development.</p>
<p>General Comments:</p>	<ol style="list-style-type: none"> 1. Encourage them to review the form more closely to capitalize all references to “Lessor” and “Lessee” throughout the document as they were not consistent. I also caught a typo on the first page, Section 5, the last phrase should say “which may now” rather than “which may no”. 2. With the removal of “Oil and Gas Terms” at the top of Page 2 please renumber the Sections in a consecutive manner. 3. LESSOR AND LESSEE are defined terms however they are not in all caps starting on Page 2. 4. Inconsistencies between language in the lease and the Wyoming Royalty Payment Act (WRPA), particularly with regard to the definition of nondeductible costs of production. These inconsistencies create ambiguity and will 	<ol style="list-style-type: none"> 1. The comment is appreciated and the suggested changes have been made. 2. The comment is appreciated and the suggested changes have been made. 3. The comment is appreciated and the suggested changes have been made. 4. The agency appreciates the comment and reference to the Royalty Payment Act. However, in the estimation of the agency, the language is clear and supportable as written given the past experience of the agency. While certain provisions in the Royalty Payment Act will necessarily be included in the lease revision, other terms in the lease contract are more tailored to the circumstance of the agency to specifically address long-

	<p>likely lead to future litigation. I also question whether it is sound policy for the state to assert protection under the WRPA, yet apparently “cherry pick” the application of certain WRPA provisions/language while customizing other lease language to expressly modify/override other WRPA provisions.</p> <ol style="list-style-type: none"> 5. The apparent desire to incorporate certain statutory and/or Board of Land Commissioners Rules language into the lease. I question the necessity of importing requirements that already exist in statute and rule. I am concerned that where variations in the language of the lease and governing statutes and rules occur, it will result in unintended consequences, not the least of which is litigation to resolve ambiguity. Apparent attempts to modernize and clarify certain lease language has resulted in additional ambiguity, in part due to poor drafting. The proposed additional language at the end of the first paragraph regarding special use lease requirements is just one example. 6. The additional proposed bond amount “to secure the payment for any damages to the surface of the land” doesn’t appear to take into account surface impact payments negotiated between the state’s grazing lessee and the oil and gas lessee. How will a bond to secure surface damage payments be integrated with any surface use agreement obligations to the surface lessee? In few, if any, cases does the state own the livestock, crops, wells and other improvements covered by the bond. Can the state demand bonding for the benefit of potential damages to a third party’s property? 7. How can state lease royalties be “otherwise 	<p>standing disagreements that have emanated from the existing lease terms.</p> <ol style="list-style-type: none"> 5. The agency has endeavored to minimize conflict and resolve ambiguity throughout the lease form, including through the inclusion of the Special Use Lease provision, which was singled out. Where the agency deemed it necessary, rule and statutory language has been inserted. Elsewhere, it has been removed or not inserted. In each instance, the decision to include or exclude language was deliberately made. 6. Surface impact payments are required and applied under a completely different premise than a bond. A bond is in place to cover multiple contingencies that have not yet occurred, where a surface impact payment is meant to compensate for defined impacts to the surface. 7. Basically, this language would only apply where the agency might take action to reinstate a lease that the lessee had mistakenly or unwittingly allowed to lapse. The premise behind the language is to generally endorse a process similar to the federal lease reinstatement procedure and aid the state’s lessees. 8. The agency appreciates the comment and reference to the Royalty Payment Act. However, in the estimation of the agency, the language is clear and supportable as written given the past experience of the agency. While certain provisions in the Royalty Payment Act will necessarily be included in the lease revision, other
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	<p>stipulated and agreed in writing”? What would this do to the lease auction process? Legal authority for this provision may be lacking. At the very least it implies the possibility of favoritism outside the public auction process.</p> <p>8. During a meeting with OSLI staff, staff advised that several changes to the lease form were being made to be consistent with Wyoming Statute §30-5-301 thru §30-5-305; however, as stated above there are several changes that are not consistent with Wyoming Statute and the OSLI Rules and Regulations. In this regard, the OSLI would be better served to refer the applicable statute and rules and regulations versus OSLI staff interpretations.</p> <p>9. In all instances where the discretion of Lessor is invoked, the word “reasonable” should be inserted in order to ensure an objective, rather than subjective, standard will govern any administrative appeal or judicial action resulting from a decision by the Lessor. Examples include:</p> <ul style="list-style-type: none"> a. Section 5(a) “such other surety as may <u>reasonably</u> be acceptable to LESSOR”; b. Section 5(a) “post any additional bond or show cause <u>reasonably</u> acceptable to LESSOR” c. Section 5(d)(iv) “the value shall be as <u>reasonably</u> approved by LESSOR” d. Section 5(d)(ix) “demonstrate to the <u>reasonable</u> satisfaction of LESSOR” e. Section 5(g) “in the form or report <u>reasonably</u> prescribed by LESSOR” <p>10. Eliminate “<u>or hereinafter in effect</u>” clause anywhere it appears, including Section 2 and Section 5. Lessee should not be forced to agree,</p>	<p>terms in the lease contract are more tailored to the circumstance of the agency to specifically address long-standing disagreements that have emanated from the existing lease terms. Where necessary, the reference to applicable statute and/or rule has been inserted.</p> <p>9. The requested terms were inserted pursuant to comment 9a., 9b., 9c. and 9d. With regard to comment 9c., the agency reserves the right to prescribe the form or report necessary to meet the agency’s need under the cited lease term. Certainly, the agency has every intention to be reasonable and will not be arbitrary or excessive in its requests under this provision of the lease.</p> <p>10. The phrase has been eliminated as requested.</p> <p>11. The lease form has been developed pursuant to W.S. 36-6-101(c). The references to statutes and rules contained in the lease were crafted to affect specific and appropriate agency intent and clarify areas of historic disagreement that arose under the existing lease contract.</p>
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	<p>on a wholesale basis, to the retroactive applicability of any and all future unknown regulations to this lease. Retroactive applicability, if any, should be determined in accordance with established principles of law governing that specific issue.</p> <p>11. In any instances where statutes are referenced, or form the basis for a provision or definition, the statutory language should speak for itself and should not be paraphrased or otherwise modified. Paraphrasing statutory language results in discrepancies between the lease language and the statutory language, and unnecessarily creates questions about which should control. Accordingly, unless it is the express intent of the SLB to modify, administratively, the language and/or requirements established by the Legislature, wherever a statute is referenced the lease form should simply say “as provided in W.S. _____.”</p>	
	12.	