
Opportunity Summary for leasing mineral rights in the Barnett Shale

1. What is the opportunity?

Since gas prices are at historical highs, Oil companies are using innovative technology to look in non-traditional places. One of the hottest current development areas in the US is the Barnett Shale, located in a large regional area around Tarrant County. What makes this formation attractive is that geological risk is low and the wells relatively easy to drill. Application of horizontal drilling and hydraulic fracturing technologies has enabled predictable and economic production rates at today's gas prices.

Development of the Barnett Shale started NW of Forth Worth and is generally moving to the SE. Our neighborhood is currently located on the eastern side of development. This doesn't mean we have less productive shale; just that our area is only now being evaluated as the play expands.

Our neighborhood is special for two reasons:

- a. Homeowners are likely to also be mineral rights owners
- b. 2 vertical wells were drilled in the open field located between North Coppell Road and HWY 121 (they were not drilled to exploit the Barnett however, and are no longer producing)

2. Who are the players?

- a. **Chesapeake Energy** - is the largest oil company participating in the Barnett Shale. They purchased the rights under DFW airport and are actively drilling in our area.
- b. **PFM** - is a third party agent that has been hired by Chesapeake to acquire mineral right leases in western side of Coppell (including our neighborhood). PFM's role is to perform title searches and to make initial contact with all mineral right owners. It is unclear what their role will be in subsequent negotiations.

3. How do I know if I own my mineral rights?

Mineral rights are registered at the Country Courthouse. If you have received a lease proposal from PFM, it means they have performed a preliminary title search to confirm your ownership. If you haven't received an offer yet, don't panic. Chances are good you own your mineral rights since the original developer of our property owned, but didn't retain, the mineral rights when the neighborhood was subdivided. PFM is sending out offers in an ad hoc manner for two probable reasons, 1) staff limitations and 2) to negotiate individually to avoid collective bargaining.

4. How are mineral rights leased?

Mineral owners typically retain permanent rights to their assets. Leases are signed for a limited time period for a specific purpose. In our case, the usual term is for 3 years of initial exploration, followed by an extension for the producing life of the well if one has been drilled. Once production stops, the lease expires and mineral rights return to the permanent owner.

Oil and gas mineral leases contain two payment clauses:

- a. Up front bonus - paid at the beginning of the lease term to the mineral owner for agreeing to the lease. It is typically quoted on a \$/acre basis, so payment will vary based on lot size.
- b. Production royalty bonus - paid as a share of revenue from well production after it is drilled

5. How will the production royalty be split?

Before drilling begins, the oil company will determine the best placement of the well (In our case, most likely to be horizontal wells drilled in a SE direction for about 3000-4000' of lateral displacement from the existing wells). The oil company will aggregate individual mineral leases into a single drilling unit that will share in the production from the well. Sharing will be based on the surface area of the

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mineral rights. For example, if the drilling unit contains 160 acres, and your individual lot is .5 acres large, your share will be 1/320 of the shared amount. Revenue is typically paid monthly based on a spot price benchmark. Expenses for production taxes and well maintenance, although usually small, will also be subtracted from the total amount paid.

6. Are there any safety or environmental issues associated with drilling and production?

Chesapeake understands that their ability to drill near populated areas depends upon being a good corporate citizen. They have an excellent safety record. Industry regulations based on 100 years of best practice have proven to be effective and reasonable. The city of Coppell has also retained a third party consultant to audit their operations.

Since the surface location of the wells will be offset to our neighborhood, there is little risk of longterm hazards. The wells are deep enough to avoid subsidence and contamination of shallow fresh water sands. There may be periods of short term inconvenience (especially noise and lighting) as the wells are drilled. Each well should take 30-45 days to drill and complete. It is currently unknown how many wells will be drilled.

7. How can we negotiate the best deal?

It is logical to think that the best way to maximize our individual reward for leasing our mineral rights is to negotiate as a group and to create a competitive bidding situation. This logic is confirmed by the practical experience of many other neighborhoods in the DFW area. It is not unusual for final prices to be 3x to 4x the original offer. An excellent example of the power of this collective approach is called the NW360 Coalition – a group of residents in Euless and Grapevine that have banded together and are negotiating both with Chesapeake and XTO.

(website reference: <http://360NW.info/> contains an excellent writeup of their experience and plans)

So far in Coppell, our HOA has contacted the HOAs of adjacent neighboring groups to form a similar coalition. This is an activity that has just started, so organization and structure is preliminary and evolving. As a first step, the following website has been created for sharing of information between residents: <http://Coppellwestsidegascoalition.info/>

The most important action to be taken immediately is to get the word out to our fellow neighbors to not sign the original offer from PFM and to establish communication networks for keeping each other informed about the status of contacts and negotiations between PFM and home owners.

In addition to financial compensation, there are important liability issues that need to be included in the final mineral lease. Two examples of these are 1) warranty of mineral ownership and 2) compensation of property damage in case of a safety incident. Both of these are not addressed in the current lease and should be negotiated collectively.

8. Does the HOA have access to legal council?

Officially no. Lawyers and other oil & gas professionals who live in our neighborhoods have volunteered their help. The NW360 group has retained a lawyer to be paid as part of their lease settlement.

There will also be increased HOA operating expenses associated with collective bargaining. Your membership in the HOA will help to offset these extra costs.

9. Can I negotiate with PFM individually?

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Yes. There is no legal requirement for you to negotiate collectively, just peer pressure from your neighbors and rejection of the logic that collective bargaining will obtain the best terms. For those who desire short term cash, there are third parties willing to buy your rights at current prices in the hope to be rewarded with better prices later. If you plan to sell your house soon, you can retain your mineral rights separately as part of the sales agreement.

10. What happens if I don't sign a lease?

If you choose not to sign, a well can be drilled, but not produced, within 340' of your property line. This will present a well positioning complexity to Chesapeake, but will not block them from drilling once a majority of leases have been obtained. If you do not sign a lease, you will not share in any lease bonus payments.

If you have further questions, please contact Philip Frink