

MEMORANDUM OF UNDERSTANDING

THIS AGREEMENT is made and entered into this 5th day of September, 2006 by and between the BOARD OF COUNTY COMMISSIONERS OF LA PLATA COUNTY, COLORADO, 1060 E. 2nd Avenue, Durango, Colorado 81301 and PETROGULF CORPORATION, a Colorado corporation, 518 17th Street, Suite 1455, Denver, CO 80202.

DEFINITIONS

Abandonment or abandoned means the permanent abandonment of a well based on the operator's filing with the COGCC.

Best Management Practices means schedules of activities, prohibitions of practices, maintenance procedures, and other management practices intended to prevent or reduce the pollution of waters of the State of Colorado as described in the regulations of the Colorado Department of Public Health and Environment, as amended from time to time.

BLM means the Bureau of Land Management.

PETROGULF means Petrogulf Corporation.

COGCC means the Colorado Oil and Gas Conservation Commission of the State of Colorado.

Conventional gas well means a well producing from a non-coalbed methane formation found in the San Juan Basin, such as the Mesa Verde or Dakota Sandstone formations.

County means the Board of County Commissioners of La Plata County.

County approved subdivision means any subdivision created pursuant to state law, which has received subdivision approval by the Board of County Commissioners since September 1, 1972.

Easement means express or implied authorization by a property owner for the use of a designated portion of his property by another, for a specified purpose.

The *Environmental Response Fund* or ERF is "an emergency reserve" of unobligated funds to be maintained by the COGCC in the amount of \$1,000,000 and used in accordance with Colorado's Oil and Gas Act and Rule 701 of the COGCC's Rules. As described in Rule 701, the ERF fund is a mechanism to plug and abandon orphan wells, perform orphaned site reclamation and remediation and to conduct other authorized environmental activities.

Fruitland Coal Well means a gas well drilled for the purpose of producing gas from the Fruitland coal seams underlying the lands described in the Infill Application.

Gas well means a well having a pressure and volume of natural gas; specifically, producing methane, often in combination with a variety of other substances such as butane, propane and carbon dioxide.

Green completion means a technique whereby gas is recovered for sale or use instead of being vented or flared during initial completion flow back operations.

Heavy equipment means individual truck/trailer combination vehicles with a gross vehicle weight exceeding 5 tons.

Infill Application means the application filed by PETROGULF with the COGCC on or about July 31st, 2006 requesting an increase of the density to one well per 80 acres of Fruitland Coal Wells in portions of La Plata County, Colorado.

Infill Application Area means the area within La Plata County described in the Infill Application.

Infill County Permit means any permit the county issues pursuant to LPLUC for minor oil and gas facilities and major oil and gas facilities related to the Infill Application.

Infill Wells means those wells contemplated to be drilled by virtue of the Infill Application.

LPLUC means the La Plata County Land Use Code as of March 21, 2006.

Low bleed means pneumatic controllers installed on field equipment to replace high bleed devices that vent small amounts of methane continuously.

Major oil and gas facilities shall have the meaning set forth in Section 90-19 of LPLUC.

Minor oil and gas facilities shall have the meaning set forth in Section 90-19 of LPLUC.

Permanent operation means operations for an Infill Well after initial drilling, completion and interim reclamation and before abandonment.

Reasonable efforts means diligent and good faith efforts to accomplish a given objective.

Right-of-way means a tract or strip of land, separate and distinct from the underlying property, owned, occupied or intended to be occupied by an oil, gas and/or water pipeline.

Road Impact Fees means the County road impact fees described in Article 3 below.

Water quality testing wells means domestic water wells within the vicinity of gas wells tested for water quality.

Well Pad means the flat graveled portion of the pad area in which permanent operations for the gas well take place and shall always, include, at a minimum, that portion of the pad area occupied within the drilling rig anchors.

RECITALS

A. La Plata County is a political subdivision of the State of Colorado authorized to act through its Board of Commissioners.

B. PETROGULF is a gas producing operator which has filed the Infill Application with the COGCC requesting an increase in the density of Fruitland Coal Wells in parts of La Plata County, Colorado. The Infill Application requests authority for new PETROGULF 80 acre Infill Fruitland Coal Wells within the Infill Application Area.

C. The parties to this Agreement have differing legal positions regarding the degree and extent of the County's authority to regulate certain aspects of oil and gas operations. The parties prefer, if possible, to avoid expending their resources in advancing their legal positions. Notwithstanding these differences and in their desire to avoid protracted formal hearings, the County and PETROGULF are willing to agree to the terms contained herein.

D. The provisions of Chapter 90 of LPLUC require PETROGULF to obtain a county permit for the construction, installation and operation of oil and gas facilities within the unincorporated areas of the county except with respect to those lands where the County's jurisdiction is preempted by federal or state law, or by Southern Ute Indian Tribal jurisdiction.

E. The County seeks to facilitate the development of oil and gas resources within the above-described areas of the county while mitigating potential impacts from such development.

F. The County has determined that potential impacts attendant to future gas development would be best mitigated for the county as a whole if future Fruitland Coal Wells are drilled on existing well pads where practical and as prescribed in LPLUC despite the fact that, in some instances, the use of existing well pads may further affect certain property owners and neighboring properties.

G. C.R.S. § 43-2-147 allows the County to, and describes the manner in which, the County shall regulate vehicular access to and from any public highway under its jurisdiction and from or to property adjoining a public highway in order to protect the public health, safety and welfare, to maintain smooth traffic flow, to maintain highway right-of-way drainage and to protect the functional level of public highways.

H. The County, as a matter of right, may intervene in the adjudicatory proceedings before the COGCC related to the Infill Application to raise environmental or public health, safety and welfare concerns. In exchange for the agreements contained herein, the County will not protest PETROGULF'S Infill Application, nor, if it intervenes in the adjudicatory proceedings related to the Infill Application, will it advocate any position inconsistent with any term contained in this Agreement.

I. PETROGULF and the County wish to have certain issues amicably resolved prior to the COGCC's adjudicatory proceedings on the Infill Application and they agree that certain provisions of this Agreement should be included (subject to COGCC approval) in the requested Infill order.

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AGREEMENT

In consideration of the mutual obligations and benefits set forth in this Agreement and for other good and valuable consideration, the receipt of which is acknowledged, PETROGULF and the County agree as follows:

ARTICLE I APPLICATION

This Agreement shall apply to lands presently within the unincorporated portions of the Infill Application Area within the County with the exception of those lands where the County's jurisdiction is preempted by federal or state law, or by Southern Ute Indian tribal jurisdiction.

ARTICLE II DENSITY AND USE OF EXISTING WELL PADS AND FACILITIES

2.1 *Density.* PETROGULF agrees that, except as provided in Article 2.2 herein or as may be otherwise permitted in the COGCC order approving PETROGULF'S Infill Application, the density of Fruitland Coal Well Pads within the Infill Application Area shall not exceed four (4) within the existing drilling and spacing units of 320 acres for the Fruitland Coal Seam formation covering lands in La Plata County, Colorado. Notwithstanding the foregoing, nothing contained in this Article II shall be construed so as to require the closure or abandonment of any existing gas well.

2.2 *Well Location; Exceptions.* The County believes that the potential impacts attendant to future gas development would be best mitigated for the County as a whole if future Fruitland Coal Wells are drilled on existing well pads ("Pad Drilling"). In support of this policy, in situations where reasonable efforts fail to produce a Surface Use Agreement concerning Pad Drilling between PETROGULF and the Surface Owner, the County, in its discretion, may approve the Infill County Permit for Pad Drilling. Special exceptions to Article 2.1 may be requested by PETROGULF in its applications for Infill County Permits. The County will grant special exceptions when the County finds that one or more of the following factors apply in a manner such that use of an existing Well Pad is rendered impractical:

- a. topographic characteristics of the site;
- b. natural resource constraints (e.g., wetlands);
- c. the location of utilities or similar services;
- d. geologic factors or where issues concerning distances between wells are present;
- e. other site conditions beyond the control of PETROGULF; or
- f. safety concerns.

In rare circumstances, the County may also, in its discretion, grant a special exception to Article 2.1 at the request of the Surface Owner and PETROGULF based upon other

impacts that may arise from Pad Drilling. Nothing herein shall be construed or applied so as to result in the complete preclusion of an Infill Well authorized by the COGCC. The limitation contained in Section 2.1 shall not apply in any instance in which the County denies a permit application to drill a well from an existing Well Pad or to expand an existing Well Pad.

2.3 *Use of Existing Infrastructure.* PETROGULF agrees, except as provided in Article 2.2, to use existing infrastructure, including but not limited to the use of existing roads, pipeline routes and Well Pads within the existing drilling windows in the Infill Application Area. Nothing contained in this Article 2.3 shall preclude PETROGULF from installing additional facilities within the existing roads, pipeline routes and Well Pads if reasonably required to produce and operate the Infill Wells. The County recognizes that some minor reconfiguration of the existing infrastructure or additional easements may be necessary due to the placement of multiple wells on existing Well Pads. With the exception of such circumstances and other operational requirements or limitations imposed by existing contractual agreements or government regulations (e.g., CDOT access permits), with the installation of each Infill Well PETROGULF shall use existing roads, easements, and pipeline routes.

2.4 *Legal Non-Conforming Uses and Setbacks.* Section 90-122(b) of LPLUC establishes certain setback requirements. In some instances, existing minor oil and gas facilities which initially met such requirements would not meet the requirements if a current application were filed due to (i) the encroachment of other development into the setback area, (ii) because the regulation was not in effect when the original installation occurred or (iii) because a waiver previously was obtained. Because the County believes that the policy of utilizing existing well pads is critical to the mitigation of the overall impact of the Infill Wells on the county as a whole, the County agrees that in those instances where the setback requirements of Sections 90-122 (b)(1) and (2) cannot be met currently, the County will consider the use of the existing Well Pad site a legal nonconforming use not subject to the requirements of Sections 90-122 (b)(1) and (2), provided that the degree of the nonconformity is not in any way increased by the placement of the Infill Well on the existing Well Pad site. The degree of existing nonconformity shall be measured from the edge of the existing Well Pad to the nearest residential structure and/or county approved subdivision as applicable. The degree of nonconformity for the new proposed Infill Well shall be measured from the edge of the new proposed Well Pad to the nearest residential structure and/or county approved subdivision as applicable. The increase, if any, in degree of nonconformity shall be the net difference between the two above measured values.

2.5 *Expansion of Existing Well Pads.* In those instances where an existing Well Pad is used for an Infill Well, PETROGULF agrees to use reasonable efforts to minimize the expansion of the area of the existing Well Pad. The reasonableness of the expansion under the circumstances shall be demonstrated by PETROGULF to the County with its Infill County Permit application. PETROGULF agrees to exercise reasonable efforts to expand existing well pads away from nearby existing impacted residential structures.

ARTICLE III PRIVATE ROADS AND ROAD IMPACT FEES

3.1 *Road Impact Fees.* County and PETROGULF have determined that specific land use activities by PETROGULF within the Infill Application Area may create impacts on County roads and, therefore, mitigation in the form of negotiated road impact fees is proper and necessary. The parties recognize that impact fees are not always a reliable or sufficient source of funds and that the County's ability to actually perform such work may be limited or hampered by reasons beyond its control. However, the County agrees to exercise good faith in its efforts to carry out the intent of this Agreement and to perform such work to the extent that monies are available and appropriated. The County shall control the sequencing and timing of such work and PETROGULF hereby waives its rights, if any, to insist upon completion of the work or to dictate the manner, sequencing and timing of the same. The County recognizes and acknowledges that the monies collected hereunder must be collected and spent in a manner consistent with the accounting practices set forth in C.R.S. § 29-1-801 *et seq.* and that such monies may only be spent on facilities that are directly and reasonably related to the mitigation of impacts related to the activities described in the Infill Application.

3.2. *Road Impact Fees Calculation and Payment.* Based upon certain agreed upon assumptions, PETROGULF and the County have agreed to estimated Road Impact Fees for minor oil and gas facilities and major oil and gas facilities with respect to the Infill Application as follows:

(a) Tier 1 facilities that are those with respect to which PETROGULF will transport produced water by pipe (except during drilling, completion and well servicing operations except for emergency situations) and the Road Impact Fee for Tier 1 facilities shall be in the amount of \$4,116.00 per facility;

(b) Tier 2 facilities are those with respect to which PETROGULF will haul the above described produced water for temporary periods not to exceed two (2) years from the date the facility is placed in service, and the Road Impact Fee for Tier 2 facilities shall be \$5,261.00 per facility; and

(c) Tier 3 facilities are those with respect to which PETROGULF likely will haul such produced water for the long-term, and the Road Impact Fee for Tier 3 facilities shall be \$7,501.00 per facility.

PETROGULF shall pay the County the Road Impact Fee due and owing for the prescribed activity prior to the County's final approval of the Infill County Permit.

3.3 *Adoption of Road Impact Fee Program.* The County is presently undertaking a feasibility study for the imposition of a county-wide impact fee program. To the extent legally permissible, the County shall use reasonable efforts to adopt a road

impact fee program applicable to those eligible properties and uses upon which the County can legally impose an impact fee pursuant to constitutional and statutory parameters. If such a program is adopted by the County and, as adopted applies to minor oil and gas facilities and major oil and gas facilities, PETROGULF'S obligation to pay the fees described in Article 3.2, other than those already paid, shall terminate.

3.4 *Submission of Information.* The County seeks to efficiently and effectively schedule maintenance and improvement projects on its county roads. The use of such roads by heavy equipment related to construction or production activities in the Infill Application Area could have an effect on such projects. The County seeks and PETROGULF agrees to provide the County, on a quarterly basis, a forecasted activity plan setting forth the expected location and duration of minor oil and gas facilities and major oil and gas facilities operations within the county for the upcoming quarter as well as the county roads to be accessed and general proposed travel or haul routes. The disclosure of such plans and routes is for informational purposes only and shall not be construed as creating any obligation on the part of PETROGULF, including, without limitation, to conduct such operations, to limit the location and duration of such operations or to follow such routes. The first submission of such information shall occur within thirty (30) days after the COGCC order approving the Infill Application. The County agrees to reciprocate and provide notice to PETROGULF of its intended projects and its expected schedule for same.

3.5 *Use of Subdivision Roads.* PETROGULF agrees that in those instances where it accesses Infill Wells in the Infill Application Area through a road or roads within a county-approved subdivision and a governing entity exists (e.g. homeowners' association) with legal authority to bind the entity and its members, and with the authority to grant access rights over such roads and/or negotiate agreements with respect to their use, PETROGULF will use reasonable efforts to negotiate a fair and reasonable road maintenance or road improvement agreement with such entity for the purpose of paying or making in-kind contributions for its pro rata share of the cost of maintaining or improving the affected road(s). Such agreements or a memorandum thereof shall be recorded with the Clerk and Recorder of La Plata County. The existence, or lack thereof, of such executed and recorded agreements shall be noted in the Infill County Permit application for informational purposes only.

3.6 *Use of Equipment.* PETROGULF agrees that:

- a. it will remove or require the removal of chains from its heavy equipment before entering a county road;
- b. all new roads associated with the Infill Wells within the Infill Application Area shall have gravel access and Well Pads with a minimum of four inches (4") of Class 6 Aggregate Base Course as defined by the Colorado Department of Transportation Standard Specifications for Road and Bridge Construction over a stabilized base, both of which shall be maintained throughout permanent operations of the Well Pad; and

c. if mud and/or debris is tracked onto the county road by PETROGULF'S equipment, PETROGULF shall remove same and restore the condition of the road as promptly as is reasonable under the circumstances.

3.7 *Produced Water Hauling.* Except during drilling, completion and well servicing operations, PETROGULF shall use reasonable efforts to transport by pipe produced water within the Infill Application Area. PETROGULF intends to expand its existing water pipeline system for the transport of produced water within the Infill Application Area, where feasible. In those instances where the utilization of a water hauling truck is required, PETROGULF agrees to strictly comply with the weight restrictions set forth in Chapter 42, Article V of the LPLUC.

ARTICLE IV AIR QUALITY

4.1 *Electrification.* PETROGULF agrees that with respect to Infill Wells within the Infill Application Area requiring long-term artificial lift, it shall utilize electric motors for all artificial lift installations provided the Well Pad is within 1320 feet of distribution voltage and the ability to do so is not cost prohibitive due to the demands of property owners from whom easements are required, topography or other physical features (e.g., the presence of a river). PETROGULF agrees that if distribution voltage is not currently within 1320 feet of the proposed Well Pad, it will contact and provide the surface owner an opportunity at the surface owner's cost to extend distribution voltage to within 1320 feet of the proposed Well Pad. It is understood that gas powered artificial lift equipment may be used prior to the time that La Plata Electric Association brings power to the site. PETROGULF agrees to request that La Plata Electric Association place the power lines underground except in areas where the topography or subsurface conditions render it infeasible or in situations in which the landowner requests overhead lines.

4.2 *Greenhouse Gas Reduction.* PETROGULF agrees to utilize reasonable efforts to minimize methane emissions by using "green completion" techniques, and the installation of "low bleed" pneumatic instrumentation, when feasible.

4.3 *Emission Control Equipment.* PETROGULF will comply with existing EPA rules and any future regulations validly adopted by an authority with appropriate jurisdiction, including regulations that may be adopted by the Southern Ute Indian Tribe.

ARTICLE V WATER QUALITY

5.1 *Storm Water Management and Spill Prevention Containment and Control.* Even if not required to do so by any applicable regulation or law, PETROGULF agrees to utilize Best Management Practices for all pad expansions and new pads and for road and pipeline development or improvements.

5.2 *Water Well Monitoring.* If a conventional gas well exists within one quarter (1/4) mile of the bottom hole location of a proposed Infill Well, then the two (2) closest water wells within a one-half (1/2) mile radius of the conventional gas well shall be sampled by PETROGULF as water quality testing wells. If possible, the water wells selected shall be on opposite sides of the existing conventional gas well not exceeding one-half (1/2) mile radius. If water wells on opposite sides of the conventional gas well cannot be identified, then the two (2) closest wells within one-half (1/2) mile radius shall be sampled. If two (2) or more conventional gas wells are located within one quarter (1/4) mile of the bottom hole location of the proposed Infill Well, then the conventional gas well closest to a proposed Infill Well shall be used for selecting wells for sampling.

If no conventional gas wells are located within one quarter (1/4) mile radius of the bottom hole location of the proposed Infill Well, then the selected water wells shall be within one quarter (1/4) mile of the bottom hole location of the proposed Infill Well. In areas where two (2) or more water wells exist within one quarter (1/4) mile of the bottom hole location of the proposed Infill Well, then the two (2) closest water wells shall be sampled by PETROGULF. Ideally, if possible, the water wells selected should be on opposite sides of the bottom hole location of the proposed Infill Well. If water wells on opposite sides of the bottom hole location of the proposed Infill Well cannot be identified, then the two (2) closest wells within one quarter (1/4) mile radius shall be sampled by PETROGULF. If two (2) water wells do not exist within one quarter (1/4) mile radius, then the closest two water wells within a one-half (1/2) mile radius shall be selected.

If no water well is located within a one quarter (1/4) mile radius area or if access is denied, a water well within one-half (1/2) mile of the bottom hole location of the Infill Well shall be selected. If there are no water quality testing wells meeting the foregoing criteria, then sampling shall not be required. If the BLM or the COGCC have already acquired data on a water well within one quarter (1/4) mile of the conventional gas well, but it is not the closest water well, it shall be given preference in selecting a water quality testing well. The "initial baseline testing" described in this paragraph shall include all major cations and anions, TDS, iron and manganese, nutrients (nitrates, nitrites, selenium), dissolved methane, pH, presence of bacteria and specific conductance and field hydrogen sulfide.

If free gas or a methane concentration level greater than 2 mg/L is detected in a water quality testing well, compositional analysis and carbon isotopic analyses of methane carbon shall be performed to determine gas type (thermogenic, biogenic or an intermediate mix of both). If the testing results reveal biogenic gas, no further isotopic testing shall be done. If the carbon isotope test results in a thermogenic or intermediate mix signature, annual testing shall be performed thereafter and an action plan shall be drafted by PETROGULF to determine the source of the gas. If the methane concentration level increases by more than 5 mg/L between sampling periods, or increase to more than 10 mg/L, an action plan shall be drafted to determine the source of the gas.

The initial baseline testing shall occur prior to the drilling of the proposed Infill Well. Within one (1) year after completion of the proposed Infill Well, a "post

completion" test shall be performed for the same parameters above and repeated three (3) and six (6) years thereafter. If no significant changes from the baseline have been identified after the third test (the six year test), no further testing shall be required. The testing schedule will restart after the drilling of a new Infill Well on an existing Well Pad if the wells to be tested include those tested for the 160 acre infill program. Additional "post completion" test(s) may be required if changes in water quality are identified during follow-up testing. The Director of the COGCC may require further water well sampling at any time in response to complaints from water well owners.

Within three (3) months of collecting the samples used for the test, copies of all test results described above shall be provided to the COGCC and the County and the landowner where the water quality testing well is located.

ARTICLE VI PLUGGED AND ABANDONED WELLS/SOIL GAS VAPOR SURVEY

A soil gas vapor-monitoring program is designed to determine a possible lack of zonal isolation along wellbores of plugged and abandoned wells. PETROGULF will attempt to identify any plugged and abandoned wells located within 0.25 miles of the bottom hole location of any Infill Well. Any plugged and abandoned well within 0.25 miles of the bottom hole of an Infill Well will be assessed for risk, taking into account cementing practices reported in the plugged and abandoned reports. PETROGULF shall notify the COGCC of all results of all risk assessments of plugging procedures. The COGCC may appropriate funds under Rule 701 (the Environmental Response Fund) to conduct soil gas monitoring tests to further define the risks. If the monitoring reveals a possible lack of zonal isolation, the COGCC may then conduct or order any necessary remediation or other authorized activities.

ARTICLE VII INCLUSION INTO COGCC ORDER

PETROGULF and the County agree to jointly request that certain conditions, as set forth in attached Exhibit A, be incorporated into the COGCC order approving the Infill Application.

ARTICLE VIII SITE SPECIFIC DEVELOPMENT PLAN AND FUTURE REGULATIONS

This Agreement shall not grant or create any common law or statutory vested development rights or exempt PETROGULF from any applicable County development review regulations or processes. The County reserves the right in the future to enact and apply prospectively oil and gas regulations that are general in nature and are applicable to all similarly situated oil and gas activities subject to land use regulation by the County, even though such regulations may be more or less stringent than the standards applicable to the Infill Wells by virtue of this Agreement.

ARTICLE IX PRESERVATION OF RIGHTS

The parties acknowledge, understand and agree that this Agreement shall not operate as a bar, constitute a waiver of any rights of the parties, or in any respect affect the ability of any party to this Agreement to assert its claims concerning the validity of the County's land use jurisdiction. Nothing in this Agreement shall be construed as an admission regarding the existence of proper jurisdictional authority or waiver by either party of any legal right or obligation, nor shall anything be construed as a bar to either party to seek any legal remedy available to it.

ARTICLE X GENERAL PROVISIONS

The following general provisions shall govern the relationship between the parties with respect to Infill Fruitland Coal Wells within the Infill Application Area.

10.1 *Effective Date and Term.* This Agreement shall be effective upon entry of the COGCC's order approving the Infill Application.

10.2 *Entire Agreement.* Except as otherwise expressly set forth herein, this Agreement embodies the complete agreement and understanding between the parties hereto with respect to the subject matter hereof and supersedes and preempts any prior understandings, agreements or representations by or between the parties, written or oral, which may have related to the subject matter hereof in any way.

10.3 *Successors and Assigns.* Except as otherwise provided herein, PETROGULF shall have the absolute right to transfer or sell any or part of its interest in the Infill Wells; provided, however, that in the event of transfer, PETROGULF'S transferees, sublessees, successors and assigns shall be bound to comply with all terms hereof.

10.4 *Counterparts.* This Agreement may be executed in one or more counterparts, each of which shall be deemed an original but all of which when taken together shall constitute a single agreement.

10.5 *Amendment.* All covenants, representations and warranties herein and all other obligations, responsibilities and terms hereof shall continue to be fully binding and enforceable on the parties until expressly superseded by written agreement of the parties. No amendment to this Agreement shall be effective unless in writing, signed by all parties who are then subject to this Agreement.

10.6 *Waiver.* No failure on the part of any party hereto to exercise and no delay in exercising any right hereunder shall operate as a waiver of such right. The remedies provided herein are cumulative and not exclusive of any remedies provided by law. No

waiver of, or failure to exercise any right hereunder shall operate to prevent future enforcement of such right.

10.7. *Notices.* Notices hereunder may be given by certified mail, return receipt requested, or by facsimile or electronic mail transmission. Notices shall be effective on receipt, provided, however, that confirmation of receipt shall be required in all instances. Notice to the respective parties shall be given to:

To the County at:

Nancy Lauro, Director
Community Development Services
La Plata County
1060 E. 2nd Avenue
Durango, Colorado 81301

With copies to:

Jeffery P. Robbins, Esq.
Goldman, Robbins & Rogers, P.C.
P.O. Box 2270
Durango, Colorado 81301

To PETROGULF at:

Charles W. Goodin
Petrogulf Corporation
518 17th Street, Suite 1455
Denver, CO 80202

With copies to:

Michael J. Wozniak
Beatty & Wozniak, P.C.
216 16th Street, Suite 1100
Denver, Colorado 80202

or to any other addresses as either party hereto may, from time to time, designate in writing and deliver in a like manner.

10.8 *Headings.* The descriptive headings of the sections of this Agreement are inserted for convenience only and shall not control or affect the meaning or construction of any of the provisions hereof.

10.9 *Further Acts.* Each of the parties shall promptly and expeditiously execute and deliver any and all documents and perform any and all acts as reasonably necessary, from time to time, to carry out the matters contemplated by this Agreement.

10.10 *No Partnership; Third Party Beneficiaries.* It is not intended by this Agreement to, and nothing contained in this agreement shall, create any partnership, joint venture or other arrangement between PETROGULF and the County. No term or provision of this Agreement is intended to or shall be for the benefit of any person, firm, organization or corporation not a party hereto and no other person, firm, organization or corporation shall have any right or cause of action hereunder.

10.11 *Severability.* The provisions of this Agreement are deemed material and nonseverable. If an action is brought that results in any provision of this Agreement being determined or declared by a Court to be illegal, invalid or unenforceable under present or future laws effective during the term of this Agreement, the parties shall negotiate in good faith for an equivalent or substitute provision or other appropriate

adjustment to this Agreement. If the parties cannot reach agreement, or if so desired by the parties, then the issues in dispute shall be submitted to a mediator acceptable to both parties for nonbinding mediation. Unless otherwise agreed to by the parties, such mediation shall occur within sixty (60) days of a party's receipt of a notice to mediate from the other party.

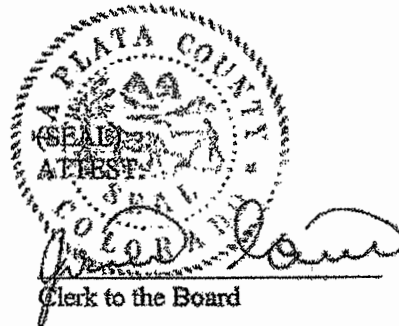
PETROGULF CORPORATION

By: Betty A. Pennington
Betty A. Pennington

Name (print): Executive Vice President

BOARD OF COUNTY COMMISSIONERS
LA PLATA COUNTY, COLORADO

Wallace White
Wallace White, Chair



Clerk to the Board

EXHIBIT A

PROPOSED CONDITIONS OF APPROVAL

Applicant Petrogulf Corporation ("PETROGULF") and Intervenor La Plata County, Colorado ("La Plata County") respectfully request that an Order issued by the Commission in Cause No. 112, Docket No. 0609-AW-16 be made subject to and conditional upon the following:

1. Compliance with all terms, conditions and provisions of prior Commission Orders in Cause No. 112, including without limitation, the specific provisions of Order No. 112-136 and Order No. 112-157 including the Rule 508j.(3)B conditions attached thereto.
2. Compliance with the terms and provisions of all of the Commission's health, safety, welfare and environmental rules and regulations now or hereafter in effect.
3. Those certain provisions as set forth in Exhibit A of the Memorandum of Understanding between PETROGULF and La Plata County as follows:

- *Surface Density*

The density of Fruitland Coal Well Pads within the Infill Application Area shall not exceed four (4) within the existing drilling and spacing units of 320 acres for the Fruitland Coal Seam formation covering lands in La Plata County, Colorado. Notwithstanding the foregoing, nothing contained in this provision shall be construed so as to require the closure or abandonment of any existing gas well.

- *Well Location; Exceptions*

The Commission may grant a special exception allowing for a greater density of Fruitland Coal Well Pads (i.e., more than 4 per 640-acre section), at the request of PETROGULF and after consultation with the Local Governmental Designee, based upon a finding by the Commission that one or more of the following factors apply in a manner such that use of an existing Well Pad is rendered impractical:

- a. topographic characteristics of the site;
- b. natural resource constraints (e.g., wetlands);
- c. the location of utilities or similar services;
- d. geologic factors or where issues concerning distances between wells are present;
- e. other site conditions beyond the control of PETROGULF; or
- f. safety concerns.

testing shall be performed thereafter and an action plan shall be drafted by PETROGULF to determine the source of the gas. If the methane concentration level increases by more than 5 mg/L between sampling periods, or increase to more than 10 mg/L, an action plan shall be drafted to determine the source of the gas.

The initial baseline testing shall occur prior to the drilling of the proposed Infill Well. Within one (1) year after completion of the proposed Infill Well, a "post completion" test shall be performed for the same parameters above and repeated three (3) and six (6) years thereafter. If no significant changes from the baseline have been identified after the third test (the six year test), no further testing shall be required. The testing schedule will restart after the drilling of a new Infill Well on an existing Well Pad if the wells to be tested include those tested for the 160 acre infill program. Additional "post completion" test(s) may be required if changes in water quality are identified during follow-up testing. The Director of the COGCC may require further water well sampling (which may include water quality monitoring) at any time in response to complaints from water well owners.

Within three (3) months of collecting the samples used for the test, copies of all test results described above shall be provided to the COGCC and the County and the landowner where the water quality testing well is located

- *Plugged and Abandoned Wells/Soil Gas Vapor Survey*

A soil gas vapor-monitoring program is designed to determine a possible lack of zonal isolation along wellbores of plugged and abandoned wells. PETROGULF will attempt to identify any plugged and abandoned wells located within 0.25 miles of the bottom hole location of any Infill Well. Any plugged and abandoned well within 0.25 miles of the bottom hole of an Infill Well will be assessed for risk, taking into account cementing practices reported in the plugged and abandoned reports. PETROGULF shall notify the COGCC of all results of all risk assessments of plugging procedures. The COGCC may appropriate funds under Rule 701 (the Environmental Response Fund) to conduct soil gas monitoring tests to further define the risks. If the monitoring reveals a possible lack of zonal isolation, the COGCC may then conduct or order any necessary remediation or other authorized activities.

4. Compliance with all applicable regulations of the BLM, BIA and the Southern Ute Indian Tribe when conducting operations on lands subject such agency's jurisdiction.

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