

Dear _____ :

The Minerals Management Service (MMS) has selected one or more Gulf of Mexico leases(s) that you operate to be included in a Royalty in Kind (RIK) program in which we will take natural gas royalties in kind beginning _____ .

This letter provides the procedures and establishes the terms and conditions under which the United States (Lessor) will take royalty gas in kind from offshore leases as defined in the Outer Continental Shelf Lands Act of 1953, 43 U.S.C. 1337(g). Our authority is the Outer Continental Shelf Lands Act at 43 U.S.C. 1353 and the royalty provisions contained in your Federal lease(s). For the purposes of this letter, royalty gas means the daily Federal lease production multiplied by the lease royalty rate unless the percentage of gas which may be taken in kind is limited by lease provision. The volumes of natural gas taken in kind by Lessor will reflect and be consistent with all grants of royalty relief.

Term

The Lessor will take all royalty gas from the properties listed in the enclosure beginning on April 1, 2003, and ending on the last day of the month subsequently designated by the Lessor as the date of termination. The Lessor will provide Lessee and Operator with a minimum 30-day prior written notice of termination of in-kind status and will provide a 45-day notice of termination, if possible.

Royalty in Kind Applicability

You must deliver all royalty gas to the Lessor from all your wells that are measured at the facility measurement points (FMPs) listed on the enclosure. In addition, you will make reasonable efforts to notify the Lessor's designated point of contact of leases that, during the period of in-kind status, begin producing natural gas that is measured at these FMPs. Royalty on natural gas from such newly producing leases will be added to the RIK volumes at the existing delivery points only upon mutual consent of the Lessor and its natural gas purchaser. Lessor will notify you whether such new production will be taken in kind and will make reasonable efforts to take in kind all production behind each FMP at which RIK gas is measured. MMS and the operator will coordinate and mutually resolve those situations where the royalty rate is modified by statute (i.e., deep water royalty relief) as they occur.

Royalty gas must be placed in marketable condition at no cost to the Lessor, even if the activities required to meet this condition are performed downstream of the point where royalty gas is delivered to the Lessor. Marketable condition means the condition generally acceptable to purchasers in the field or area. Questions regarding marketable condition should be directed to the Lessor's Program Coordinator (under "Lessor Point of Contact" at the end of this letter).

If you are also a payor on the referenced property(s), please review your estimated payments. You should recoup the estimated payment if this property(s) is being entirely taken in kind or reduce the estimated payment to reflect only the in-value portion. Please be advised that MMS will not pay interest on estimates we consider excessive.

The amount of any flash gas allocable to the lease obtained downstream of the FMP will be included in the adjustments provided for volumetric make-up in the subsequent month as described under "Balancing Account and Imbalances." Royalty gas delivered to the Lessor includes rights to process royalty gas to extract natural gas liquids.

The Lessor is currently evaluating, by pipeline system, the feasibility of taking retrograde or drip condensate (retrograde) in kind. As we complete the analysis on each pipeline system, we will notify you of the RIK procedures on retrograde for that system. Until that notice, the Lessor will elect not to receive an allocation of retrograde.

Royalty Gas Delivery

The Lessor will take delivery of the royalty gas at the delivery point. The Lessee must deliver or accomplish delivery of royalty gas to the Lessor at the delivery point at the same frequency as it is produced and transported from the property. Only in the case of normal operational imbalances or subsequent month imbalance adjustments (see "Balancing Account and Imbalances") will the Lessee deliver more or less than the royalty share to the Lessor. Unless otherwise agreed, delivery will be assumed to be daily. Lessor does not require you to process the royalty gas.

The delivery point for royalty gas produced from the leases is as follows:

- For properties connected to a third party pipeline through producer owned lateral line(s), the delivery point is the downstream terminus of the producer owned lateral line(s).
- For properties directly connected to a third party pipeline, the delivery point is the FMP approved by MMS as the royalty settlement point.

If your records show that there is more than one approved FMP, consult with us and we will designate, in writing, one or more FMP(s) as the delivery point(s).

Fulfillment of Royalty Obligations

Delivery of the accurate volume of royalty gas (taking into account the effects of normal operational imbalances) in accordance with the terms of this letter will satisfy in full the Lessee's royalty obligation to the Lessor. However, the rights, duties, and obligations that currently exist between the Lessor, Lessee, and Operator for natural gas avoidably lost prior to the FMP or gas used on or for the benefit of the lease under 30 CFR part 202 remain in effect.

All rent or minimum royalty obligations on any property in this program remain the responsibility of the Lessee. If MMS believes the Lessee owes minimum royalties, we will issue an appropriate order to pay. The Lessee will have 30 days to review the bill and make payment or appeal the bill.

Lessor Obligation to Take

The Lessor agrees to take 100 percent of the royalty gas delivered daily for the account of the Lessor or its designee at the delivery point. The Lessor, using customary industry practices outlined by the Gas Industry Standards Board (GISB) or North American Energy Standards Board (NAESB) standards and the Council of Petroleum Accountants Societies (COPAS) White Paper on Producer and Operator Roles and Responsibilities for nominating and scheduling transportation services, will exercise its best efforts to minimize the occurrence of imbalances with you and other Lessees. Where possible, you will use a predetermined allocation equal to the royalty rate.

Communication with Lessor

No later than 10 calendar days before the first day of each month, you must notify the Lessor of the daily royalty gas volumes anticipated for the following month of production in writing via facsimile at (303) 231-3846 or e-mail addressed to mailbox rik.gas.team@mms.gov. The Lessor understands that any such estimate is not a warranty of actual deliveries to be made but is provided to facilitate planning.

You must also use reasonable efforts, consistent with industry practice, to inform the Lessor regarding significant changes in gas production levels and/or royalty shares anticipated for project properties. Such communication must occur as soon as practicable after you know of such anticipated changes in production levels.

Responsibilities for Penalties

To facilitate timely and accurate custody transfer of royalty gas, you will communicate with the Lessor using customary industry practices regarding volumes of royalty gas to be nominated for movement beyond the delivery point(s). The Lessee will pay all transportation-related penalties incurred beyond the delivery point resulting from any failure of the Lessee to make royalty gas volumes available to the Lessor consistent with your communication regarding volumes to be delivered. This does not apply to normal production variances or to emergency operational situations where penalties result despite your reasonable efforts to communicate with the Lessor.

The Lessee will incur no transportation or royalty-related penalties because of the Lessor's failure to nominate or take delivery of gas volumes consistent with your communications.

Balancing Account and Imbalances (Lease Level Imbalances)

Imbalances between delivered and entitled volumes of royalty gas will be jointly monitored by you and MMS. You will take timely action to remedy such imbalances through adjustments to royalty gas volumes delivered to MMS. Such volume adjustments will be identified in your communication of royalty gas volumes anticipated before the month of production (see above under “Communication with Lessor”).

Requirements for handling imbalances are outlined below:

- Imbalances will be determined on the basis of the difference between the royalty share of production and the actual volumes delivered. These imbalances will be maintained at a lease, agreement, or FMP level. All royalty gas, including flash gas, will be balanced at the same level.
- You, as the Operator, must provide the lease imbalance statement to the Lessor point of contact, as described under “Lessor Point of Contact, Imbalance Statements”, no later than 60 days after the end of the month of production. Your imbalance statement must specify total production, MMS’ entitled share, volumes delivered, whether quantities are reported in Mcf or MMBtu, Btu content, the pressure base used in measurements, the monthly imbalance, and the cumulative imbalance.

Imbalances will be remedied in the production month following the month that the imbalance is identified. Imbalances not remedied within 120 days of the end of the production month will be considered non-routine and will be resolved as follows:

- Mutually agreed upon make-up delivery schedule, or
- Cash out payment based on the Lessor’s sales price net of transportation costs from the lease for each month of the imbalance. Interest will accrue from 60 days after written notification that the cash out payment is due.

If you and the Lessor have agreed upon a make-up delivery schedule to remedy those imbalances that are not resolved within 120 days, you must keep proper documentation showing how your production availables for the make-up months were calculated (i.e., the anticipated production plus or minus the agreed upon make-up amount).

Routine imbalances remaining upon cessation of the royalty-in-kind term or cessation of production will be settled on the basis of the Lessor’s sales price net of transportation costs from the lease for the final month of in-kind delivery. Lessees will report the imbalance volume and value on the Report of Royalty Sales and Remittance (Form MMS-2014) as either a positive or a negative for the final month of delivery. Interest will accrue from 60 days after written notification that the cash out payment is due.

Volume Reconciliation

The MMS analysts will monitor and reconcile production and volumes delivered with additional data, including pipeline data. The MMS will attempt to reconcile volumes as soon as practicable. Reconciliation will involve communication between you and the Lessor. Upon project termination, you, as the Operator, must issue a final gas imbalance statement. You will settle in accordance with the section "Balancing Account and Imbalances."

Reporting

You must continue to report natural gas production on the Oil and Gas Operations Report (OGOR) under requirements specified in MMS regulations and the MMS *Minerals Production Reporter Handbook* at <http://www.mrm.mms.gov/ReportingServices/PDFDocs/ProductionHB.pdf>. You will not be required to report natural gas information for the leases in this program on the Form MMS-2014 or other similar form for the term during which the Lessor takes royalty in kind, except under provisions described below in this section and under provisions described under "Balancing Account and Imbalances." Reporting and payment requirements for production and royalties for any crude oil or condensate for the leases included in this natural gas royalty-in-kind program will not change. Reporting will not change for leases not included in this program. If you have reporting issues, please see our website at <http://www.mrm.mms.gov/ReportingServices/RepServhome.htm> for a complete list of MRM company representatives and their telephone numbers.

You must report any transportation allowances and any final imbalances on your Form MMS-2014. For delivery points of properties connected to the third party pipeline via a producer owned lateral line, you must report the producer owned lateral line charges as a transportation allowance on your Form MMS-2014. You will report separate entries for the allocated volume and values of transportation costs and final imbalances for each of the lease(s) identified in the enclosure. The payor code you will use for this Form MMS-2014 is your existing applicable code.

Lessor's Designee

At times, the Lessor may act by or through a duly authorized designee. In such event, the Lessor will provide you with prior written notification of the identity of its designee(s) including the person to contact. Such notification will include specific duties that will be handled by the designee on behalf of the Lessor. The Lessor also will provide written notification to you when the designee is no longer authorized to act on Lessor's behalf for the purposes of this letter. You are authorized to communicate with the designee as specified in the notification. You will not be required to direct communications to both the Lessor and its designee. For purposes of this letter, if the Lessor notifies you that it will use a designee, references to the Lessor shall refer to the Lessor's designee.

The Lessor requires the designee to agree that, when acting on behalf of the Lessor, the designee must comply with all provisions of this letter that are applicable to the Lessor.

Audit Rights

The Lessor may audit your records regarding all information relevant to volumes and qualities of royalty gas produced, stored, used on the lease, measured, delivered, and, if applicable, transported. The MMS reserves the right to examine the financial records of you and the Lessees of the subject properties related to any transportation expenditures incurred prior to the delivery point.

Lessees, Operators, and revenue payors must maintain all records of transactions mentioned in the above paragraph for a period of 7 years from the day on which the relevant transaction occurred unless MMS notifies the record holder of an audit or investigation. When an audit or investigation is underway, records must be maintained until the record holder is released in writing from the obligation to maintain the records.

Lessor Point of Contact

The Operator should keep copies of all correspondence between Operator and Lessor on file. Points of contact for the Lessor are as follows:

Lessor Program Coordinator:

Ms. Pamela Rieger

Telephone: 303-231-3020; Fax: 303-231-3846

E-mail: pamela.rieger@mms.gov

Volume Avails and New Lease Production:

Ms. Karen Bigelow

Telephone: 303-231-3890; Fax: 303-231-3846

E-mail: karen.bigelow@mms.gov

Mr. Michael DeBerard

Telephone: 303-231-3884; Fax: 303-231-3846

E-mail: michael.deberard@mms.gov

Imbalance Statements:

Fax/E-Mail:

RIK Gas Team

Fax: 303-231-3846 or 303-231-3849

E-mail: rik.gas.team@mms.gov

Regular Mail:

Attention: RIK Gas Team

P.O. Box 25165, MS330B2

Denver, CO 80225-0165

Physical Address (Overnight)

Attention: RIK Gas Team

MS 330B2

Bldg. 85, 6th and Kipling

Denver Federal Center

Denver, CO 80225

Scheduling, Transportation, and Daily Imbalance Issues:

(MMS' gas purchaser assumes all responsibilities of the Lessor for these issues)
(MMS will notify you of its gas purchaser's point of contact)

Electronic Funds Transfer:

Ms. Norma Yagnich
Telephone: 303-231-3345; Fax: 303-231-3501
E-mail: norma.yagnich@mms.gov

The Lessor acknowledges that you have given proper notice when you communicate with the Lessor using the telephone number, fax number, or email address given above, provided any telephone communication regarding volumes is confirmed by fax or email no later than 1 business day after telephone communication occurs. The Lessor further agrees to make arrangements to receive such communications regarding gas scheduling issues on a 7-day-a-week, 24-hour-a-day basis. Operators and Lessees should communicate with the above points of contact to answer any further questions.

Paperwork Reduction Act

The Paperwork Reduction Act of 1995 requires us to inform you that the information being collected is necessary to document fulfillment of royalty obligations on minerals removed from leases on Federal lands. This information collection is approved by the Office of Management and Budget (OMB) and is titled "Royalty-in-Kind (RIK) Pilot Program—Directed Communications by Operators of Federal Oil and Gas Leases (OMB Control Number 1010-0126, expiration date May 31, 2003)." We will use this information to maintain and audit lease accounts, and we estimate the burden for reporting electronically is 1 hour per response.

Comments on the accuracy of this estimate or suggestions for reducing this burden should be directed to the Information Collection Clearance Officer, Minerals Management Service, 1849 C Street, NW, MS 4230, Washington, DC 20240. Proprietary information submitted to the U.S. Department of the Interior is protected in accordance with standards established by the Federal Oil and Gas Royalty Management Act of 1982 (30 U.S.C. 1733), the Freedom of Information Act (5 U.S.C. 552(b)(4)), and the Departmental Regulations (43 CFR 2). An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB number.

Sincerely,

Milton K. Dial
Assistant Program Director
for Royalty in Kind

Enclosure

Enclosure

PROPERTIES:

Lease/Agreement

Number FMP Number FMP Location Pipeline