

MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT

THIS MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT made and entered into on this 25th day of April, 1989, but effective as of the 17th day of March, 1989, by and between Smith-Gordy Methane Company, a Texas joint venture composed of Lester H. Smith and Russell D. Gordy, both of Harris County, Texas (herein called "Smith-Gordy"), with address of 1225 North Loop West, Suite 1050, Houston, Texas 77008, and the other parties whose names appear on the signature pages hereof, with address of 601 Jefferson Street, Suite 3600, Houston, Texas 77002 ("the Cullen Group");

W I T N E S S E T H:

1.

Smith-Gordy and the Cullen Group have entered into a Participation Agreement (herein called "the Participation Agreement") dated April 25, 1989, but effective as of March 17, 1989, providing for the sale by Smith-Gordy to the Cullen Group, subject to an overriding royalty interest and to reversionary interests after the recoupment by the Cullen Group of certain costs, amounts and expenses, of interests in leases and agreements pursuant to a Development Agreement (herein called "the Development Agreement") dated April 12, 1989, effective as of March 17, 1989, between McKenzie Methane Corporation (herein called "McKenzie") and Smith-Gordy which provides for the development and production of coalbed gas and occluded gas from coal seams, together with other minerals as provided therein, from the lands (herein called "the Contract Area") covered by and pursuant to the terms of the leases and contracts described in Exhibit "A" attached hereto and made a part hereof. The Development Agreement designates McKenzie as Operator to conduct operations on the Contract Area for the development and production of such coalbed gas and occluded gas and other minerals on behalf of itself and Smith-Gordy in accordance with and subject to the terms of the Development Agreement and an Operating Agreement attached to and made a part of the Development Agreement (herein called "the Operating Agreement").

2.

The Development Agreement and the Operating Agreement provide, among other matters, that the parties thereto (and their successors) are to bear and share in the manner and percentages provided therein the costs and expenses incurred in the development and production of coalbed gas and occluded gas and other minerals from the Contract Area. The Participation Agreement provides, among other matters, that Smith-Gordy and the Cullen Group will bear and share such costs and expenses to be borne by Smith-Gordy in the manner set forth in the Participation Agreement, and each such party grants to the other in the Participation Agreement liens and security interests covering their interests in the Contract Area, the leasehold equipment thereon and the production therefrom to secure the payment of such party's share of such costs and expenses. The purpose of this Memorandum of Participation Agreement and Financing Statement is to afford notice to third parties of the existence of the Participation Agreement and to secure and perfect the mutual liens and security interests granted by Smith-Gordy and the Cullen Group to each other therein. This Memorandum of Participation Agreement and Financing Statement incorporates by reference all of the terms, covenants and conditions of the Participation Agreement, the Development Agreement and the Operating Agreement, including but not limited to the lien and security interest provisions contained in the Participation Agreement. Among other matters, the Participation Agreement specifically provides to the effect as follows:

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Harpold, Mr. Donald Fitzgerald

1. Smith-Gordy is to manage the jointly-owned properties in the Contract Area as permitted and required by, and within the limits of, the Participation Agreement;
2. The liability of the parties shall be several, not joint or collective, and each party (including the respective members of the Cullen Group) shall be responsible only for its share of obligations thereunder and shall be liable only for its proportionate share of the costs and expenses incurred in developing and operating the Contract Area as provided in the Participation Agreement;
3. The Cullen Group thereby grants to Smith-Gordy a lien upon its coalbed gas, occluded gas and other mineral leasehold rights in the Contract Area, and a security interest in its share of coalbed gas, occluded gas and other minerals when extracted and in its interest in all equipment on the Contract Area, to secure the payment by the Cullen Group of its share of costs and expenses, together with interest thereon at the rate provided in the Participation Agreement; and
4. Smith-Gordy thereby grants to the Cullen Group a lien upon its coalbed gas, occluded gas and other mineral leasehold rights in the Contract Area, and a security interest in its share of coalbed gas, occluded gas and other minerals when extracted and in its interest in all equipment on the Contract Area, to secure the payment by Smith-Gordy of its share of costs and expenses, together with interest thereon at the rate provided in the Participation Agreement.

3.

Executed copies of the Participation Agreement are in the possession of Smith-Gordy and the Cullen Group. To the extent that the Participation Agreement expires, terminates or does not continue in force and effect as to lands, or portions thereof, covered by the leases and contracts described in Exhibit "A" attached hereto so that the provisions thereof and the liens and security interests referenced herein are no longer applicable to such lands or portions thereof, the parties hereto, upon the request of either, shall execute a recordable release hereof which describes such lands or portions thereof to which the Participation Agreement has expired or terminated or are no longer in effect.

4.

It is understood between Smith-Gordy and the Cullen Group that, as to certain of the leases and contracts described in Exhibit "A" attached hereto, prior consent or approval of assignments thereof and/or mortgages or pledges encumbering McKenzie's interest and the interest of Smith-Gordy in such leases and contracts is required from the lessors of those leases or from the parties with whom Smith-Gordy or its predecessors in interest have contracted. The parties agree that no such assignment or assignments of such leases or contracts shall be made, and in no event shall either the Participation Agreement or this Memorandum of Participation Agreement and Financing Statement constitute or be deemed to constitute an assignment or encumbrance of, or an agreement to assign or encumber, any interest of Smith-Gordy thereunder, until the requisite consent has been obtained from the lessors of such respective leases, from the respective parties with whom Smith-Gordy or its predecessors have contracted, or from their respective successors in interest.

5.

It is further understood between Smith-Gordy and the Cullen Group that the Contract Area may be enlarged from time to time as such parties acquire additional leases or contractual rights thereto as provided in the Development Agreement and Participation Agreement, and Smith-Gordy and the Cullen Group agree to amend this Memorandum of Participation Agreement and Financing Statement from time to time as such leases or contract rights are acquired so as to revise Exhibit "A" attached hereto to reflect that such leases and contract rights so acquired and the interests of Smith-Gordy and the Cullen Group therein are subject to the terms of the Participation Agreement.

6.

In the event that any phrase, clause, sentence, section, paragraph or provision of this Memorandum of Participation Agreement and Financing Statement shall be declared invalid, illegal or unenforceable in any respect by a final decree of a court having jurisdiction with respect hereto or to any portion of the Contract Area, such decree shall in no event affect, prejudice or disturb the validity of any other phrase, clause, sentence, section, paragraph or provision hereof, or the validity of the same phrase, clause, sentence, section, paragraph or provision in any other jurisdiction.

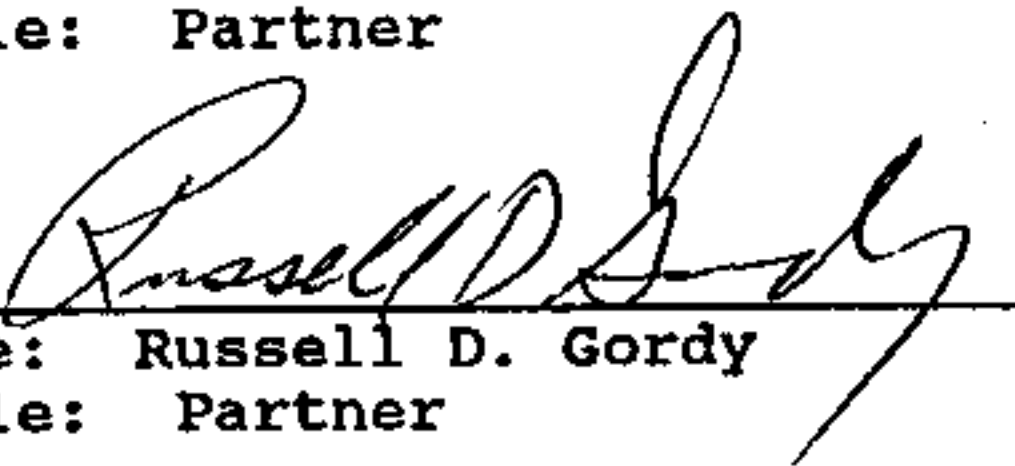
7.

This Memorandum of Participation Agreement and Financing Statement shall be binding upon and shall inure to the benefit of the parties hereto and their respective heirs, devisees, successors and assigns. This Memorandum of Participation Agreement and Financing Statement is executed in multiple originals on the date first shown above. The undersigned each agrees that the signature and acknowledgment pages hereof taken from one or more counterparts of this instrument may be combined into one document for recording, notice and all other purposes to the same extent as if one counterpart hereof were executed and acknowledged by all of them.

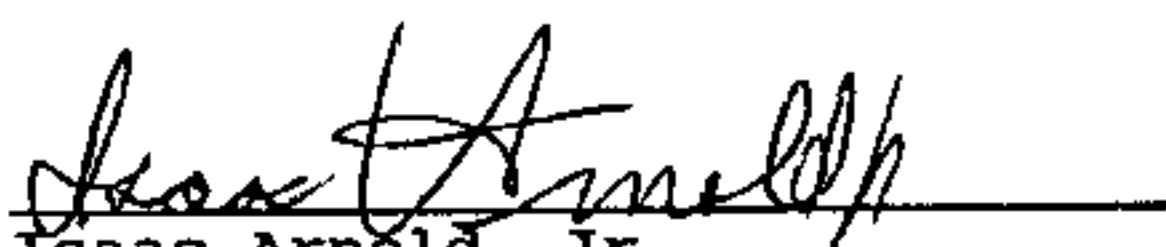
SMITH-GORDY METHANE COMPANY

By: 

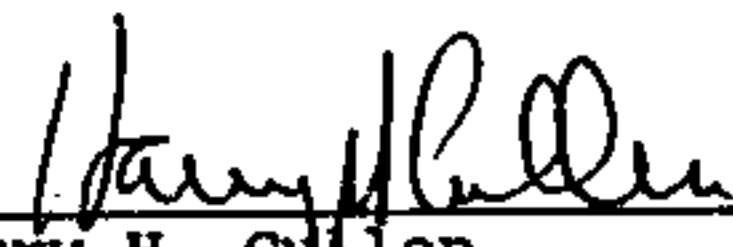
Name: Lester H. Smith
Title: Partner

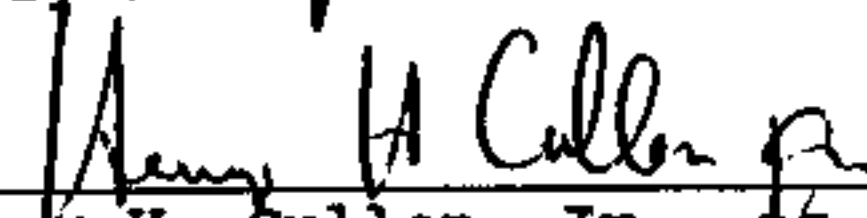
By: 

Name: Russell D. Gordy
Title: Partner


Isaac Arnold, Jr.

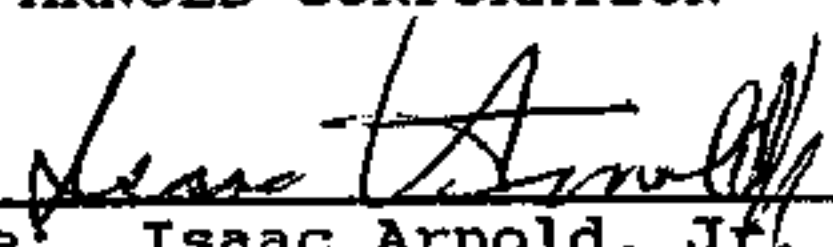

Isaac Arnold, III, as his sole
and separate property

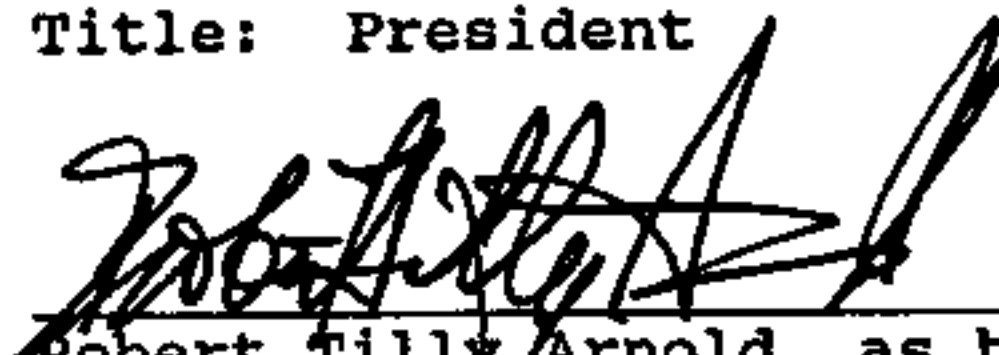

Harry H. Cullen


Harry H. Cullen, Jr., as his
sole and separate property


Katherine Cullen McCord, as her
sole and separate property

THE ARNOLD CORPORATION

By: 
Name: Isaac Arnold, Jr.
Title: President


Robert Tilly Arnold, as his sole
and separate property

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OK
FILED

Antoinette Arnold Wallin May 4. 1966
Antoinette Arnold Wallin, as her sole and separate property

Roy H. Cullen
Roy H. Cullen, as his sole and separate property

Joe Barnhart
Joe Barnhart

Robert J. Barnhart
Robert J. Barnhart, as his sole and separate property

Wilhelmina B. Traylor
Wilhelmina B. Traylor, as her sole and separate property

Douglas B. Marshall, Jr.
Douglas B. Marshall, Jr.

MARSHALL OMAN EXPLORATION, INC.

By: Dee S. Osborne
Name: Dee S. Osborne
Title: President
Vice

Joseph D. Jamail, Jr.
Joseph D. Jamail, Jr.

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This Instrument Was Prepared By:

W. E. McDonald
Harpold, McDonald, Fitzgerald, Mueller & Hall
One Greenway Plaza East, Suite 820
Houston, Texas 77046-0195

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that Lester H. Smith and Russell D. Gordy, known to me to be the persons whose names as General Partners of SMITH-GORDY METHANE COMPANY, a Texas joint venture, are signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, each acknowledged before me on this day that, being informed of the contents of said instrument, they, in their capacities as such General Partners and in behalf of said joint venture executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 2ND day of May, 1989.



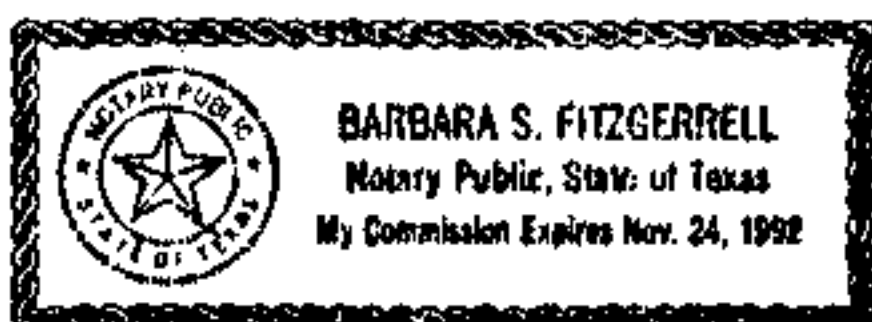
Linda J. Grothues
LINDA J. GROTHUES
(Print Name)
Notary Public in and for
the State of T E X A S

My Commission Expires:
1-31-91

THE STATE OF TEXAS §
COUNTY OF HARRIS §

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I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that HARRY H. CULLEN, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

BOOK
Given under my hand and seal of office this 19 day of May, 1989.



(S E A L)

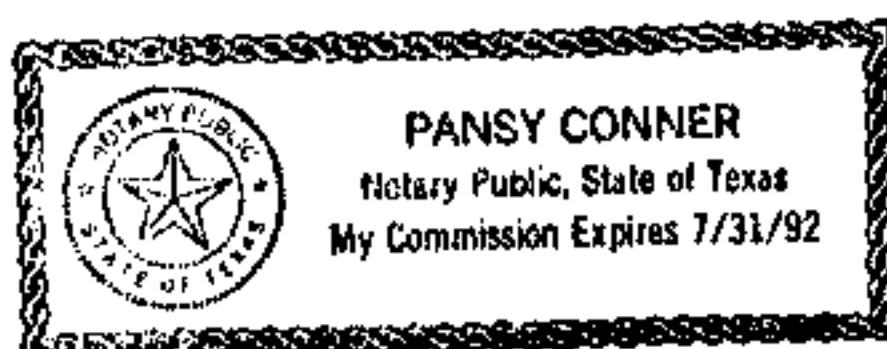
My Commission Expires:

Barbara S. Fitzgerald
(Print Name)
Notary Public in and for
the State of T E X A S

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that HARRY H. CULLEN, JR., known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

June Given under my hand and seal of office this 7th day of *May*, 1989.



Pansy Conner

(Print Name)
Notary Public in and for
the State of T E X A S

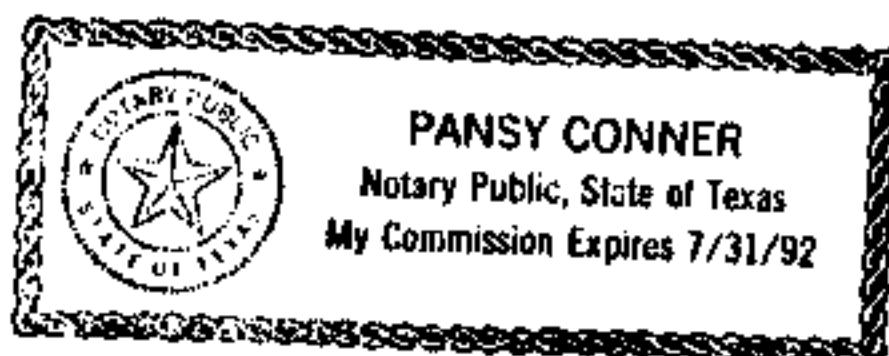
(S E A L)

My Commission Expires:

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that KATHERINE CULLEN MCCORD, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, she executed the same voluntarily on the day the same bears date.

June Given under my hand and seal of office this 7th day of *May*, 1989.



Pansy Conner

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:

BOOK 248 PAGE 416

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ISAAC ARNOLD, JR., known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 15th day of May, 1989.

Wanda S. Black

WANDA S. BLACK

(Print Name)

Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:

6/30/92

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that Isaac Arnold, Jr., known to me to be the person whose name as President of THE ARNOLD CORPORATION, a corporation, is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he, in his capacity as President and in behalf of said corporation executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 15th day of May, 1989.

Wanda S. Black

WANDA S. BLACK

(Print Name)

Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:

6/30/92

BOOK 248 PAGE 417

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ISAAC ARNOLD, III, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 19 day of May, 1989.



Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

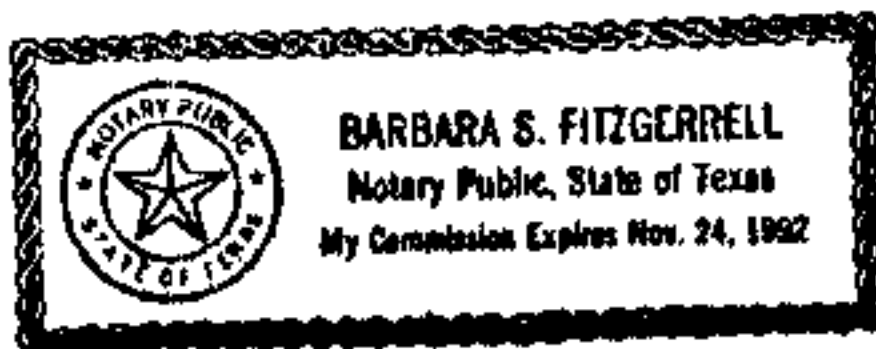
(S E A L)

My Commission Expires:

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ROBERT TILLY ARNOLD, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 23 day of May, 1989.



Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

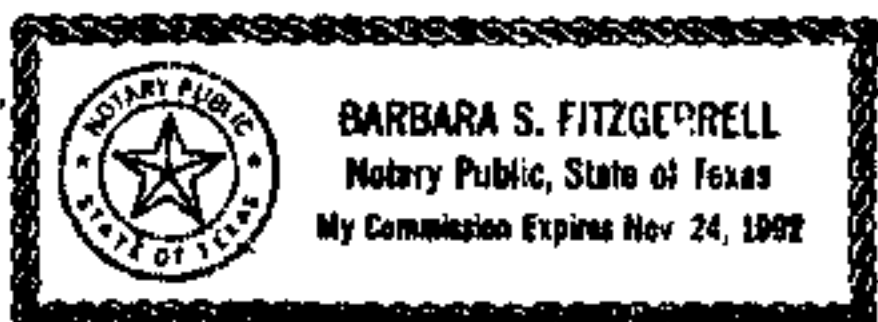
My Commission Expires:

BOOK 248 PAGE 418

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ANTOINETTE ARNOLD WALLIN, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, she executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 22 day of May, 1989.



Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

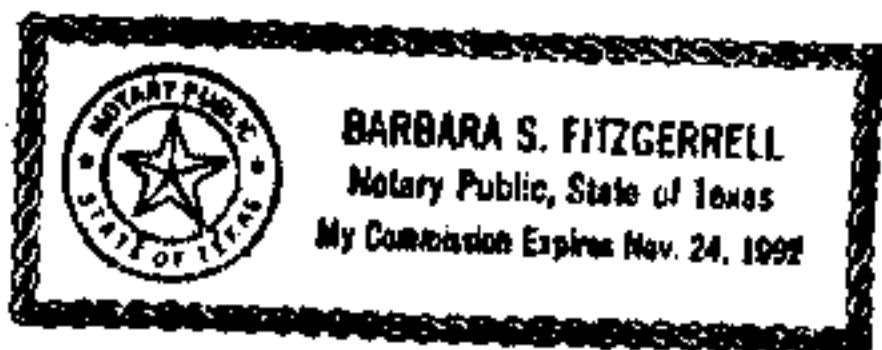
(S E A L)

My Commission Expires:

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ROY H. CULLEN, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 18 day of May, 1989.



Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:

BOOK 248 PAGE 419

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that JOE BARNHART, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 1 day of May, 1989.

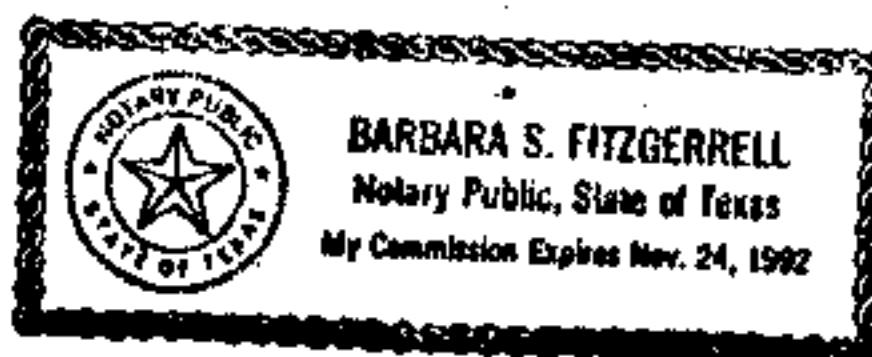
June

Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:



THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ROBERT J. BARNHART, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 1 day of May, 1989.

June

Barbara S. Fitzgerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:



THE STATE OF TEXAS §
 §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that WILHELMINA B. TRAYLOR, known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, she executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 1 day of ~~May~~ June, 1989.

Barbara S. FitzGerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:



THE STATE OF TEXAS §
 §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that DOUGLAS B. MARSHALL, JR., known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 30 day of May, 1989.

Barbara S. FitzGerald

(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:



BOOK 248 PAGE 421

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that ^{Dee S. Osborne} ~~Dee S. Osborne~~, known to me to be the person whose name as ^{President} ~~President~~ of MARSHALL OMAN EXPLORATION, INC., a corporation, is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he, in his capacity as President and in behalf of said corporation executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 2nd day of May, 1989.

June

Susan Blackstock



(Print Name)
Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:

THE STATE OF TEXAS §
COUNTY OF HARRIS §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that JOSEPH D. JAMAIL, JR., known to me to be the person whose name is signed to the foregoing MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT, acknowledged before me on this day that, being informed of the contents of said instrument, he executed the same voluntarily on the day the same bears date.

Given under my hand and seal of office this 5th day of May, 1989.

June

89 JUL 28 AM 9:52

Denise L. Davidson
JUDGE OF PROBATE

Denise L. Davidson

DENISE L. DAVIDSON
(Print Name)

Notary Public in and for
the State of T E X A S

(S E A L)

My Commission Expires:
10-5-89

1. Deed Tax \$ _____
2. Mtg. Tax _____
3. Recording Fee 30.00
4. Indexing Fee 19.00
TOTAL 49.00

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