

ACTION FORM BRYAN CITY COUNCIL

DATE OF COUNCIL MEETING: January 14, 2014		DATE SUBMITTED: January 6, 2014	
DEPARTMENT OF ORIGIN: Water Services		SUBMITTED BY: J. Barfknecht	
MEETING TYPE:	CLASSIFICATION:	ORDINANCE:	STRATEGIC INITIATIVE:
<input type="checkbox"/> BCD	<input type="checkbox"/> PUBLIC HEARING	<input type="checkbox"/> 1ST READING	<input type="checkbox"/> PUBLIC SAFETY
<input type="checkbox"/> SPECIAL	<input type="checkbox"/> CONSENT	<input type="checkbox"/> 2ND READING	<input type="checkbox"/> SERVICE
<input checked="" type="checkbox"/> REGULAR	<input checked="" type="checkbox"/> STATUTORY		<input checked="" type="checkbox"/> ECONOMIC DEVELOP.
<input type="checkbox"/> WORKSHOP	<input type="checkbox"/> REGULAR		<input checked="" type="checkbox"/> INFRASTRUCTURE
			<input checked="" type="checkbox"/> QUALITY OF LIFE
AGENDA ITEM DESCRIPTION: A resolution establishing the criteria, standard terms, and form of lease agreement to be used by the City Manager in negotiation of oil, gas and mineral interests owned by the City, on behalf of the City without further action by the City Council.			
SUMMARY STATEMENT: Recent attention has been placed on oil, gas and mineral interests for property owned by the City of Bryan. Currently, execution of leases of City-owned interests is limited solely to the City Council. Delegation of this responsibility to the City Manager without further City Council action is believed to be in the best interest of the City by streamlining the negotiation and approval process. Establishing legal authority for assignment of City-owned interests by the City Manager is the first step needed in this process. City Council consideration for establishing legal authority by amending Chapter 78 "Natural Resources" of the City of Bryan Code of Ordinances is presented in a separate action form at the January 14, 2014 Council meeting. This action form focuses solely on approval of a resolution establishing the criteria, standard terms and lease agreement form for the City Manager's execution of lease of City-owned oil, gas, and mineral interests.			
Pursuant to the above mentioned amendment to the City of Bryan Code of Ordinances, the City Manager may enter, on behalf of the City without further City Council action, an agreement for leases of oil, gas, and mineral interest owned by the City provided the following is met:			
<ul style="list-style-type: none"> (i). The lessor must be an adjacent mineral interest owner or one who currently holds a lease of the oil, gas or mineral interests of adjacent property. (ii). The lease must provide the City will receive a bonus of at least \$1,200.00 per net mineral acre and a minimum 25% royalty. (iii). The term of the lease may not exceed three (3) years. (iv). No surface drilling will be allowed. All extractions will have to be done horizontally. The lessor must obtain a permit for horizontal oil and gas drilling, provide liability insurance in an amount set by the City and comply with all state and federal regulations and city ordinances. (v). The lease agreement must be in conformance with the approved lease agreement form ("Exhibit A" of the proposed resolution). 			
STAFF ANALYSIS AND RECOMMENDATION: Water Services respectfully requests City Council to adopt the proposed resolution supporting the City Manger's ability to enter into leases for oil, gas and mineral interest owned by the City on behalf of the City without further City Council action. Delegation of this responsibility to the City Manager without further City Council action is believed to be in the best interest of the City by streamlining the negotiation and approval process.			
OPTIONS (In Suggested Order of Staff Preference):			
1) Approve recommended resolution.			

- 2) Approve the resolution with modifications.
- 3) Do not approve resolution and provide direction.

ATTACHMENTS: Proposed Resolution

FUNDING SOURCE: N/A

APPROVALS: J. Barfknecht 1/6/14

APPROVED FOR SUBMITTAL: Kean Register, 1/6/2013

APPROVED FOR SUBMITTAL: Janis K. Hampton, 1/6/2013

Revised 04/2013

RESOLUTION NO. _____

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF BRYAN, TEXAS APPROVING AND ADOPTING THE CRITERIA, STANDARD TERMS AND THE FORM OF LEASE AGREEMENT FOR LEASES OF OIL, GAS, AND MINERAL INTERESTS OWNED BY THE CITY WHICH BY ORDINANCE NO. ____ MAY BE EXECUTED BY THE CITY MANAGER ON BEHALF OF THE CITY WITHOUT FURTHER ACTION BY THE CITY COUNCIL; AND PROVIDING AN EFFECTIVE DATE.

WHEREAS, Section 253.005 of the Texas Local Government Code authorizes the lease of oil, gas and mineral interests owned by the City on terms approved by the City Council; and

WHEREAS, a lease of oil, gas and mineral interests pursuant to the authority provided by Section 253.005 of the Texas Local Government Code is not a “sale” of City land and is, thus, not subject to the requirements of Section 253.001 of the Texas Local Government Code, Section 272.001 of the Texas Local Government Code or other law governing the sale of municipal land; and,

WHEREAS, the City Council finds that lease of the mineral rights described herein are for the benefit of the City; and,

WHEREAS, the City Council determines it to be most efficient for the City Council to approve and adopt by resolution certain criteria, standard terms and the form of lease agreement for leases of oil, gas and mineral interests owned by the City, which may be executed by the City Manager, without further City Council action.

NOW, THEREFORE, BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF BRYAN, TEXAS, THAT:

1.

That the findings set forth in the preamble to this Resolution are hereby in all things approved and adopted.

2.

The City Manager may, at his/her discretion and for best value received, enter into on behalf of the City without further city council action, leases of oil, gas and mineral interest owned by the city pursuant to Ordinance NO. ____, provided the following criteria, hereby established, is satisfied:

- (i). The Lessor must be an adjacent mineral interest owner or one who currently holds a lease of the oil, gas or mineral interests of adjacent property.
- (ii). The Lease must provide the City will receive a bonus of at least \$1,200.00 per net mineral acre and a minimum 25% royalty.
- (iii). The term of the lease may not exceed three (3) years.
- (iv). No surface drilling will be allowed. All extractions will have to be done horizontally. The lessor must obtain a permit for horizontal oil and gas drilling, provide liability insurance in an amount set by the City and comply with all state and federal regulations and city ordinances.

(v). The Lease agreement must be in conformance with the attached Exhibit "A".

3.

That this Resolution shall become effective on _____.

APPROVED AND ADOPTED BY THE CITY COUNCIL OF THE CITY OF BRYAN ON THIS 14th
DAY OF JANUARY, 2014.

CITY OF BRYAN:

ATTEST:

Jason P. Bienski, Mayor

Mary Lynne Stratta, City Secretary

APPROVED AS TO FORM:

Janis Hampton, City Attorney

EXHIBIT "A"

NOTICE OF CONFIDENTIALITY RIGHTS: IF YOU ARE A NATURAL PERSON, YOU MAY REMOVE OR STRIKE ANY OR ALL OF THE FOLLOWING INFORMATION FROM THIS INSTRUMENT BEFORE IT IS FILED FOR RECORD IN THE PUBLIC RECORDS: YOUR SOCIAL SECURITY NUMBER OR YOUR DRIVER'S LICENSE NUMBER.

**OIL AND GAS LEASE
(Non-Surface Use)**

THIS AGREEMENT made this ___ day of _____, 201_, between THE CITY OF BRYAN, TEXAS, a home rule municipal corporation; whose address for record purposes is 300 South Texas Avenue, Bryan, Brazos County, Texas 77803, hereinafter referred to as Lessor, and _____, whose address for record purposes is _____, hereinafter referred to as Lessee;

WITNESSETH:

1. Lessor, in consideration of TEN AND NO/100 (\$10.00) DOLLARS and other good and valuable consideration, the sufficiency and receipt of which is hereby acknowledged, and of the covenants and agreements of Lessee hereinafter contained, does hereby GRANT, LEASE and LET unto Lessee the land covered hereby for the sole and only purpose of exploring, drilling and producing oil and gas. The land covered hereby, containing _____ acres of land, more or less, and herein called "land" or "lands" or "Leased Premises", is located in the County of Brazos, State of Texas, and is more particularly described as follows:

Being ___ acres of land, more or less, lying and being situated in the _____
_____ to The City of
Bryan, recorded in Volume ___, Page ___ of the Deed Records of Brazos
County, Texas.

2. Subject to the other provisions hereof, this Lease shall be for a term of three (3) years from this date (called "Primary Term") and as long thereafter as oil or gas is produced in paying quantities ("Paying Quantities") from said Land with royalties to be paid as follows:

(a) On all oil, condensate and liquid hydrocarbons, TWENTY-FIVE percent (25.0%) of that produced and saved from the said lands and lands pooled therewith, the same to be delivered to Lessor into the storage tanks or into the pipeline to which the wells may be connected, or, at Lessor's option, such oil and liquid hydrocarbons shall be sold with Lessee's oil and liquid hydrocarbons at the same price received by Lessee (but in no event for less than the market value thereof in the event the sale is to an affiliate or subsidiary of Lessee or in a sale that is not an arm's length transaction), or at Lessor's option, such products shall be delivered to Lessor at the wells into tanks or other receptacles located on said lands to be furnished by Lessor. Lessor's options hereunder may be exercised from time to time, and the

exercise or failure to exercise an option at any time shall not constitute a waiver of Lessor's rights to exercise further options.

(b) On all gas produced from said lands and lands pooled therewith, including casing head gas and residue gas at the tailgate of any plant through which gas produced from said lands may be processed, TWENTY-FIVE percent (25.0%) of the market value of the gas at the place of use or sale by Lessee, not to exceed the price Lessee receives in an arm's length transaction with a non-related third party, or at Lessor's option, TWENTY-FIVE percent (25.0%) of the gas, in kind, at the well or at the outlet side of the separator, hereinafter provided for, or at the tailgate of any plant through which gas is processed, as the case may be. Prior to the use or sale of all gas produced from said lands, Lessee shall run such gas through a field-type separator or other comparable equipment ordinarily used in the industry for the purpose of separating, extracting and saving liquid and liquefiable hydrocarbons recoverable from the gas; provided, however, Lessee shall not be required to run the gas through a field-type separator or comparable equipment if the gas is to be processed in a recycling, absorption, pressuring or other plant belonging wholly or in part to Lessee or any subsidiary company, or if the liquid hydrocarbon content of the gas is so small as to make the installation and operation of field-type separators or comparable equipment unprofitable, or if the pressure of the gas is such that running the gas through separators or comparable equipment would diminish the ability to sell and deliver the separated gas against existing gathering system or pipe line pressures.

(c) On condensate and all other products separated, extracted or manufactured from gas produced from said lands or lands pooled therewith by any extraction, cryogenic, absorption, pressuring or other plant belonging wholly or in part to Lessee or any company controlled in whole or in part by Lessee, TWENTY-FIVE percent (25.0%) of the market value at the plant of all such condensate and other products so separated, extracted, or manufactured, or, at Lessor's option, TWENTY-FIVE percent (25.0%) of such condensate or other products in kind shall be delivered to Lessor at the plant.

(d) On all liquid hydrocarbons extracted by Lessee or an affiliate or affiliates of Lessee from gas produced from said lands or lands pooled therewith, TWENTY-FIVE percent (25.0%) of all such liquid hydrocarbon products, the same to be delivered at the point of extraction to the credit of Lessor into the pipe line, if any, at such point of extraction; provided, however, that should Lessee make "arm's length" sales of gas produced from the premises to any third party or parties not an affiliate or affiliates of Lessee, receiving for such sale or sales a cash consideration and/or a portion of the liquid hydrocarbon products that might hereafter be extracted or manufactured from such gas by said third party or parties, then Lessor shall receive a royalty on such gas so sold TWENTY-FIVE percent (25.0%) of the cash consideration and/or portion of the liquid hydrocarbon products received by Lessee for the sale of such gas.

(e) On all other minerals mined or marketed by Lessee from said lands or lands pooled therewith, TWENTY-FIVE percent (25.0%) of the market value of such minerals.

(f) Notwithstanding anything to the contrary contained herein, on any oil, gas or other hydrocarbon products sold for Lessor by Lessee, Lessor is not entitled to receive a higher net price from an arm's length purchaser than Lessee receives from any oil, gas or other hydrocarbon product(s) produced from a well (or wells) located on the Leased Premises or on lands pooled therewith.

(g) If at any time or times either during or after the primary term there is a well or wells capable of producing gas only or gas and liquefiable hydrocarbons, but gas is not actually sold or used off the premises in Paying Quantities, it shall nevertheless be considered that gas is being produced and marketed in Paying Quantities during all of such time or times if within ninety (90) days after the completion of any such well or within ninety (90) days after the cessation of marketing the production therefrom, Lessee shall pay as an advance royalty to Lessor the sum of _____ times the number of acres of the Leased Premises included within the drilling unit and/or Proration Unit assigned to each well, which payment shall serve to continue this Lease in force, to the extent, but only to the extent that actual production would keep this Lease in force, for a period of one (1) year from the date of completion of said well or the cessation of gas production, as the case may be. In the event actual sales or use of gas off the premises occur during the year for which any such payment of shut-in gas royalty has been made, Lessee shall pay royalty at the rate and in the manner herein provided on such sale or use, and shall not be entitled to credit against such royalty due on actual sales or use as the result of the payment of shut-in gas royalty herein provided. The Lessee's right to maintain such Lease by such shut-in gas royalty payments shall not exceed a total of twenty-four (24) months in the aggregate and is subject to the provisions of Paragraph 12 of this Lease.

(h) If this Lease now or hereafter covers separate tracts, no pooling or unitization of royalty interest as between any such separate tracts is intended or shall be implied or result merely from the inclusion of such separate tracts within this Lease but Lessee shall have the right to assign a well for proration purposes all or portions of such separate tracts and to allocate the royalty between the separate tracts based on the proportion which the surface acreage of each separate tract in the proration unit bears to the entire acreage in the proration unit. As used herein, the words "separate tract" mean any tract with royalty ownership differing, now or hereafter, either as to parties or amounts, from that as to any other part of the Leased Premises.

3. Subject to the provisions and restrictions of Paragraph 18 of this Lease and the restrictions on the size of the Proration Units contained in Paragraph 29 of this Lease, Lessee is hereby granted the right, at its option, to pool or unitize any land covered by this Lease with any other land lease or leases as to oil so as to establish Proration Units. The acreage from the Leased Premises included within a pooled unit formed under the pooling authority granted by this Lease, on which pooled unit there is located a well that is producing in Paying Quantities as that term is defined in Paragraph 23(b) of this Lease shall be considered to be a "Proration Unit".

Notwithstanding the above language, Lessee shall, exercise said option as to each desired unit by executing an Instrument identifying such unit and filing it for record in the public office in which this Lease is recorded with a file-stamped copy of the same being furnished to the Lessor herein or their successors in interest. Each of said options may be exercised by Lessee at any time and from time to time while this Lease is in force, and whether before or after production has been established either on said land, or on the portion of said land included in the unit, or on other land unitized therewith. Any operations conducted on any part of such unitized land shall be considered for all purposes, except the payment of royalty, operations conducted upon said land under this Lease. There shall be allocated to the land covered by this Lease within each such unit that proportion of the total production of unitized oil or gas from the unit, after deducting any used in lease or unit operations, which the number of surface acres in such land covered by this Lease within the unit bears to the total number of surface acres in the unit, and the production so allocated shall be considered for all purposes, including payment or delivery of royalty, overriding royalty and other payments out of production of unitized oil or gas from the land. The formation of any unit hereunder which includes land not covered by this Lease shall

not have the effect of exchanging or transferring any interest under this Lease (including, without limitation, any shut-in royalty which may become payable under this Lease) between parties owning interests in land covered by this Lease and Parties owning interest in land not covered by this Lease. Lessee may not so release as to lands within a unit while there are operations thereon for unitized oil or gas unless all pooled leases are released as to lands within the unit. At any time while this Lease is in force, Lessee may dissolve any unit established hereunder by filing for record in the public office where this Lease is recorded a declaration to that effect, if at that time no Operations are being conducted thereon for unitized oil or gas and a file-stamped copy of such recorded declaration shall be furnished to the Lessor herein or their successors in Interest. Subject to the provisions of this Paragraph 3, a unit once established hereunder shall remain in force so long, as any Lease subject thereto shall remain in force.

4. This Lease is binding upon and inures to the benefit of the Lessors, Lessees and their respective heirs, successors and assigns.

5. Subject to the provisions outlined in this Lease, no change or division in the ownership of said land, royalties, or other monies, or any part thereof, howsoever effected, shall increase the obligations or diminish the rights of Lessee. Notwithstanding any other actual or constructive knowledge or notice thereof of or to Lessee, its successors or assigns, no change or division in the ownership of said land or of the royalties, or other monies, or the right to receive the same, howsoever effected, shall be binding upon the then record owner of this Lease until thirty (30) days after there has been furnished to such record owner at his or its principal place of business by Lessor or Lessor's heirs, successors or assigns, notice of such change or division, supported by copies of the instruments which have been properly filed for record and which evidence such change or division, and of such court records and proceedings, or other documents as shall be reasonably necessary in the opinion of such record owner to establish the validity of such change or division. If any such change in ownership occurs by reason of the death of the owner, Lessee may, nevertheless pay or tender such royalties, or other moneys, or part thereof, to the credit of the decedent in the depository bank provided for above.

6. Lessor makes no warranty of title whatsoever. This Lease is delivered by Lessor and accepted by Lessee without representation or warranty express, or implied by Lessor and no other warranty of any kind, whether statutory or otherwise, shall be implied or deemed to exist by virtue of any term or provision hereof or by the execution or delivery hereof by Lessor.

7. The following agreements and provisions shall supersede and govern the provisions contained in the first six (6) paragraphs of this Lease to the contrary, and shall inure to the benefit of, and be binding upon the parties hereto and their respective heirs, representatives, successors and assigns.

8. Time is of the essence in this Lease.

9. This Lease covers only oil and gas, including all other gaseous and liquid hydrocarbons, as well as such other minerals or substances maybe produced incidental to and as a part of or mixed with oil, gas and other liquid or gaseous hydrocarbons, but this Lease does not cover: (i) fissionable materials, coal, lignite, gravel, uranium, uranium ores, vanadium, plutonium, sand, rock, stone, fuller's earth, commercial clays, or other fissionable minerals or materials; (ii) any water (except water associated with the recovery of oil or gas covered by this Lease on these premises only but not water used in secondary or tertiary water flood operations); (iii) all sulphur (except that produced as herein provided in conjunction and associated with oil or

gas covered by this Lease); and (iv) all other minerals or substances of any type which shall be produced from the Leased Premises separate and apart from, or Independently of, oil, gas or other liquid or gaseous hydrocarbons. Any reference to any other mineral's whatsoever as being included in this Lease by Lessor or Lessee is hereby void and considered deleted.

10. At the expiration of the initial Primary Term or any extension thereof, or the expiration of any drilling operations in progress at the end of the Primary Term or any extension thereof, this Lease shall terminate as to all of the land one hundred feet (100') below the base of the deepest producing horizon or stratigraphic equivalent of the deepest producing depth, established under the terms of this Lease, whichever is the greatest depth.

11. At the expiration of the Primary Term hereof, or at the expiration of any drilling operations in progress at the end of the Primary Term, this Lease shall terminate as to all of the land covered hereby except as to those lands which are included within the designated geographical boundaries of a pooled unit or Proration Unit containing the acreage required or limited under Paragraph 29 below. If said lands are not then included in a pooled unit or Proration Unit, then this Lease shall terminate as to all depths and lands not so included as herein provided.

12. With regard to Lessee's right to maintain this Lease by shut-in payments for recurring periods not to exceed two (2) years in the aggregate it is intended by Lessor and Lessee that the provisions of this Paragraph will maintain this Lease in force in those situations where the shut-in of a well by Lessee results from situations beyond the reasonable control of Lessee, including, but not limited to: (a) lack of a market; (b) failure of any purchaser to take gas production; or (c) shut-in as a result of Lessee's obligation to make up over production under any applicable regulations. Lessee agrees that all gas produced from the Leased Premises that is not processed in a plant or plants from which products derived there from and the residue gas is ratably allocated to the Leased Premises for the payment of royalty shall, if economically feasible to do so before the same is sold or used for any purpose or transported from the Leased Premises, be passed through a conventional separator designed and operated to effect the maximum economical recovery of liquids therefrom.

As such monthly payments are made as provided in Paragraph 2(f) above, they shall serve to continue this Lease in force with respect to any such well for the above described period from the date such well is shut-in or completion of said well or the date of cessation of production, as the case may be, but not more than a two (2) years total during the term of this Lease. Lessee shall pay such shut-in royalty at such rate and in the manner herein provided to Lessor, and Lessee shall not be entitled to credit the same against any such royalty due on actual sales or use. Should the total of the shut-in periods total in the aggregate more than twenty-four (24) months then this Lease shall terminate in accordance with the other provisions hereof as though there was no production from said well or wells.

13. (a) Lessee shall initiate the payment of royalties under this Lease within ninety (90) days following the production of oil or gas produced from the Leased Premises. If not paid within said ninety (90) days, royalties shall be deemed to be delinquent unless the failure of Lessee to timely commence royalty payments as provided herein is due to a legitimate title problem, the delay of royalty owners in executing and returning to Lessee appropriate title curative instruments (but not division orders whose contents alter, amend, or add to this Lease Agreement), or some other circumstances reasonably beyond the control of Lessee. Lessee shall pay interest on the amount of delinquent royalty at a rate of interest equal to twelve percent

(12.0%) per annum, or the highest interest rate then permitted by law, whichever is less, calculated from thirty (30) days following the receipt of payment on production of oil or gas by Lessee and continuing until the date that the payment of royalties is initiated by Lessee. After royalty payments commence, royalty payments will be paid on a monthly basis, subject to previously described interest penalty for delays of payment. In the event title matters are shown to exist which make curative work necessary, royalties payable shall be suspended only to the extent that they are adversely affected by such title problem or dispute. Division Orders which alter, add to, or amend any provisions or language in this Lease shall not be used as a basis for suspending royalty payments, and any payments suspended for such reason shall accrue interest as provided in this Sub-Paragraph 13(a);

(b) Further, Lessor and Lessee agree that, in the event of production hereunder, and upon the execution by Lessor of the initial Division Order in accordance with the applicable laws of the State of Texas for or on behalf of the Lessee, its successors and assigns, or the operator, or the purchaser of such production, then no further Division Orders shall be required of Lessor until a change in the interest of ownership shall have been recorded in the land records of the County in which the Land is located, and the Lessee agrees that it will cause such operator or purchaser of production to be subject to the terms of this Lease and provision, and;

(c) Acceptance by Lessor of royalties which are past due shall not act as a waiver or estoppel of its right to receive or recover all interest due thereon under the provisions hereof unless the written acceptance or acknowledgment by Lessor to Lessee expressly so provides. Any tender or payment to Lessor of a sum less than the total amount due to Lessor hereunder which is made or intended to be made as an offer of settlement or accord and satisfaction by or on behalf of Lessee must be accompanied by a Notice of Settlement Offer, so denominated, addressed to Lessor. Any such offer of settlement submitted solely by the tender of a check containing language of settlement or accord and satisfaction printed or otherwise Inserted thereon shall not be deemed an offer of settlement or accord and satisfaction, unless preceded by such a Notice of Settlement Offer. Lessee shall pay all reasonable attorneys' fees incurred by Lessor in connection with any lawsuit in which Lessor is successful in recovering any royalties or interest or in terminating this Lease due to Lessee's failure to pay royalties within the periods set forth herein. If royalty payments are not being timely paid by Lessee to Lessor, then Lessor may, at Lessor's election, require accounting and payment of royalties to Lessor directly from the purchaser of production rather than from Lessee.

(d) In the event Lessee shall be delinquent with any payment to Lessor under the terms of this Lease Agreement for a period in excess of one hundred eighty (180) days, Lessor shall have the right to terminate this Agreement following sixty (60) days' written notice to Lessee of such delinquency and default. The notice shall be sent as set forth in Paragraph 24 of this Lease. Lessee shall have the right to maintain the Lease by payment to Lessor of all delinquent sums and interest thereon prior to the expiration of the sixtieth (60th) day following said notice. In the event of such declared forfeiture by Lessor, Lessee shall lose all of its rights and estates under all producing acreage hereunder; however, forfeiture shall not relieve Lessee from its responsibility of paying accrued royalties and interests thereon. This termination provision applies to Bankruptcy provisions. Lessor shall not have a right to terminate this Lease in the event Lessee has a good faith reason why such payment was not made.

14. Lessee also agrees that unless Lessor shall have given prior written consent to the contrary, none of the Leased Premises shall ever be included by Lessee within a unit for oil, a unit

for gas, or a unit for oil and gas wherein, as to each and every producing horizon, zone, strata or formation, Lessor and Lessor heirs, successors or assigns, do not share in production of oil and gas from the date of first production to the date that production ceases to maintain such unit in force and effect.

15. If Lessee should sell oil or gas produced under this Lease to any subsidiary, parent, or affiliate of Lessee or to any person or entity otherwise than in a bona fide arm's length transaction, then the royalty on oil or gas so sold shall be the greater of: (a) TWENTY-FIVE percent (25.0%) of the amount realized from the first sale that does constitute bona fide arm's length transaction; or (b) TWENTY-FIVE percent (25.0%) of the market value at the well of the gas so sold, whichever is greater.

16. Lessor's royalty shall be calculated free and clear of all costs, expenses and deductions for exploration, transportation, pipelining, drilling, development and production, including, but not limited to costs of dehydration, storage, compression, separation by mechanical means, stabilization of the hydrocarbons at the well, and any other cost or expense needed to make the product marketable or to transport it to market; but said royalty shall bear its proportionate share of severance and other taxes based upon production.

17. As used in this Lease, a "Well Having a Horizontal Drainhole" means any well in which either a) the horizontal displacement from vertical within the formation in which the well is completed exceeds 150 feet, or b) the horizontal displacement from vertical of the well bore within the formation in which the well is completed exceeds the actual vertical depth within such formation penetrated by such well bore.

18. Lessee agrees that, in the event Lessee exercises its right to form a pooled unit in accordance with the terms and provisions of Paragraph 3, Paragraph 14, Paragraph 29 and this Paragraph 18, then such authority shall be exercised as follows: all of the Leased Premises shall be included in such unit.

19. Lessee agrees to furnish Lessor within ninety (90) days after the termination of this Lease [or within thirty (30) days if the instrument is prepared by Lessor and delivered to Lessee], a duly executed and acknowledged instrument releasing or evidencing the termination of this Lease as to all or any portion of the Leased Premises that shall have terminated.

20. If there are royalty interests in oil and gas in the Leased Premises now owned by parties other than Lessor, Lessor makes no warranty or representation that this Lease grants Lessee the power or authority to pool such royalty interests, but in the event of pooling hereunder, Lessor's royalty on production from the pooled unit shall be calculated and paid as if Lessee had the power and had exercised the power to pool such royalty interests in the Leased Premises, whether or not Lessee in fact has such authority.

21. Lessee shall meter or gauge all oil and gas at the well site for the purpose of accounting for all production from each well completed and, further, shall provide monthly to Lessor, upon Lessor's request a copy of the accountings made. Lessor, its agents, successors and assigns, shall have the right to observe and record the readings on any gauges, meters or measuring devices that may be installed at any time, at the discretion of Lessor at Lessor's own risk. Upon written request by Lessor, Lessee shall furnish to Lessor a copy of all run tickets on any wells drilled on the Leased Premises or any well which includes any part of the Leased Premises at no more than monthly intervals. Lessee agrees to send notice to its oil transport

company that Lessor shall have access, at reasonable times during normal business hours, to complete information concerning payments made to Lessee for production from the Leased Premises.

22. Lessor shall have the right to audit records pertaining to wells drilled on the subject Leased Premises in Lessee's office by previously arranged appointment, Monday through Friday from 8:00 a.m. to 5:00 p.m., at no cost to Lessee.

23. (a) If this Lease becomes productive and the royalty from production payable to Lessor during any producing year does not equal \$100.00 per acre after the end of the Primary Term for each net mineral acre owned by Lessor and being kept in force by production as of the first of each producing year, then within sixty (60) days after the end of the producing year, Lessee shall pay Lessor, at Lessor's address on file with Lessee, the difference between the amount of royalty paid to Lessor and the Minimum Royalty sum provided for herein. A producing year, for this Lease, shall be deemed to commence on the first day of the calendar month following the day on which production commences. The amount set forth in this Paragraph is referred to herein as "Minimum Royalty."

This Paragraph shall not be construed to permit Lessee to maintain this Lease, as to acreage that has not been previously included in a producing unit, by making a minimum production payment. Minimum Royalty payments shall be due by Lessee to Lessor on a prorated daily basis up through the date that Lessee properly records its release of this Lease in the Official Public Records of the County encompassing said lands. Payment of Minimum Royalties shall not, however, relieve Lessee from damages accruing to Lessor from Lessee's failure to timely release this Lease of record at the appropriate date that this Lease, or parts thereof, becomes unproductive.

(b) For purposes of this Lease, for a well to be considered as "Producing in Paying Quantities," the well must have production equal to or greater than the Minimum Royalty amount set forth in Paragraph 23(a) above.

24. In order to be effective any notice, communication, document or transmittal required or permitted to be delivered hereunder may be delivered in person or shall be deemed to be delivered and given, whether actually received or not, on the fourth (4th) calendar day after the same has been deposited in the United States Mail, postage prepaid, certified mail, return receipt requested, addressed to the parties at the addresses shown and initially set forth in this Lease Agreement, or at such other addresses as may hereafter be specified by the party or parties directing the same by written notice in the manner set forth herein. Any notice by Lessor to Lessee under this Lease shall include notification to be to the address of Lessee as set forth on Page 1 of this Lease.

25. As used in this Agreement and Lease, the word "Lessor" and the word "Lessee" shall include in each instance of use of each respective word both the singular and plural of each such word as the context of this instrument would permit or require in its meaning, grammatically or substantively.

26. Further, as used in this Agreement and Lease, the masculine, feminine or neuter genders shall each be deemed to include the others when the context so requires. The singular shall include the plural and the plural shall include the singular wherever the context so permits or requires.

27. This Agreement and Lease is being delivered and is intended to be performed in the State of Texas and shall be enforced and construed according to the laws of the State of Texas and any action demanding jurisdiction and venue of any of the Parties hereto shall be in Brazos County, Texas.

28. In case any one or more of the provisions contained in this Agreement shall for any reason be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision hereof, and this Agreement shall be construed as if such invalid, illegal or unenforceable provision had never been contained herein.

29. The following provision regarding the size of Proration Units shall control over any conflicting provisions contained in this Lease. The classification given by the Texas Railroad Commission or its successor governmental authority shall determine if a well is classified as an "Oil Well" or as a "Gas Well", and notwithstanding any language contained in this Lease or any addendum to this Lease, at the termination of the Primary Term of this Lease:

(a) Each producing vertical Oil Well producing in Paying Quantities, as that term is defined in Paragraph 23 above, shall hold this Lease in force as to only that portion of the Leased Premises located within one Proration Unit containing not more than eighty (80) acres in as nearly as reasonably possible a square or rectangular from the Surface down to a depth of one hundred feet (100') below the total producing depth of such well, and shall be that acreage designated by Lessee as the acreage to be attributed to said well by instrument filed for record in the office of the County Clerk where such well is located within thirty (30) days after its completion; provided, however, if governmental authorities having jurisdiction thereof should prescribe or permit smaller drilling units or Proration Units which will permit the allocation to such unit and the well thereon of the maximum producing allowable then such acreage shall be reduced to the acreage allowed within such smaller unit.

(b) Each producing vertical Gas Well producing in Paying Quantities, as that term is defined in Paragraph 23 above, shall hold this Lease in force as to only that portion of the Leased Premises located within one Proration Unit containing not more than one hundred sixty (160) acres in as nearly as reasonably possible a square or rectangular from the Surface down to a depth of one hundred (100) feet below the total producing depth of such well, and shall be that acreage designated by Lessee as the acreage to be attributed to said well by instrument filed for record in the office of the County Clerk where such well is located within thirty (30) days after its completion; provided, however, if governmental authorities having jurisdiction thereof should prescribe or permit smaller drilling units or Proration Unit which will permit the allocation to such unit and the well thereon of the maximum producing allowable then such acreage shall be reduced to the acreage allowed within such smaller drilling unit.

(c) Each producing Gas Well and Oil Well drilled with a Horizontal Drain Hole producing in Paying Quantities, as defined in Paragraph 23 above, shall hold this Lease in force as to only that portion of the Lease Premises located within one Proration Unit containing not more than the acreage set forth below in as nearly as reasonably possible a square or rectangular form down to the depth of one hundred (100) feet below the total producing depth of such well, and shall be that acreage designated by as the acreage to be attributed to said well by instrument filed for record in the office of the County Clerk where such well is located within thirty (30) days after its completion; provided, however, if governmental authorities having jurisdiction thereof should prescribe or permit smaller drilling units which will permit the

allocation to such unit and the Well thereon of the maximum producing allowable, then such acreage shall be reduced to the acreage allowed within such smaller drilling units. If the well is classified as a "Horizontal Drainhole Well" by the Railroad Commission, the Proration Unit shall be limited to the following maximum amount of acreage depending on the length of the lateral horizontal drainhole displacement within the productive formation:

Horizontal Drainhole Displacement

100' to 1500'	160 acres
1501' to 5000'	320 acres
5001' and longer	700 acres

30. This Lease is a non-surface use lease, and Lessee shall not have the right to use any of the surface of the Leased Premises for drilling, storing, producing or transporting oil, gas and other minerals.

31. The Lease shall contain no warranty or title by The City of Bryan ("City") express or implied; and any warranties that might arise by common law and the warranties in Section 2.023 of the Texas Property Code (or its successors) are excluded.

Without the limitation as to the disclaimer by City of warrants set forth hereinabove, City makes no representation or warranty, express or implied or arising by operation of law with respect to any matter concerning the property, including, without limitation, the following: (i) title, (ii) habitability, merchantability or suitability or fitness of the property for a particular purpose or use, (iii) the nature and condition of the property, including without limitation, water, soil and geology, location of cemeteries, zoning, easement rights, water and sewage facilities or other governmental rights or obligations, (iv) completeness of accuracy of permits, surveys or reports concerning the property, (v) tax consequences, (vi) compliance of all or any part of the property with applicable environmental laws, rules or regulations with respect to health, the environment, endangered species and wetlands (collectively, "Environmental Laws") including, without limitation, the Comprehensive Environment Response Compensation and Liability Act of 1980, as amended, the Resource Conservation and Recovery Act of 1976, as amended, the Endangered Species Act (16 U.S.C. §1531, et seq.) as amended, the Texas Water Code, as amended, the Texas Natural Resource Code, as amended, and the Texas Solid Waste Disposal Act, as amended, (vii) the existence of asbestos, oil, arsenic, petroleum or chemical liquids or solids, liquid or gaseous products or hazardous substances as those terms and similar terms are defined or used in applicable environmental laws, (viii) nature and extent of right-of-way, leases, encumbrances, licenses, reservations, conditions or other similar matters, or (ix) compliance with any law, ordinance or regulation of any governmental entity or body. Conveyance of the property is made on an "as is," "where is," and "with all faults" basis, and the warranties and covenants set forth in Section 2.023 of the Texas Property Code do not apply to this conveyance. Lessee acknowledges that Lessee has had the full, complete and unfettered right to inspect the property to Lessee's satisfaction and that the granting of the lease of the property hereby made was in part based upon the fact that this conveyance was made by City without warranty or representation. In addition, Lessee and anyone claiming by, through or under Lessee, hereby fully releases the City, City's employees, officers, representatives, attorneys and agents from any and all claims against any of them for any cost, loss, liability, damage, expense, demand, action or cause of action arising from or related to any defects, errors or omissions or other conditions whatsoever of the property. This covenant releasing

the City shall be a covenant running with the land.

IN WITNESS THEREOF, this instrument is executed on the date first above written.

LESSOR:
THE CITY OF BRYAN, TEXAS

Kean Register, City Manager

Authorized by Resolution No. _____

LESSEE:
(NAME)

Name: _____

Title: _____