

**STATE OF NEW YORK  
DEPARTMENT OF ENVIRONMENTAL CONSERVATION**

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In the Matter of the Integration of Interests Pursuant to  
Environmental Conservation Law ("ECL") § 23-0901(3)  
Within an Individual Spacing Unit Known As

DEC Order No. DMN 07-34

Well Name: Usack 1 (the "Well")  
API Number: 31-015-22933-00-00  
Well Operator: Chesapeake Appalachia, LLC

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Whereas:

1. The Department of Environmental Conservation ("Department") issued a permit to drill the Well on July 17, 2001. The Well is presently owned by Chesapeake Appalachia, LLC ("Chesapeake" or "the well operator").
2. Sections 0501 (Well Permits), 0503 (Well Spacing in Oil and Natural Gas Pools and Fields) and 0901 (Compulsory Integration and Unitization in Oil and Natural Gas Pools and Fields) of Article 23 of the ECL were amended on August 2, 2005 (the "new statute").
3. ECL 23-0501(1)(b) of the new statute provides for the establishment of statewide spacing for gas wells, and ECL 23-0503(3) provides for issuance of spacing orders for proposed spacing units which do not conform to statewide spacing.
4. Pursuant to ECL 23-0503(3) and 0503(5), on August 1, 2007, the Department issued a spacing order establishing a non-conforming Spacing Unit for the well (DEC Spacing Order No. DMN 07-NCU-02).
5. Attached to this Order as Exhibit A is a map of the Spacing Unit for the well, and a tabulation of tracts therein is attached as Exhibit B.
6. In accordance with ECL 23-0901(3), the matter of integration of interests within the spacing unit was heard before Department on September 25, 2007 at the New York State Department of Environmental Conservation, 625 Broadway, Room PA-129, Albany, New York 12233 ("compulsory integration hearing"). The affidavit of publication attached as Exhibit C

attests that notice of this hearing was provided pursuant to ECL 23-0901(3)(c) and DEC Program Policy DMN-1.

7. Objections were stated at the compulsory integration hearing that raised substantive and significant issues regarding notice, elections, or integration of interests in the spacing unit as set forth on Exhibit D.

8. Pursuant to ECL 23-0901(3)(d), the matter was referred to the Department's Office of Hearings and Mediation Services for adjudicatory proceedings under 6 NYCRR part 624.

9. A legislative hearing and issues conference were duly noticed and conducted before Chief Administrative Law Judge (ALJ) James T. McClymonds on May 13, 2008. After the issues conference, the Chief ALJ issued a ruling on issues and party status on November 4, 2009 (see Matter of Drumm 1, et al., Ruling of the Chief ALJ on issues and Party Status, November 4, 2009).

10. On administrative appeal, the Commissioner issued an interim decision modifying in part and otherwise concurring with the Chief ALJ's rulings (see Matter of Beach W1, et al., Interim Decision of the Commissioner, Aug. 26, 2011). The Commissioner remanded the matter to the Chief ALJ for further proceedings consistent with the interim decision.

11. The issues on remand were resolved by the parties without the need for adjudication. Accordingly, this Order may be issued without further hearings.

#### FINAL ORDER OF INTEGRATION:

NOW, THEREFORE, having found that due, proper and sufficient notice was given; that all substantive and significant issues have been resolved; and that compulsory integration of interests in the spacing unit as set forth on Exhibit D will serve to protect correlative rights and is necessary to carry out the policy provisions of ECL 23-0301, it is hereby ORDERED that:

I. The subject spacing unit is integrated pursuant to ECL §23-0901(3) with respect to the Black River formation and includes the whole or partial tracts listed on Exhibit B. All operations including, but not limited to, the commencement, drilling, sampling, logging, testing, completion, reworking, sidetracking, deepening, re-completing, plugging, plugging back or operation of a well or the existence of a shut-in well upon any portion of the spacing unit shall be deemed for all purposes the conduct of such operations upon each separately owned tract wholly

or partially within the spacing unit, as listed on Exhibit B, by the owner or several owners thereof. That portion of production allocated to each tract in the spacing unit shall, when produced, be deemed for all purposes to have been produced from such tract by a well drilled thereon. A mineral interest owner's right to well data from the operator and access to the well site are subject to the following provisions:

A. Integrated royalty owners, participating owners, and non-participating owners shall have access to well data pursuant to the time periods and confidentiality protections in ECL 23-0313.

B. The operator shall provide each integrated participating and non-participating owner reasonable access to the well site. Site access provided by this Order shall not be exercised in a manner interfering with the well operator's conduct of an operation.

II. The well operator indicated in the caption on page 1 of this Order is the operator of the spacing unit.

III. The well operator shall file a copy of this Order, including the Exhibits thereto, in the office of the County Clerk in the county or counties where the spacing unit is wholly or partially located. The Order shall be filed against all tracts in the spacing unit. The well operator shall also file, in the same manner, any updates to Exhibit D which result after the date of this Order from ownership changes, tax map revisions or corrections, resolution of title disputes and/or other revisions to property and ownership descriptions, provided that the unit boundary as shown on Exhibit A has not changed. The well operator must provide a copy of any such update to the Department, by certified mail, post-marked on the same date that such is filed in the office of the County Clerk. The updated Exhibit D shall be accepted and deemed incorporated into this Order; no further order of the Department shall be required.

IV. Tracts listed on Exhibit D are hereby integrated, on a non-surface entry basis, as set forth therein. Any person taking title by operation of law to any oil and gas interests listed on Exhibit D shall take such interests subject to the terms and conditions of this Order, and shall be subject to all liabilities and benefits associated therewith, unless such person, within sixty days of the taking of such interest, elects to be an integrated royalty owner, as defined at ECL 23-0901(3)(a)(3), and notifies the well operator of such election.

V. The following provisions shall apply to all integrated participating owners and integrated non-participating owners in the spacing unit:

A. The owner shall be liable for its proportionate share of all costs and expenses, including taxes, and claims of third parties related to the well, operations thereon and in conjunction therewith, and shall be entitled to its proportionate share of all benefits therefrom. If an owner's share of production is subject to a risk penalty as defined by ECL 23-0901(3)(a)(4), the well operator shall establish a risk penalty account for such owner and all costs, expenses and benefits attributable to such owner shall be reflected in the penalty account;

B. The well operator shall hold any funds paid by the owner or recouped through the risk penalty attributable to the plugging and abandonment costs of the well, as estimated prior to the drilling of the well, in an interest bearing account until such funds are required and utilized for such purpose;

C. The owner shall be liable for and shall indemnify all other persons participating in the development of the well, whether participating owners, non-participating owners or otherwise, including the well operator, from and against all claims arising out of the owner's non-payment of rentals, royalties and other payments or burdens on the oil and gas rights that such owner contributes to the spacing unit and from and against all claims associated with the loss or failure of title to the oil and gas rights the owner contributes to the spacing unit;

D. The well operator shall have a first lien on the production of the owner to pay any outstanding costs, expenses or claims and the well operator shall be entitled to withhold and retain for the purposes of set off any revenue or production owed or due to the owner under an order of integration. Nothing in this paragraph shall affect the well operator's right to collect any outstanding amounts incurred nor the right of any fee owner of oil and gas interests to collect any amounts owed under the terms of any lease from such owner. The exercise of any remedy shall not preclude the well operator from seeking any other remedies available under the law;

E. Whether or not the owner is subject to a risk penalty, the well operator shall submit to the owner a written authority for expenditure of the estimated costs associated with the construction of any facilities not included in well costs beyond the surface equipment at the wellhead to the first point of interconnection with other facilities that commingle production from a group of wells that includes the well, including, but not limited to, pipe, compression, processing, treating, dehydrating or separating equipment, fixtures, related buildings and other equipment. The owner shall have thirty days to elect to participate and pay its proportionate share of such estimated cost, the failure of which shall be deemed to be an election by the owner not to participate. If the owner elects not to participate or is deemed to have elected not to participate, the well operator shall be entitled to retain for its own account all of the owner's share of production from the well until the well operator has recouped from the net proceeds of

the owner`s share of production the owner`s share of the actual costs of the facilities, plus a risk penalty of one hundred percent of such costs. Any such amounts shall be added to the risk penalty account for such owner;

F. If the owner is not subject to a risk penalty, the owner shall have the right to take its share of gas or oil production in kind and shall be responsible for its transportation and marketing arrangements downstream of the facilities constructed pursuant to paragraph E of this section. The owner`s election to take in kind must be conveyed to the well operator no later than fourteen days prior to first production from the well or upon seventy-five days written notice to well operator at any time following first production from the well subject to the expiration of any existing contracts;

G. If the owner is not subject to a risk penalty and does not take its share of gas or oil production in kind, the well operator shall market the owner`s share of production from the well ratably with its own share of production from the well for the account of the owner. The well operator shall pay the owner based on the price received by the well operator for production in the general area less (1) the owner`s proportionate share of all costs incurred by the well operator for transporting, treating, processing, or otherwise making the production marketable, and (2) a marketing fee not to exceed five percent of the sales price of the production;

H. The well operator shall be entitled to propose and conduct a subsequent operation on a well, meaning any reworking, sidetracking, deepening, re-completing or plugging back of the well or the drilling of a lateral or an infill well in the formation for which the unit was created. Owners shall be provided with a written authorization for expenditure of the estimated costs of the subsequent operation. An owner shall not be entitled to participate in a subsequent operation as long as the owner is in a risk penalty phase. If a subsequent operation is proposed while an owner is in a risk penalty phase, the owner`s proportionate share of the actual cost of the subsequent operation plus two hundred percent of such actual costs shall be added to the risk penalty account for such owner. The owner not in a risk penalty phase shall have thirty days to elect and pay its proportionate share of the estimated costs, unless a drilling rig is on location, in which event notice of a subsequent operation may be given by telephone and the owner shall have forty-eight hours, exclusive of Saturday, Sunday and legal holidays, to make an election and thirty days to pay the owner`s proportionate share of costs. The failure of any such owner to elect and pay in a timely manner shall be deemed an election by the owner not to participate in the subsequent operation. If such owner elects or is deemed to have elected not to participate in the subsequent operation, the well operator shall be entitled to retain all of the owner`s proportionate share of production from the well until the well operator has recouped the

proportionate share of the actual costs of the subsequent operation attributable to such owner, plus two hundred percent of such actual costs; and

I. The well operator, on behalf of the owner, shall be entitled to conduct all acts associated with the well and necessary facilities related thereto, including without limitation: conducting title examination and curative work on the tracts included in the spacing unit; arranging for contract services or employees of the well operator, at the customary salaries, wages and benefits of such employees, to oversee the operation and maintenance of the well and the facilities in the production unit associated with the well; arranging for and maintaining required financial security for well bonds and insurance; discharging litigation, claims of third parties and disputing tax assessments; developing and implementing emergency responses and dealing with catastrophic events; and arranging for the storage, transporting and disposal of produced water, by-products or refuse associated with production and maintenance facilities.

VI. The following additional provisions shall apply to the well operator:

A. The well operator shall hold any funds paid by integrated participating owners for estimated well costs in an interest bearing account until such funds are required and utilized to pay actual well costs. Accrued interest shall be applied to each participating owner's share of additional costs, or refunded pursuant to Paragraph C of this Section.

B. Within ninety days of the date of this Order, the well operator shall provide integrated participating and non-participating owners with an itemized statement (calculated as of the date of this Order) of actual well costs incurred, the amount held in escrow for plugging, abandonment and reclamation, and actual well production, including actual well revenue.

C. No later than the date of the statement required by Paragraph B of this Section, the well operator shall refund to the integrated participating owners any amount paid by the integrated participating owners or withheld from the owners' share of production which, as of the statement date, exceeds the total of actual well costs incurred plus any estimated plugging, abandonment and reclamation costs, which may be held in escrow pursuant to Paragraph B of Section V of this Order. If the statement shows that well production exceeds actual well costs incurred plus any estimated plugging, abandonment and reclamation costs, the well operator shall also pay (no later than the date of the statement required by Paragraph B of this Section) the owners their proportionate share of well production as provided for in Section V, Paragraph G of this Order. If the statement shows that actual well costs and the amount held in escrow for plugging, abandonment and reclamation exceed the estimated well costs paid by the integrated participating owner and the owner's proportionate share of well production, the owner shall pay

to the well operator the owner's proportionate share of the additional well costs within 30 days of the date of the statement.

D. If recoupment as provided for in ECL 23-0901(3)(a)(1) has occurred prior to the date of this order, the well operator will compensate non-participating owners for their proportionate working interest share of production, if any, minus their proportionate share of costs, which occurred after recoupment. Compensation shall occur no later than 90 days after issuance of this order, and shall be accompanied by an accounting of production proceeds received to date.

E. Regardless of whether recoupment has occurred, the well operator must, no later than 90 days after issuance of this order, release any applicable royalties held in escrow pursuant to any previous Stipulation, including royalties due to the well operator's lessors, integrated royalty owners and integrated non-participating owners of leased tracts. The well operator is authorized to release to itself any excess royalties held in escrow pursuant to any previous stipulation.

VII. The well operator may charge participating and non-participating owners a customary fixed rate for supervision of ongoing operations. Supervision includes the following:

A. Wages, benefits and expenses of field personnel directly employed in well operations or while in transit to or from the well, and

B. Transportation of company labor, contract personnel and material necessary for well operations, subject to standard industry limitations on transportation as set forth in Section III.4 of the Council of Petroleum Accountants Societies (COPAS) – 1995 Accounting Procedure, Joint Operations.

VIII. Written communications required by this Order shall be transmitted by United States Postal Service, private courier service or hand-delivered as follows.

A. Communication from integrated owners, the well operator and other interested persons to the Department shall be made to:

Director, Bureau of Oil and Gas Permitting and Management  
New York State Department of Environmental Conservation  
Division of Mineral Resources  
625 Broadway, 3<sup>rd</sup> Floor  
Albany, NY 12233-6500  
Phone: (518) 402-8056

B. Communication from integrated owners and the Department to the well operator shall be made as stated below, unless the well operator has informed the integrated owners and the Department of a change in writing in accordance with this Section.

Mike Brownell  
Chesapeake Appalachia, LLC  
300 N. 2nd Street, 5th Floor  
Harrisburg, PA 17101  
Phone: (717) 230-8620

C. Communication from the well operator and the Department to integrated owners shall be made to the addresses listed on Exhibit D, unless the integrated owners have informed the well operator and the Department of address changes in writing in accordance with this Section.



IX. This order is effective on the date it is signed, and is final and binding upon the well operator, all integrated owners and their heirs, successors and assigns.

NEW YORK STATE DEPARTMENT OF ENVIRONMENTAL  
CONSERVATION

by: \_\_\_\_\_ /s/  
Joseph J. Martens  
Commissioner

Dated: June 18, 2012  
Albany, New York

TO: Director, Bureau of Oil & Gas Permitting and Management, Division of Mineral  
Resources, NYSDEC  
Mineral Resources Program Attorney, Office of General Counsel, NYSDEC  
Well Operator  
Integrated Owners Listed on Exhibit D