

FARMOUT & PARTICIPATION AGREEMENT

This Agreement dated the ____ day of _____, _____.

BETWEEN / AMONG:

_, a body corporate, having an office in the City of _____, in the Province of Alberta
(hereinafter referred to as "_")

OF THE FIRST PART

- and -

_, a body corporate, having an office in the City of _____, in the Province of Alberta
(hereinafter referred to as "_")

OF THE SECOND PART

WHEREAS the Farmee desires the right to acquire an interest in the Title Documents and the Farmout Lands upon the terms and conditions hereinafter set forth;

NOW THEREFORE, in consideration of the premises and the covenants and agreements herein contained, it is agreed by the parties as follows:

1.00 **DEFINITIONS**

The following terms and expressions shall have the meanings hereinafter assigned to them, namely:

- (a) "Abandon" or "Abandonment" and the derivatives thereof means the proper plugging and abandoning of a well in compliance with all Regulations and shall also include the restoration of the wellsite to the satisfaction of any governmental body having jurisdiction with respect thereto and to the reasonable satisfaction of the owner or occupier of the surface, and the furnishing of satisfactory evidence by Farmee to Farmor of the performance hereunder if so requested;
- (b) "Accounting Procedure" means the Exhibit entitled "Accounting Procedure" attached to and made a part of the Operating Procedure;
- (c) "Agreement" means this agreement and the Schedules attached thereto;
- (d) "Cap" or "Capping" means to seal and shut in a well prior to installation of a wellhead so as to enable that well to be Completed at a later date;
- (e) "Capping Costs" means the costs of Capping a well.
- (f) "Complete" or "Completion" and the derivatives thereof means in the case of a well capable of producing Petroleum Substances in at least Paying Quantities:
 - (i) in the case of an oil well, the acquisition and installation of production casing in the hole (exclusive of surface and intermediate casing) and all other equipment, materials and services required for completion of the well up to and including the outlet valve at the

wellhead, and the conduct of a cumulative production test sufficient to establish the initial producibility of the well; and

- (ii) in the case of a gas well, the acquisition and installation of production casing in the hole (exclusive of surface and intermediate casing) and all other equipment, materials and services required for completion of the well up to and including the outlet valve at the wellhead and running adequate back pressure tests and a sustained production test consisting of an absolute open flow potential test sufficient to establish the initial producibility of the well;
- (g) "Completion Costs" means the costs of Completing a well;
- (h) "Contract Depth" means a depth sufficient to penetrate at least _____ metres into the Formation or to a final total depth of _____ metres subsurface, whichever depth first occurs;
- (i) "Drilling" and the derivatives thereof means all activities incidental to the drilling of a well and all services in respect thereof including, without restricting the generality of the foregoing, the acquisition of all surface rights, construction of access roadways and wellsite, drilling, testing, logging and the acquisition and installation of all surface and intermediate casing as well as material and services in respect thereof;
- (j) "Drilling Costs" means the costs of Drilling a well;
- (k) "Drilling Parties" means those parties participating in all costs associated with the Test Well as such parties are identified in Subclause 5.02;
- (l) "Earning Depth" means _____;
- (m) "Effective Date" means _____;
- (n) "Equip" or "Equipping" and the derivatives thereof means the acquisition and installation of equipment beyond the outlet valve at the wellhead required to produce Petroleum Substances from a well, including without limiting the generality of the foregoing:
- (i) in the case of an oil well, the acquisition and installation of pumping equipment, flowlines, production tankage and all other equipment necessary for the production of Petroleum Substances; and
 - (ii) in the case of a gas well, the acquisition and installation of compressors, separators, heaters, treaters, dehydrators or other hydrate control facilities, production test tanks and all other equipment necessary for the production of Petroleum Substances
- but specifically excluding any equipment required to Complete the well and any costs incurred beyond the point of entry into a gathering system, plant or other common facility which is or will be operated pursuant to a separate agreement.
- (o) "Equipping Costs" means the costs of Equipping a well;
- (p) "Farmee" means FARMEE;
- (q) "Farmor" means FARMOR;

- (r) "Farmout Lands" means the lands set forth and described in Schedule "A" attached hereto and includes the Petroleum Substances within, upon or under such lands to the extent that such substances are granted by the Title Documents;
- (s) "Lands" means all formations penetrated by the Test Well which underlie _____, in Township ____, Range ____, West of the Meridian and includes the Petroleum Substances therein, together with the right to explore for and recover same;
- (t) "Operate" and "Operating" and the derivatives thereof means to carry out functions similar to those imposed on an operator pursuant to the Operating Procedure after earning has occurred in the Test Well Spacing Unit, exclusive of the operation of any production facility, together with such additional duties imposed by this Agreement;
- (u) "Operating Costs" means all monies expended (exclusive of Drilling Costs, Capping Costs, Completion Costs and Equipping Costs) to Operate a well for the recovery of Petroleum Substances, as more particularly set forth in the Accounting Procedure;
- (v) "Operating Procedure" means the Schedule, if any, hereto entitled "CAPL Operating Procedure";
- * (w) **"Option Lands" means the lands designated as such in Schedule "A" attached hereto and includes the Petroleum Substances within, upon or under such lands to the extent that such substances are granted by the Title Documents;**
- * (x) **"Option Well" means a well that the Farmee may drill pursuant to the Clause entitled "Option Well";**
- (a) "Overriding Royalty" means that interest in the Petroleum Substances which may be reserved to Farmor under this Agreement and as described in detail in the Royalty Procedure;
- (b) "Paying Quantities" means the anticipated output from a well of that quantity of Petroleum Substances which would reasonably warrant incurring (or having incurred) the Completion Costs and Equipping Costs of the well, considering the anticipated Operating Costs associated therewith, the kind and quality of Petroleum Substances indicated, the anticipated availability of facilities for treating and processing such Petroleum Substances and the anticipated cost of such services, the anticipated availability of markets for such Petroleum Substances, the anticipated availability of transportation service for the delivery of such production to market and the anticipated cost of such service, the royalties and other burdens payable by the Farmee with respect to such production, the probable life of the well and the anticipated price to be received for the Petroleum Substances produced therefrom as and when sold;
- (c) "Payout" means that point in time when Farmee's share of the gross income attributable to the production of or allocation of production of Petroleum Substances from the Test Well Spacing Unit equals for the first time Farmee's share of the total Drilling, Completion, Capping, Equipping and Operating Costs of the Test Well, including payment of the royalties payable to the lessor under the Title Documents, any other encumbrances as may be set forth in Schedule "A" and the Overriding Royalty payable to Farmor pursuant to this Agreement, but less any payments received by Farmee related to the Test Well pursuant to any incentives, credits, payments or grants, governmental or otherwise;
- (d) "Participant" means (hereinafter sometimes referred to as "_");

- (e) "Petroleum Substances" means petroleum, natural gas and every other mineral or substance, or any of them, in which an interest in or the right to explore for is granted or acquired under the Title Documents insofar as they relate to the Farmout Lands;
- (f) "Regulations" means all statutes, laws, rules, orders and regulations in effect from time to time made by governments or governmental boards or agencies having jurisdiction over the Farmout Lands and over the operations to be conducted thereon;
- (g) "Rentals" or "Rental Payments" means all rents, renewals, taxes, penalties and other payments together with compensatory royalty and drilling deferment penalties payable with respect to the Title Documents, but shall not include the initial consideration paid by Farmor with respect to any of the Title Documents;
- (h) "Royalty Procedure" means the Schedule, if any, hereto entitled "Royalty Procedure";
- (i) "Spacing Unit" means at the relevant time with respect to which the term is used herein:
 - (i) with respect to a well which has not been Completed for the production of Petroleum Substances, the area allocated by the Regulations for the purpose of drilling that well, provided that in the absence of such allocation, the spacing unit for the well shall be deemed to be the quarter-section, unit or similar geographical area which includes the bottomhole co-ordinates of the well; and
 - (ii) in every other case, the area allocated to the well pursuant to the Regulations for the purpose of producing Petroleum Substances in each zone from which such Petroleum Substances are to be produced;
- (j) "Spud" means with respect to a well, that a drilling rig of adequate capacity to drill that well to Contract Depth is rigged-up on location and that a drilling bit has penetrated the surface therefrom;
- (k) "Test Well" means the well or wells drilled by Farmee as one of the Drilling Parties pursuant to the Clause hereof entitled "Test Well";
- (l) "Test Well Spacing Unit" means the Spacing Unit of the Test Well; and
- (m) "Title Documents" means the documents set forth and described as such in Schedule "A" attached hereto and any renewals or extensions thereof or further Title Documents issued pursuant thereto insofar as they relate to the Farmout Lands.

2.00 SCHEDULES

The following Schedules are attached hereto and incorporated into this Agreement:

- * (a) Schedule "A" which sets forth the Farmout (**and Option**) Lands and the Title Documents;
- (a) Schedule "B" which is the Operating Procedure, the Accounting Procedure and the Assignment Procedure;
- (b) Schedule "C" which is the Royalty Procedure; and
- (c) Schedule "D" which comprises the Well Information Requirements of Farmor.

3.00 **TITLE**

3.01 **Requisite Authority**

Each of the parties hereto represents and warrants that it has the requisite capacity, power and authority to execute this Agreement and to perform the obligations to which it thereby becomes subject.

3.02 **Farmor Makes No Warranty of Title**

Farmor does not warrant title to the Farmout Lands or the Title Documents or agree to convey to Farmee any better title thereto than Farmor has on the Effective Date. Farmor, to the extent of its interest in the Title Documents and Farmout Lands, covenants that the Farmout Lands are only encumbered by the applicable lessor's royalty and any other encumbrances as set forth in Schedule "A", and that it has complied with all the terms of the Title Documents to the extent necessary to maintain them in force as of the Effective Date.

3.03 **Responsibility for Encumbrances**

Except as otherwise provided herein, if the interest of any party in the Lands is now or hereafter shall become encumbered by any royalty, overriding royalty, production payment or other charge of a similar nature, other than the lessor's royalty under the Title Documents, other encumbrances as set forth in Schedule "A" and the Overriding Royalty reserved to Farmor hereunder which shall be borne as herein provided, such royalty, overriding royalty, production payment or other charge of a similar nature shall be charged to and paid entirely by the party whose interest is or becomes thus encumbered.

4.00 **PARTIES**

4.01 **More than One Farmor Party**

Reference in this Agreement to "Farmor" shall mean collectively or individually, as the context requires, all the parties hereinbefore identified as comprising Farmor and where the terms of this Agreement require notice or information to be delivered to or received from Farmor, a separate notice shall be required for each party comprising Farmor.

4.02 **Interests of Farmor Parties**

All rights, duties, obligations, elections and privileges to which Farmor is entitled under this Agreement shall be shared and may be separately exercised by each Farmor party in the following percentages of interest:

%
%

5.00 **TEST WELL**

5.01 **Farmee to Spud Test Well**

On or before _____, _____, Farmee as one of the Drilling Parties, shall Spud the Test Well at a location of its choice on the Farmout Lands and shall diligently and continuously, at the sole cost, risk and expense of the Drilling Cost Interests, drill same to at least Contract Depth, log, test to the reasonable satisfaction of Farmor all formations prospective of containing Petroleum Substances

and either Complete, Cap or Abandon it in accordance with the terms of this Agreement and the Regulations.

5.02 **Drilling Cost Interests**

All costs associated with the Test Well shall be shared by the Drilling Parties in the following percentages:

%

%

in this Agreement sometimes referred to as the "Drilling Cost Interests".

5.03 **Capping of Test Well**

If the Test Well is Capped for lack of an available natural gas market, Farmee agrees to make diligent efforts to obtain a market and to Complete and Equip the Test Well for production at its sole cost, risk and expense in accordance with the Drilling Cost Interests, at such time as a market is available.

6.00 **OPERATIONS**

6.01 **Operations Conducted in Proper Manner**

Farmee shall, in conducting all Operations hereunder:

- (a) comply on a timely basis with the provisions of the schedule attached hereto, entitled "Well Information Requirements of Farmor"; and
- (b) perform in a diligent and workmanlike manner, in accordance with good oilfield practice and in strict compliance with the terms of the Title Documents, this Agreement and the Regulations.

7.00 **INSURANCE**

7.01 **Farmee to Maintain Insurance**

The kinds and amounts of insurance to be carried by Farmee in conducting operations with respect to the Farmout Lands shall not be less than those amounts provided in Clause 311A of the Operating Procedure. In addition to the policies of insurance required under Clause 311A of the Operating Procedure, Farmee shall obtain and maintain control of well insurance to the extent of a minimum of five million dollars (\$5,000,000) with respect to each well Drilled hereunder and each such policy shall also include the waivers of subrogation required by Clause 311 A of the Operating Procedure. All costs of insurance maintained by Farmee pursuant to this Clause shall be borne solely by Farmee and, upon request of Farmor or Participant, Farmee shall promptly provide such party with evidence that such insurance is maintained by Farmee, including a copy of any particular policy of insurance if so requested by thereby.

8.00 **SUBSTITUTE WELL**

8.01 **Drilling of Substitute Well**

If in the Drilling or Completing of the Test Well, Farmee encounters Operating difficulties (which shall not include lack of finances) or impenetrable formations that in Farmee's reasonable opinion make such Drilling or Completion of the Test Well inadvisable, Farmee shall promptly notify Farmor of the problems so encountered. Farmee may terminate such Drilling or Completion of the Test Well after first obtaining the written consent of Farmor, which consent shall not be unreasonably withheld.

Within thirty (30) days of receipt by Farmor of notification that the Test Well has been Abandoned, Farmee may commence Drilling a substitute well at a location of its choice on the Farmout Lands. The substitute well shall be deemed to be the Test Well and all provisions of this Agreement which apply to the Test Well shall apply, mutatis mutandis, with the same force and effect to the substitute well.

9.00 **INTEREST EARNED**

9.01 **Interest to be Earned by Farmee - Test Well**

Provided Farmee has fulfilled its obligations pursuant to the Clause entitled "Test Well" hereof and provided further that Farmee is not in default of any term or condition of this Agreement, then Farmee shall have earned and Farmor shall convey to or hold in trust for Farmee:

- (a) One hundred percent (100%) of Farmor's interest down to Earning Depth in the Title Documents and Farmout Lands insofar as they comprise the Test Well Spacing Unit, subject to the lessor's royalty, any other encumbrances as set forth in Schedule "A" and the Overriding Royalty reserved to Farmor and calculated in accordance with the Royalty Procedure which shall govern all subsequent Operations as between Farmor and Farmee on the Test Well Spacing Unit until conversion of such Overriding Royalty as provided herein; and
- (b) percent (%) of Farmor's interest down to Earning Depth in the balance of the Farmout Lands and in the Title Documents pertaining thereto.

10.00 **OPTION WELL**

10.01 **Option Well Election**

- * **If Farmee has fulfilled its obligations pursuant to the Clause entitled "Test Well" hereof and if Farmee is not in default of any term or condition of this Agreement, Farmee shall have the option, for a period of _____ (____) days from rig release date of the Test Well, to elect by notice in writing to Farmor and Participant to drill an Option Well at a location of its choice on the Option Lands. Should Farmee elect to drill an Option Well, it shall have a further _____ (____) days from such election date in which to Spud such well.**

10.02 **Test Well Provisions Apply**

- * **If Farmee elects to drill an Option Well as provided in the preceding Subclause, then all the provisions of this Agreement including the rights of the Participant which apply to the Test Well and the Farmout Lands shall apply mutatis mutandis to the Option Well and the Option Lands.**

11.00 **JOINT OPERATIONS**

11.01 **Operating Procedure to Govern**

Forthwith upon Farmee having earned its interest in the Farmout Lands, the Farmout Lands excluding the Test Well Spacing Unit and the Title Documents as they relate thereto shall become subject to the Operating Procedure which shall govern all future Operations of the parties with respect to the exploration, development and maintenance of such Farmout Lands and Title Documents.

11.02 **Appointment of Operator**

OPERATOR is hereby appointed the Operator under the Operating Procedure, accepts such appointment and agrees to assume the duties, obligations and rights of the Operator under the Operating Procedure.

11.03 **Interests Subsequent to Earning**

After Farmee has earned its interest in the Farmout Lands, the Farmout Lands excluding the Test Well Spacing Unit and the Title Documents as they relate thereto shall be held by the parties in the following undivided percentages of interest (hereinafter called the "participating interests"):

Farmee %
Farmor %
Participant %

11.04 **Proposal of Joint Operations**

Notwithstanding anything herein contained, the parties agree that no party shall propose any joint operations pursuant to the Operating Procedure until such time as Farmee has earned its complete interest under this Agreement or its right to earn has expired or been surrendered, whichever first occurs.

12.00 **CONVERSION OF OVERRIDING ROYALTY**

12.01 **Initial Information to Farmor**

In addition to providing Farmor with all information with respect to the Test Well as required hereunder, Farmee shall furnish Farmor, within ninety (90) days of Completion of the Test Well, with an accurate and itemized record of all Drilling, Completion, Capping, Equipping and Operating Costs incurred by Farmee with respect to the Test Well.

12.02 **Monthly Information to Farmor**

Farmee shall thereafter provide to Farmor, at the end of each month for the immediately preceding calendar month, an accurate and itemized record of all production received from the Test Well, the disposition thereof and the revenues received therefrom, together with such other information as to the Operation of or production received from the Test Well as may be reasonably requested by Farmor. In addition, Farmee shall provide Farmor, at regular intervals not to exceed three (3) months in duration, with Payout statements setting forth the remaining Drilling, Capping, Completing, Equipping and Operating Costs to be recovered from the revenues received from the production obtained from or allocated to the Test Well.

12.03 **Farmor's Right to Convert**

- (a) Upon Payout being reached, and upon Farmor being furnished with all the information required to be furnished by Farmee pursuant to the preceding Subclauses of this Clause, Farmee shall immediately send written notice of Payout to Farmor. Farmor shall then have the right and option for a period of thirty (30) days from receipt of such notice to elect by notice in writing to Farmee to convert the Overriding Royalty attributable to production from the Test Well as provided in the Royalty Procedure to an undivided percent (%) participating interest in the Title Documents and Farmout Lands insofar as they comprise the Test Well Spacing Unit, the well thereon, all equipment therein and thereon and all production therefrom. Provided however that if a party comprising Farmor converts its Overriding Royalty to an undivided participating interest as herein provided, it shall not bear any part of the remaining Overriding Royalty payable to a party comprising Farmor which has not converted to a participating interest.

Failure by Farmor to elect to convert its Overriding Royalty within the thirty (30) day period shall be deemed to be an election not to make such conversion.

- (b) Upon receipt of such notice by Farmee, Farmor and Farmee shall adjust accounts accordingly as of the date that Payout was reached, at which time the Royalty Procedure shall be deemed to be terminated with respect to the Test Well and the Test Well Spacing Unit and the provisions of the Operating Procedure shall apply, mutatis mutandis, to govern the relationship of Farmor and Farmee with respect to all future Operations on the Test Well and Test Well Spacing Unit.

12.04 **Deemed Conversion Upon Abandonment**

In the event that the Test Well is dry and Abandoned, Farmor shall be deemed to have elected to convert its Overriding Royalty hereunder to an undivided percent (%) participating interest in the Title Documents and Farmout Lands insofar as they comprise the Test Well Spacing Unit, the well thereon and all equipment therein and thereon. The effective date of such election will be the first day of the month following the month in which the Test Well is Abandoned.

12.05 **Right of Farmor to Audit**

Farmor shall have the right, at its sole cost and expense, from and after the date of earning until two (2) years after the receipt of notice of Payout of the Test Well, to conduct an inspection and audit of Farmee's books, records and accounts as they relate to the Test Well.

12.06 **Equalization Applied to Payout Account**

If, prior to Payout being reached, the Test Well becomes a unit facility under a unit or pooling agreement and thereby creates an equalization of investment credit or debit, the amount of such credit or debit shall be applied to the Payout account of the Test Well.

12.07 **Farmor Entitled to Interest in Contract and Facility**

In the event that Farmor elects to convert its share of the Overriding Royalty to an undivided interest in the Test Well, it shall then be entitled to an assignment by Farmee of a like interest with respect to the Test Well in any contract for sale of the Petroleum Substances from the Test Well and, subject to reimbursement, the use of sufficient capacity in any facility through which Petroleum Substances are being handled or processed for its share of production from the Test Well.

13.00 **APPLICATION OF OPERATING PROCEDURE**

13.01 **Incorporation of Clauses**

The following Clauses (including all Clauses contained within referenced Articles) of the Operating Procedure shall apply, mutatis mutandis, to this Agreement and to all Operations of Farmee carried out with respect to the Farmout Lands pursuant to this Agreement and shall be deemed to be incorporated herein and where reference in such Clauses is made to "Operator" the word "_" shall be substituted therefor and, similarly, "Joint-Operator" shall be substituted by "Farmor" and "Participant", and "joint lands" shall be substituted by "Farmout Lands", provided, however, that nothing in any of the Clauses of the Operating Procedure that are incorporated by reference into this Agreement shall be interpreted to require Farmor to pay all or any portion of the cost or assume any of the risk of any Operation conducted pursuant hereto.

THIS IS A 20-PAGE DOCUMENT, including schedules.