

1493

MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT

THIS MEMORANDUM OF PARTICIPATION AGREEMENT AND FINANCING STATEMENT made and entered into on this 10th day of May, 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 HAK Partners-I, a Texas joint venture whose Managing Partner is Mitchell Gilbert, with address of 800 Americana Building, Houston, Texas 77002 ("HAK Partners");

W I T N E S S E T H:

1.

Smith-Gordy and HAK Partners have entered into a Participation Agreement (herein called "the Participation Agreement") dated May 10, 1989, but effective as of March 17, 1989, providing for the sale by Smith-Gordy to HAK Partners, subject to an overriding royalty interest and to reversionary interests after the recoupment by HAK Partners of certain costs, amounts and expenses, of interests in leases and agreements pursuant to a Development Agreement (herein called "the Development Agreement") dated May 4, 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. Smith-Gordy and HAK Partners have also entered into a Management Contract (herein called "the Management Contract") of even date with and effective as of the same date as the Participation Agreement which provides for Smith-Gordy to manage the jointly-owned properties in the Contract Area as permitted and required by, and within the limits of, the Management Contract. 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 HAK Partners 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 HAK Partners 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,

Harold McDonald, Fitzgerald, Mueller & Hall

248 PAGE 423

the Management Contract, 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:

1. The liability of the parties shall be several, not joint or collective, and each party 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;
2. HAK Partners 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 HAK Partners of its share of costs and expenses, together with interest thereon at the rate provided in the Participation Agreement; and
3. Smith-Gordy thereby grants to HAK Partners 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.

BOOK 248 PAGE 424

3.

Executed copies of the Participation Agreement and the Management Contract are in the possession of Smith-Gordy and HAK Partners. 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 HAK Partners 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, the Management Contract 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 HAK Partners 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 the Participation Agreement, and Smith-Gordy and HAK Partners 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 HAK Partners therein are subject to the terms of the Participation Agreement and the Management Contract.

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 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

HAK PARTNERS-I

By: 

Name: Mitchell Gilbert

Title: Managing Partner

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 26 day of May, 1989.

Loretta W. Goodenbour
Loretta W. Goodenbour

(Print Name)

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

(S E A L)

My Commission Expires:

3-8-90

THE STATE OF HAWAII §
COUNTY OF HONOLULU §

I, the undersigned notary public in and for the state and county aforesaid, duly authorized to take acknowledgments, hereby certify on this day that Mitchell Gilbert, known to me to be the person whose name as Managing Partner of HAK PARTNERS-I, a Texas joint venture, 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 such Managing Partner 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 18 day of May, 1989.

Luanne Sala
Luanne Sala

(Print Name)

Notary Public in and for
the State of H A W A I I

(S E A L)

My Commission Expires:

Luanne Sala
Notary Public, State of Hawaii

My commission expires January 24, 1992

BOOK 248 PAGE 426

EXHIBIT "A"

Attached to and made a part of the Memorandum of Participation Agreement and Financing Statement dated effective as of March 17, 1989, between Smith-Gordy Methane Company and HAK Partners-I

SAN JUAN AREA

Contracts:

1. (COSJUAN 701) Agreement for Purchase and Sale dated November 1, 1988, effective July 7, 1988, between Carbon River Energy Partnership (Seller) and McKenzie Methane Corporation (Purchaser), whereby Purchaser acquired the rights of Seller, subject to a 2% overriding royalty interest, in the (COSJUAN 700) Exploration and Production Agreement dated November 4, 1986, between Ladd Petroleum Corporation and Carbon River Energy Partnership, a memorandum dated September 3, 1987, of which is recorded in reception #552821, La Plata County, Colorado.

BOOK 248 PAGE 427

CAHABA AREA

Lease:

1. (AL2 001) Coal Seam Gas Agreement and Option dated September 30, 1988, between USX Corporation, as Lessor, and McKenzie Methane Corporation, as Lessee, recorded by a Memorandum of Lease dated November 30, 1988, in Book 222, Page 386, Shelby County, Alabama.

CAINWOOD AREA

Contract:

1. (AL3 700) Agreement dated July 26, 1988 by Gas Technologies, Inc., as Assignor, and McKenzie Methane Corporation, as Assignee, covering the leases described below:
- a. Lease No.: AL3 001
Lease Date: April 29, 1987
Lessor: James M. Cain, Sr., et ux
Lessee: Gas Technologies, Inc.
Recorded In: Book 951, Page 309
Tuscaloosa County, AL
- b. Lease No.: AL3 002
Lease Date: May 14, 1987
Lessor: Mary C. J. Meriwether and
Willis J. Meriwether, Jr.,
Executors and Trustees
Lessee: Gas Technologies, Inc.
Recorded In: Book 951, Page 305
Tuscaloosa County, AL
- c. Lease No.: AL3 003
Lease Date: May 22, 1987
Lessor: Percy L. Spiller, et al
Lessee: Gas Technologies, Inc.
Recorded In: Book 951, Page 299
Tuscaloosa County, AL

CAINWOOD AREA CONTINUED

Leases continued

d. Lease No.: AL3 004

Lease Date: May 15, 1987

Lessor: Charles W. Newton, et al

Lessee: Gas Technologies, Inc.

Recorded In: Book 951, Page 302

Tuscaloosa County, AL

e. Lease No.: AL3 005

Lease Date: May 28, 1987

Lessor: Wilma L. Keeth

Lessee: Gas Technologies, Inc.

Recorded In: Book 951, Page 295

Tuscaloosa County, AL

f. Lease No.: AL3 006

Lease Date: June 4, 1987

Lessor: Eugenia A. Poellnitz, et al

Lessee: Gas Technologies, Inc.

Recorded In: Book 951, Page 292

Tuscaloosa County, AL

g. Lease No.: AL3 007

Lease Date: June 4, 1987

Lessor: Robert W. Poellnitz, Executor

Lessee: Gas Technologies, Inc.

Recorded In: Book 951, Page 288

Tuscaloosa County, AL

h. Lease No.: AL3 008

Lease Date: September 24, 1987

Lessor: Wilbur C. Balk, et ux

Lessee: Gas Technologies, Inc.

Recorded In: Book 957, Page 372

Tuscaloosa County, AL

i. Lease No.: AL3 009

Lease Date: September 17, 1987

Lessor: Doris N. Hinton

Lessee: Gas Technologies, Inc.

Recorded In: Book 957, Page 375

Tuscaloosa County, AL

j. Lease No.: AL3 010

Lease Date: June 8, 1987

Lessor: Turpin Vise, et ux

Lessee: Gas Technologies, Inc.

Recorded In: Book 951, Page 284

Tuscaloosa County, AL

k. Lease No.: AL3 011

Lease Date: September 25, 1987

Lessor: Emmett O. Dendy, et al

Lessee: Gas Technologies, Inc.

Recorded In: Book 957, Page 368

Tuscaloosa County, AL

NARROWS AREA

Contract:

1. Agreement dated June 6, 1988 by Jern, Ltd., and McKenzie Petroleum Company covering the leases described below:

- a. (AL1 001A) Occluded Gas Lease dated May 20, 1983 from United States Steel Corporation, as Lessor, to De-Gas, as Lessee, (the "U.S. Steel Lease"), a declaration of which is filed of record in Book 495, Page 49, Jefferson County, Alabama Probate Records.

BOOK 248 PAGE 428

NARROWS AREA CONTINUED

Leases continued

- b. (AL1 002) Oil and Gas Lease dated July 7, 1982 from The Board of Trustees of the University of Alabama, as Lessor, to Diamond B. Energy, Inc., as amended by Agreement dated April 3, 1987, (the "University Lease"), as recorded in Book 471, Page 475, in the Jefferson County Probate Records.

BOOK 248 PAGE 429

RECORDING FEES

Recording Fee	\$ <u>17.50</u>
Index Fee	<u>5.00</u>
TOTAL	<u>22.50</u>

I CERTIFY TO
INSTRUMENT WAS FILED

89 JUL 28 AM 9:56

JUDGE OF PROBATE