A WYOMING LIMITED LIABILITY COMPANY

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

PART 1

SUMMARY OF THE JOINT VENTURE PROSPECT

SUMMARY OF THE JOINT VENTURE PROSPECT

The information contained in Part 1 of the Confidential Private Placement Memorandum – Summary of the Joint Venture Prospect is delivered separately along with the following:

Confidential Purchaser Suitability Questionnaire

Application, Subscription and Customer Agreement

Joint Venture Agreement Signature Execution Page and Limited Power of Attorney

Joint Operating Agreement Signature Execution Page

Joint Operating Agreement – Exhibit A – Scope of Operation and Legal Description

Joint Operating Agreement – Exhibit B – Confidentiality, Non-disclosure, Non-competition, Non-circumvention Agreement

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CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

PART 2

MANAGEMENT

MANAGEMENT

The management of the Operations and other business of the Venture shall be the responsibility of all the Venturers. All Venturers (Participants) in the Joint Venture are provided extensive and significant management powers. Venturers are and will be expected to exercise such powers and are prohibited from relying on the Managing Joint Venturer for the success or profitability of the Venture. The Agreement provides for the appointment of Signal Oil llc as Managing Venturer.

All decisions concerning the day-to-day affairs and the operations of the Venture by the Managing Venturer during the period so designated shall be binding upon each of the Venturers and the Venture.

Signal Oil llc, the Managing Venturer, was formed for the principal purpose of reviewing oil and gas drilling and development prospects, prospect and leasehold acquisitions, mining properties, and agro-forestry as well as other lucrative resource and land based endeavors, upon which partnerships and Joint Ventures may be formed by Signal Oil llc as general partner and/or Managing Venturer. Signal Oil llc will engage in exploration, development, production and management activities. It is intended that the services that Signal Oil llc will provide to the Venture in connection with its operations will be supplied by Signal Oil llc to other partnerships, Joint Ventures or entities with which Signal Oil llc may participate in connection with oil and gas exploration, development, production and management activities.

The Managing Venturer may and frequently does rely upon the services and advice of consultants who are available to the Managing Venturer on a contract basis. The Managing Venturer may employ such geologists and engineers on a consulting basis in the area in which the Prospect is located in order to have available the benefit of their specific knowledge of the area. Signal Oil llc, in its individual capacity, or through an affiliated entity, and not as Managing Venturer intends to be the Operator of the Prospect, but retains the right to nominate a qualified and experienced sub-operator or contract operator to perform this function.

ABOUT SIGNAL OIL LLC

Signal Oil llc is an independent energy company engaged in the exploration, development and production of oil and natural gas. Our current operations are focused in proven, producing oil and natural gas geologic trends principally in Wyoming, Utah, Nevada, Texas, New Mexico, Michigan, and in the U.S. Mid-Continent. The company has also been involved in various stages of exploration and the development of prospects in South America, Canada and Australia.

Historically, the principals of the company have engaged, under earlier corporate entities, in drilling a mix of relatively shallow oil and gas wells (from 2,500 to 5,500 feet) including some very shallow coal bed methane wells. The majority of the wells drilled were for oil reserves. These wells were all normally pressured, relatively low cost and low risk, developmental type wells.

A good number of mid-depth wells (from 9,000 to 13,000 feet) were targeted from the mid to late 1990's until recently in West Texas and New Mexico principally seeking reserves from the Pennsylvanian and Devonian rocks with very good success. Both drilling and completion costs were significantly higher due mainly to the increased depth and strong competition for leases. Risk increased but remained, in our opinion, moderate. However, these deeper wells have significantly greater economic potential by far. We typically seek to sell a larger portion of these deeper prospects to reduce our exploration risk and financial exposure while retaining significant upside potential. More recently, we have begun to retain larger percentages of, and increased our exposure to, higher cost, higher potential wells.

As a result of the maturity of the world's oil and natural gas reservoirs, accelerating production decline rates and the focus on much more complex and deep prospects both on and offshore, technology has become increasingly critical to the oil and gas industry. History has shown that those companies who can more rapidly adapt to and apply advanced technology reap benefits often far exceeding the cost. Technology is an important aspect of our exploration and development approach, as it provides us with more efficient tools to find and produce oil and natural gas. We have invested a substantial amount of our time and resources in learning when, where and how to apply advanced technology in our efforts to discover and develop oil and gas reserves.

We remain at our core a growth company as we always have been. We literally started from nothing. We look back at our history of operations with a fixture of pride, humility and gratitude. This last point is particularly directed to our employees and our joint venture partners –without whom nothing is possible.

We have ambitious objectives for the next five years. We would like for this next stage of our growth to follow in the tracks of our history. Join with us in the creation of a good long-term investment.

BUSINESS STRATEGY: GROWTH THROUGH THE DRILL BIT

Our objective is to create value through the execution of a business strategy designed to capitalize on our strengths. Key elements of our business strategy include:

Grow Primarily through Drilling
We are pursuing an active technology-driven exploration drilling program. We generate exploration prospects using both surface geomorphic and sub-surface geological mapping, through geological and geophysical analysis of satellite data, surface sourced and airborne gravity and magnetics, geo-chemical surveys, 2-D and 3-D seismic and other data. Our ability to successfully define and drill exploration prospects is demonstrated by an exploratory drilling success rate over 80%.

Focus on Prolific and Industry-Proven Trends
We have broadened the scope of our operations to include certain areas where we may gain larger leasehold positions, face less competition, have an increase in efficiency and a greater impact as a company.

Maintain a Balanced Exploration Drilling Portfolio
We seek to balance our drilling program between projects with relatively lower risk and moderate potential and drilling prospects that have relatively higher risk and substantial potential. We will continue to expand our exploratory drilling portfolio, including lease acquisition with exploration potential.

Manage Risk Exposure by Market Testing Prospects and Optimizing Working Interest
We seek to limit our financial and operating risks by varying our level of participation in drilling prospects with differing risk profiles and by seeking additional technical input and economic review from knowledgeable industry participants regarding our prospects. Additionally, we rely on advanced technologies like satellite multi-spectral analysis, 3-D seismic and aero-magnetic surveys to better define geologic risks, thereby enhancing the results of our drilling efforts. The use of satellite multi-spectral analysis or 3-D seismic analysis, or for that matter, any particular scientific exploration 'tool' does not guarantee that hydrocarbons are present or, if present,

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that they can be recovered economically. We also seek to operate our projects in order to better control drilling costs and the timing of drilling.

Exploration Approach

We typically seek to explore in locations within our areas of expertise that we believe have (1) longer-lived, reserve-proven trends, (2) numerous accumulations of normally pressured reserves at shallow depths and in geologic traps that require advanced technology to define or (3) the potential for large accumulations of deeper reserves.

Even in the relatively lower-risk reserve-proven trends, our use of current and advanced industry technology is instrumental in our exploration approach, significantly reducing geologic risk and allowing optimized reserve development.

We maintain a flexible and diversified approach to project identification by focusing on the estimated financial results of a project area rather that limiting our focus to any one method or source for obtaining leads for new project areas. Our current project areas result from leads developed primarily by our internal staff. Additionally, we monitor competitor activity and review outside prospects generated by small, independent “prospect generators,” or our Joint Venture partners. We complement our exploratory drilling portfolio through the use of these outside sources of project generation and typically retain operation rights. Specific drill sites are typically chosen by our own staff.

Operating Approach

Our management, a practicing geologist and petroleum landman, has extensive experience in the development and management of exploration projects in West Texas, South Texas, New Mexico and Wyoming and believes that this experience in the heart of the oil and gas industry has provided the skills and knowledge necessary to operate conventionally almost anywhere. We believe that our experience in the acquisition, development, processing and analysis of satellite, surface and airborne magnetic and gravity data, geochemical and seismic projects is a core competency to our continued success. We maintain a commitment to innovation and invention and strive to continuously improve our efficiency, productivity and quality of our work in exploring, drilling and completing our field wells.

We generally seek to obtain lease operator status and control over field operations, and in particular, seek to control decisions regarding exploration survey design parameters and drilling and completion methods. As part of a defense against competition, we typically secure our drilling permits as late as possible, in order not to ‘telegraph’ our drilling intentions to competition, gaining us time to evaluate productivity and then to acquire more leasehold before our competition can act. In conjunction with this, we typically attempt to remain low key and do not typically provide press releases or interviews relating to our drilling or development plans. While much of what we do becomes of public record at some point, our experience has shown that a great advantage is frequently ‘innocently given away’ to competitors. We intend to remain reticent and to diligently work our business plan.

We emphasize preplanning in project development to lower capital and operational cost and to efficiently integrate potential well locations into the existing and planned infrastructure, including gathering systems and other surface facilities. In constructing surface facilities, we seek to use reliable, high quality, used equipment in place of new equipment to achieve cost savings. We also seek to minimize cycle time from drilling to hook-up of wells, thereby accelerating cash flow and improving ultimate project economics. We seek to use advanced production techniques to exploit and expand our reserve base.

Oil and Gas Properties

We follow the successful efforts method of accounting for oil and gas producing activities. Costs to drill exploratory wells that do not find proved reserves, geological and geophysical costs, delay rentals and costs of carrying and retaining unproved properties are expensed. Costs incurred for exploratory wells that find reserves that cannot yet be classified as proved are capitalized if (i) the well has found a sufficient quantity of reserves to justify its completions a producing well and (ii) we are making sufficient progress assessing the reserves and the economic and operating viability of the project. Well costs are expensed if a determination as to whether proved reserves were found cannot be made within one year. The status of suspended well costs is monitored continuously and reviewed not less than quarterly. This ‘framework’ is designed to remain flexible and such procedures frequently vary in response to the needs of Interest owners and advice of counsel.

SIGNAL OIL LLC

The manager of Signal Oil llc, Mr. J.S. Foster, is a long time independent oil and gas operator, petroleum landman and practicing geologist. An active member of the American Association of Petroleum Landmen, the American Association of Petroleum Geologists, the International Oil Scouts Association and the Geological Society of America, he has been engaged in the Petroleum and Minerals Industry in the Southwest for his entire adult life. He has held or currently holds memberships in professional organizations such as the Independent Petroleum Association of America (IPAA), the Texas Alliance of Oil and Gas Producers, the Texas Independent Producers and Royalty Owners Association, the Permian Basin Petroleum Association, the Society of Economic Mineralogists and Paleontologists (SEPM), Houston Geological Society, West Texas Geological Society, and the Post Carbon Society.

Growing up in West Texas ranch country meant growing up around the oilfields, too. Mr. Foster worked in and around the oilfields in West Texas from a young age. After college, he gained experience as an operator/trainee, an ‘oil well shooter,’ and then field engineer for Welex, a Halliburton Company, West Texas Division. Since 1986 Mr. Foster has been engaged in acquiring and developing mineral acreage for production, focusing first in West Texas and South Texas, and on a more limited basis in New Mexico with a growing emphasis in Kansas, Wyoming, Utah, and Nevada.

In 1992, acting as company geologist and landman, Mr. Foster joined with a partner, to form an oil and gas exploration company that completed fifteen wells out of sixteen attempts as commercial producers. He continued to drill and develop oil and gas properties with a high success rate, having drilled around 80 individual wells to date. Mr. Foster and his investor partners agreed to sell most of the properties they were operating when oil and gas prices started to reach high levels in order to recapitalize and refocus on long term goals.

Signal Oil llc was formed to continue to capitalize on the opportunities available to U.S.-based independent oil companies using the latest technology and exploiting quality lease positions once held by major oil companies. As well, Signal Oil llc was created to look beyond current domestic opportunities and to seek a possible entry into the foreign realm where many outstanding opportunities are available that can significantly benefit from experience and technology heretofore either never applied or unavailable in certain areas overseas. On account of these changes and proposed expansion of corporate ownership to include other parties, the formation of additional corporate entities is planned, possibly including formation of or acquisition of a drilling company or drilling equipment for

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company use. Foster intends to develop the company(ies) through acquired producing working, royalty and mineral interests in the various petroleum provinces and select oil and gas plays where our experience, skills, and size can work to our favor, in addition to growing by participation in various drilling and development projects operated by other companies.

INDEMNIFICATION

The Venture has agreed to defend and hold the Managing Venturer harmless and to indemnify it, under certain circumstances, with respect to suits or proceedings (including appeals) to which the Managing Venturer may be a party or witness or threatened to be made a party or witness, and any investigation that could lead to such an action, suit or proceeding, by reason of the fact that it is, or was, the Managing Venturer of the Venture. Under such indemnification provisions, the Venture has agreed to pay the Managing Venturer's expenses, including attorneys' fees and judgments or amounts paid in settlement. See Article X of the Joint Venture Agreement attached hereto as Exhibit "B."

The Agreement also provides that each Venturer shall indemnify, defend and hold harmless the Venture and all other Venturers (including Signal Oil llc and/or its designated affiliate as the Operator, Sub-Operator or Managing Venturer) in certain circumstances from and against any loss, claim, cause of action, item of damages, expense and cost (including attorneys' fees and court costs) arising directly or indirectly out of any act of such Venturer that is inconsistent with the delegated rights and authority of the Managing Venturer of the Venture.

CONFLICTS OF INTEREST

The Managing Venturer will have the authority to purchase properties for the Venture for exploration and development purposes, including the authority to purchase properties for the Venture from Signal Oil llc or its affiliates in their individual capacities. The Managing Venturer will be permitted to purchase oil and gas properties for its own account regardless of what business, if any, is conducted by the Venture. Since the control of the Venture expenditures is at the discretion of the Managing Venturer at all times during the term of its office as Managing Venturer, conflicts of interest may arise.

The Venture is expected to enter into an Acquisition or Drilling and Completion Contract with Signal Oil llc and/or its affiliated operating company in its individual capacity, concerning the re-entry and/or drilling, testing and, if attempted, the completion or re-completion of the Prospect Well (and certain other services) for the drilling and completion prices. Pursuant to such contracts, Signal Oil llc will be entitled to any amounts representing the differences, if any, between the Turnkey[*] acquisition and/or drilling and completion prices and the actual costs to Signal Oil llc of the services it is obligated to perform pursuant to such contracts. Neither the Acquisition or Turnkey Drilling and Completion Contracts nor the Turnkey drilling and completion prices have been the subject of arm's-length negotiations, although the Managing Venturer believes the Turnkey drilling and completion prices allocable to drilling, testing and completing the initial wells are at or competitive with rates charged by third parties for similar wells in the locality.
If, after the Venture acquires the Prospect Well site, the Venture later determines that the Prospect site is unsuitable for oil and gas exploration by the Venture because of, among other things, lack of funds or high risks involved, or if the Prospect site has been downgraded by events occurring after the assignment to the Venture to the point that exploration would no longer be desirable or if the Venture determines that the best interest of the Venture would otherwise be served, it may Farmout the Prospect or sell or otherwise dispose of the Venture's interest therein. The decision with respect to making a Farmout and the terms of a Farmout may involve conflicts of interest, as the Managing Venturer may benefit from cost savings and reduction of risk.

In connection with establishing the terms of loans or advances to the Venture, commercial banks may consider cash balances of the Venture which are not required for the conduct of Venture business operations. To the extent the terms of such loans may be affected by the Venture's deposits, the Managing Venturer may have an incentive to maintain a larger portion of the Venture assets in the form of cash balances than would otherwise be necessary.

Most of the areas of conflict of interest described above are common to many oil and gas drilling programs. The terms of the Agreement are intended to ameliorate the conflicts of interest inherent in such a situation to the extent practicable, taking into consideration the uncertainties involved in attempting to determine in advance the location of the Prospect to be pursued by the Venture, the progress of drilling and/or other exploratory activity in the area of the Prospect sites and the outcome of exploration operations.

Additional, potential, conflicts of interest are:

a. **Prior and Subsequent Activities of the Managing Joint Venturer and/or the Operator**. The company(ies) will be actively engaged in other oil and gas acquisitions and operations. Such activities could create conflicts of interest with this Joint Venture. Both the Managing Venturer and the Operator anticipate sponsoring, managing, participating in and/or operating other partnerships, joint ventures, or drilling and development programs, including other programs in the area of this Joint Venture project. Such activities may create conflicts of interest between this Joint Venture and the company’s interest. In all such instances of operation and/or management of drilling programs for the account of others, the company and its management, where potential conflicts may arise, will attempt to deal fairly and in good faith with this Joint Venture and its Participants.

b. **Receipt of Compensation Regardless of Profitability**. The Company (Managing Venturer and/or Operator) will receive compensation from the program regardless of whether it operates at a profit or a loss.

c. **Operating Agreement**. The Managing Venturer will serve as agent for Participants under the Joint Operating Agreement (JOA). In making decisions about operations, the Company will or may be subject to conflicts between its interests and the interests of the Participants.

[*] if applicable

d. **Turnkey Contract**[*]. Under Turnkey Contracts, if applicable, the Company will cause all operations for the benefit of the Participants to be performed for a fixed price, and will realize a profit to the extent such fixed price exceeds the costs incurred by the Company in performing under Turnkey Contracts.

e. **Independent Decisions by the Company**. Substantially all of the terms of this Venture, as well as those relating to operations, were determined or contracted for by the Company prior to the formation of the Venture. Such terms included, without being an exclusive listing thereof, the following matters: (1) the terms and conditions of the acquisition of the leasehold acreage; (2) the terms of the Operating Agreement; (3) contributions by the Company to the costs of operations. Such terms were not negotiated with the Participants and such transactions may be deemed to have been entered into without the benefit of arms-length negotiations. Legal counsel, who might have negotiated more favorable terms for you and the other investors in the Venture and the agreements, has not separately represented you and/or other Participants.

f. **Acquisition of Other Oil and Gas Properties**. The company, subject to applicable Area of Mutual Interest (AMI) agreements, may acquire oil and gas leasehold properties for the drilling of wells thereon in the same general area, adjoining or offsetting the oil and gas leases on which the Wells are located.

g. **Related Party Transactions**. The company (Managing Venturer and/or Operator) may, in the future, engage in transactions with third parties which should be considered affiliates of the Company or its shareholders, officers and directors. There transactions could materially impact Participants in the Venture or the company's contractual obligations to the Venture.

h. **Geological Report**. The geological report for the Prospect Well(s) was prepared, entirely or in part, by the staff, or principal(s) of the Operator and/or Managing Venturer and may not be entirely independent. This lack of independence in the preparation of the report may affect its reliability since the Managing Venturer and/or the Operator has an incentive to prepare a more positive report than an independent geologist.

i. **Conflicts Concerning Legal Counsel**. It is anticipated that legal counsel to the Managing Venturer will also serve as legal counsel to the Joint Venture and that this dual representation will continue in the future. If a future dispute arises between the Managing Venturer and you and/or other Participants, then the Managing Venture will cause you and/or others to retain separate counsel. Likewise, if counsel advises that it believes its representation of the Joint Venture will be adversely affected by its responsibilities to the Managing Venturer, then the Managing Venturer will cause you and/or others to retain separate counsel.

j. **Lack of Independent Underwriter and Due Diligence Investigation**. There were no independent underwriters involved in the existing and proposed business activities of the Joint Venture or Managing Venturer. This means there is no due diligence report available on the partnership of the Managing Venturer. The Managing General Partner, without arms' length negotiations between you and other investors, has determined the terms of this Venture, the partnership agreement and the Drilling and Operating Agreement. Legal counsel, who might have negotiated more favorable terms for you and the other investors in the Venture and the agreements, has not separately represented you and the other investors.

k. **Regarding Order of Pipeline Construction and Drilling Commitments**. A conflict of interest may be created by the right of the Managing Venturer to determine the order of priority for constructing gathering lines which may be required to connect certain of the Venture's wells in the gathering system. Also, certain injection wells may be shared or utilized by more than one Joint Venture.

l. **Conflicts Regarding Roll-ups**. It is possible at some time in the future; the Joint Venture may become involved in a roll-up. In general, a roll-up means a transaction involving the acquisition, merger, conversion, or consolidation of the Joint Venture with or into another Joint Venture, or company or other entity and the issuance of securities by the roll-up entity to Participants and others involved. A roll-up will also include any change in the rights, preferences, and privileges of yours and/or others involved in the Joint Venture. Some of the changes that could occur include, increasing the compensation to the Managing Venturer, amending your voting rights, and materially altering the duration of the Joint Venture. As a Participant, you may be offered choices such as accepting securities in the roll-up entity; remaining a partner in the Joint Venture and preserving your interests in the Joint Venture property; and/or receiving cash for your pro-rata share of Joint Venture ownership.

BECAUSE OF THESE CONFLICTS OF INTEREST AND RISKS, INVESTORS MUST BE WILLING TO ACCEPT THE POTENTIAL THAT THEY WILL NOT RECEIVE A FULL RETURN OF CAPITAL ON THIS INVESTMENT. INVESTORS SHOULD NOT ASSUME THAT THE FOREGOING ARE THE ONLY CONFLICTS AND RISKS. OTHER RISKS MAY BE INHERENT IN THE PERSONAL CIRCUMSTANCES OF THE INVESTOR. ALL POTENTIAL INVESTORS SHOULD SEEK INDEPENDENT INVESTMENT ADVICE.

WHILE THE CONFLICTS OF INTEREST DESCRIBED ABOVE CANNOT BE ELIMINATED, THE MANAGING VENTURER BELIEVES THAT SUCH POTENTIAL CONFLICTS WILL NOT MATERIALLY AFFECT ITS ABILITY TO ACT IN THE BEST INTEREST OF THE JOINT VENTURE AND THE JOINT VENTURE PARTICIPANTS.

LEGAL PROCEEDINGS, ARBITRATION, AND NOTICE(S)

Legal Proceedings

Signal Oil llc is not aware of any legal proceeding pending or filed against the company affecting this property, as of the date of the composition of this Confidential Memorandum. It's managing principal is engaged in working to finalize certain unresolved federal tax matters related to filings which were affected by a divorce and estate matters related to death of former spouse.

Arbitration

The terms of the Joint Venture Agreement and the terms of the definitive JOA constitute an agreement(s) by and between all parties to arbitrate any and all controversies between them, in lieu of suit.

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[*] if applicable

Notice of Disputes
The terms of the Joint Venture Agreement and the terms of the definitive JOA constitute an agreement(s) by and between all parties requiring proper and specific notice of disputes, if any arise between the parties. Failure to adhere to the terms of this "Notice of Disputes" clause may result in dismissal, with prejudice, of any improperly filed suit.

Notice (Effective)
Proper and effective notice for legal purposes is set forth in the definitive JOA and in the Joint Venture Agreement for the Managing Venturer and for the Operating Company. Such proper notice requires notice to the official registered agent of the company, as set forth on the records of the State of Nevada.

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CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

PART 3

THE JOINT VENTURE

The Joint Venture

The Joint Venture shall have the status of a general partnership under the laws of the State of Texas, and the Joint Venturers shall have the status of general partners therein. (See "Risk Factors - Specific Risks of the Venture: Nature of the Liability of a Venturer.") Subscribers will not become Joint Venturers and their purchase of Joint Venture working interest (in the form of Units of Joint Venture Interest) shall not become final until after the expiration period of any rescission period and unless accepted into the Venture by the Managing Joint Venturer.

The principal office for the Joint Venture is set forth on the title page to this Confidential Private Placement Memorandum and set forth in Article I, Section 1.5 of the specific Joint Venture Agreement. The Venture is and will remain a separate legal entity from Signal Oil llc or any affiliate(s) thereof. The rights of the Venturers will be defined by this Agreement. Venturers subscribing will acquire Interest solely in the Joint Venture and its property and shall not, by such subscription, be acquiring ownership or title to Signal Oil llc or any affiliate thereof.

INVESTMENT OBJECTIVES

The Joint Venture's principal investment objectives are to invest the subscription proceeds in the exploration for and drilling and development of oil and natural gas well(s), which are:

1. **Provide monthly cash distributions to Participants until the well(s) are depleted or sold**. The Managing Joint Venturer may contract with other company(ies) and personnel not affiliated with it, to acquire prospect(s) for the Joint Venture and to prepare various geologic, economic, and engineering reports on the merits of those aspects of the prospect. In any case, the potential for significant economic returns will be demonstrated and economic production is anticipated for at least 10 years.
2. **Obtain tax deductions in the current year from intangible drilling costs, lease and well expense, and depletion allowance(s), or in the case of producing properties for IRS Section 179 expensing, to offset a portion of your taxable income, subject to the "at risk" rules.** Such deductions are taken against ordinary income (salary, interest, and investment income) in the year deductions are incurred. Most states also allow this type of deduction against the state income tax.
3. **Offset a portion of taxable income generated by the Joint Venture with tax deductions from ongoing operations (LOE) and cost or percentage depletion, and if appropriate, percentage depletion allowance, which is anticipated to range from 15% to 20%.** This could substantially reduce the effective tax rate on Joint Venture revenues.

Attainment of the Joint Venture's investment objectives will depend on many factors, including the ability of the Managing Joint Venturer to select suitable well(s) that will be productive and produce enough revenue to return the investment made. The success of the Joint Venture depends largely on future economic conditions, especially the future price of natural gas and crude oil which is volatile and which may decrease. The business operations of the Joint Venture involves a high degree of risk, and the nature of the oil and gas business and petroleum geology are such that many uncertainties arise, accordingly, there can be no guarantee or assurance that the foregoing objectives will be attained.

ELEMENTS OF THE JOINT VENTURE

Signal Oil llc and/or its designated affiliate, as Managing Venturer, will invite qualified parties to become Joint Venturers (Venturers) in the Venture, which will be formed under Texas law and be governed by the Joint Venture Agreement (the Agreement), the Model Form Joint Operating Agreement, and the Texas Uniform Partnership Act (Texas UPA). Applications will be accepted only from prospective Venturers who represent to the Managing Venturer that they meet certain suitability standards and requirements. The Managing Venturer and/or its affiliates may participate in Units with respect to which it or its affiliates will be a Venturer subject to the same obligations and limitations as any other Venturer except for certain limitations relating to transferability of such Units.

The Venture's operations will be conducted under the Joint Venture Agreement, which names Signal Oil llc as Managing Venturer. The Venturers will have all of the rights and will be subject to all of the liabilities of a general partner under the Texas UPA. Participants are provided extensive and significant management powers. Participants are and will be expected to exercise such powers and must not rely on the Managing Joint Venturer for the success or profitability of the Joint Venture.

The Managing Venturer shall have the authority to manage the day-to-day operations, as hereinafter defined. See "Plan of Organization and Suitability Standards" and the Joint Venture Agreement attached hereto as Exhibit B.

COMPLETION ASSESSMENTS

The Venture may request each Venturer to contribute additional capital to the Venture not to exceed the sum set forth herein (See "Investment Summary") per Unit (the Completion Assessment) for the purpose of completion, re-entry, workover, stimulation or re-completion procedures the prospect well(s) if such completion attempt is warranted with respect thereto based upon the affirmative vote of the Venturers. Such completion activities are proposed to be undertaken pursuant to a Turnkey[1] completion contract to be entered into between the Venturer and Signal Oil llc in its individual capacity. The failure of a Venturer to contribute his/her proportionate share of a Completion Assessment with seven (7) days from the delivery of a notice by electronic mail, postal mail, overnight delivery (FedEx, etc.,) or personal delivery shall be deemed a negative vote for completion and a request that his/her Interest in the Joint Venture be abandoned (proportionately to the number of wells that completion funds are submitted for with respect to multi-well drilling ventures), and he/she shall be effectively withdrawn as a Participant in the Joint Venture with no further benefits, rights, or obligations with respect to the sharing of income, gains, and losses with respect to the prospect well(s). In the case of multi-well drilling ventures, such Participant shall have no further benefits, rights, or obligations with respect to the sharing of income, gains, losses, with respect to any well for which the Venturer does not contribute his/her/its proportionate share of completions funds. See "Additional Assessments and Financing of Additional Venture Activities," "Specific Risks of the Joint Venture, Failure to Pay Completion or Mandatory Assessments."

[1] If applicable

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Optional Additional and Other Assessments

Subsequent to initial operations, optional additional assessments may be requested by the Venture for the purpose of undertaking subsequent operations. The Venturers shall have the election as to whether or not the Venture shall commence or undertake subsequent operations and whether or not to pay any such optional additional assessments and participate in subsequent operations. If the Venturers determine by a vote that the Venture requires additional capital for the purpose of continuing Venture operations, each Venturer shall, within fourteen (14) days after the vote, or such deadline as required in the definitive Operating Agreement, contribute the additional funds. When paid, such funds shall be treated as capital contributions to the Venture. Each Venturer shall contribute his pro rata share of the additional capital based on the amount of initial capital contributed unless the Venturers unanimously agree upon a different basis for determining the amount for each Venturer's contribution. The procedure for calling such other assessments, as well as the rights and obligations of Venturers upon failure of a Venturer to contribute such assessments, shall be the same as determined herein with respect to optional additional assessments. See "Additional Assessments and Financing of Additional Venture Activities."

Extent of Turnkey Contracts

The turnkey contract* applies only to the acquisition of the prospect, leasehold, and drilling and/or re-entry and testing of one (1) prospect well(s). The extent of the turnkey contract for completing and equipping the prospect wells applies only to the customary completion practices for the subject well in the known targeted potential pay zone (non typical or “stray” zones will constitute an additional completion attempt separate from any turnkey attempt, unless such zone(s) is the only potential pay, and the installment of typical production facilities for same including flowlines and measurement facilities but not including gas transmission pipelines or pumping equipment unless specifically set forth in the agreements. In all other matters, the costs and expenses will be billed as typical lease operating expenses.

Management and Managing Venturer’s Contribution(s)

The management of the operations and other business of the Venture shall be the responsibility of all of the Venturers. Each Joint Venturer has the right to be, and will be, involved in making Venture decisions. **Each Joint Venturer is provided extensive and significant management powers in this Joint Venture and will be expected to exercise same and must not rely on the Managing Joint Venturer for the success or profitability of the Venture**. The Agreement provides that Signal Oil llc. is the Managing Venturer, and the Venturers, by a vote of 51% in Interest, may remove the Managing Venturer. All decisions concerning the day-to-day affairs and operations of the Venture by the Managing Venturer, during the period so designated, shall be binding upon each of the Venturers and the Venture.

The Managing Venturer will contribute to the Venture, at a minimum, in cash or in kind, no less than one percent of initial venture capitalization. Signal Oil llc's participation in additional working interests, if any, may be outside the Venture as an industry participant.

Distribution of Revenues

Subject to a vote to the contrary, net Venture revenues which, in the sole judgment of the Managing Venturer, are not required to meet obligations of the Venture or held for working capital reserves shall be distributed as often as practicable to the Venturers. It is anticipated that revenue distribution, once enacted, will be conducted on a quarterly basis.

Reservation of Right to Change or Move Location

The Operator and/or Managing Joint Venturer reserves the right to change or move the proposed well location or substitute comparable drilling or re-entry sites for the proposed well(s) to be drilled in this Venture (if any) in the event additional geological information is obtained which indicates such change, as necessary to conform to drilling schedules or farm-out agreements, as business strategy to prevent revealing company drilling intentions which may jeopardize key leasehold control or key leases cannot be timely acquired. Any substituted well locations or drill sites will compare favorably with or improve upon the general character of the prospect described regarding degree of risk, drilling depth and cost. Further, the Operator and/or Managing Joint Venturer reserves the right to complete the well in a shallower pay zone and/or forego drilling to the proposed target formation on account of impenetrable substances, reservoir pressure, lost circulation, hole problems, etc, or any problem(s) which may endanger the integrity of the well itself.

Costs of Organization

When the Venture commences initial operations, Signal Oil llc will be responsible for payment of costs pursuant to the terms of the Turnkey Contract*. Signal Oil llc. will be responsible for all costs in the event the Venture does not commence initial operations or if initial capitalization is not received. See "Plan of Organization and Suitability Standards – Organizational Costs."

Compensation and Reimbursement

Signal Oil llc will receive a fee in an amount, if any, equal to the difference between the turnkey drilling* and/or acquisition price and the actual cost to Signal Oil llc of the services it is obligated to provide pursuant to the Turnkey Drilling Contract from which Signal Oil llc will pay all Venture and Organizational Costs. Likewise, if a turnkey completion attempt is deemed advisable on the prospect wells, Signal Oil llc. will receive an amount, if any, equal to the difference between the turnkey completion price and the actual cost to Signal Oil llc of the services it is obligated to provide pursuant to the Turnkey* Completion Contract. Signal Oil llc and/or the operating company may receive what may be considered additional compensation in connection with consulting fees, operating agreements, reimbursement of direct expenses paid for the Venture, and other transactions which may arise in connection with the operations of the Venture. The operating company, prospect generating geologists and/or certain consultants or affiliates of the operating company may retain, as a part of their compensation and fees, overriding royalty interests as set forth in the Investment Summary.

* If applicable

Return on Investment

There is absolutely no assurance that the proposed well to be acquired, drilled or re-entered (if any) and, if appropriate, completed or re-completed, will produce any hydrocarbons or merchantable products in commercial quantities. However, all purchasers of Units will participate in any production from the proposed well, in proportion to their Interest.

Tax Status

The Venture does not intend to seek a ruling from the Internal Revenue Service with respect to whether it will be treated for federal income tax purposes as a partnership rather than an association taxable as a corporation. In addition, the Venture does not presently intend to seek a ruling from the Internal Revenue Service on any other federal or state tax matter that may arise in connection with the formation, organization and/or operation of the Venture. See "Tax Considerations."

Conflicts of Interest

The Managing Venturer is and intends to become a Venturer and/or an operator in other entities engaged in operations similar to that of the Venture or otherwise make or arrange for similar operations as those contemplated for the Venture. Such activities may place constraints on the time that Signal Oil llc. and its officers may have to devote to Venture activities.

Neither the Turnkey* Acquisition and/or Drilling Contract nor the Turnkey* Completion or Re-Completion Contract (if a completion attempt is deemed advisable) to be entered between the Venture and Signal Oil llc. nor the turnkey drilling and completion prices have been the subject of arm's length negotiations. The turnkey price may exceed the cost to Signal Oil llc of acquiring the prospect and performing the services pursuant to the Turnkey* Drilling Contract. The turnkey completion price may exceed the cost to Signal Oil llc of performing the services described in the Turnkey Completion Contract.

Improper Reliance on Promises, Projections or Opinions

No one has been authorized to make any oral promises, projections or opinions concerning future events or expected production except as set forth within this Memorandum and any other document used in connection with the placement of these Units. Oral statements, which differ from the written data provided prospective purchasers **HAVE NOT BEEN AUTHORIZED AND SHOULD NOT BE RELIED UPON UNDER ANY CIRCUMSTANCES**. Opinions of possible future events are based on various subjective determinations and assumptions. All projections by their very nature are inherently subject to uncertainty, and a prospective investor should understand that written projections, if provided, may not be achieved, that underlying assumptions may prove inaccurate, that historical production levels may not be sustained, and that operations may be unprofitable in the aggregate because oil and/or gas is not produced in commercial quantities.

Plan of Organization and Suitability Standards

Eligible Potential Venturers

The Managing Venturer reserves the right to refuse to accept the application of any person. Participation in the Venture is intended only for persons meeting certain minimum suitability standards and who are able to make the representations contained in the "QUESTIONNAIRE" annexed hereto and "Application and Subscription Agreement" also annexed hereto (which documents are delivered upon request of Applicant intent upon Subscribing into the Joint Venture).

Venturers' Capital Contributions

Joint Venturer's initial capital contributions may be accepted by the Managing Venturer in the per Unit amount(s) set forth herein relating to this specific Joint Venture or the Authority for Expenditure (AFE). Capital contributions must be paid in full, in cash, upon application; however, the Managing Joint Venturer, in its sole discretion, may accept payment for a fraction of a Unit, typically one-half Unit, thereby reducing the Venturer's initial capital contribution proportionately.

In the event the Venture has not received the requisite initial capital contributions by the close of the capitalization period, or if the Venture is unable to acquire the Prospect or commence initial operations, all funds and other consideration received by Signal Oil llc with applications will be returned in full, without interest. If subscriber funds have been deposited into a bank and then are to be returned, the Managing Joint Venturer shall not be obligated to return such funds without such deposit first "clearing" its bank depository. When out of state funds are involved, such time period can take as long as three weeks. The Managing Joint Venturer will return such funds as promptly as the banking system will provide for such possibility.

After the Venture attains initial capital contributions, the funds will be released and advanced for purpose of commencing preparatory operations. At such time, the Managing Joint Venturer shall continue to accept applications for participation in the Joint Venture until the Venture is fully capitalized or the capitalization period expires. After the sale of four (4) Units, if insufficient application funds are received from Venturers and industry participants to meet the minimum capital requirements to drill the well, the Managing Joint Venturer may purchase sufficient Units or working interests to meet the remaining minimum capital obligations.

Suitability Standards

Prospective Venturers must be qualified, as determined by the Managing Venturer in its sole discretion, from the signed QUESTIONNAIRE delivered prior to the time of participation in the Venture and from such other information available to the Managing Venturer. The Managing Venturer intends that subscribers will be accredited investors.

Per Regulation D, Rules 505 and 506 of the Dodd Frank Wall Street Reform and Consumer Protection Act, signed into law on July 21, 2010, an accredited investor includes:

- Certain types of financial institutions such as banks, broker-dealers and investment companies;
- Entities with total assets in excess of $5 million (not formed for the purpose of investing in the Venture);
- Any director, executive officer or general partner of the Company;

- Any natural person whose net worth alone or jointly with spouse exceeds $1 million excluding the value of the investor's primary residence. The exclusion of the value of the primary residence was added by Section 413 of the Dodd Frank Wall Street Reform and Consumer Protection Act;
- Any natural person whose individual income exceeds $200,000 (or jointly with spouse, $300,000) for each of the past two years, and a reasonable expectation of the same income level in the current year;
- Any trust with assets greater than $5 million that are managed by a sophisticated trustee and not formed for the specific purpose of investing in the Venture; and
- Any entity in which all of the equity owners are accredited investors.

The Managing Venturer may, at its discretion, consider participation of no more than 35 non-accredited investors. The Managing Venturer will consider the following factors in determining the suitability of a prospective non-accredited investor:

- Prospective Venturer's net worth of $500,000 or more; or
- Prospective Venturer's net worth of not less than $300,000 and some portion of taxable income for the previous year was, or some portion of estimated taxable income for the current year will be, subject to federal income tax at the highest marginal tax bracket applicable to such year; and
- Such other factors as are more fully set forth in the QUESTIONNAIRE attached hereto.

RESCISSION PERIOD

Participants may rescind their investment within five (5) business days of Signal Oil llc's receipt of the Participant's investment. The Subscriber shall have the right to rescind his/her/its Application and Subscription, and the Managing Venturer shall return Participant's funds, in full, upon receipt of Participant's written notice through electronic mail or overnight delivery of election to rescind. The Managing Venturer shall not be compelled to remit funds from its account unless and until the subscriber's funds have cleared the banking system and are fully and properly credited into the Managing Venturer's account(s).

PARTICIPATION IN UNITS BY MANAGING VENTURER

Signal Oil llc., as Managing Venturer, and its affiliates and/or its officers, directors or employees may participate in the initial capitalization of the Venture on the same terms and conditions (except transferability) as all other Venturers and thereby acquire interests. Alternatively, it may participate in the Working Interests as an industry participant. Such participation may be made for the purpose of completing the initial capitalization. See "Limited Transferability and Rights of First Refusal."

ORGANIZATIONAL COSTS

Consulting fees equal to not more than 15 percent (15%) of the total initial capitalization and sale of working interests to third parties may be paid by the Managing Venturer as part of Organizational Costs. Consulting fees not in excess of fifteen percent (15%) may also be paid by the Managing Venturer on behalf of the Venture upon the collection of any completion assessment, if applicable. All organization costs of the initial capitalization will be paid by Signal Oil llc pursuant to the Turnkey Drilling Contract* when the Venture is fully capitalized and commences operations. If the capitalization amount is not received, Signal Oil llc will be responsible for the payment of all organizational costs.

LIMITED TRANSFERABILITY AND RIGHTS OF FIRST REFUSAL

The Joint Venture Agreement provides that a Venturer (except, in certain circumstances where the Managing Venturer or its affiliates acquire Units of Interest) is obligated to hold his Interest and is prohibited from transferring, assigning or otherwise disposing of same without first satisfying certain conditions. One such condition provides that the Managing Venturer may request an opinion of counsel (the cost of which shall be borne by the transferor) to the effect that such transaction will not result in certain adverse tax consequences or violations of law. In addition, the Units are subject to certain rights of first refusal. Finally, no person will be admitted as a substitute Venturer without prior written approval of the Venturers by a vote. (See Article VI to the "JOINT VENTURE AGREEMENT" annexed hereto as Exhibit "B".)

NO RIGHT OF PRESENTMENT

Neither the Venture nor the Managing Venturer has obligated itself to repurchase, redeem or allow withdrawal, and has not established a procedure for repurchasing, redemption or withdrawal, and has no present plan to repurchase, redeem or allow withdrawal of any Units of Interest from the Venturers, other than the abandonment provisions relating to failure to pay certain assessments.

ALL DEVELOPMENT ON AN "IN OR OUT" BASIS

The Agreement provides that all development of the leasehold estate is to be performed on an "in or out" basis wherein those Venturers who acquire Interest in and to the assigned Venture property by participation in the initial drilling or development Venture thereon may continue to participate in the development of the prospect acreage through the exercise of their first right of refusal to participate in additional ventures proposed by the Managing Venturer. If a Venturer fails or refuses to participate in any subsequent, consecutive venture proposed by the Managing Venturer, then that Venturer relinquishes any and all rights of refusal or participation from that point and retains only the Interest acquired by him/her to that point. Any additional participation in further development of the property after relinquishing that right will be at the will and wishes of the Managing Venturer, exclusively. This is a common term with respect to many prospects and their development. It is intended to promote the continued development of the leasehold and prospect and to prevent the encumbering of same to the damage of the Venture and Venturers thereto and to save and protect the leasehold from loss due to breach of the continuous development lease clause(s). This "in or out" clause will be strictly observed.

Additional Assessments and Financing of Additional Venture Activities

Completion Assessments*

Under the Agreement, the costs of initial operations will be funded from initial venture capital (including completion assessments, if any, if further enhancement of production on the Prospect Well is necessary). The Agreement provides that the Venture may request each Venturer to contribute additional capital to the Venture in an amount(s) not to exceed the amount herein stated per Unit as a completion, re-entry, workover or re-completion assessment for the purpose of funding the Venturers' allocable portion of completing the Prospect Well if such completion attempt is warranted. Such completion activities are proposed to be undertaken pursuant to a Completion Contract to be entered into between the Joint Venture and Signal Oil llc in its individual capacity. Industry participants will bear their own allocable percentage of completion costs.

The failure of a Venturer to contribute his (her) proportionate share of a completion assessment within seven (7) days from delivery of a notice by electronic mail, postal mail, overnight delivery (FedEx, et.al.,) or personal delivery shall be deemed to be a negative vote for completion and a request that his (her) Interest in the Joint Venture be abandoned, and he (she) shall be effectively withdrawn as a Participant in the Joint Venture with no further benefits, rights or obligations with respect to the sharing of income, gains and losses with respect to the well to which the Completion Assessment relates.

If less than all Venturers pay the required completion assessment, if called for by the Venture, the Managing Venturer shall have the option to:

1. pay the unpaid portion of such assessment and thereafter accede to the Non-Consenting Venturers' Interest in the Venture,
2. allow any or all consenting Venturers to pay such assessment and therefore be entitled to accede to the Interest of the Non-Consenting Venturer,
3. secure the funds from other sources including, but not limited to, loans and/or the proceeds of the sale of the Non-Consenting Venturers' Units to third parties,
4. Farmout the Prospect, or
5. abandon the operation for which the Completion Assessment was requested, which may entail abandoning the Prospect.

The Agreement authorizes the Managing Venturer to reflect the withdrawal and reallocation of Units formerly owned by non-consenting Venturers. Abandonment of a Venturer's Interests shall not affect his liabilities as a Venturer under the Agreement or the Texas UPA.

Leasehold Costs

The cost of acquiring oil and gas leasehold or similar interests is a capital expenditure that must be recovered through depletion deductions if the lease is productive. The portion of IDCs and equipping costs required to be capitalized is also capitalized as a portion of the leasehold cost. Certain other expenses, such as certain geophysical costs and syndication expenses are also required to be capitalized as a portion of the leasehold costs and recovered through depletion deductions if the lease is productive. If a lease is proved worthless and abandoned, the capitalized cost less any depletion claimed may be deducted, subject to basis and at risk rules, as a loss in the year the lease becomes worthless.

Geophysical Costs

The cost of geophysical exploration must be capitalized as a lease acquisition cost if a property is acquired or retained on the basis of data from such exploration. Otherwise, such costs may be deducted as ordinary expenses.

Operating Expenses

Venturers and their Units will also be subject to assessments for their proportionate share of lease operating expenses (LOE) for producing Venture wells pursuant to the Joint Venture Agreement. Such LOE will accrue monthly and be accounted for and deducted or “netted out” against revenues on a quarterly basis. When ongoing operations create lease operating expenses without production income to offset them (usually a temporary feature) the Venturers are obligated to pay their proportionate share to the Managing Venturer and/or Operator subject to quarterly billing. It is not anticipated that any expenses incurred pursuant to the operating Agreement will be excessive or unnecessary; therefore, it is anticipated such expenses will be deductible in the year paid. However, because of the factual nature of the proper characterization of such expenses and costs, no assurances can be given that the deduction of a particular item will not be successfully challenged by the IRS. Failure of a Joint Venturer to make payment for his/her/its proportional share of invoiced operating expenses in the calendar year that the expense is incurred will create a situation wherein the business expense deduction normally attributable to that Venturer is disallowed by the IRS. In short, only LOE sums paid for in the current calendar year may be deducted as a business expense.

Optional Additional Assessments

The Managing Venturer anticipates that initial Venture capital, with industry participants’ capital, will be sufficient to pay for the drilling and testing of the Prospect Well, pursuant to initial operations only. However, following the expenditure or commitment of initial Venture capital it is possible that the Managing Venturer will deem it appropriate to conduct subsequent operations on the Prospect. Everything other than the drilling, testing and completing of the Prospect Well and the production of oil and/or gas therefrom should be considered to be subsequent operations of the Venture and may require financing greatly in excess of the Initial Venture Capital.

If the Venture determines that a subsequent operation, for which optional additional assessments will be requested, should be commenced; written notice of the proposed operation will be given to the Venturers. The notice given by the Venture to the Venturers will specify the nature and purpose of the subsequent operation, will describe the effect of not participating in the subsequent operation and estimate each Venturer's proportionate share of the expenditure necessary to finance the subsequent operation. Within fourteen (14) days after the notice is mailed, a venturer may elect by vote to participate in the subsequent operation described in the notice by sending to the managing venturer payment in the amount of such venturer's proportionate share of the expenditure necessary

* If applicable

to finance the subsequent operation, as such share is more fully described in the notice. the venturer's payment must be postmarked no later than fourteen (14) days after the initial notice and must be received by the managing venturer no later than twenty-one (21) days after such notice. Thereafter, the Venture shall be under no obligation to include such Venturer in such subsequent operations.

Venturers who elect to Vote to participate in subsequent operations (hereinafter referred to as Participating Venturers) will do so by paying their proportionate share of the optional additional assessment required from the Participating Venturers for the expenses for the subsequent operations. The Managing Venturer will estimate the complete cost of the subsequent operation and each Venturer's proportionate share of the expenses thereof. The Managing Venturer may choose to request payment in full of such expenses or any portion thereof. The estimate shall not be conclusive as to the expenses incurred and additional contributions by Participating Venturers for the subsequent operation may be necessary. Such additional amounts will be billed by the Managing Venturer to the Venturers, but such amounts shall not be deemed an asset of the Venture until received.

In the event optional additional assessment proceeds are not paid to the Managing Venturer by the due date stated in the notice or the bill sent to the Venturers (who previously agreed to pay some), and if the Managing Venturer (or other Venturers) does not elect to pay the unpaid assessment, the Managing Venturer shall have the right, but not the obligation, to abandon the proposed subsequent operation and refund the optional additional assessments previously paid by the Venturers. In that event, the Venture may sell or farmout to any person or entity the Prospect (subject to an appropriate Vote of the Venturers) or portions thereof upon such terms as the Venture shall deem appropriate. In the event that the Managing Venturer (or other Venturers) should elect to pay such unpaid assessment, the non-participating Venturer will be subject to a penalty of 500% of the amount in default, and such amount will be assessed against the non-participating Venturer and paid to the person who has paid the non-participating Venturer's assessment.

In addition, any non-participating Venturer remaining in default of his payment obligations may, in the sole discretion of the Managing Venturer, be precluded from participating in future subsequent operations of the Venture. The interest in any further subsequent operations that would otherwise have been available to a non-participating Venturer shall be at the option of the Managing Venturer either (i) acquired by the Managing Venturer, (ii) offered to the remaining Participating Venturers (or Substitute Venturers) on a proportionate basis, or (iii) offered to third parties.

Although a non-participating Venturer remaining in default of his payment obligations may have no right to participate in any further subsequent Operations, the Managing Venturer may, in the exercise of its sole and absolute discretion, allow any or all non-participating Venturers to participate in further subsequent operations. However, such non-participating Venturer shall not be given such opportunity until all Participating Venturers in the subsequent operation immediately preceding the further subsequent operation have had an opportunity to continue to participate in such subsequent operation. Nothing shall prevent the Managing Venturer from electing to exclude any non-participating Venturer from any further subsequent operations.

FAILURE TO PAY TOTAL ESTIMATED OPTIONAL ADDITIONAL ASSESSMENT

In the event a Venturer contributes his proportionate share of the estimated costs of any subsequent operation requested in the notice of optional additional assessment (and, therefore, becomes a Participating Venturer) but fails to contribute the entire estimated costs of the subsequent operation which may be called in a subsequent notice (to be used for completion efforts or continued efforts relating to such subsequent operation), such non-contributing Venturer shall be subject to a penalty of 500% of the amount remaining unpaid, and in such event he (she) shall be treated as a non-participating Venturer.

OTHER ASSESSMENTS

If the Venturers determines that the Venture requires additional capital for the purpose of continuing Venture operations, each Venturer shall, within seven (7) days after the vote, contribute the additional funds, which, when paid, shall be treated as capital contributions to the Venture. Each Venturer shall contribute his pro rata share of the additional capital based on the amount of initial capital contributed unless the Venturers unanimously agree upon a different basis for determining the amount for each Venturers' contribution. The procedure for calling for such other assessments, as well as the rights and obligations of Venturers upon failure of a Venturer to contribute appropriate assessments, shall be the same as determined herein with respect to optional additional assessments. In addition, even if such an assessment is not made, all Venturers shall remain liable for Venture obligations in accordance with the Texas UPA.

SPECIAL ASSESSMENTS

Special assessments may be requested by the Managing Venturer in the event the Venture votes to: 1) deepen a well bore; 2) sidetrack a well bore; 3) plug back or squeeze cement the well bore and attempt completion in a higher or lower zone; 4) conduct any activity for the purpose of enhancing production; 5) install pumping equipment not provided for in the initial operations; 6) acquire and install any type of gas compression, production or treatment facilities; 7) install gathering or transmission pipelines; 8) complete any zones in addition to the first completion. The costs for such special assessments are typically not covered under the initial capitalization and will require additional funding, which may be substantial.

PAYMENT OF COSTS THROUGH UTILIZATION OF REVENUES

To the extent the Venture may have its own revenues, such revenues may also be utilized in the payment of certain costs incurred by the Venture, including operating expenses. To the extent Venture revenues are utilized and reinvested, federal income tax liability and/or deductions may accrue to the Venturers even though no funds are actually distributed to the Venturers. Revenues will be utilized typically for short term activities such as Completion of a Venture well in progress and the payment of certain equipment costs.

FARMOUT OR DISPOSAL/SALE OF PROSPECTS BY THE VENTURE

In the event that the Venture should determine that additional Venture activities are not justified, the Venture will use its best efforts to dispose of the Prospect on the best terms available for the benefit of the Venture, subject to appropriate Venturers' vote.

Although the Venture does not presently intend to farmout the Prospect, it has the authority to do so. The Venture may farmout portions of the Prospect if the Venturers determine that the best interest of the Venture would be served. If the Venture farms-out a leasehold interest, the Venture will make every effort to retain such economic interest and concessions therein as are consistent with industry practice.

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TITLE TO VENTURE PROPERTIES

Title to Venture properties will be held in the name of the Venture, except that title to such properties may be held temporarily in the name of nominees (including the Managing Venturer or an affiliate) in order to facilitate the acquisition of such properties by the Venture and for other valid purposes. The Managing Venturer will use its best efforts to have title transferred to the Venture upon completion of the Prospect Well. The Managing Venturer does not guarantee legal title to the Prospect but will obtain an attorney's title opinion with respect to the drill site on the Prospect prior to the commencement of any activities.

It will be the policy of the Managing Venturer that immediately after properties are acquired by the Venture, title documents relating to the properties will be recorded in the required office of the appropriate governmental agency or authority in the name of the Venture. All files of the Managing Venturer will indicate that such properties are held in the name of the Venture. If the Managing Venturer, affiliate or other nominee holds Venture properties in its own name, such properties, in the event of such holder's insolvency, might be subject to the claims of creditors of such holder who did not have actual notice of the existence of the Venture and of the Interest of the Venture in such properties.

OPERATING AGREEMENT

The AAPL Joint Operating Agreement (JOA) attached to and made a part of this memorandum and shall be the dominant agreement of the Venture pursuant to the Joint Venture Agreement and the terms therein. The Venture, upon acquisition of the Prospect, intends to enter into an Operating Agreement with Signal Oil llc or its designated affiliate or sub-operator, in its individual capacity, as the Operator. Joint Venturers will be required to countersign the Joint Venture's Operating Agreement along with their specific subscription agreements. Signal Oil llc, as intended Operator or sub-Operator, will be responsible for causing and/or conducting operations on the Prospect, overseeing production, employing field personnel, keeping production records, and other related matters. The Venturers retain the right to select another Operator to replace Signal Oil llc. at any time upon a 51% vote in Interest. Proxy votes and split-interest votes are specifically not allowed under the Joint Venture agreement.

If for federal income tax purposes, the Operating Agreement or operations thereunder are regarded as a partnership, the Joint Venture and the Joint Venture Partners, individually, elect to be excluded from the application of all provisions of Subchapter K, Chapter 1, subtitle A of the Internal Revenue Code of 1954.

The Joint Venture will pay to the Operator monthly operating overhead sums as set forth in the definitive JOA, and such sums may be deducted from the revenue stream of the well(s).

MARKETING OF PRODUCTION

Signal Oil llc, as Operator or sub-Operator, will market the oil and/or gas production, if any, of the Venture. On behalf of the Venture, the Managing Venturer may execute contracts for the sale of oil, gas or other hydrocarbons. The limited Power of Attorney for the JVA specifies that the Managing Venturer and/or Operator may execute such documents as necessary to conduct the business of the Venture relating to marketing of production. See "Competition, Markets and Regulation."

FAIR AND REASONABLE

The Managing Venturer will not sell, transfer or convey any property to, or purchase any property from, the partnership except pursuant to transactions that are fair and reasonable. Further, the Managing Venturer will not take any action with respect to the assets or property of the partnership that does not primarily benefit the partnership.

INSURANCE

Signal Oil llc. and/or its affiliated operating company intends to maintain or benefit from, as additional insured, various types of insurance coverages in such amounts as it deems appropriate. Signal Oil llc or its affiliate, as Operator, intends, although it is not required to, carry fire, lightning or explosion insurance for the benefit of the Venture. Further, Signal Oil llc. and/or the Operator intend to acquire insurance to protect the Venture in case of a blowout. Also, although it is proposed that Signal Oil llc and/or the Operator will set surface casing or acquire said well under these conditions, below the level of all know producing fresh water zones, it intends to secure insurance to protect the Venture in the event that salt water produced from the well contaminates existing fresh water zones or reservoirs. If any of the aforementioned events should occur, and the Venture has not obtained adequate insurance for such event, and the Venture is held liable for any resulting loss, it would reduce the cash available from the Venture for distributions and might severely adversely affect the Venture, including but not limited to total loss of all Venture assets, and the Venturers, will be jointly and severally liable therefor. See "Risk Factors - Specific Risks of the Venture: Nature of the Liability of a Joint Venturer."

SERVICES PROVIDED

The Managing Venturer, the Operator and affiliates will provide technical services and perform such acts, employ such persons and execute such agreements as may be necessary or in its judgment, appropriate, in order to contract for the drilling, testing and, if appropriate, completion of the Prospect and provide for production facilities. The Managing Venturer will be responsible to the Venture for the Operation of the Prospect. The Managing Venturer will pay and collect all monies the Venture is obligated to pay and collect. The Managing Venturer presently intends that all drilling, testing and, if appropriate, completion services for the Venture will be carried on by unaffiliated independent contractors.

VENTURERS' AUTHORITY TO REPLACE SIGNAL OIL LLC

Notwithstanding the initial appointment of Signal Oil llc herein to the aforementioned capacities (i.e., Managing Venturer and/or Operator or sub- Operator), the Agreement provides that the management of the Operations and other business of the Venture shall be the responsibility of all the Venturers. The Agreement provides for the appointment of Signal Oil llc as Managing Venturer. The Venturers, by a vote of 51% in Interest, have the absolute authority to replace Signal Oil llc or any other Managing Venturer or Operator at any time (other than retroactively). All proposed Venturers are required to acknowledge, warrant and represent that they possess the experience to select appropriate replacement Managing Venturers; are not relying on the managerial efforts of Signal Oil llc. for the success of the Venture; and that their experience and knowledge enable them to effectively exercise the managerial power and authority conferred upon them by the Joint Venture Agreement. Such qualifications are required as a prerequisite to becoming a Venturer as described herein.

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PARTICIPATION IN COSTS AND REVENUES WITHIN VENTURE

OPERATING COSTS SHARED

All deductions, credits and net losses of the Joint Venture will be allocated as set forth on the chart on the first page of this Memorandum.

All customary expenses of operation and production incurred by the Venture in connection with the production and marketing of any oil and gas found by the Venture from initial operations will be allocated one hundred (100%) percent to the Venturers (proportionately reduced) subject to adjustments for failure to participate in completion assessments, and regardless of whether such costs would be deemed currently deductible or capital expenditures for federal income tax purposes.

COMPENSATION AND REIMBURSEMENT

In the event the Venture is fully capitalized and commences initial operations, the Managing Venturer and/or the Operating Company will receive certain consideration and reimbursement, both directly and indirectly, for serving as Managing Venturer of the Venture.

MONTHLY REIMBURSEMENT TO MANAGING VENTURER AND/OR OPERATOR

Signal Oil llc, as Operator, or its replacement or sub-operator shall receive on a monthly basis an administrative fee (operating overhead) which is charged per participant and/or subject to a minimum gross monthly charge as set forth in the Exhibit “C” to the Joint Operating Agreement(s),(subject to annual review and maintenance per the COPAS Agreement) from the Venture for its general and administrative expenses allocable to the Venture, including maintaining office functions, information management, interface between Joint Venturers, operations, regulatory, and accounting and revenue distribution. Only a part of the Managing Venturer's total general and administrative expenses are allocable to the Venture. Typically engineering, geological, legal and accounting expenses pertinent to each specific venture are allocated to such venture. Expenses related to field operations and personnel in the field, including company personnel and consultants are chargeable to the Joint Venture. Such allocation shall be determined by the accountant for the Venture and shall be calculated in accordance with generally accepted accounting principles.

ONE-TIME MANAGEMENT FEES FROM TURNKEY CONTRACTS*

As a Management Fee for the supervision and management of the affairs of the Venture during the exploration, acquisition, workover, drilling and/or testing periods of initial operations, the Managing Venturer will receive an amount equal to the excess, if any, of the Turnkey acquisition and drilling price over the actual cost of its obligations pursuant to the Turnkey Acquisition and Drilling Contract. Likewise, during the completion period of initial operations, if completion or re-completion is attempted, the Managing Venturer will receive an amount, if any, of the Turnkey completion or re-completion price over the actual costs of its obligations pursuant to the Turnkey Completion Contract. Signal Oil llc cannot accurately predict the actual amount constituting compensation under the Turnkey contracts to Signal Oil llc and its affiliates. Costs to be expended under the Turnkey contracts are a direct result of the drilling and completion risks encountered. During drilling and completion operations, a variety of conditions may be encountered, such as loss of circulation, blow-outs, detachment and/or loss of drilling equipment, necessity for the purchase and installation of down-hole equipment to keep the well-bore intact, and repair of inadequate cement to hold production casing in place. As such costs are unpredictable with any degree of certainty, in the unlikely event of totally uneventful operations; compensation payable pursuant to the Turnkey contracts could be substantial. Likewise, in the unlikely event that a series of major difficulties is encountered, these costs could equal or exceed the amount of initial venture capital, and Signal Oil llc would be individually responsible for such excess costs. Signal Oil llc may use any funds it receives from management fees and/or profits, if any, from Turnkey contracts for the general operating and/or administrative expenses of Signal Oil llc, including, but not limited to, employee salaries and office expenses of Signal Oil llc. Signal Oil llc may also be obligated to pay sums to one or more contract operating company(ies) for its management responsibilities relating to operations during acquisition, re-entry, drilling, completion, and operating of the proposed property.

Such one-time management fees apply only in the case of Turnkey contracts, which are not applied in all cases. For instance, certain joint ventures provide for a Turnkey Drilling Contract, but upon completion of the Turnkey contract by drilling and testing the well, completion and equipping the well is done on an industry or non-Turnkey basis wherein each Joint Venturer pays a proportionate share of actual cost.

COMPENSATION

Participation in Revenues. The Issuer or the Managing Venturer, or their affiliates, contractors, and employees may own an overriding royalty interest or true royalty on minerals owned in the proposed Joint Venture well(s) in addition to any working Interest purchased and/or any carried working Interest acquired in the structure of the Joint Venture. If the proposed well(s) is completed and production occurs in commercial quantities, such overriding royalty interest will result in additional compensation to the holder there of.

Reimbursement of Expenses. The Issuer and its agents will be paid from initial capital for expenses incurred in connection with the Venture, including Venture expenses, postage, printing, legal, due diligence fees, consulting fees, and other general and administrative overhead.

Forfeiture of Completion Contributions. To the extent that the Issuer demands an additional mandatory assessment which is not paid and thereby accedes to the interest of a Participant who forfeited the Unit of Interest, such an event may be deemed additional compensation to the Issuer.

Back-in After Payout (WI)

Signal Oil llc and certain third parties and/or affiliates, if applicable, in this Venture (See Investment Summary, Confidential Memorandum Part 1; Source and Application of Proceeds), in aggregate, may intend to retain a working Interest after payout of the Venture's initial investment. At such time as payout is achieved, this working Interest and net revenue Interests of the Venturers will be proportionately reduced to that amount set forth under Source and Application of Proceeds; Investment Summary Page, to the Confidential Private Placement Memorandum, to the credit of Signal Oil llc and/or said third parties or affiliates, in aggregate, and this interest may be held outside the Venture. If a back-in after payout interest is or is not to be retained, such will be reflected in the Investment Summary, Confidential Memorandum Part 1.

* if applicable

Transfer of Units

The Agreement provides for a right of first refusal to the Managing Venturer and the Venturers regarding the sale of Units by a Venturer. If the income received from any such Unit purchased by the Managing Venturer or the price received by the Managing Venturer on subsequent resale exceeds the price paid, such excess may be considered to be additional compensation to the Managing Venturer. For a more detailed description of these rights and obligations, see "Joint Venture Agreement" annexed as Exhibit "B" hereto.

Withdrawal Due to Completion Assessments

To the extent that the Managing Venturer advances a non-consenting venturer's completion assessment and succeeds to the abandonment interest or advances a non-paying Venturer's Completion Assessment, such amount may be deemed to be additional compensation to the Managing Venturer.

REPORTS TO PARTICIPANTS

The following reports may be provided to Participants as appropriate and specific to given venture.

DRILL, TEST, AND COMPLETION REPORTS

Accumulated Drilling, Workover, Completion and Stimulation reports will be provided. Following the conclusion of drilling and testing, the results of testing data obtained and the company's technical evaluation will be furnished to Participants in order to provide them with a basis upon which to elect between meeting the completion assessment or forfeiting their Interest in the prospect.

OPERATIONS REPORTS

Periodic operations reports will be provided covering any operations performed on the well. Lease Operating Statements and Joint Interest Billings will convey the majority of information and will be produced quarterly.

QUARTERLY AND/OR ANNUAL REPORTS

First production sales revenue is typically disbursed to Participants as soon as possible after payments from crude oil and natural gas purchases are made to the Venture's Revenue Accounting department. Subsequently, Joint Interest Billings (JIBs) and Lease Operating statements along with revenue distribution will be provided on a quarterly schedule.

Quarterly and/or annually and if annually, prior to April 15 of each calendar year, the Company will furnish each Participant with a written report summarizing production and expenditures during the sequential producing month or preceding calendar year. Such report will contain all information required for income tax reporting purposes.

RECORDS

Information as to the project will be maintained at the Company's office in Houston, Texas, or at such location as the company's principal operations offices may be located, and any Participant shall be permitted to inspect such records during normal business hours. Well files and operations records will be maintained with the operating company.

PRODUCTION AND REVENUE REPORTS

Each Participant will receive ongoing reports concurrent with production and revenue reporting for each producing well or lease. This may include reports filed with state agencies such as the Texas Railroad Commission and revenue statements from crude oil purchasers.

A prospective Venturer is urged to read the balance of this Memorandum, which details the information in this summary and contains other important information about the Venture.

Electronic Signatures Valid, Legal and Enforceable

Electronic signatures facilitate faster and more secure document signing for the public and private sector, with the flexibility to choose the option that is most efficient for each organization, department, or project. With the passage of the United States (U.S.) Electronic Signatures in Global and National Commerce (ESIGN) Act in 2000, electronic signatures became legal in every state and U.S. territory where federal law applies. When federal law does not apply, most U.S. states have adopted the Uniform Electronic Transactions Act (UETA).

Electronic Signatures in Global and National Commerce (ESIGN) Act.

The ESIGN Act granted electronic signatures the same legal status as handwritten signatures throughout the U.S., greatly simplifying and expediting how organizations gather, track, and manage signatures, and approvals on agreements and documents of all kinds. Under the ESIGN Act, an electronic signature is defined as any electronic process associated with an agreement that indicates acceptance of that agreement. The ESIGN Act:

- Provides that any law with a requirement for a signature may be satisfied by an electronic signature.
- Allows electronically executed agreements to be presented as evidence in court.
- Prevents denial of legal effect, validity, or enforceability of an electronically signed document solely because it is in electronic form.

Under the ESIGN Act, an electronic signature is defined as "an electronic sound, symbol, or process attached to or logically associated with a contract or other record and executed or adopted by a person with the intent to sign the record." In simple terms, electronic signatures are legally recognized as a viable method to indicate agreement to a contract.

Uniform Electronic Transactions Act (UETA).

In 1999, the Uniform Law Commission drafted the model Uniform Electronic Transactions Act or UETA to provide a legal framework for the use of electronic signatures in each state. The following key legal terms are outlined in UETA:

1. A record or signature can’t be denied legal effect or enforceability simply because it’s in electronic form.
2. A contract can’t be denied legal effect or enforceability simply because an electronic record was used in its formation.
3. If a law requires a record to be in writing, an electronic record satisfies the law.
4. If a law requires a signature, an electronic signature satisfies the law.

The parties hereto agree that this agreement may be electronically signed. The parties agree that the electronic signatures appearing on this agreement are the same as handwritten signatures for the purposes of validity, enforceability, and admissibility. All parties signing electronically shall receive a true digital copy of the documents so executed. Any party, proposing to participate and refusing electronic signature shall download and print the appropriate documents and execute same with hand written signature, delivering same per Joint Venture Manager’s directions.

FURTHER INFORMATION

Signal Oil llc will make available to any potential Venturer, or his representative, accountant, tax advisor, or attorney, any other information deemed necessary and appropriate by the potential Venturer, or such other person, if any, including geological information, to the extent such information is available to Signal Oil llc or may be obtained by it without unreasonable cost or effort. Such information should not be relied upon unless the same is authorized by an officer of Signal Oil llc.

A WYOMING LIMITED LIABILITY COMPANY

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

PART 4

IMPORTANT NOTICES & DISCLAIMERS
RISK DISCUSSION

Important Notices, Disclaimers and Risk Discussion

THIS DOCUMENT IS CONFIDENTIAL AND CONTAINS PROPRIETARY INFORMATION. IT IS INTENDED FOR THE EXCLUSIVE USE OF THE PARTY TO WHOM IT WAS DIRECTLY DELIVERED FROM THE ISSUER. ANY REPRODUCTION OR DISTRIBUTION OF THIS MEMORANDUM IN WHOLE OR IN PART, OR THE DIVULGENCE OF ANY OF THE INFORMATION CONTAINED HEREIN WITHOUT THE PRIOR WRITTEN CONSENT OF SIGNAL OIL LLC. ("SIGNAL".) IS PROHIBITED.

UNITS OF JOINT VENTURE INTEREST

SIGNAL OIL LLC. AND/OR ITS DESIGNATED AFFILIATE, THE MANAGING JOINT VENTURER, (SOMETIMES HEREIN REFERRED TO AS THE MANAGING VENTURER OR SIGNAL OIL LLC.) INTENDS TO RECEIVE APPLICATIONS FOR UP TO THE MAXIMUM NUMBER OF UNITS OF JOINT VENTURE INTEREST (THE UNITS) INDICATED IN THE SUMMARY OF THE JOINT VENTURE PROGRAM OF THIS MEMORANDUM IN SIGNAL OIL LLC.'S JOINT VENTURE, NAMED HEREINABOVE, A TEXAS JOINT VENTURE (THE VENTURE) THAT HAS BEEN FORMED FOR THE SEARCH FOR AND PRODUCTION AND SALE OF OIL AND/OR NATURAL GAS.

UNITS ARE SUBJECT TO COMPLETION ASSESSMENTS IN THE AMOUNT PER UNIT SET FORTH HEREIN. A PARTICIPANT'S FAILURE TO PAY A COMPLETION ASSESSMENT WILL RESULT IN THE PROPORTIONAL ABANDONMENT OF THE PARTICIPANT'S INTEREST AND/OR THE PARTICIPANT'S WITHDRAWAL FROM THE VENTURE.

THIS MEMORANDUM DOES NOT CONSTITUTE AN OFFER OR A SOLICITATION TO ACCEPT AND/OR MAKE SUBSCRIPTIONS TO THE UNITS OR TO SELL AND/OR BUY THE UNITS IN ANY JURISDICTION IN WHICH SUCH AN OFFER OR SOLICITATION IS NOT AUTHORIZED, OR IN WHICH THE PERSON MAKING SUCH OFFER IS NOT QUALIFIED TO DO SO, OR TO ANY PERSON TO WHOM IT IS UNLAWFUL TO MAKE AN OFFER OR SOLICITATION. ACCEPTANCE OF YOUR SUBSCRIPTION FOR UNIT(S) SHALL BE MADE ONLY AFTER YOU HAVE BEEN DELIVERED A CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM, IN ITS ENTIRETY, AND IT HAS BEEN DETERMINED THAT YOU SATISFY THE REQUIREMENTS NECESSARY TO ENABLE THE ISSUER TO CLAIM AN EXEMPTION FROM REGISTRATION AS WELL AS SATISFYING THE SUITABILITY FACTORS AS SET FORTH HEREIN. THE JOINT VENTURE UNITS HEREIN MAY NOT BE DIRECTLY OR INDIRECTLY OFFERED, SOLD OR DELIVERED TO ANY PERSON IN ANY JURISDICTION EXCEPT IN COMPLIANCE WITH LAW.

THIS MEMORANDUM IS EMPLOYED SOLELY IN CONNECTION WITH THE PRIVATE VENTURE OF THE UNITS OF INTEREST. DELIVERY OF THIS MEMORANDUM TO ANY OTHER PERSON OR IN ANY OTHER MANNER IS NOT TO BE CONSTRUED AS AN OFFER. PURCHASE OF THE UNITS MAY BE MADE ONLY BY PERSONS TO WHOM ACTUAL OFFERS ARE MADE AND ONLY IN ACCORDANCE WITH THE PROCEDURES DESCRIBED HEREIN. ALL SUBSCRIPTIONS ARE SUBJECT TO ACCEPTANCE OR REJECTION BY THE ISSUER AT ITS SOLE DISCRETION.

THE JOINT VENTURE INTERESTS DESCRIBED HEREIN MAY NOT HAVE BEEN QUALIFIED WITH OTHER STATE SECURITIES AUTHORITIES IN RELIANCE UPON THE ISSUER'S BELIEF THAT THE JOINT VENTURE WILL BE CONDUCTED IN A MANNER THAT BRINGS IT THE APPROPRIATE EXEMPTION FROM QUALIFICATION OR REGISTRATION. THE JOINT VENTURE INTERESTS DESCRIBED HEREIN HAVE NOT BEEN REGISTERED WITH OR APPROVED (OR DISAPPROVED) BY ANY STATE SECURITIES COMMISSION NOR HAS ANY SUCH COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS MEMORANDUM. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THE PARTICIPATION UNITS IN THIS JOINT VENTURE ARE NOT SECURITIES WITHIN THE MEANING OF SECURITY LAWS OF THE UNITED STATES, OR ANY STATE OR TERRITORY, AND HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), OR REGISTERED UNDER THE SECURITY LAWS OF ANY STATE.

THE MANAGING VENTURER INTENDS TO QUALIFY THE UNITS OF JOINT VENTURE INTERESTS AS TRANSACTIONS EXEMPT FROM THE REGISTRATION REQUIREMENTS OF FEDERAL AND STATE SECURITIES LAWS AND REGULATIONS, AS MAY BE APPLICABLE.

CONTENT OF THE MEMORANDUM

ANY ALTERATION, ADDITION, OR DELETION IN THIS AGREEMENT MADE WITHOUT THE EXPRESS WRITTEN CONSENT OF ALL PARTIES HERETO SHALL BE WITHOUT ANY FORCE OR EFFECT, AND THIS AGREEMENT SHALL REMAIN ENFORCEABLE ACCORDING TO ITS ORIGINAL TENOR.

THE INFORMATION CONTAINED IN THIS MEMORANDUM HAS BEEN OBTAINED FROM SOURCES BELIEVED BY SIGNAL OIL LLC.TO BE RELIABLE; HOWEVER, THE MANAGING JOINT VENTURER DOES NOT MAKE AND EXPRESSLY DISCLAIMS ANY REPRESENTATION OR WARRANT AS TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED HEREIN, AND NONE MAY BE IMPLIED; HOWEVER, NEITHER THE DELIVERY OF THIS MEMORANDUM NOR ANY PARTICIPATION IN THE UNITS DESCRIBED HEREIN SHALL, UNDER ANY CIRCUMSTANCES, CREATE ANY IMPLICATION THAT THE INFORMATION CONTAINED HEREIN IS TRUE AND ACCURATE AS OF ANY TIME SUBSEQUENT TO THE DATE HEREOF. NO PERSON OTHER THAN SIGNAL OIL LLC. AND ITS AUTHORIZED CONTRACTORS AND AGENTS HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION IN CONNECTION WITH THE INTERESTS DESCRIBED HEREIN, AND, IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATIONS MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY SIGNAL OIL LLC. NO PERSON HAS BEEN AUTHORIZED TO MAKE ANY REPRESENTATIONS OTHER THAN THOSE CONTAINED IN THIS MEMORANDUM. PROJECTIONS MAY BE CONTAINED IN THIS MEMORANDUM, AND ANY OTHER PROJECTIONS THAT DO NOT CONFORM TO THOSE IN THIS MEMORANDUM SHOULD BE DISREGARDED.

THE PURPOSE OF THIS MEMORANDUM IS TO PROVIDE THE PROSPECTIVE VENTURER WITH INFORMATION THAT SIGNAL OIL LLC. BELIEVES IS PERTINENT IN MAKING AN INFORMED DECISION AS TO PARTICIPATION IN THE VENTURE. IT IS RECOGNIZED THAT ADDITIONAL INFORMATION MAY BE DESIRED BY A PROSPECTIVE VENTURER PRIOR TO MAKING HIS DECISION. THEREFORE, EACH PROPOSED VENTURER IS ENCOURAGED TO MAKE FURTHER INQUIRY IN AN EFFORT TO SATISFACTORILY ANSWER ANY QUESTIONS HE OR SHE MAY HAVE. REQUESTS FOR FURTHER INFORMATION SHOULD BE MADE TO SIGNAL OIL LLC., AND SUCH INFORMATION SHOULD ONLY BE RELIED UPON WHEN FURNISHED IN WRITTEN FORM AND SIGNED BY AN OFFICER OF SIGNAL OIL LLC.

PROSPECTIVE VENTURERS ARE NOT TO CONSTRUE THE CONTENTS OF THIS MEMORANDUM OR ANY SUBSEQUENT COMMUNICATION FROM SIGNAL OIL LLC. OR ANY AFFILIATE AS INVESTMENT, LEGAL OR TAX ADVICE. EACH PERSON IS ENCOURAGED TO SEEK INDEPENDENT LEGAL AND TAX ADVICE REGARDING HIS PARTICULAR SITUATION AND, MORE SPECIFICALLY, ANY PARTICIPATION IN THE VENTURE REFERRED TO HEREIN. SIGNAL OIL LLC.MAKES NO REPRESENTATIONS AS TO THE EFFECT OF PARTICIPATION IN UNITS DESCRIBED HEREIN ON THE PARTICULAR FEDERAL OR STATE INCOME TAX SITUATION OF ANY PROSPECTIVE JOINT VENTURER.

ANY COMMUNICATION REGARDING PARTICIPATION IN THE UNITS DESCRIBED HEREIN SHALL ONLY BE MADE THROUGH PERSONAL NEGOTIATIONS BETWEEN A PROSPECTIVE VENTURER AND AN AUTHORIZED REPRESENTATIVE OF SIGNAL OIL LLC. SUCH PERSONAL

NEGOTIATIONS ARE INTENDED BY SIGNAL OIL LLC.TO INSURE, AMONG OTHER THINGS, ADHERENCE TO THE SUITABILITY STANDARDS REQUIRED OF POTENTIAL VENTURERS AND TO PROVIDE POTENTIAL VENTURERS THE OPPORTUNITY TO SEEK SUCH EXPLANATIONS AND/OR ADDITIONAL INFORMATION ABOUT THE VENTURE AS THEY MAY DESIRE.

EACH PROSPECTIVE VENTURER MUST EXECUTE A CONFIDENTIALITY AND NON-COMPETE AGREEMENT, QUESTIONNAIRE, APPLICATION AND SUBSCRIPTION AGREEMENT AND A RECEIPT FOR HIS COPY OF THIS MEMORANDUM AND SHALL FURTHER, BY THE EXECUTION THEREOF, MAKE THOSE REPRESENTATIONS REFERRED TO THEREIN. ANY PARTICIPANT IN THIS JOINT VENTURE ACKNOWLEDGES THAT THE REPRESENTATIONS, WARRANTIES AND STATEMENTS MADE AND SET FORTH IN THE QUESTIONNAIRE AND APPLICATION AND SUBSCRIPTION AGREEMENT WILL BE USED AND RELIED UPON TO CONDITION HIS/HER ACCEPTANCE IN THE JOINT VENTURE AND THAT JOINT VENTURER INDEMNIFIES AND AGREES TO HOLD HARMLESS THE MANAGING VENTURER, OPERATOR, OTHER JOINT VENTURERS, AFFILIATE(S), THEIR OWNER(S), OFFICER(S), CONTRACTOR(S), AGENT(S), DIRECTOR(S), PARTNER(S), AND ATTORNEY(IES) FROM ANY AND ALL LOSS, DAMAGE, LIABILITY AND EXPENSE INCLUDING REASONABLE ATTORNEY'S FEES AND COSTS OF DEFENSE. (SEE "PLAN OF ORGANIZATION AND SUITABILITY STANDARDS.").

CONFIDENTIALITY AND NONDISCLOSURE

THIS MEMORANDUM CONTAINS CERTAIN INFORMATION OF A HIGHLY CONFIDENTIAL AND PROPRIETARY NATURE. THE RECEIPT OF THIS MEMORANDUM CONSTITUTES AN AGREEMENT ON THE PART OF THE RECIPIENT TO MAINTAIN THE CONFIDENTIALITY OF THE INFORMATION CONTAINED HEREIN OR ANY ADDITIONAL INFORMATION SUBSEQUENTLY DELIVERED IN CONNECTION HEREWITH. PROSPECTIVE INVESTORS WHO ACCEPT THIS MEMORANDUM OR BECOME AWARE OF THE STATE SECURITIES LAW RESTRICTIONS PLACED UPON THEIR ABILITY TO DISCLOSE TO OTHERS INFORMATION CONTAINED HEREIN OR TO PARTICIPATE IN OR OTHERWISE EFFECT OR FACILITATE ANY TRANSACTIONS RELATING TO THE VENTURE. PROSPECTIVE INVESTORS WHO CANNOT COMPLY FULLY WITH SUCH RESTRICTIONS SHOULD NOT REVIEW THE INFORMATION CONTAINED HEREIN AND SHOULD RETURN ALL HARD COPIES TO THE ISSUER AND DESTROY ALL DIGITAL COPIES.

THIS PRIVATE PLACEMENT MEMORANDUM AND THE EXHIBITS HERETO (COLLECTIVELY, THE MEMORANDUM) HAVE BEEN SUBMITTED ON A CONFIDENTIAL BASIS FOR USE BY A LIMITED NUMBER OF ACCREDITED AND/OR QUALIFIED INVESTORS SOLELY FOR, AND SHOULD BE USED ONLY IN CONNECTION WITH, A PROSPECTIVE INVESTOR'S CONSIDERATION OF AN INVESTMENT IN THE JOINT VENTURE INTERESTS DESCRIBED HEREIN. ITS USE FOR ANY OTHER PURPOSE IS NOT AUTHORIZED.

ANY REPRODUCTION OR DISTRIBUTION OF THIS MEMORANDUM IN WHOLE OR IN PART, OR THE DIVULGENCE OF ANY OF THE INFORMATION CONTAINED HEREIN WITHOUT THE PRIOR WRITTEN CONSENT OF SIGNAL OIL LLC. IS PROHIBITED.

PROJECTIONS AND PREDICTIONS

ALTHOUGH FINANCIAL ILLUSTRATIONS AS TO THE POSSIBLE ECONOMIC POTENTIAL OF THE BUSINESS OPPORTUNITY ARE PROVIDED, SUCH ILLUSTRATIONS REPRESENT PROJECTIONS OF POSSIBLE FUTURE EVENTS THAT MAY WELL NOT COME TO PASS. THE RESULTS OF AN INVESTMENT WILL DEPEND ON A NUMBER OF HIGHLY UNCERTAIN FACTORS. ANY OTHER PROJECTIONS OR OTHER REPRESENTATIONS MADE IN CONNECTION WITH THIS MEMORANDUM REGARDING FUTURE REVENUES OR RETURN ON INVESTMENT ARE NOT AUTHORIZED AND, IF MADE, MUST NOT BE RELIED UPON.

REPURCHASE OF UNITS

ALTHOUGH THE MANAGING JOINT VENTURER RETAINS THE OPTION AND MAY OFFER TO DO SO, EVERY INVESTOR SHOULD BE AWARE THAT THE MANAGING JOINT VENTURER HAS NO OBLIGATION, NOR DOES IT CURRENTLY HAVE ANY INTENTION, TO REPURCHASE ANY JOINT VENTURE UNITS FROM INVESTORS IN THE EVENT THAT, FOR ANY REASON, AN INVESTOR WISHES TO TERMINATE HIS/HER PARTICIPATION.

REPORTS TO PARTICIPANTS

THE MANAGING VENTURER SHALL PROVIDE ACCESS TO PARTICIPANTS, CERTAIN INFORMATION AND REPORTS WHICH INCLUDE, AT A MINIMUM, DRILLING AND OPERATIONAL REPORTS, GROSS AND NET PRODUCTION FROM LEASE(S), MARKETED VALUE OF ALL PRODUCTION, WELLHEAD SEVERANCE TAXES PAID, STATEMENT OF LEASE OPERATING EXPENSES, STATEMENT REFLECTING PARTICIPANTS PRO RATA SHARE OF TAX BENEFITS, AMONG OTHERS. SEE ARTICLE VII OF THE JOINT VENTURE AGREEMENT, WHICH IS ANNEXED HERETO AS EXHIBIT "B".

SUITABLE INVESTORS

THIS INVESTMENT IS, IN GENERAL, ONLY SUITABLE FOR PERSONS WHO ARE **ACCREDITED INVESTORS** AS THAT TERM IS DEFINED IN RULE 501 OF SECURITIES AND EXCHANGE COMMISSION REGULATION D. THE MANAGING JOINT VENTURER MAY, HOWEVER, MAKE EXCEPTIONS TO THIS GENERAL SUITABILITY STANDARD AND PERMIT SALES TO PERSONS WHO ARE NOT ACCREDITED INVESTORS IF SUCH PERSONS ARE ABLE TO DEMONSTRATE THEIR FINANCIAL SOPHISTICATION AND SUITABILITY TO THE SATISFACTION OF THE MANAGING JOINT VENTURER. NOTWITHSTANDING THE FOREGOING, JOINT VENTURE INTERESTS WILL NOT, UNDER ANY CIRCUMSTANCES, BE SOLD TO MORE THAN 35 PERSONS WHO ARE NOT ACCREDITED INVESTORS.

JOINT VENTURE UNITS WILL ONLY BE SOLD TO AN INVESTOR WITH RESPECT TO WHOM THE MANAGING JOINT VENTURER HAS REASONABLE GROUNDS TO BELIEVE, AND DOES BELIEVE, IMMEDIATELY PRIOR TO SALE, AFTER MAKING REASONABLE INQUIRY, EITHER (1) THAT SUCH INVESTOR HAS SUCH KNOWLEDGE AND EXPERIENCE IN FINANCIAL AND BUSINESS MATTERS THAT HE/SHE IS CAPABLE OF EVALUATING THE MERITS AND THE RISKS OF THIS INVESTMENT, OR (2) THAT SUCH INVESTOR AND HIS/HER PURCHASER REPRESENTATIVE (AS THAT TERM IS DEFINED IN SECURITIES AND EXCHANGE COMMISSION REGULATION D PROMULGATED UNDER THE SECURITIES ACT OF 1933, AS AMENDED) TOGETHER HAVE SUCH KNOWLEDGE AND EXPERIENCE IN BUSINESS AND FINANCIAL MATTERS THAT THEY ARE CAPABLE OF EVALUATING THE MERITS AND RISKS OF THIS INVESTMENT AND THAT SUCH INVESTOR IS ABLE TO BEAR THE ECONOMIC RISK OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

FURTHERMORE, JOINT VENTURE UNITS WILL ONLY BE SOLD TO INVESTORS WHO MAKE A WRITTEN REPRESENTATION THAT THEY ARE THE SOLE AND TRUE PARTY IN INTEREST AND ARE NOT PURCHASING THE ADDITIONAL JOINT VENTURE UNITS FOR THE BENEFIT OF ANY OTHER PERSON (OR THAT THEY ARE PURCHASING FOR ANOTHER PERSON WHO MEETS ALL THE CONDITIONS SET FORTH HEREIN).

NO ONE SHOULD PARTICIPATE IN THE VENTURE UNLESS HIS OBJECTIVE IS TO SECURE AN ECONOMIC PROFIT SEPARATE AND APART FROM ANY TAX BENEFITS THAT MAY FLOW FROM THE VENTURE.

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THE JOINT VENTURE UNITS OF INTEREST REFERRED TO HEREIN ARE SUBJECT TO WITHDRAWAL, CANCELLATION, OR MODIFICATION BY THE ISSUER WITHOUT NOTICE. THE ISSUER RESERVES THE RIGHT, IN ITS SOLE DISCRETION, TO REJECT ANY SUBSCRIPTION IN WHOLE OR IN PART FOR ANY REASON OR TO ALLOT TO ANY SUBSCRIBER LESS THAN THE TOTAL VENTURE INTEREST SUBSCRIBED FOR OR TO WAIVE CONDITIONS TO THE PURCHASE OF INTERESTS IN THE JOINT VENTURE.

INVESTOR RESPONSIBILITY

EACH INVESTOR MUST RELY ON HIS OWN REPRESENTATIVE AS TO LEGAL, INCOME TAX AND RELATED MATTERS. PROSPECTIVE INVESTORS ARE NOT TO CONSTRUE THE CONTENTS OF THIS MEMORANDUM OR ANY WRITTEN OR ORAL COMMUNICATION WHETHER A PRIOR OR SUBSEQUENT COMMUNICATION FROM THE MANAGING JOINT VENTURER OR ITS EMPLOYEES AS INVESTMENT, LEGAL OR TAX ADVICE. EACH PROSPECTIVE INVESTOR SHOULD CONSULT HIS OR HER OWN ATTORNEY, BUSINESS ADVISOR AND TAX ADVISOR AS TO LEGAL, BUSINESS, TAX AND RELATED MATTERS CONCERNING THIS VENTURE AND CONCERNING THIS INVESTMENT. NO REPRESENTATION IS MADE REGARDING THE LEGALITY OF AN INVESTMENT HEREIN BY ANY PURCHASER UNDER APPROPRIATE LEGAL INVESTMENT OR SIMILAR LAWS.

EACH JOINT VENTURER HAS THE RIGHT TO BE, AND WILL BE, INVOLVED IN MAKING VENTURE DECISIONS. EACH JOINT VENTURER IS PROVIDED EXTENSIVE AND SIGNIFICANT MANAGEMENT POWERS IN THIS JOINT VENTURE AND WILL BE EXPECTED TO EXERCISE SAME AND MUST NOT RELY ON THE MANAGING JOINT VENTURER FOR THE SUCCESS OR PROFITABILITY OF THE VENTURE. CITES: YOUMANS V. SIMON, 791.2D 341 (5TH CIR.1986); S.E.C. V. HOWEY, 328 U.S. 293, 66 CT. 1100, 90 L.ED. 1244 (1946); SPARKS V. BAXTER, 854 F.2D 110 (5TH CIR. 1988; KAUFAM V. MAGID, 539 F. SUPP, 1088 (1982); CADIZ V. JIMENEZ, 579 F. SUPP.1176 (1983); SEC V. KINLAW SECURITIES CORP, N.D.,TX, 1998; WILLIAMSON V. TUCKER, 632 F.2D 579 (5TH CIR. 1981); RUSSELL V. FRENCH, 709 S.W.2D 312 TEX.APP.(1986).

ALL PROPOSED VENTURERS ARE REQUIRED TO ACKNOWLEDGE, WARRANT AND REPRESENT THAT THEY POSSESS THE REQUISITE BUSINESS KNOWLEDGE AND EXPERIENCE TO SELECT APPROPRIATE MANAGING VENTURERS, THAT THE JOINT VENTURERS ARE NOT RELYING ON THE MANAGERIAL EFFORTS OF SIGNAL OIL LLC.FOR THE SUCCESS OF THE VENTURE, AND THAT THEIR EXPERIENCE AND KNOWLEDGE ENABLE THEM TO EFFECTIVELY EXERCISE THE MANAGERIAL POWERS AND AUTHORITY CONFERRED UPON THEM BY THE JOINT VENTURE AGREEMENT.

THERE IS GENERAL LIABILITY OF ALL PARTICIPANTS. REVENUE FROM THE VENTURE IS SPECULATIVE AND RETURN OF INVESTMENT IS CONTINGENT ON REVENUES FROM THE SALES OF OIL AND GAS PRODUCTION. INVESTMENT IS SUBJECT TO OTHER RISKS AND CONFLICTS OF INTEREST, MORE FULLY DESCRIBED HEREIN. SEE “RISK FACTORS” AND “CONFLICTS OF INTEREST” FOR A DETAILED DESCRIPTION OF SOME OF THE RISKS DESCRIBED HEREIN.

JOINT VENTURE PARTICIPANTS

THIS MEMORANDUM IS PREPARED SOLELY FOR THE BENEFIT OF QUALIFIED PERSONS ACCEPTABLE TO THE MANAGING VENTURER WHO MEET THE SUITABILITY STANDARDS SET BY THE MANAGING VENTURER. (SEE “PLAN OF ORGANIZATION AND SUITABILITY STANDARDS.”) THIS INVESTMENT IS SPECULATIVE AND SUITABLE ONLY FOR PERSONS WHO HAVE SUBSTANTIAL FINANCIAL RESOURCES AND MEET CERTAIN SUITABILITY REQUIREMENTS, WHO DO NOT ANTICIPATE THAT THEY WILL BE REQUIRED TO LIQUIDATE ANY INVESTMENT ACQUIRED HEREUNDER IN THE FORESEEABLE FUTURE, AND WHO UNDERSTAND OR HAVE BEEN ADVISED WITH RESPECT TO ANY RISK FACTORS ASSOCIATED WITH THIS VENTURE. THERE MAY BE MATERIAL INVESTMENT RISKS ASSOCIATED WITH THIS VENTURE THAT CANNOT BE IDENTIFIED AT THIS TIME. (SEE “RISK FACTORS.”)

SUBSTANTIAL RESTRICTIONS WILL BE IMPOSED ON ANY SALE OR TRANSFER OF ANY OF THE SECURITIES OFFERED HEREBY. THERE IS NO PUBLIC MARKET FOR THE UNITS AND THERE IS ILLIQUIDITY OF THE INVESTMENT AND AN INABILITY TO SELL OR TRANSFER UNITS. INVESTORS SHOULD BE MADE AWARE THAT THEY WILL BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

EACH INVESTOR IS HEREBY GIVEN AN OPPORTUNITY TO ASK QUESTIONS OF AND RECEIVE ANSWERS FROM, THE OFFICERS AND DIRECTORS OF THE MANAGING JOINT VENTURER OR ANY PERSON ACTING ON ITS BEHALF CONCERNING THE TERMS AND CONDITIONS OF THIS MEMORANDUM AND TO OBTAIN ANY ADDITIONAL INFORMATION TO THE EXTENT THE MANAGING JOINT VENTURER POSSESSES SUCH INFORMATION (OR CAN ACQUIRE IT WITHOUT UNREASONABLE EFFORT AND EXPENSE) NECESSARY TO VERIFY THE ACCURACY OF THE INFORMATION CONTAINED IN THIS MEMORANDUM. FURTHERMORE, THE MANAGING JOINT VENTURER HAS OR WILL HAVE VARIOUS DOCUMENTS CONNECTED WITH THE PROPOSED BUSINESS OF THE JOINT VENTURE. ALL SUCH DOCUMENTS ARE AVAILABLE TO THE PROSPECTIVE INVESTOR. IF YOU HAVE ANY QUESTIONS WHATSOEVER REGARDING THIS CONFIDENTIAL MEMORANDUM AND ITS TERMS AND CONDITIONS, OR DESIRE ANY ADDITIONAL INFORMATION OR DOCUMENTS TO VERIFY OR SUPPLEMENT THE INFORMATION CONTAINED IN THIS MEMORANDUM, PLEASE CONTACT:

SIGNAL OIL LLC.
1321 UPLAND DRIVE, SUITE 5866
HOUSTON, TEXAS 77043
1-833-OIL-O-OIL
1-833-645-0645

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NOTICE(S) AND DISCLAIMER(S)

BY ACCEPTANCE OF THIS CONFIDENTIAL MEMORANDUM, PROSPECTIVE INVESTORS RECOGNIZE AND ACCEPT THE NEED TO CONDUCT THEIR OWN THOROUGH INVESTIGATION AND DUE DILIGENCE BEFORE CONSIDERING A PURCHASE OF THE VENTURE. THE CONTENTS OF THIS CONFIDENTIAL MEMORANDUM SHOULD NOT BE CONSIDERED TO BE INVESTMENT, TAX, OR LEGAL ADVICE, AND EACH PROSPECTIVE INVESTOR SHOULD CONSULT WITH HIS OR HER OWN COUNSEL AND ADVISORS AS TO ALL MATTERS CONCERNING AN INVESTMENT IN THIS VENTURE.

IRS CIRCULAR 230 DISCLOSURE

TO ENSURE COMPLIANCE WITH U.S. TREASURY REGULATIONS GOVERNING TAX PRACTICE, WE INFORM YOU THAT ANY U. S. FEDERAL TAX ADVICE CONTAINED IN THIS COMMUNICATION, INCLUDING ANY APPENDICES, IS NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED, FOR THE PURPOSE OF (I) AVOIDING ANY PENALTIES UNDER U. S. FEDERAL TAX LAW, OR (II) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TRANSACTION OR MATTER ADDRESSED HEREIN.

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION (NASAA) LEGEND

IN MAKING AN INVESTMENT DECISION, INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE ISSUER AND THE TERMS OF THE VENTURE INCLUDING THE MERITS AND RISKS INVOLVED. THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS DOCUMENT. ANY REPRESENTATION TO THE CONTRARY IS UNLAWFUL.

THESE JOINT VENTURE UNITS MAY BE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER FEDERAL AND STATE SECURITIES LAWS. INVESTORS SHOULD BE AWARE THAT THEY MAY BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

EXEMPT FROM SECURITIES REGISTRATION NOTICE

THE MANAGING VENTURER INTENDS TO QUALIFY THE UNITS OF THE JOINT VENTURE AS TRANSACTIONS EXEMPT FROM THE REGISTRATION REQUIREMENTS OF FEDERAL AND STATE SECURITIES LAWS AND REGULATIONS, ACCORDINGLY THE UNITS OF INTEREST TO BE OFFERED HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED IN RELIANCE UPON EXEMPTIONS FROM THE REGISTRATIONS PROVIDED IN SECTION(S) 3(B) OF THAT ACT AND REGULATIONS PROMULGATED THEREUNDER AND ESTABLISHED PRECEDENT. THE UNITS ARE AVAILABLE TO PROSPECTIVE PURCHASERS WHO ARE ACCREDITED AS SO DEFINED AND/OR CERTAIN QUALIFIED INVESTORS, AS SO DEFINED; HOWEVER, THERE SHALL BE NO MORE THAN THIRTY FIVE (35) PURCHASERS ALLOWED TO ACQUIRE UNITS WHO ARE NON-ACCREDITED. NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES LAW ADMINISTRATOR HAS PASSED ON OR ENDORSED THE MERITS, ACCURACY, OR ADEQUACY OF THE VENTURE OR THESE JOINT VENTURE PARTICIPATION UNITS.

REGULATION D PRIVATE PLACEMENT VENTURES

THE NATIONAL SECURITIES MARKETS IMPROVEMENT ACT ("NSMIA") AMENDED SECTION 18 OF THE SECURITIES ACT OF 1933 TO EXEMPT FROM STATE REGULATION ANY OFFER OR SALE OF SECURITIES EXEMPT FROM REGISTRATION PURSUANT TO THE SECURITIES AND EXCHANGE COMMISSION RULES OR REGULATIONS ISSUED UNDER SECTION 4(2) OF THE SECURITIES ACT OF 1933. ACCORDINGLY, VENTURES EXEMPT FROM FEDERAL REGISTRATION REQUIREMENTS PURSUANT TO REGULATION D ARE EXEMPT FROM STATE REGISTRATION OTHER THAN NOTICE FILINGS/STATE FEES. SHOULD A VENTURE FAIL TO COMPLY WITH REGULATION D BUT STILL BE EXEMPT FROM FEDERAL REGISTRATION PURSUANT TO SECTION 4(2), SUCH VENTURE WOULD BE SUBJECT TO STATE REGULATION TO THE SAME EXTENT AS BEFORE THE ENACTMENT OF NSMIA.

Electronic Signatures Valid, Legal and Enforceable

Electronic signatures facilitate faster and more secure document signing for the public and private sector, with the flexibility to choose the option that is most efficient for each organization, department, or project. With the passage of the United States (U.S.) Electronic Signatures in Global and National Commerce (ESIGN) Act in 2000, electronic signatures became legal in every state and U.S. territory where federal law applies. When federal law does not apply, most U.S. states have adopted the Uniform Electronic Transactions Act (UETA).

Electronic Signatures in Global and National Commerce (ESIGN) Act.

The ESIGN Act granted electronic signatures the same legal status as handwritten signatures throughout the U.S., greatly simplifying and expediting how organizations gather, track, and manage signatures, and approvals on agreements and documents of all kinds. Under the ESIGN Act, an electronic signature is defined as any electronic process associated with an agreement that indicates acceptance of that agreement. The ESIGN Act:

- Provides that any law with a requirement for a signature may be satisfied by an electronic signature.
- Allows electronically executed agreements to be presented as evidence in court.
- Prevents denial of legal effect, validity, or enforceability of an electronically signed document solely because it is in electronic form.

Under the ESIGN Act, an electronic signature is defined as "an electronic sound, symbol, or process attached to or logically associated with a contract or other record and executed or adopted by a person with the intent to sign the record." In simple terms, electronic signatures are legally recognized as a viable method to indicate agreement to a contract.

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Uniform Electronic Transactions Act (UETA).

In 1999, the Uniform Law Commission drafted the model Uniform Electronic Transactions Act or UETA to provide a legal framework for the use of electronic signatures in each state. The following key legal terms are outlined in UETA:

1. A record or signature can't be denied legal effect or enforceability simply because it's in electronic form.
2. A contract can't be denied legal effect or enforceability simply because an electronic record was used in its formation.
3. If a law requires a record to be in writing, an electronic record satisfies the law.
4. If a law requires a signature, an electronic signature satisfies the law.

The parties hereto agree that this agreement may be electronically signed. The parties agree that the electronic signatures appearing on this agreement are the same as handwritten signatures for the purposes of validity, enforceability, and admissibility. All parties signing electronically shall receive a true digital copy of the documents so executed. Any party, proposing to participate and refusing electronic signature shall download and print the appropriate documents and execute same with hand written signature, delivering same per Joint Venture Manager's directions.

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State Disclaimers

Prior to participation, each person should review the applicable state legend, if any, should the Interests described herein be deemed to be "securities."

For residents of all states, the presence of a legend for any given state reflects only that a legend may be required by that state and should not be construed to mean any offer or sale may be made in any particular state. This memorandum may be supplemented by additional state legends. If you are uncertain as to whether or not offers or sales may be lawfully made in any given state, you are advised to contact the Managing Joint Venturer for a current list of states in which offers or sales may be lawfully made.

For Alabama Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under the Alabama Securities Act. A registration statement relating to these Joint Venture Units has not been filed with the Alabama Securities Commission.

For Alaska Residents

The Joint Venture Units referred to herein have not been registered with the Administrator of Securities of the state of Alaska under provisions of 3 AAC 08.500.3 AAC 08.506. The investor is advised that the administrator has made only a cursory review of the registration statement and has not reviewed this document since the Venture is not required to be filed with the administrator. The fact of registration does not mean that the administrator has passed in any way upon the merits, recommended or approved the Venture. Any representation to the contrary is a violation of A.S.45.55.170.

For Arizona Residents

The Joint Venture Units referred to herein are offered pursuant to an exemption from registration with the United States Securities and Exchange Commission. The Commission does not pass upon the merits of any securities nor does it pass upon the accuracy or completeness of any Venture circular or other selling literature.

The Joint Venture Units referred to herein have not been registered under the Securities Act of Arizona, as amended (the "Arizona Act") and cannot be resold unless registered under the Arizona Act or an exemption from registration is available.

For Arkansas Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under Section 23-42-504(a)(14) of the Arkansas Securities Act and Section 4(2) of the Securities Act of 1933. As amended, a registration statement relating to the Joint Venture Units referred to herein has not been filed with the Arkansas Securities Department or with the Securities and Exchange Commission.

For California Residents

The Joint Venture Units referred to herein have not been qualified under the California Corporate Securities Act of 1968, as amended, by reason of specific exemptions thereunder relating to the nature of this Venture. These Units cannot be sold, transferred or otherwise disposed of to any person or entity unless subsequently qualified under the Corporate Securities Act of 1968, as amended, if such qualification is required.

For Colorado Residents

This information is distributed pursuant to an exemption for small ventures under the rules of the Colorado Securities Division.

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended or the Colorado Securities Act of 1981, by reason of specific exemptions thereunder relating to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are registered or an exemption from registration is available.

For Connecticut Residents

The Joint Venture Units referred to herein have not been approved or disapproved by the Banking Commissioner of the State of Connecticut. These Joint Venture Units have not been registered under Section 36-485 of the Connecticut Uniform Securities Act and cannot be resold without registration under Section 36-485 of the Act or an exemption from registration pursuant to Section 36-490 of the Act.

For Delaware Residents

The Joint Venture Units referred to herein have not been registered under the Delaware Securities Act and are offered pursuant to a claim of exemption under Section 7309(b) (9) of the Delaware Securities Act and Rule 9 (b) (9) (11) thereunder. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered under the Act or an exemption from registration is available.

For District of Columbia Residents

The Joint Venture Units referred to herein have not been registered under the District of Columbia Securities Act since such act does not require registration of this Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered under the Securities Act of 1933, as amended, or and exemption from registration is available.

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For Florida Residents

The Joint Venture Units referred to herein will be sold to, and acquired by the holder in a transaction exempt under 517.061 of the Florida Securities Act. The Units have not been registered under said Act in the State of Florida.

In addition, all Florida residents shall have the privilege of voiding the purchase within three (3) days after the first tender of consideration is made by such purchaser to the issuer, an agent of the issuer, or an escrow agent or within 3 days after the availability of that privilege is communicated to such purchaser, whichever occurs later. Prospective purchasers are hereby notified of such privilege.

For Georgia Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or Section 10-5-5 of the Georgia Securities Act of 1973 and are being sold in reliance upon exemptions therefrom. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Hawaii Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Hawaii Uniform Securities Act (modified), by reason of specific exemptions thereunder relating to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Idaho Residents

The Joint Venture Units referred to herein have not been registered under the Idaho Securities Act (the "act") and may be transferred or resold by residents of Idaho only if registered pursuant to the provisions of the Act or if an exemption from registration is available.

For Illinois Residents

The Joint Venture Units referred to herein have not been approved or disapproved by the secretary of state of Illinois or the State of Illinois, nor has the Secretary of State of Illinois or the State of Illinois passed upon the accuracy or adequacy of this Venture. Any representation to the contrary is a criminal offense.

For Indiana Residents

The Joint Venture Units referred to herein have not been registered under Section 3 of Chapter 23 the Indiana Blue Sky Law and are offered pursuant to an exemption pursuant to Section 23-2-1-2(b)(10) thereof. These Units may be transferred or resold only if subsequently registered or if an exemption from registration is available.

For Iowa Residents

The Joint Venture Units referred to herein have not been registered under the Iowa Uniform Securities Act (the "act") and are offered pursuant to a claim of exemption under Section 502.203(9) of the Act. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Kansas Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under the Kansas Securities Act. A registration statement relating to these Joint Venture Units has not been filed with the Kansas Securities Commission. Therefore, these Units Cannot be resold or otherwise transferred unless they are registered under applicable securities laws or an exemption from registration is available.

For Kentucky Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under the Kentucky Securities Act. The Kentucky Securities Administrator neither recommends nor endorses the purchase of any venture, nor has the administrator passed upon the accuracy or adequacy of the information provided herein. Any representation to the contrary is a criminal offense.

For Louisiana Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Louisiana Securities Law, by reason of specific exemptions thereunder due to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Maine Residents

The Joint Venture Units referred to herein are being sold pursuant to an exemption from registration with the bank superintendent of the State of Maine under Section 10502(2)(r) of Title 32 of the Maine Revised Statutes. These Joint Venture Units may be deemed restricted and as such the holder may not be able to resell these Joint Venture Units unless pursuant to registration under state or federal securities laws or unless an exemption under such laws exists.

For Maryland Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Maryland Securities Act, by reason of specific exemptions thereunder relating to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

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FOR MASSACHUSETTS RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933.AS AMENDED, OR THE MASSACHUSETTS UNIFORM SECURITIES ACT, BY REASON OF SPECIFIC EXEMPTIONS HEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR MICHIGAN RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN MAY BE SOLD TO AND/OR ACQUIRED BY THE HOLDER IN A TRANSACTION EXEMPT UNDER THE MICHIGAN UNIFORM SECURITIES ACT, SECTION 451.802(B) (21). THE UNITS CANNOT BE SOLD OR TRANSFERRED EXCEPT IN A TRANSACTION WHICH IS EXEMPT UNDER SUCH ACT OR PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER SUCH ACT. THE MICHIGAN SECURITIES ACT PROVIDES THAT THIS MEMORANDUM MUST BE PROVIDED TO THE PROSPECTIVE PURCHASERS AT LEAST FORTY-EIGHT (48) HOURS PRIOR TO ANY SALE OF THE JOINT VENTURE UNITS OFFERED HEREIN.

FOR MINNESOTA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. THE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE REVISED MINNESOTA UNIFORM SECURITIES ACT (MUSA), EFFECTIVE AUGUST 2007, BY REASON OF SPECIFIC EXEMPTIONS HEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR MISSISSIPPI RESIDENTS

THE SECRETARY OF STATE DOES NOT RECOMMEND OR ENDORSE THE PURCHASE OF ANY JOINT VENTURE UNITS REFERRED TO HEREIN, NOR DOES THE SECRETARY OF STATE PASS UPON THE TRUTH, MERITS, OR COMPLETENESS OF ANY VENTURE MEMORANDUM FILED WITH THE SECRETARY OF STATE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THE JOINT VENTURE UNITS REFERRED TO HEREIN ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE.

FOR MISSOURI RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN WILL NOT KNOWINGLY BE SOLD TO RESIDENTS OF MISSOURI. THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY.

FOR MONTANA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT 1933, AS AMENDED, OR THE SECURITIES ACT OF MONTANA, BY REASON OF SPECIFIC EXEMPTIONS HEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR NEBRASKA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE SECURITIES ACT OF NEBRASKA, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR NEVADA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE NEVADA SECURITIES ACT, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR NEW HAMPSHIRE RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE NEW HAMPSHIRE UNIFORM SECURITIES ACT, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR NEW JERSEY RESIDENTS

THE ATTORNEY GENERAL OF THE STATE OF NEW JERSEY HAS NOT PASSED ON OR ENDORSED THE MERITS OF THIS VENTURE. THE FILING OF THE VENTURE REFERRED TO HEREIN WITH THE BUREAU OF SECURITIES DOES NOT CONSTITUTE APPROVAL OF THE ISSUE OF THE SALE THEREOF BY THE BUREAU OF SECURITIES OR THE DEPARTMENT OF LAW AND PUBLIC SAFETY OF THE STATE OF NEW JERSEY, AND REPRESENTATION TO THE CONTRARY IS UNLAWFUL.

FOR NEW MEXICO RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES BUREAU OF THE NEW MEXICO DEPARTMENT OF REGULATION AND LICENSING, NOR HAS THE SECURITIES BUREAU PASSED UPON THE ACCURACY OR ADEQUACY OF THIS VENTURE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

FOR NEW YORK RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN FILED WITH OR REVIEWED BY THE ATTORNEY GENERAL OF THE STATE OF NEW YORK PRIOR TO ITS ISSUANCE AND USE. NEITHER THE ATTORNEY GENERAL NOR THE STATE OF NEW YORK, NOR ANY

OTHER AGENCY, HAS PASSED ON OR ENDORSED THE MERITS OF THIS VENTURE. ANY REPRESENTATION(S) TO THE CONTRARY ARE UNLAWFUL.

FOR NORTH CAROLINA RESIDENTS

THESE JOINT VENTURE UNITS ARE OFFERED PURSUANT TO A CLAIM OF EXEMPTION UNDER THE NORTH CAROLINA SECURITIES ACT. THE NORTH CAROLINA SECURITIES ADMINISTRATOR NEITHER RECOMMENDS NOR ENDORSES THE PURCHASE OF ANY VENTURE.

THESE JOINT VENTURE UNITS ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND THE APPLICABLE STATE SECURITIES LAWS PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM.

FOR NORTH DAKOTA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY.

FOR OHIO RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE OHIO SECURITIES ACT, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR OKLAHOMA RESIDENTS

THE JOINT VENTURE UNITS REPRESENTED BY THIS DOCUMENT HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933 OR THE OKLAHOMA SECURITIES ACT. THESE JOINT VENTURE UNITS HAVE BEEN ACQUIRED FOR INVESTMENT AND MAY NOT BE RESOLD OR TRANSFERRED FOR VALUE IN THE ABSENCE OF AN EFFECTIVE REGISTRATION OF THEM UNDER THE SECURITIES ACT OF 1933 AND/OR THE OKLAHOMA SECURITIES ACT OR AN OPINION OF COUNSEL SATISFACTORY TO THE ISSUER THAT SUCH REGISTRATION IS NOT REQUIRED UNDER SUCH ACT OR ACTS.

FOR OREGON RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS VENTURE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THE JOINT VENTURE UNITS REFERRED TO HEREIN ARE SUBJECT TO RESTRICTION OF TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE SECURITIES ACT OF 1933, AS AMENDED AND IF APPLICABLE, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM.

FOR PENNSYLVANIA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN WILL NOT KNOWINGLY BE SOLD TO RESIDENTS OF PENNSYLVANIA. THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS VENTURE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

FOR RHODE ISLAND RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE BLUE SKY LAWS OF RHODE ISLAND, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE JOINT VENTURE UNITS CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR SOUTH CAROLINA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS VENTURE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THESE JOINT VENTURE UNITS ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE SECURITIES ACT OF 1933, AS AMENDED AND THE APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM.

FOR SOUTH DAKOTA RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY.

FOR TENNESSEE RESIDENTS

THE JOINT VENTURE UNITS REFERRED TO HEREIN HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE TENNESSEE SECURITIES ACT OF 1980, BY REASON OF SPECIFIC EXEMPTIONS HEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE SECURITIES CANNOT BE SOLD, TRANSFERRED, OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS THEY ARE SUBSEQUENTLY REGISTERED OR AN EXEMPTION FROM REGISTRATION IS AVAILABLE.

FOR TEXAS RESIDENTS

THESE JOINT VENTURE UNITS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE TEXAS SECURITIES ACT, BY REASON OF SPECIFIC EXEMPTIONS THEREUNDER RELATING TO THE LIMITED AVAILABILITY OF THE VENTURE. THESE UNITS CANNOT BE SOLD, TRANSFERRED OR OTHERWISE DISPOSED OF TO ANY PERSON OR ENTITY UNLESS SUBSEQUENTLY REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE TEXAS SECURITIES ACT, IF SUCH REGISTRATION IS REQUIRED.

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For Utah Residents

The Joint Venture Units referred to herein have not been registered under the Utah Uniform Securities Act. The Joint Venture Units sold pursuant to this memorandum cannot be resold unless they are registered under the Utah Uniform Securities Act or unless an exemption from registration is available. These Joint Venture Units are subject to substantial restrictions on transferability and resale as described in the Joint Venture Agreement.

For Vermont Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Vermont Securities Act, by reason of specific exemptions hereunder relating to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Virginia Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Virginia Securities Act, by reason of specific exemptions hereunder relating to the limited availability of the Venture. These Joint Venture Units cannot be sold, transferred, or otherwise disposed of to any person or entity unless they are subsequently registered or an exemption from registration is available.

For Washington Residents

The Joint Venture Units referred to herein have not been registered under the Securities Act of 1933, as amended, or the Securities Act of Washington, Chapter 21.20 RCW. These Joint Venture Units cannot be resold unless they are registered under the Securities Act Of Washington, Chapter 21.20 RCW, or unless an exemption from registration is available.

For West Virginia Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under the Uniform Securities Act. A registration statement relating to these Joint Venture Units has not been filed with the West Virginia Securities Commissioner.

For Wisconsin Residents

The Joint Venture Units referred to herein have not been recommended by any federal or state securities commission or regulatory authority.

For Wyoming Residents

The Joint Venture Units referred to herein are offered pursuant to a claim of exemption under the Wyoming Securities Act. A registration statement relating to these Joint Venture Units has not been filed with the Wyoming Securities Commission. Therefore, these Joint Venture Units cannot be resold or otherwise transferred unless they are registered under applicable securities laws exemption from registration is available.

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Forward – Looking Statements (Safe-Harbor Provisions)

This Confidential Private Placement Memorandum includes forward-looking statements within the meaning of Section 27a of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements give our current expectations or forecasts of future events. These statements might include projections and estimates concerning the timing and success of specific projects and future efforts. The statements contained in all parts of this document, including, but not limited to, those relating to our schedule, targets, estimates, or results of future drilling, including the number, timing, and results of wells, budgeted wells, increases in wells, the timing and risk involved in drilling follow-up wells, expected working or net revenue interests, planned expenditures, prospects budgeted and other future capital expenditures, risk profile of natural gas and oil exploration, acquisition of 2-D and 3-D seismic data and other exploration data (including number, timing and size of projects), planned evaluation of leases, minerals or prospects, probability of prospects having natural gas and oil, expected or estimated daily or periodic production rates, cumulative production volumes, or proved producible reserves, proved developed or undeveloped reserves, increases in reserves, items of income and expense including, without limitation, lease operating expenses, production taxes, ad valorem taxation, abandonment costs, general and administrative costs, catastrophic overhead costs, acreage, working capital requirements, hedging activities, the ability of expected sources of liquidity to implement our business strategy, future exploration activity, production rates, financing for a current or any future exploration or development program or joint venture, growth in production, development of new drilling programs, participation of our industry partners, funding for any particular proposed operations, hedging of production and exploration and development expenditures, and any and all other statements regarding future operations, financial results, business plans, and cash needs and other statements that are not historical facts are forward-looking statements.

In accordance with the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995, the Company notes that statements contained herein, that look forward in time, which include everything other than historical information and which express or involve discussions with respect to expectations, beliefs, plans, projections, assumptions, goals, objectives, or future events or performance that are not historical fact, all of which involve risks and uncertainties, always including, but not limited to significant market price volatility, and which may affect the Company's actual results of operations are considered forward looking statements.

When used in this document, the following words in any form "anticipate," "expect," "objective," "budgeted," "planned," "targeted," "potential," "goal," "estimate," "project," "predict," "forecast," "pursue," "continue," "believe," "may," "should," "will," "intend," or similar terms; or by statements indicating certain actions that may, could, or might, occur, including references to assumptions indicate forward looking statements. Such statements involve risks and uncertainties, including but not limited to, those relating to economic downturn and credit crisis, our dependence on exploratory drilling activities, the volatility of oil and gas sales prices, the need to replace reserves depleted by production, operating risks of natural gas and oil operations, our dependence on our key personnel, factors that affect our ability to manage our growth and achieve our business strategy, technological changes, our significant capital requirements, the potential impact of government regulations, adverse regulatory determinations, litigation, competition, the uncertainty of reserve information and future net revenue estimates, property acquisition risks, availability of rigs and other equipment, access to pipelines and gathering systems, adverse weather conditions, availability of financing, financial condition of our industry partners and the counterparties to our hedges and business contracts, ability to obtain permits and other factors detailed herein and as updated and amended. Some factors that could cause actual results to differ from those expressed or implied in forward-looking statements are described herein under the headings of "Risk Factors," "General Risks of Oil and Gas Ventures," and "Specific Risks of the Joint Venture," and in other sections of this document. Other factors that could cause actual results to differ include the loss of or mechanical failure of the wellbore(s) or drilling operations, uncontrolled blowout from the well, catastrophic fire, a casualty loss, litigation for damages, the size and encountering granite or other impenetrable substance during drilling operations, the size and growth of the market for the company's products, lack of a market for produced products, pricing pressures, market volatility, the effect of competition, the company's ability to fund its capital requirements in the near term and in the long term, etc. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual outcomes may vary materially and significantly from those indicated.

Our forward looking statements are based on assumptions and analyses made by us in light of our experience and our perception of historical trends, current conditions, expected future developments, and other factors that we believe are appropriate under the circumstances. Although we believe the expectations and forecasts reflected in these and other forward-looking statements are reliable and reasonable, we can give no assurance that they will prove to have been correct or accurate. Investing in oil and gas private placements, forestry partnerships, natural resources, farmland and other real estate, stocks, bonds, other securities and similar investments is speculative and carries risk(s) that cannot be completely eliminated. They can be affected by inaccurate assumptions and/or by the aforementioned known and unknown risks and uncertainties. Any investment should be made only after consulting with a trusted investment advisor and only after reviewing the private placement memorandum and related venture materials and conducting a thorough due diligence effort. Be advised that the purchase of Units of Interest, in this or any joint venture or partnership is a high risk investment and may result in the loss of your entire investment or a significant portion thereof.

All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by reference to these risks and uncertainties. You should not place undue reliance on forward-looking statements. Each forward-looking statement speaks only as of the date of the particular statement and are subject to change without notice and we (the company) undertake(s) no obligation to update or revise any forward-looking statement. New risks and uncertainties arise from time to time, and it is impossible to predict these events and how they may affect the company or its joint ventures. We urge you to carefully review and consider the disclosures made in this document and other reports and filings connected with this document.

In addition, any projections and representations, written or oral that do not conform to this Confidential Memorandum, shall have no force or effect and must be disregarded and not relied upon. No representation or warranty can be given that the estimates, opinions or assumptions made in or referenced by this Confidential Private Placement Memorandum will prove to be accurate. Prospective Participants should carefully review the assumptions set forth in or referenced by this private placement memorandum.

There is no such thing as "no risk". Past performance does not guarantee future results.

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Risk Factors

PARTICIPATION IN THE VENTURE INVOLVES A HIGH DEGREE OF FINANCIAL RISK.

THE BUSINESS ACTIVITIES OF SIGNAL OIL LLC. (SIGNAL OIL LLC.) AND THE PROPERTY(IES) WE DEVELOP AND MANAGE ARE SUBJECT TO SIGNIFICANT HAZARDS AND RISKS, INCLUDING THOSE DESCRIBED BELOW. IF ANY SUCH EVENTS SHOULD OCCUR, OUR JOINT VENTURE(S), OUR BUSINESS, FINANCIAL CONDITION, LIQUIDITY AND/OR RESULTS OF OPERATIONS COULD BE MATERIALLY HARMED, AND HOLDERS OF JOINT VENTURE INTERESTS COULD ALSO BE HARMED ON ACCOUNT OF LOSS OF VALUE TO VENTURE PROPERTY(IES) AND PROBLEMS WITH ONGOING OPERATIONS. HOLDERS OF JOINT VENTURE INTERESTS COULD LOSE ALL OR PART OF THEIR INVESTMENTS, THEORETICALLY.

UNITS OF INTEREST (PARTICIPATION) SHOULD BE PURCHASED ONLY BY PERSONS WHO CAN AFFORD TO SUSTAIN THE LOSS OF THEIR ENTIRE INVESTMENT AND HAVE NO NEED FOR LIQUIDITY FROM SUCH INVESTMENT. IN EVALUATING AN INVESTMENT IN THE COMPANY AND ITS BUSINESS PRIOR TO PURCHASE, PROSPECTIVE INVESTORS SHOULD CAREFULLY CONSIDER THE FOLLOWING RISK FACTORS RELATING TO THE BUSINESS OF THE COMPANY AND THE VENTURE, TOGETHER WITH THE INFORMATION AND FINANCIAL DATA SET FORTH IN THIS MEMORANDUM.

RISK DISCUSSION

Risk can be defined as uncertainty; the uncertainty that the actual return on an investment will be different from its expected return or of not knowing what's going to happen to your investment. Risk is measured in a variety of ways, the most common of which are standard deviation or Beta. These measurements show how much variation there is on an investment's return.

The return on an investment should compensate for the level of risk undertaken. On average, riskier investments can be expected to have higher returns and less risky investments have lower returns. Therefore, if you desire lower risk, you must accept lower returns and if you want higher returns, you should be prepared to accept more risk.

Oil and gas drilling, development, and production involves a variety of significant risks and is marked by unprofitable efforts, not only from dry holes, but from wells which, though productive, do not produce oil and gas in sufficient quantities to return any profit or a reasonably expected profit on the amounts expended. The selection of leases, drill sites and the drilling of wells are not exact sciences, and the results of such drilling cannot be predicted. In fact, the ratio of productive oil and gas wells overall has been low when compared to the total number of wells drilled. Even though a well is drilled in an area adjacent to known and existing production, there is no assurance that such drilling will locate the oil and/or gas sands or that such sands, if located, will have the attributes necessary for commercial production sufficient to recoup the capital expended in placing such a well in production. A well may also be ruined or rendered dry or noncommercial during either drilling or completion due to technical or mechanical difficulties. Should a well be successfully drilled to the required depth, and tests thereafter indicate hydrocarbon bearing formations with sufficient porosity and permeability to warrant completion, there is still no assurance the production will be obtained or that any well or all sums expended thereon will be recouped through production. The extent and value of a well, any underlying reservoir of oil or gas, and the amount and rate of future production cannot be determined with reasonable accuracy unless and until the well has a history of continuous production over a period of time sufficient to provide a reservoir engineer with data upon which an evaluation may be reasonably based.

The initial potential (IP) of a well, as determined by a test that is run following completion, will not always be determinative of actual production. Generally, initial production of oil wells is closer to initial potential on the basis of the tests that are run. In the case of gas wells, ultimate production rates can be as low as 10% to 25% of the initial potential numbers.

GENERAL INVESTMENT RISKS

1. Market Risk. Market risk is the risk of the general or entire market declining and causing your ownership position to lose value. Although, all investments are exposed to market risk, it primarily affects common stocks and financial instruments. The energy markets are typically volatile and can rapidly decline or increase on a daily basis. As well, the daily market price of produced crude oil and natural gas fluctuates on a daily basis and in a wide range.
2. Speculative Risk. Speculative risk takes many forms. It can include the risk of an individual firm or individual industry and their ability to make money and pay their debts. Companies in their growth or decline stages of the business cycle are sometimes referred to as being speculative. Speculative risk involves the probability of a company suffering losses or profits less than expected for a given period because of adverse circumstances in that particular company's industry. Risk can also be caused by such factors as worldwide recession, governmental and regulatory administration and policy, inflation, poor management planning, trade restrictions, or possible hostile relationships with a foreign country where a majority of the company's goods are marketed.
3. Interest Rate Risk. Interest rate risk is the change in investment value caused by the change in current interest rates. This is a major risk affecting all fixed income investors. While this should not directly affect Participants in this specific Venture, it may affect their income from other investments and damage their ability to tolerate the risks or any potential losses attendant with this specific Joint Venture.
4. Leverage Risk. Leverage risk involves losing all or part of an original investment when the original investment was made using borrowed money which, even after its loss, must then be paid back. This can lead to a situation where the investor can lose more than the entire investment by losing the entire investment and then having to pay back the borrowed money without any investment gains or principal coming to hand. Leveraging investments in oil and gas drilling Joint Ventures is not advisable, and Participants herein will represent that they are not investing borrowed funds.
5. Inflation Risk. Inflation risk, also called general economic risk or purchasing power risk, is the risk that the return realized on an investment will not be sufficient to offset the loss of purchasing power due to inflation. Oil and gas market prices have outpaced inflation significantly and, indeed, are an important reason for making the investment. Oil is priced worldwide in U.S. dollars, making ownership of oil a hedge against inflation.

6. Manager Risk. Joint Ventures, by their nature, are designed for a specific business purpose and are, therefore, typically actively managed. Manager risk is the danger that the manager will make poor choices that lead to losses or subpar returns for the Participants. Given that the Participants in this Joint Venture are empowered to conduct the business of the Venture and to make decisions for the Venture, and that the initial plan and business of the Joint Venture is clearly indicated, manager risk is ameliorated.

GENERAL RISKS OF OIL AND GAS VENTURES

7. Risks Inherent in Oil and Gas Exploration. Oil and gas development involves a high degree of risk, and is frequently marked by unprofitable efforts, not only from dry holes, but from wells which, though productive, do not produce oil and gas in sufficient quantities to return a profit on the amounts expended. The results of any well cannot be determined in advance. The selection of leases and drill sites and the drilling of wells are not exact sciences and the results of such drilling cannot be accurately predicted. In fact, the ratio of productive oil and gas wells has been low when compared to the total number of wells drilled. Even though a well may be drilled in an area adjacent to known and existing production, there is no assurance that such drilling will locate the oil and/or gas sands or formations or that such sands or formations, if located, will have the attributes necessary for commercial production sufficient to recoup the capital expended in placing such well in production. A well may also be ruined or rendered dry or noncommercial during either drilling or completion due to technical or mechanical difficulties. Should a well be successfully drilled to the required depth, and tests thereafter indicate the hydro-carbon bearing formations with sufficient porosity and permeability to warrant completion, there is still no assurance that production will be obtained or that any or all sums expended thereon will be recouped through production. The extent and value of a well, any underlying reservoir of oil or gas, and the amount and rate of future production cannot be determined with reasonable accuracy unless and until the well has a history of continuous production over a period of time sufficient to provide a reservoir engineer with data upon which an evaluation may be reasonably based.

8. Curtailment, Delay or Cancellation of Drilling Activities. The costs of drilling, completing and operating wells are often uncertain, and the drilling operations may be curtailed, delayed or canceled as a result of a variety of factors including, but not limited to:

   - delays in obtaining regulatory approvals and drilling permits;
   - unexpected drilling conditions;
   - pressure or irregularities in formations;
   - equipment failures or accidents;
   - fires, explosions, blowouts and surface cratering;
   - marine risks such as capsizing, collisions, and hurricanes;
   - other adverse weather conditions;
   - shortages and delays in the delivery of equipment;
   - shortages or the inability to contract rigs and suppliers needed for operations;
   - increases in the costs of drilling rigs and crews, fracture stimulation crews and equipment, chemicals and supplies;
   - lack of qualified personnel to conduct day to day operations; and
   - title problems.

   Certain future drilling activities may not be successful and, if unsuccessful, this failure could have an adverse effect on our future results of operations and financial condition. Holders of Joint Venture Interest receive no return on their investment when drilling activities are not productive, and Venturers can lose their entire investment. While all drilling, whether developmental or exploratory, involves these risks, exploratory drilling involves greater risks of dry holes or failure to find commercial quantities of hydrocarbons.

9. Prevailing Prices. The prevailing prices of oil and natural gas affect the cost of and the demand for drilling rigs, production equipment and related services. However, changes in costs may not occur simultaneously with corresponding changes in prices. The availability of drilling rigs can vary significantly from region to region at any particular time. Although land drilling rigs can be moved from one region to another in response to changes in levels of demand, an undersupply of rigs in any region may result in drilling delays and higher drilling costs for the rigs that are available in that region. In addition, any economic and financial crisis can adversely affect the financial condition of drilling contractors, which may constrain the availability of drilling services in some areas.

10. Regulatory Approval and Drilling Permits. Another significant risk inherent in drilling plans is the need to obtain drilling permits from local, state, federal and other governmental authorities, as appropriate. Delays in obtaining regulatory approvals and drilling permits, including delays which jeopardize our ability to realize the potential benefits from leased properties within the applicable lease periods, the failure to obtain a drilling permit for a well, or the receipt of a permit with unreasonable conditions or costs could have materially adverse effect on our ability to explore on or develop our properties.

11. Unconventional Shale Plays. Drilling results in various unconventional shale plays, such as Bone Springs, Wolfcamp, Cline, Strawn, Woodford, Niobrara, Mancos, Eagle Ford, Utica, Marcellus, Chainman, and Tuscaloosa, may be more uncertain than in unconventional shale plays that are more developed and have longer expected production histories. For example, our experience with horizontal drilling in these shales, as well as the industry's drilling and production history, is more limited than in other plays and in exploration and development of conventional oil and gas resources. Drilling and completion techniques that have proven to be successful in certain unconventional (shale plays) and conventional plays to maximize recoveries are being used in the early development of new plays; however, we can provide no assurance of the ultimate success of these drilling and completion techniques.

12. Drilling Location Inventories for Multi-Year Programs. In addition, a significant part of our strategy involves increasing our drilling location inventories for multi-year programs scheduled out over several years. Such multi-year drilling inventories can be more susceptible to long-term horizon uncertainties that could materially alter the occurrence or timing of actual drilling. Because of these uncertainties, we do not know if the potential drilling locations will ever be drilled, or if we will be able to produce oil or natural gas from these or any other potential drilling locations.

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13. Volatile Oil and Natural Gas Prices. The volatility of oil and natural gas prices significantly affects cash flows to the Operator and the Joint Venture as well as capital resources and could hamper our ability to produce oil and gas economically. Oil and natural gas prices are volatile, and a decline in prices would adversely affect both the Operator and the Joint Venture's profitability and financial condition. The oil and gas industry has historically been cyclical, and prices for oil and natural gas have been highly volatile. Historically, the industry has experienced severe downturns characterized by oversupply and/or weak demand. While higher oil and natural gas prices have contributed to positive earnings over several years, long-term supply and demand for oil and natural gas is uncertain and subject to a myriad of factors such as:

    - the domestic and foreign supply of oil and gas;
    - the ability of the Organization of Petroleum Exporting Countries, (OPEC) to set and maintain oil production levels;
    - oil and gas production by non-OPEC countries;
    - the level of worldwide oil exploration and production activity;
    - the price and availability of alternative fuels;
    - weather conditions;
    - the demand for energy, which is affected by world population growth; economic development; and worldwide economic and business conditions;
    - pipeline, transportation, or refining capacity constraints in a regional or localized area may put downward pressure on the realized price for oil or natural gas;
    - the price of foreign imports;
    - the costs of exploring for, producing and delivering oil and gas;
    - political and economic uncertainty and socio-political unrest;
    - political conditions in oil and gas producing regions, including terrorism, provocative incidents, police action and war(s); and
    - domestic and foreign governmental regulations.

    Decreases in oil and natural gas prices from current levels could adversely affect revenues, net income, cash flow, and proved reserves. Significant price decreases could have a material adverse effect on our operations and limit our ability to fund capital expenditures. Without the ability to fund capital expenditures, we would be unable to replace reserves and production.

14. Operating and Environmental Risks and Hazards. Oil and natural gas operations are subject to many risks, including well blowouts, craterings, explosions, uncontrollable flows of oil, natural gas, or well fluids, fires, adverse weather such as hurricanes in the Gulf Coast region, tornadoes, freezing conditions, formations with abnormal pressures, pipeline ruptures or spills, pollution, releases of toxic gas, and other environmental risks and hazards. If any of these types of events occurs, we could sustain substantial losses.

    We typically maintain insurance against some, but not all, of these potential risks and losses. We have significant but limited coverage for sudden environmental damages. We do not believe that insurance coverage for the full potential liability that could be caused by sudden environmental damages or insurance coverage for environmental damage that occurs over time is available at a reasonable cost. In addition, pollution and environmental risks generally are not fully insurable. Further, we may elect not to obtain other insurance coverage under circumstances where we believe that the cost of available insurance is excessive relative to the risks presented. Accordingly, we may be subject to liability or may lose substantial portions of certain properties in the event of environmental or other damages. If a significant accident or other event occurs and is not fully covered by insurance, we could suffer a material loss, which could affect sponsored Joint Ventures thereon.

    Following the severe Atlantic hurricanes in 2004, 2005, and 2008, the insurance markets suffered significant losses. As a result, insurance coverage has become substantially more expensive and future availability and costs of coverage are uncertain.

15. Environmental Concerns and Pollution. Various local, state and federal environmental control agencies may impose regulations that could have a significant impact on the operation of the Venture or could substantially increase the costs of operating a well. A spill, fire, or other uncontained release of dangerous or polluting chemicals, including hydrocarbons, could cause an uninsured or inadequately insured loss to the Joint Venture. The Joint Venture should benefit from insurance coverage held by the Operator and contractors and vendors to the Joint Venture operations.

16. Severe Weather Conditions. Joint Venture operations may be materially affected by severe weather conditions in areas where we operate. This may entail the evacuation of personnel and stoppage of operations and services. If there is damage to rigs or other structures, this may cause a suspension of activities until repairs are made. The time frame for such circumstances cannot be predetermined and may be substantial. Any of these events may have a material adverse effect on the Venture's, Operator's or Managing Joint Venturer's financial capacity and standing or ability to continue or to make progress. Such events will likely have a materially adverse effect on operating revenue for all parties concerned.

17. Regulations Regarding Hydraulic Fracturing. Several proposals are before the U.S. Congress that, if implemented, would either prohibit or restrict the practice of hydraulic fracturing or subject the process to regulation under the Safe Drinking Water Act. Several states are considering legislation to regulate hydraulic fracturing practices that could impose more stringent permitting, transparency, and well construction requirements on hydraulic-fracturing operations or otherwise seek to ban fracturing activities altogether. In addition, some municipalities have significantly limited or prohibited drilling activities and/or hydraulic fracturing, or are considering doing so. The Company routinely uses fracturing techniques in the U.S. and other regions to expand the available space for natural gas and oil to migrate toward the wellbore. It is typically done at substantial depths in very tight formations.

    Although it is not possible at this time to predict the final outcome of the legislation regarding hydraulic fracturing, any new federal, state, or local restrictions on hydraulic fracturing that may be imposed in areas in which we conduct business could result in increased compliance costs or additional operating restrictions in the U.S. Such restrictions could render certain drilling prospects and leases uneconomic, and a sponsored Joint Venture may lose value and potential income as a result.

18. Achieving and Managing Future Growth. The Company has experienced growth in the past primarily through the expansion of our drilling program. Future growth may place strains on our financial, technical, operational and administrative resources

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and cause us to rely more on project partners and independent contractors, possibly negatively affecting our financial condition and the results of operations. The Company's ability to grow will depend on a number of factors including our ability to:

- obtain leases and/or options on properties, including those for which we have geological and geophysical data;
- acquire additional exploration, geological, geophysical, petrophysical and related data;
- identify and acquire new exploratory or developmental prospects;
- develop existing prospects;
- continue to attract and retain skilled personnel; and
- to maintain or enter into new relationships with project partners and independent contractors;

In addition, the Company's ability to grow will depend on the following:

- the results of our company sponsored Joint Ventures and our company drilling efforts;
- hydrocarbon (crude oil and natural gas) and other production (i.e. Helium) prices; and
- our access to capital.

The Company may not be successful in upgrading our technical, operations and administrative resources or in increasing our ability to internally provide certain of the services currently provided by outside sources, and we may not be able to maintain or enter into new relationships with project partners and independent contractors. The company's inability to manage growth may adversely affect our financial condition and the results of our operations may be negatively affected which, in turn, could adversely affect the revenues and returns to our Joint Venture Participants.

19. Ability of Suppliers to Meet Demand for Field Services and Equipment. During periods of high demand, particularly when oil and natural gas prices are relatively high, well service providers and related equipment and personnel may be in short supply. These shortages can cause escalating prices, delays in drilling and other exploration activities and the possibility of poor quality service performance coupled with potential damage to downhole reservoirs, well bores and equipment as well as personnel injuries. Such pressures may increase the actual cost of services, extend the time to secure such services and add costs for damages due to accidents sustained from improper use or overuse of equipment and inexperienced personnel.

20. Proposed Drilling Schedule. The company's final determination of whether to drill any scheduled or budgeted wells will be dependent on a number of factors, including:

- the results of our exploration efforts and the acquisition, processing, analysis, and review of a variety of exploration data, including:
  - satellite imagery; airborne data acquisition including hyperspectral imaging;
  - gravity, magnetic, magneto-telluric, radar, radiometric, surface and subsurface sourced geochemistry;
  - two (2D) and three (3D) dimensional seismic, geomorphic mapping and subsurface mapping;
  - petrophysical data and analysis; and
  - other forms of exploration information and techniques;
- the availability of sufficient capital resources to the other Participants and the Company for the drilling of the prospects;
- the approval of the prospects by the other Participants after additional data has been compiled;
- economic and industry conditions at the time of drilling, including prevailing and anticipated prices for oil, natural gas and helium
- the availability of leases and timely drilling permits on reasonable terms for the prospects.

Although the Company has identified and budgeted for numerous drilling prospects, we may not be able to acquire leases or drill those prospects within our expected time frame or at all. Wells that are currently part of our capital budget may be based on statistical results of drilling activities in other project areas that we believe are geologically similar rather than on analysis of seismic or other exploration data in the prospect area, in which case actual drilling and results are likely to vary, possibly materially, from those statistical results. In addition, our drilling schedule may vary from our expectations because of future uncertainties.

21. Catastrophic Events. The company's oil and gas operations are subject to unforeseen occurrences that have affected us from time to time and that may damage or destroy assets, interrupt operations and have other significant adverse effects. Examples of catastrophic risks include lightning, hurricanes, fires, explosions, and blowouts (uncontrolled flows from a wellbore). Although we intend to maintain insurance coverage against property and casualty losses, there can be no assurance that such insurance will adequately protect the company or its Joint Venture Participants against liability from all potential consequences and damages, whether naturally occurring or manmade. Moreover, some forms of insurance may be unavailable in the future or be available only on terms that are deemed economically unacceptable.

22. International Operations. The scope and extent of any exploration efforts or other operations of the Company outside of the U.S. means we may become exposed to the risks inherent in doing business abroad. These risks include the following:

- currency exchange rate fluctuations, devaluations, and restrictions on currency repatriation;
- unfavorable taxes, tax increases, and retroactive tax claims;
- the disruption of operations from labor and political disturbances;
- insurrection, war, or acts of terrorism that may disrupt or limit markets;
- expropriation or seizure of our property;
- nullification, modification, or renegotiation of existing contracts;
- corruption and crime from a variety of sources;
- regional economic downturns;
- import/export quotas and other forms of public and governmental regulation; and
- inability to obtain or retain licenses required for operations.

We cannot predict the nature of foreign governmental regulations applicable to our operations that may be enacted in the future. In many cases, our direct or indirect customer will be a foreign government, which can increase our exposure to these risks. These and other factors could have a material adverse effect on our financial condition, results of operation, and cash flows.

23. Use of Initial Potential Figures in Geological Reports and Maps. The initial potential of a well, as determined by a test that is run following completion, will not always be determinative of actual production and should not be considered indicative of the amount of oil and gas a well can be expected to produce on a sustained basis. Generally, initial production of oil wells is closer to initial potential determined on the basis of the tests that are run. In the case of gas wells, ultimate production rates can be as low as 10% to 25% of the initial potential figures. Prospective Participants, when viewing initial potential figures as an indication of the extent to which a well may actually produce or has produced, should keep in mind that actual production is generally less than the initial potential figures reported to the state agencies regulating oil and gas production in their jurisdictions.

24. Regulation and Marketability of Gas or Oil Discovered. The availability of a ready market for oil or gas, if any, discovered on the Prospect and the price obtained therefor will depend upon numerous factors, including:

    - the extent of domestic production and foreign imports of gas and/or oil;
    - the proximity and capacity of pipelines, intrastate and interstate market demands;
    - the extent and effect of federal regulations on the sale of oil and/or natural gas in interstate and intrastate commerce; and
    - other government regulations affecting the production and transportation of oil and/or gas.

    In addition, certain daily allowable production constraints may change from time to time, the effect of which cannot be predicted by management. Both natural gas and oil production can be curtailed on account of regulation, effects of competition, lack of pipeline capacity or refinery and storage capacity matters. There is no assurance that the Venture will be able to market any oil or gas found by it at favorable prices, if at all. See "Competition, Markets and Regulation."

25. Delay in Distributions of Income. Unavailability of or delay in connection with pipelines or other transportation systems, unavailability of or delay in obtaining necessary materials for completion of a well, repayment of loans (if any) obtained by the Venture to finance drilling or other activities, delays in obtaining satisfactory contracts and connections for oil and/or gas wells, delays in obtaining assignments, delays in obtaining division orders and other circumstances may delay the distribution of income, if any, for significant periods after discovery of oil and gas, if any.

26. New Technology. New technology may cause our current exploration and drilling methods to become obsolete. The oil and gas industry is subject to rapid and significant advancements in technology, including the introduction of new products and services using new technologies. As competitors use or develop new technologies, we may be placed at a competitive disadvantage, and competitive pressures may force us to implement new technologies at a substantial cost. In addition, competitors may have greater financial, technical, and personnel resources that allow them to enjoy technological advantages and may in the future allow them to implement new technologies before we can. We cannot be certain that we will be able to implement new technologies on a timely basis or at a cost that is acceptable to us or our Joint Venture structure. If we are not able to maintain technological advancements consistent with industry standards, our operations and financial condition may be adversely affected.

27. Possible Shortages and Reduced Availability of Equipment and Materials. Under some conditions, well service providers and related equipment and personnel can be in short supply. This can cause escalating prices, the possibility of poorly rendered services coupled with potential damage to downhole reservoirs and personnel injuries. Such pressures can increase the actual cost of services, extend the time to secure such services and add costs for damages due to accidents sustained from the overuse of equipment and inexperienced personnel.

28. Competition in the Oil and Gas Industry. We face intense competition from major oil companies, independent oil and natural gas exploration and production companies, financial buyers, and institutional and individual investors who seek oil and natural gas property investments throughout the world, as well as the equipment, expertise, labor, and materials required to operate oil and natural gas properties.

29. Competition the Oil and Gas Exploration and Production Industry. We compete with major integrated and other independent oil and gas companies; other joint ventures and individuals for the acquisition of oil and gas leases, properties and reserves; equipment and labor required to explore, develop and operate those properties; and the marketing of oil and natural gas production. Higher recent crude oil and natural gas prices have increased the costs of properties available for acquisitions, and there are a greater number of companies with the financial resources to pursue acquisition opportunities. We may not be successful in acquiring and developing profitable properties in the face of this competition.

30. Competitors Financial and Other Resources. Many of our competitors have financial and other resources substantially larger than those we possess or those available to this Joint Venture. They have established strategic long-term positions and maintain strong relationships in areas in which we may seek new entry. As a consequence, we may be at a competitive disadvantage in bidding for drilling rights or buying leaseholds to develop. In addition, our larger competitors may have a competitive advantage when responding to factors that affect demand for oil and natural gas production, such as changing worldwide prices and levels of production, the cost and availability of alternative fuels and the application of governmental regulations. We also compete for human resources, including geologists, geophysicists, engineers and other specialists. The need for talented people across all disciplines in the industry has grown while the number of people available has been constrained. Such an inferior competitive position could have a material adverse effect upon the productivity, marketability and profitability of the Venture. See "Competition, Markets and Regulation."

31. Information Gained from Development of Joint Venture Property. A great deal of information becomes public through required regulatory filings. Such information is frequently used by competitors and mineral owners who may acquire drill sites, mineral leases, etc. on nearby or offsetting tracts. Such tracts may be or become unavailable to the Joint Venture, or if available, at a much higher cost. Due to the limited financial capacity of the Managing Joint Venturer, the Operator, and the

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Joint Venture, and the ongoing obligations of each, it is unlikely that these offsetting effects can be prevented and may lead to loss of potential development and perhaps drainage of the Joint Venture property.

32. Drilling, Operational and Environmental Hazards. Hazards such as difficult to drill or impervious formations, lost circulation, unusual formation pressures, hydrogen sulfide (poisonous) gas or water flows, and other unforeseen conditions are sometimes encountered in drilling wells. Additionally, it is not unusual to encounter unexpected problems or conditions which necessitate the abandonment of the proposed Joint Venture's well(s). Sometimes, substantial uninsured liabilities to third parties or governmental agencies may be incurred, the payment of which would reduce the funds available for distribution to the Participants or result in the loss of the oil and gas properties. The Company expects to carry certain insurance, including comprehensive general liability, automobile liability insurance, worker's compensation insurance, well control or "blowout" insurance (including clean up and containment, above ground pollution liability, and cost to redrill) and care, custody and control endorsement.

33. Laws and Regulations Relating to Environmental Protection. International, federal, state and/or local laws and regulations may restrict the types, quantities and concentrations of various substances that can be released into the environment in connection with drilling and production activities. They may limit or prohibit drilling activities on specified lands within wilderness, wetlands and other protected areas; they may require remedial measures to mitigate pollution from former operations, such as pit closure and plugging abandoned wells; or they may impose substantial liabilities for pollution resulting from production and drilling operations. The failure to comply with these laws and regulations may result in the assessment of administrative, civil and criminal penalties, imposition of investigatory or remedial obligations or the issuance of injunctions prohibiting or limiting the extent of our operations. Public interest in the protection of the environment has increased dramatically in recent years. The trend of applying more expansive and stricter environmental legislation and regulations to the natural gas and oil industry could continue, resulting in increased costs of doing business and consequently affecting our profitability. To the extent laws are enacted or other governmental action is taken that restricts drilling or imposes more stringent and costly waste handling, disposal and cleanup requirements, our business and prospects could be adversely affected and our investment returns could be interrupted or reduced.

The Joint Venture's operations may generate waste that may be subject to federal Resource Conservation and Recovery Act ("RCRA") and comparable state statues. The U.S. Environmental Protection Agency (EPA) and various state agencies have limited the approved methods of disposal for certain hazardous and nonhazardous waste. Furthermore, certain waste generated by our natural gas and oil operations that are currently exempt from treatment as hazardous waste may in the future be designated as hazardous waste and therefore become subject to more rigorous and costly operating and disposal requirements.

The Managing Joint Venturer and/or the operating company currently owns or leases numerous properties that for many years have been used for the exploration and production of natural gas and oil. Although we believe that we have implemented appropriate operating and waste disposal practices, prior owners and operators of these properties may not have used similar practices, and hydrocarbons or other waste may have been disposed of or released on or under the properties we own or lease or on or under locations where such waste have been taken for disposal. In addition, many of these properties have been operated by third parties whose treatment and disposal or release of hydrocarbons or other waste was not under our control. These properties and the waste disposed thereon may be subject to the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), or RCRA and analogous state laws as well as state laws governing the management of natural gas and oil waste. Under these laws, we could be required to remove or remediate previously disposed waste (including waste disposed of or released by prior owners or operators) or property contamination (including groundwater contamination) or to perform remedial plugging operations to prevent future contamination.

CERCLA, also known as the Superfund law, and analogous state laws impose liability, without regard to fault or the legality of the original conduct, on specified classes of persons that are considered to have contributed to the release of a hazardous substance into the environment. These classes of persons include the owner or operator of the disposal site or sites where the release occurred and companies that disposed or arranged for the disposal of the hazardous substances found at the site. Persons who are or were responsible for releases of hazardous substances under CERCLA may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources and for the costs of certain health studies, and it is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by the hazardous substances released into the environment.

The Joint Venture's operations may be subject to the Clean Air Act (CAA) and comparable state and local requirements. In 1990, Congress adopted amendments to the CAA containing provisions that have resulted in the gradual imposition of certain pollution control requirement with respect to air emissions from our operations. The EPA and states have developed and continue to develop regulations to implement these requirements. We may be required to incur certain capital expenditures in the next several years for air pollution control equipment in connection with maintaining or obtaining operating permits and approvals addressing other air emission-related issues. However, we do not believe our operations will be materially adversely affected by any such requirements.

Our operations have been, and at times in the future may be, affected by political developments and by federal, state, provincial and local laws and regulations such as restrictions or stoppage of granting drilling permits, creating and mandating onerous additional requirements to satisfy authorities such as surface and subsurface water studies, wildlife impact studies, testing requirements prior to drilling, complicated and peculiar access restrictions, seasonal restrictions, required compliance and agreement with lawsuits filed between states or agencies, restrictions on production, changes in taxes, royalties and other amounts payable to governments or governmental agencies, price controls or environmental protections laws and regulations. Despite the constitution and various rulings, it is not unusual for some regulatory requirements to be applied retroactively.

Both federal and state authorities generally require that leaseholders have substantial net worth or post bonds or other acceptable assurances that their various requirements will be met. The cost of these bonds or other assurances can be substantial, and we may not be able to obtain bonds or other assurances in all cases. Under certain circumstances, federal or state authorities may require any of our operations on their leases to be suspended or terminated. Any such suspension or

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termination could have a material adverse effect on our operations and investment returns to the Joint Venture, if any, could be severely delayed, reduced or eliminated.

The operating company also is subject to a variety of federal, state, local and international permitting and registration requirements relating to protection of the environment. We believe we are in substantial compliance with current applicable environmental laws and regulations and that continued compliance with existing requirements will not have a material adverse effect on us.

34. Disputes with Vendors and Possible Liens. It is anticipated that the Operator will contract directly with various providers of goods and/or services necessary to conduct the operations of the Joint Venture. From time to time, disputes may arise between the Operator and certain vendors with whom it contracts for goods and services for a variety of reasons. For example, the Operator may dispute certain charges reflected on invoices tendered by a vendor, question the workmanlike manner in which the services were performed, or challenge the quality of the goods or equipment provided. When a dispute cannot be resolved amicably, a lawsuit may be filed to resolve the dispute. Vendors who have provided goods and /or rendered services to the Operator with respect to the prospect well(s) may be permitted, under applicable law, to file material and/or mechanic's liens with respect to the prospect well, the filing of which may be necessary in order to perfect a lien claim pending resolution of the dispute. Such a lien could permit a vendor, upon the exercise of judicial or administrative remedies, to suspend the disbursement of production proceeds, to seize the interests of Participants or to seize the prospect well and its associated equipment in order to secure or pay the amount of such claim. If a given lien is ultimately determined to be valid, it could ultimately permit the vendor to satisfy its claim out of production proceeds, the value of mineral leases or the value of the prospect well and associated equipment. Under such circumstances, the Venture, even though having paid the Operator, will be adversely affected.

35. Production Decline. Production from oil and/or gas wells, by its very nature, will decline over time. The actual decline curve of any well is subject to numerous factors and specific conditions that cannot, in normal circumstances, be calculated in advance.

36. Replacing Our Reserves. The company must make substantial capital expenditures to find, acquire, develop and produce oil and natural gas reserves. Future cash flows and the availability of financing are subject to a number of factors, such as the level of production from existing wells, prices received for oil and natural gas sales, our success in locating and acquiring new reserves, and the timely functioning of private equity investment in our company sponsored Joint Ventures. When oil and natural gas prices decrease or if we encounter operating difficulties that result in our cash flows from operations being less than expected, we must reduce our capital expenditures unless we can raise additional funds through our company sponsored Joint Ventures or divestment of assets. Private placement financing may not always be available to us on a timely basis or in sufficient amounts or on acceptable terms, and the proceeds offered to us for potential divestitures may not always be of acceptable value to us.

37. Substantial Capital Requirements. The company has experienced and expects to continue to experience substantial capital needs as a result of its active exploration, development and acquisition efforts. The company expects that additional external financing will be required in the future to fund our growth. We may not be able to obtain additional financing, and financing from sources other than our sponsored Joint Ventures or from asset divestitures may not be available on a timely basis or on terms acceptable to us. Economic and financial crises have had an adverse impact on our ability to obtain additional financing. Without additional capital resources, the Company may be forced to limit or defer our planned oil and natural gas exploration and drilling programs by releasing drilling rigs and deferring hydraulic fracturing, completion and hookup of wells to pipelines and thereby adversely affect our production, cash flow and the recoverability and ultimate value of our oil and natural gas properties. This, in turn, can negatively affect our business, financial condition, results of operations as well as those of our Joint Ventures.

When company revenues decrease due to lower oil or natural gas prices, decreased production, or other reasons, and if we cannot obtain further timely, acceptable financing through our sponsored Joint Ventures or through the sale of non-core assets or through other arrangements, then our ability to execute development plans, replace our reserves, or maintain production levels could be greatly limited.

While there is rising interest and demand for direct ownership through private placements of oil, natural gas and other natural resources, there are also constraints on such capital formation on account of the ongoing global and domestic economic and financial crisis and the uncertainty surrounding these phenomena. Continued adverse conditions that negatively affect our economy can adversely affect our ability to fund our Joint Ventures in a timely or acceptable fashion and thereby decrease our ability to operate in the manner we intend or to timely place ourselves and our Joint Ventures in the best situations for optimum returns.

38. Reserve Data and Future Net Cash Flows. Our reserve data and estimated discounted future net cash flows are estimates based on assumptions that may be inaccurate and are based on existing economic and operating conditions that may change in the future. There are numerous uncertainties inherent in estimating oil and natural gas reserves and their estimated value, including many factors beyond the control of the Joint Venture. Reservoir engineering is a subjective and inexact process of estimating underground accumulations of oil and natural gas that cannot be measured in an exact manner and is based on assumptions that may vary considerably from actual results. The reserve data produced by the Joint Venture represents only estimates. Accordingly, reserve estimates may be subject to upward or downward adjustment, and actual production, revenue and expenditures with respect to our reserves likely will vary, possibly materially, from estimates.

Changes in interpretations as to classification standards of reserves or disagreements with our interpretations could cause us to write down those reserves. A significant portion of our reserves are proved undeveloped, and some of our wells have produced for a relatively short time. Because most of our reserve estimates are calculated using volumetric analysis, those estimates are less reliable than estimates based on a lengthy production history. Volumetric analysis involves estimating the volume of a reservoir based on the net feet of pay in a producing formation or on a subsurface structure and an estimation of the area covered by the structure based on seismic analysis or subsurface mapping. In addition, realization or recognition of our proved undeveloped reserves will depend on our development schedule and plans. Lack of certainty with respect to the

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development plans for proved undeveloped reserves could cause the discontinuation of the classification of these reserves as proved.

39. Field Wide Depletion of Reserves in Target (or other) Formation. Primary stage production from the target formation will lead to depletion of the finite reserves in place. Extensive production in the local area by the Joint Venture's operations and/or operations of offsetting operators and competitors may lead to field wide depletion of the producing reservoir at a much earlier date than anticipated at the undertaking of this Joint Venture. This may lead to a situation wherein cumulative production from Venture well(s) may be inadequate to provide for return of original investment and can also lead to drilling problems experienced while drilling the Venture's well(s).

40. Recovery of Initial Investment. Because drilling activity may be stronger in a specific section of the country, prices of goods and services utilized to engage in drilling and in the cost of leasehold interests suitable for a project of this type may be higher even though prices may be lower on a nationwide basis. If such a situation occurs in the area of this Prospect, an investment in the program may be more expensive than might otherwise be the case. In addition, because of the amount of capital required to engage in operations, payout (that point in time at which the initial capital contributions of the Participants have been returned to them in full), could be lengthened, depending upon the amount of production obtained. There are no assurances that the prices of oil and gas will remain where they are currently situated, nor can any assurance be made that production levels can be sustained from the well(s) in quantities sufficient to reach payout at any time in the future. That will depend on factors beyond the control of the Issuer, Managing Joint Venturer and/or the operating company.

41. Litigation. Any constituent could bring suit or allege a violation of an existing contract. We could become subject to litigation that, if not resolved in our favor and not sufficiently insured against, could have a material adverse effect on the company. In today's overly litigious society, the company could be subjected to lawsuits and litigation at any time. Typically, we cannot foresee such actions nor predict the outcome of these cases. Insurance to eliminate, reduce or ameliorate the risks associated with litigation may not be applicable or sufficient in all cases, insurers may not remain solvent, and policies may not be available to the company. To the extent that future litigation matters are not resolved in our favor and are not covered by insurance, a material adverse effect on our financial results and condition could result. Such adverse effect could also adversely affect our ability to function effectively or suitably as Managing Joint Venturer or Operator.

42. Insurance against Operational Risks. Exploration for and production of oil and natural gas can be hazardous, involving unforeseen occurrences such as blowouts, cratering, fires and loss of well control, which can result in damage to and destruction of wells or production facilities, injury to persons, loss of life, or damage to property or the environment. We typically maintain insurance against certain losses or liabilities arising from our operations in accordance with customary industry practices and in amounts that management believes to be prudent; however, insurance is not available to us against all operational risks. In response to large underwriting losses experienced by the insurance industry from hurricane damage to rigs and equipment and a variety of other cases, insurance carriers have reduced capacity for certain types of damage and substantially increased premium rates.

    In accordance with customary industry practices, we maintain insurance against some, but not all, potential losses. We do not carry business interruption insurance or protect against lost revenues. We cannot assure you that any insurance we obtain will be adequate to cover any losses or liabilities. We cannot predict continued availability of insurance or the availability of insurance at premium levels that justifies its purchase. We may elect to self-insure if we believe that the cost of available insurance is excessive relative to the risks presented. In addition, pollution and environmental risks generally are not fully insurable. The occurrence of an event not fully covered by insurance could have a material adverse effect on our financial condition and results of operations which, in turn, would most likely adversely affect our Joint Venture Participants.

    We participate in a number of wells on a non-operated basis and may be accordingly limited in our ability to control the risks associated with such oil and natural gas operations.

43. Ability to Accept Risks. Participation in the Venture will be offered solely to prospective Venturers who are willing and can afford to accept and bear for an indefinite period of time the substantial risks described herein, who do not require immediate income from their capital contributions in the Venture, and whose annual recurring income is subject to the highest federal income tax rate or who are otherwise qualified. See "Plan of Organization and Suitability Standards."

Risks Specific to Mineral & Lease Acquisitions

1. Title to Properties. We often will hold lease positions in a 'street name' or in the name of a third party (under legal contract) in an effort not to expose our exploration and acquisition plans to competition. As is customary in our industry, we generally rely upon the judgment of natural gas and oil lease brokers or independent landmen who perform the field work in examining records in the appropriate governmental offices and abstract facilities before attempting to acquire or place under lease a specific mineral interest and before drilling a well on a leased tract. We believe we have satisfactory title to all our acquired leases and to our producing properties in accordance with standards generally accepted in the oil and natural gas industry.

2. Title Deficiencies. We purchase minerals, royalties, oil and gas term leases, and working and revenue interests in the natural gas and oil leasehold interests upon which we will perform our exploration activities from third parties or directly from the fee mineral owners. Our properties are subject to customary royalty interests, liens incident to operating agreements, liens for current taxes and other burdens, which we believe do not materially interfere with the use of or affect the value of these properties. Burdens on properties may include:

    - A fixed timeframe on the primary term of any lease, which without continuous development, the lease will expire and we would lose further rights for development;
    - Customary royalty interest;
    - Liens incident to operating agreements and for current taxes;
    - Obligations or duties under applicable laws;
    - Development obligations under oil and gas leases; or
    - Burdens such as net profit interests.

The existence of a material title deficiency can render a lease worthless and can adversely affect our results of operations and financial condition. As is customary in our industry, we generally rely upon the judgment of natural gas and oil lease brokers or independent landmen who perform the field work in examining records in the appropriate governmental offices and abstract facilities before attempting to acquire or place under lease a specific mineral interest and before drilling a well on a leased tract. We believe we have satisfactory title to all our acquired leases and to our producing properties in accordance with standards generally accepted in the oil and natural gas industry. Title insurance covering mineral leaseholds is not generally available and, in all instances, we forego the expense of retaining lawyers to examine the title to the mineral interest to be placed under lease or already placed under lease until the drilling block is assembled and ready to be drilled. Even then, particularly in urban settings, the cost of performed detailed title work can be expensive.

The company, in some cases, performs curative work to correct deficiencies in the marketability or adequacy of the title to us. The work might include obtaining affidavits of heirship or causing an estate to be administered. In cases involving more serious title problems, the amount paid for affected natural gas and oil leases can be generally lost, and the target area can become undrillable. The failure of title may not be discovered until after a well is drilled, in which case we may lose the lease and the right to produce all or a portion of the minerals under the property.

3. Third Party Commitments. The company may own less than 100% of the working interest in certain leases acquired by us, and other parties will own the remaining portion of the working interest. Financial risks are inherent in any operation where the cost of drilling, equipping, completing and operating wells is shared by more than one person. The company could be held liable for joint activity obligations of the other working interest owners such as nonpayment of costs and liabilities arising from the actions of the other working interest owners. In addition, the current economic downturn, the credit crisis and the decline in natural gas and oil prices may increase the likelihood that some of these working interest owners, particularly those that are smaller and less established, are not able to fulfill their joint activity obligations. Many of our project partners have experienced liquidity and cash flow problems. These problems may lead our partners to attempt to delay the pace of drilling or project development in order to preserve cash. A partner may be unable or unwilling to pay its share of project costs. In the event any of our project partners do not pay their share of such costs, we would likely have to pay those costs, and we may be unsuccessful in any efforts to recover these costs from our partners, which could materially adversely affect our financial condition and our ability to function effectively, suitably or on a timely basis as Operator or Managing Joint Venturer of our sponsored Joint Ventures.

4. Lease Acquisition on State and Federal Lands. Some of our operations are conducted on federal lands pursuant to oil and gas leases administered by the Bureau of Land Management (BLM), the Minerals Management Service (MMS), the General Land Office (GLO) or appropriate state agency. These leases contain relatively standardized terms and require compliance with detailed regulations and orders, which are subject to change. In addition to permits required from other regulatory agencies, lessees must obtain a permit from the BLM, MMS, GLO or other agency before drilling and comply with regulations governing, among other things, engineering and construction specifications for production facilities, safety procedures, the valuation of production and payment of royalties, the removal of facilities, and the posting of substantial cash bonds to ensure that lessee obligations are met. Under certain circumstances, the agency as applicable, may require our operations on state or federal leases to be suspended or terminated.

Investigations, including a title opinion of local counsel, are generally made before commencement of drilling operations. Even then, particularly in urban settings, the cost of performing detailed title work can be expensive. We may choose to forego detailed title examination by title lawyers on a portion of the minerals or mineral leases that we intend to acquire or place into a drilling unit or conduct less title work that we have traditionally performed. No title opinion or detailed title work is necessary for a validly existing and documented lease on minerals owned by a sovereign state or under federal ownership.

In acquiring prospective leases, minerals, drilling prospects or producing properties, we assess the potentially recoverable reserves, future oil and natural gas prices, potential liabilities and other factors relating to the properties. Our assessments are generally inexact and their accuracy is inherently uncertain. Our review of a subject property in connection with our acquisition assessment will not reveal all existing problems or permit us to become sufficiently familiar with the property to assess fully its deficiencies and capabilities. We may not inspect every lease, drilling prospect, producing property or well and we may not be able to observe structural or environmental problems even when we do inspect such property. If problems are identified, the seller may be unwilling or unable to provide effective contractual protections against all or a part of those problems. Any acquisition of mineral, leasehold, prospect, or producing property may not be economically successful and unsuccessful acquisitions may have a material adverse effect on our financial condition and future results of operations, as well as have an adverse effect on our Joint Ventures.

5. Lease(s) Undrillable. Drilling and development is always the intention when acquiring oil and gas leases. In certain cases, drilling and development of some leasehold may be prevented by federal or state policy or arbitrary regulatory changes. It is also common that leases are not drilled because of a downturn in the industry and the operating company is unable to acquire funding to undertake operations on the subject leasehold. Some modern leases include extension clauses which usually require additional payments to maintain the right to drill. Further, additional or new geological or geophysical information can be interpreted in such a way as to render a lease undrillable on account of lacking geological merit.

SPECIFIC RISKS OF THE JOINT VENTURE

1. New Venture Operations. The Venture is newly formed and has limited financial resources; however, upon initial capitalization, along with the participation of industry participants (including SIGNAL OIL LLC.), it is anticipated that funds will be sufficient to drill and test the Prospect Well and/or meet the obligations set forth.

2. Managing Joint Venturer's Limited Operating History. The Managing Joint Venturer, (SIGNAL OIL LLC.) has a limited operating history, and any investor must consider the risks, expenses, and difficulties frequently encountered by early stage companies in rapidly evolving markets. The failure rate of such companies in highly competitive markets and the problems and delays frequently encountered in the early stages of development must be considered. While other companies may be utilized to replace SIGNAL OIL LLC., such transition can also be problematic for the Joint Venture's business.

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3. Capitalization Period Extensions. Extension(s) of the capitalization period may be made by the Managing Joint Venturer in the exercise of its sole and absolute discretion. Thus, the exact time frame within which Venture operations will commence cannot be determined with any degree of certainty.

4. Termination of Segregated Account(s). Subscription proceeds, once released from segregated account(s) may be paid from the Joint Venture to Signal Oil llc.or to its affiliated operating company, as part of the Turnkey Drilling Contract or the Turnkey Completion Contract, as appropriate. Upon payment into SIGNAL OIL LLC., such funds shall become corporate assets and may be deposited into accounts in the name of Signal Oil llc.or its affiliates, including, but not limited to, SIGNAL OIL LLC.'s general operating account and as a result, in the event of SIGNAL OIL LLC.'s or any affiliate's insolvency, might be subject to claims of general creditors of Signal Oil llc.or their entities. Such event would have a financially adverse impact upon the Joint Venture and its Participants.

5. Limited Assets of the Company. As of the date of this Memorandum, the Managing Joint Venturer has limited assets and limited cash flow and may be obligated to direct these limited funds towards maintaining other lease(s) and operations in an untimely fashion. The Managing Joint Venturer believes that the proceeds from this Joint Venture will adequately capitalize it and sustain it for the proposed operations. However, if only a fraction of this Joint Venture is sold, or if certain assumptions in this Memorandum prove incorrect, the Managing Joint Venturer may then have inadequate funds to fully develop the proposed business and may need other capital investment to fully implement the Joint Venture's proposed operations.

6. Single Completion Attempt. The Issuer and its Operator affiliate will drill and complete the proposed well(s) through a single completion attempt intended to achieve initial production on a Turnkey basis[*] at a price per Unit as set forth herein as the purchase price for each Unit of Interest. Pursuant to this Turnkey arrangement, the Issuer will receive a fixed Turnkey price. The primary purpose of this Turnkey arrangement is to shift the risk of cost overruns of the drilling and completing phases of the proposed well(s) through initial production from the Joint Venture Participant to the Issuer. Thus each Participant must rely on the company's financial ability to pay the actual drilling and completion costs of the proposed well(s) in excess of the Turnkey price per Unit. The Issuer believes that its financial resources are sufficient to fulfill our financial obligations under the Turnkey arrangement. However, there is no assurance that the actual costs of drilling and completing the proposed well(s) will not exceed the Turnkey price or that the Issuer will have sufficient financial resources to fulfill its obligations without impairing its ability to perform our Turnkey function. If the Issuer is unable to pay the entire costs or drilling and completing the proposed well(s), the purchasers of the Units ("Participants") may be required either to pay such unpaid amounts or to risk having liens filed against the proposed well(s) for the unpaid amounts and to suffer possible foreclosure by any lien holders that may result in reduction, delay or elimination of revenues from the proposed well(s) or possible forfeiture of the working interest in the proposed well(s).

7. Best Efforts Venture. Under the terms of the Venture, the Units are being sold on a "best efforts" basis. Therefore there can be no assurance that any or all of the Units offered hereby will be sold. If all of the Units offered hereby are not sold, the Company will be limited in its ability to conduct its business.

8. Non-Transferability, Lack of Liquidity of Interest and Limited Qualification of the Venture. A Venturer has the status of a general partner under the provisions of the Texas UPA, and as such, is a co-owner of specific Venture property, holding as a tenant in partnership. A Venturer's right in specific Venture property is not assignable except in connection with the assignment of rights of all of the Venturers in the same property. Venturers should not expect to be able to readily liquidate their Interest, if needed, and, therefore, the Units may not represent satisfactory collateral for a loan. There is no public market for the Units of Interest and such a market will, in all probability, never develop. Even if a market develops for such Units, there can be no assurance as to the value which an investor partner could receive for his Interests. See Article VI of the "Joint Venture Agreement" attached hereto as Exhibit "B" and "Limited Transferability and Rights of First Refusal."

9. Discretion in Application of Proceeds. The Managing Joint Venturer has broad discretion to adjust the application and allocation of the net proceeds from initial capital in order to address changed circumstances and opportunities. The Company has provisions in its charter, by-laws, or other contracts providing for indemnification of its officers and directors which allows the Company, among other things, to pay for the expenses of an officer or director in connection with legal proceedings brought about because of the person's position with the Company. This could have the effect of making it more difficult for the shareholders to recover against the officers and/or directors of the Company for alleged breaches of fiduciary duties and other matters.

10. Arbitrary Determination of Unit Price. The Venture price of the Units and the underlying assets comprising the Units was determined solely by Signal Oil llc. based on its estimates of contemplated financial needs for the operations of the Joint Venture, principally the drilling and completion of the prospect well(s). No investment banker or other appraiser was consulted regarding such price and terms. The Unit price bears no relationship to the potential value of the Prospect well and does not necessarily bear any relationship to the asset value of the Company or to any other recognized criteria of value. Although the company believes that the amounts to be paid by the Joint Venturers under the Turnkey Contract are reasonable under the circumstances consistent with standard industry pricing practices in the area of operation and consistent with the type of terms that are ordinarily developed through arm's length bargaining, there is no assurance that the IRS will not take a contrary position and seek to reduce the deductible development expenses of the Joint Venture. NO PERSON SHOULD ACQUIRE JOINT VENTURE UNITS OF INTEREST IN THIS JOINT VENTURE IF HE BELIEVES THAT THE VENTURE PRICE OR THE TERMS ARE UNFAIR OR UNREASONABLE IN ANY RESPECT.

11. Risks of Principal Transactions. Transactions involving Venture and sales utilizing confidential private placement memoranda are subject to extensive regulation at both the federal and state levels by various regulatory organizations that are charged with protecting the Interests of investors. In addition, self-regulatory organizations such as the SEC and FINRA require strict compliance with their laws, rules and regulations. It is not uncommon for non-compliance with these

[*] If applicable

regulations to be charged and even the defense against such a claim is costly and may negatively affect the issuer and/or Managing Joint Venturer. Failure to comply with any of these laws, rules or regulations could result in fines, suspensions and other restrictions, which could have a material adverse effect upon the Managing Joint Venturer or Issuer's situation will subject the Company's capital to risk.

12. Investment Required During Drilling and Testing. The terms of the Joint Venture frequently require substantially the entire total purchase price for each Unit to be paid during the drilling and testing phase. Consequently, in the event that the drilling and testing of the well (s) does not result in the production of oil and/or gas in commercial quantities, purchasers of Units shall incur a loss on substantially all of the investment required to be made hereunder in connection with the purchase of Units.

13. Nature of the Liability of a Venturer. Each of the Venturers shall have the status of a Joint Venturer in a Joint Venture, which is a general partnership formed for a specific and narrowly defined business purpose. Venturers shall therefore have joint and several liability for all of the debts, obligations, acts, omissions, risks and liabilities of the Venture, which Signal Oil llc.believes will be ameliorated by adherence to the Joint Venture Agreements and the provision of necessary and proper insurance coverage with respect to Venture operations, to the extent that such insurance can be obtained at reasonable cost to the Venture. There is no assurance that all risks and liabilities that exist or may arise can be adequately insured against. See "Risk Factors - Specific Risks of the Venture: Uninsured Risks." The general discussions herein concerning partnerships also apply to the Venture.

    The Texas UPA provides that every partner of a general partnership is an agent of such partnership for the purposes of its business, and that the act of every partner for apparently carrying on in the usual way the business of such partnership binds the partnership, unless the partner so acting has in fact no authority to act for the partnership in the particular matter in question, and the person with whom he is dealing has knowledge of the fact that he has no such authority. The Texas UPA further provides that a general partnership (and each partner thereof) is liable to third parties for losses, injuries or penalties arising out of the wrongful acts or omissions of any partner acting in the ordinary course of the business of such partnership or acting with the authority of his co-partners.

    The Agreement provides that no Venturer (other than the Managing Venturer or by a Vote of the Venturers) shall have any right or authority to take any action on behalf or in the name of the Venture or to obligate the Venture to any third party for any reason or in any matter whatsoever, and that each Venturer shall indemnify, defend and hold harmless the Venture and all other Venturers (including Signal Oil llc.as the Managing Venturer) from and against any loss, claim, cause of action, item of damages, expense or cost (including attorneys' fees and court costs) arising directly or indirectly out of any act of such Venturer in breach of the Agreement. Further, the Agreement provides that any act of any Venturer inconsistent with the delegated rights and authority of the Managing Venturer shall constitute a breach thereof by the Venturer so acting, rendering such Venturer liable for damages and subject to expulsion from the Venture.

    The Venture may be dissolved by, among other things, the death, disability or bankruptcy of any Venturer. Upon dissolution, the Venture is not terminated, but continues until the winding up of Venture affairs is completed. Where the dissolution of the Venture is caused by, among other things, the death, disability or bankruptcy of a Venturer, each Venturer is liable, except under certain circumstances, to his Co-Venturers for his share of any liability created by any Venturer acting for the Venture as if the Venture had not been dissolved. Absent an agreement to the contrary by and between a Venturer, the Venture, the creditors of the Venture and the persons or venture continuing the business of the Venture, the dissolution of the Venture does not of itself discharge the existing liability of any Venturer. In the event that the business of the Venture is continued without the liquidation or the winding-up of its affairs, the creditors of the first or dissolved Venture are also creditors of the venture so continuing the business. Under the Agreement, only the Managing Venturer may conduct Operations relating to creditors whether before or after dissolution of the Venture.

    The Agreement provides that each Venturer waives his right to cause or obtain the dissolution and liquidation of the Venture, except upon the occurrence of certain specified events, or to withdraw from the Venture for any reason, and provides, except upon the occurrence of certain special events, for the continuation of the Venture upon the occurrence of any event which would otherwise give rise to the dissolution and liquidation of the Venture under applicable law. Furthermore, each person proposing to become a Venturer shall represent and warrant to the Venture, as an express condition to the acceptance of his application that he possesses the requisite financial suitability and capacity to participate in the Venture upon the terms and conditions established therefore, and that he is not, as of the date of such application and has not been at any time during the ninety (90) day period immediately preceding the date of such proposed participation insolvent or an adjudicated bankrupt under the federal bankruptcy statutes.

14. Failure to Pay Completion or Mandatory Assessments. The Venturers may be called upon to pay completion assessments or obligatory workover, re-entry or stimulation assessments not to exceed that amount set forth in the Summary of the Joint Venture Program of this memorandum for the Venturer's allocable share of the Turnkey Completion Contract[*]. The payment of the completion or other secondary assessment is subject to a vote. The failure of a Venturer to contribute his/her proportionate share of a completion assessment within seven (7) days from delivery of a notice by electronic mail, postal mail, overnight delivery (FedEx, et.al.,) or personal delivery shall be deemed a negative vote for completion and a request that his/her Interest in the Venture be abandoned, and he/she shall be effectively withdrawn as a Participant in the Venture with no further benefits, rights or obligations with respect to sharing of income, gains and losses with respect to the Venture. See "Additional Assessments and Financing of Additional Venture Activities."

15. Failure to Pay Optional Additional Assessments. Because Venturers are not subject to mandatory additional assessments for additional capital contributions to the Venture for subsequent operations, capital shortages could result in a loss of substantial opportunities to the Venture and, therefore, to the Venturers. Venturers electing not to participate in any proposed subsequent

[*] If applicable

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operation will be subject to a penalty of 500% of the amount in default, which penalty will paid to the Venturer who has paid the defaulting Venturer's assessment. See "Conflicts of Interest, "Additional Assessments and Financing of Additional Venture Activities."

16. Company as Nominee. Signal Oil llc.or its affiliates or contracted agents will be the nominal title holder of the leased acreage assigned to the Joint Venture. As such, Signal Oil llc.or its affiliates or contracted agents will receive the payment for the sale of oil and gas production from the purchaser thereof. If Signal Oil llc.or its affiliates or contracted agents should experience financial difficulties, its creditors may claim an interest in the oil and gas leases as well as the payment of the production therefrom.

17. Cash Distributions to Participants. The amount and timing of any cash distributions to the investor Participants are dependent upon numerous factors that are beyond the control of the Managing Joint Venturer, the Operating Company, and industry partners. Such factors may include, but are not limited to, delays in obtaining the following:

- Suitable connections to pipelines or other transportation systems
- Satisfactory purchase contracts for natural gas production
- Division orders
- Assignments pursuant to completion of designated farm out conditions and terms

and other delays. Moreover, the amount of future distributions may vary considerably as a result of the variations in the prevailing market prices of and the demand for crude oil and natural gas and the availability of alternative markets in the fields where the Prospects are located. While the Operator and Managing Joint Venturer believe that conditions related to this Prospect are adequate and operable, there can be no assurance that the Joint Venture will be able to make regular distributions to the Participants; however, the Joint Venture will endeavor to make such distributions quarterly.

18. Earned but Undistributed Income. The Participants have no right to demand distribution of Joint Venture income, therefore, each Venturer may incur tax liability with respect to income earned by the Venture and might have to pay taxes on his (her) allocable share of such income regardless of whether such income is actually distributed to him (her) by the Joint Venture.

19. Sharing of Risks. The Participants will bear all of the financial risk associated with the Venture's working interest in a nonproductive or marginally productive Venture well and might be liable for Venture obligations in excess of their capital contributions. See "Participation in Costs and Revenues within Venture." In addition, each of the Venturers shall have the status of general partners in a general partnership and shall therefore have joint and several liability for all of the debts, obligations, acts, omissions, risks, and liabilities of the Venture. See "Risk Factors – Specific Risks of the Venture: Nature of the Liability of a Venturer."

20. Inability to Meet Obligations. The inability of one or more of our working interest partners to meet their obligations may adversely affect our financial results. A very substantial portion of our accounts receivable result from oil and natural gas sales or joint interest billings to third parties in the energy industry. This concentration of customers and joint interest owners may impact our overall financial results and increase our credit risk in that these entities may be similarly affected by various economic and other conditions, such as global and domestic economic and financial crises.

21. Lack of Diversity. Subscription amounts should be sufficient to pay for initial operations with respect to the Prospect Well(s) only. To the extent such well(s) is a dry hole, Venturers should be prepared to lose their entire investment unless there are additional wells specified herein that are planned, intended or funded and that may serve to recoup losses.

22. Conflicts of Interest. There are conflicts of interest inherent in the activities of the Joint Venture. Signal Oil llc.and/or its affiliates presently act and intend to act in the future as investors, general partners and Joint Venturers of other partnerships and ventures, intend to manage other drilling ventures and own and operate other oil and gas properties on its own behalf as well as on behalf of others. In addition, Signal Oil llc.is a working interest owner. Any conflicts of interest could adversely affect the Venture and/or the interests of the Venturers. See "Conflicts of Interest."

23. Signal Oil llc.Dependency on Key Officer. SIGNAL OIL LLC.'s ability to manage Venture affairs is predominantly dependent upon Signal Oil llc director and principal executive officer. (See "Management.") We depend to a large extent on the services of certain key management personnel, including our executive officers and other key employees and contractors who have extensive experience in our industry. The loss of any of these individuals could have a material adverse effect on our operations. Our success will be dependent on our ability to continue to employ and retain skilled management and technical personnel.

24. Life Insurance. At present the Company has no Key Man life insurance on the life of any key officer or employee. The Company intends to obtain Key Man life insurance in the amount of $1,000,000 on the life of the Company's executive manager who serves as the Company's principal operating person. The death benefit payable under the policy will be payable in full to the Company or its designee(s), which may change from time to time.

25. Surrounding Production. Although there have been wells drilled, tested and completed on acreage in the vicinity of the Prospect Well, the production from such wells should not be deemed a guarantee that any well to be drilled upon the Prospect will be a commercially productive well. See "Geological Information" attached hereto as Exhibit "D".

26. Geological Opinions, Maps, Inferences, Statistics and Projections. The Managing Joint Venturer has provided certain geological opinions, potential statistics and well information regarding the Prospect and surrounding region. The Managing Joint Venturer cannot and does not guarantee the accuracy or correctness of any of the interpretations made by any geologist, engineer or consultant to the Joint Venture, the Operating Company, or the Issuer. The Managing Joint Venturer shall not be liable or responsible for any loss, costs, damages or expenses incurred or sustained by any Venturer based upon that Venturer's reliance upon information contained or interpreted from statistics or opinions expressed by others. The production map(s) may contain possible fault and fracture lines for illustration purposes only and not as a predictor of things to come for the Joint Venture. The Managing Joint Venture cannot assure, nor does it guarantee, the surrounding well positions, fault or fracture lengths, bore hole depths or lengths, formation intervals, identified operators, or the well names or amounts of production, even though the Managing Joint Venturer believes such information to come from reliable sources and to be both current and accurate.

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27. Participation with or Joint Venture Use of Third Party Operators and Consultants. Subject to contractual agreements, the Managing Joint Venturer may, in certain areas and circumstances, utilize the services of a third party operator that is not affiliated with the Issuer or the Joint Venture. In such case, the Issuer may or may not contract for Turnkey services with the third party operator and/or with independent oil and gas consultants. In any case, the Managing Joint Venturer will have no authority or control over many aspects of the third party operator's or independent consultant's conduct of business and operations. The success and efficiency of oil and gas operations on a property, whether regarding drilling, re-entry, workover, stimulation, completion or production operations depends in large measure on whether the operator and/or the supervising independent consultant properly performs its function and meets its intended obligations. The failure of such operator and/or independent consultants and their contractors to perform their services in a proper manner could result in materially adverse consequences to the owners of Interests in that particular property, including the Joint Venture.

28. Compensation and Reimbursement to Managing Venturer Regardless of Profitability. The Managing Joint Venturer may receive certain fees and other compensation, payments and reimbursements regardless of profitability or loss of the Joint Venture. See "Participation in Costs and Revenues within Venture," "Compensation and Reimbursement" AND "Conflicts of Interest."

29. Uninsured Risks. The Venture's Operations will be subject to all of the operating risks normally connected with exploring for, drilling and producing oil and gas, such as blow-outs and pollution, lightning strikes, theft and vandalism, any of which could result in the Venture incurring substantial losses or liabilities. Although the JVA provides for the securing of such insurance as the Managing Venturer deems necessary and appropriate, certain risks are uninsurable and others may be either uninsured or only partially insured because of high premium costs or other reasons. In the event the Venture incurs uninsured losses or liabilities, the Venture's funds available for exploration and development will be reduced, and Venture assets may be substantially reduced or lost completely. For a discussion of the Venturer's liability, see "Risk Factors - Specific Risks of the Venture: Nature of the Liability of a Venturer."

30. Environmental Risks, Laws and Regulations. The company's oil and gas operations, like those of the entire industry, are subject to environmental risks such as oil spills, produced water spills, gas leaks, and ruptures and discharges of substances or gases that could expose us to substantial liability for pollution and other environmental damage. Our operations are also subject to numerous United States federal, state, local and foreign environmental laws and regulations. Non-compliance with these laws and regulations may subject us to administrative, civil or criminal penalties, remedial clean ups and natural resource damages or other liabilities. In addition, increasingly stringent environmental regulations have resulted and will likely continue to result in higher capital expenditures and operating expenses for us and the oil and gas industry in general.

    Concerns have been raised in certain jurisdictions where we have operations concerning the safety and environmental impact of the drilling and development of both conventional and unconventional resources, particularly using the process of hydraulic fracturing. While we believe these operations can be conducted safely and with minimal impact on the environment, regulatory bodies are responding to those concerns and may impose moratoriums and new regulations on such drilling operations that would likely have the effect of prohibiting or delaying such operations and increasing their cost. In certain areas, governmental regulatory bodies have imposed a moratorium prohibiting hydraulic fracturing which directly impacts the ability of the oil and gas operators to effectively stimulate drilled wells, and to establish economic production, thus drilling operations have all but ceased and, attendant with this cessation, there is no further lease development, and no cash flows are generated for any Participant.

31. Drilling Risks and Commercially Unsuccessful Wells (Dry Holes). Exploration for oil and gas is speculative by its very nature, and involves a high risk of loss. A large number of wells result in dry holes, and others do not produce oil or gas in sufficient quantities to make them commercially profitable to compete and/or produce. Still others might experience production decline that is rapid and irregular. Initial production from a well (if any) does not accurately indicate any consistent level of production to be derived therefrom. Many risks are involved that experience, knowledge, scientific information and careful evaluation cannot avoid. Since initial capitalization will be sufficient to drill only the Prospect Well, the drilling of a dry hole would mean that the Participants would receive no financial return from the Venture. Therefore, Participants must be prepared to lose substantially all of their capital contribution as there can be no assurance that the Prospect Wells will result in oil or gas production or that production, if obtained, will be profitable for Venturers.

32. Operating and Other Casualty Risks. The natural gas and oil business involves operating hazards such as:

    - well blowouts;
    - mechanical failures;
    - explosions;
    - uncontrollable flows of oil, natural gas or well fluids;
    - fires;
    - geologic formation with abnormal pressures;
    - pipeline ruptures or spills;
    - releases of toxic gases; and
    - other environmental hazards and risks.

    Any of these hazards and risks can result in the loss of hydrocarbons, environmental pollution, personal injury claims and other damage to our properties and the property of others.

33. Poor Production and/or Slow Rate of Return on Investment. It is possible that wells drilled, completed and equipped for production by the Joint Venture may not produce in sufficient quantities to pay for the cost of acquiring, drilling, re-entering, completing, re-completing, stimulating, and/or equipping such well(s) even if tax benefits are considered. Likewise, there is a risk that you will not receive a rate of return on your investment that is competitive with other types of investments. Further, neither the Managing Joint Venturer nor any other party can accurately predict the quantity, if any, of hydrocarbons that may be recoverable from any well(s). Your investment may only be recoverable through distributions of funds received from the sale of oil and gas from this Joint Venture's wells. All such distributions should be considered "return of capital" until you have received 100% of your original investment.

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34. Revenues or Production Might Vary Significantly from Projections. In acquiring producing properties, we assess the recoverable reserves, future natural gas and oil prices, operating costs, potential liabilities and other factors relating to the properties. The company's assessments are necessarily inexact and their accuracy is inherently uncertain. Our review of a subject property in connection with our acquisition assessment may not reveal all existing or potential problems or permit us to become sufficiently familiar with the property to assess fully its deficiencies and capabilities. We may not inspect every well, and we may not be able to observe structural and environmental problems even when we do inspect a well. If problems are identified, the seller may be unwilling or unable to provide effective contractual protection against all or part of those problems. Any acquisition of property interests may not be economically successful, and unsuccessful acquisitions may have a material adverse effect on our financial condition, and that of our sponsored Joint Ventures and future results of operations.

35. Accessibility to Pipelines and/or Transportation Systems. It is typical that the Managing Venturer has no present written agreement (gas contract) to use any pipeline for transmission of oil or natural gas. When and where there is already established a pipeline connection on the subject lease, it is anticipated that the original gas contract, which is already in place, will continue in full force and effect with the continued production of the lease. Although this is customary, the terms may not be as favorable to the Joint Venture as desired or up to current market standards. The Managing Joint Venturer and/or Operator will endeavor to achieve the most favorable and beneficial terms possible relating to the sales of both oil and gas. See "Additional Assessments and Financing of Additional Venture Activities."

36. Oilfield Equipment. The successful execution of contracts requires a high degree of reliability of a variety of oilfield equipment. Breakdowns and failures not only add to the costs of executing a project, but they can also delay the completions of subsequent operations that are intended to utilize the same assets. The Company inspects and reviews all major and most minor equipment either owned or contracted, but we have little or no control over vendors' or third parties' equipment. Although the company works to see that all equipment is in good working order, breakdowns and failures can and often do, occur.

37. Activities on Properties We Do Not Operate. We do not operate all of the properties in which we have an interest. As a result, we have limited ability to exercise influence over, and control the risks associated with, operations of these properties. The failure of an operator of our wells to adequately perform operations, an operator's breach of the applicable agreements or an operator's failure to act in ways that are in our best interests could reduce our production and revenues or could create liability for us for the operator's failure to properly maintain the well and facilities and to adhere to applicable safety and environmental standards. With respect to properties that we do not operate, any of the following events could significantly and adversely affect our anticipated exploration and development activities:

- The operator could refuse to initiate exploration or development projects.
- If we proceed with any of those projects the operator has refused to initiate, we may not receive any funding from the operator with respect to that project.
- The operator may initiate exploration or development projects on a different schedule than we would prefer.
- The operator may propose greater capital expenditures than we wish, including expenditures to drill more wells or build more facilities on a project than we have funds for, which may mean that we cannot participate in those projects or participate in a substantial amount of the revenues from those projects.
- The operator may not have sufficient expertise or resources.

38. General Economic Conditions. The financial success of the Joint Venture and/or the Operating Company may be sensitive to adverse changes in general economic conditions in the United States, such as recession, inflation, unemployment, and interest rates. Such changes could reduce demand in the marketplace for crude oil and natural gas. The Managing Joint Venturer and Operator believe that global demand and economic conditions will maintain product demand and price; however, there is no control over these changes.

39. Long Term Nature of Investment. An investment in this Joint Venture may be long term and illiquid. Prospective investors will be required to represent that they are purchasing Units of Interest for their own account and not with a view towards resale or distribution. Accordingly, purchasers must be willing to bear the economic risk of their investment for an indefinite period of time. It is likely that Participants will not be able to liquidate their investment in the event of emergency.

40. Units Are Not Registered Securities. We have not registered the Units under the Securities Act of 1933, as amended (the 1933 Act). Instead, we are relying on registration exemptions available under the 1933 Act and the rules and regulations promulgated under that Act. Further, the Units are being offered and sold pursuant to registration exemption requirements of the various states in which the Units are being offered; however, there is no assurance that this Joint Venture qualifies or will continue to qualify under the registration exemptions of the 1933 Act or applicable state laws due to, among other things, the adequacy of disclosure and the manner of distribution of this Venture, similar Ventures to be conducted by us or our affiliates in the future, or the retroactive change in any applicable securities laws or regulations. If such sale were to fail to qualify for these exemptions, purchasers may seek rescission of their purchases. If and to the extent suits for rescission were to be brought against the Issuer and successfully_concluded for failure to register this Venture or other Ventures made or to be made by the 1933 Act, or for acts or omissions constituting certain prohibited practices under the Securities Exchange Act of 1934, our capital and assets could be adversely affected, thus jeopardizing our ability to continue to serve as Managing Joint Venturer or as the Operator (affiliate) of the proposed Joint Venture well(s).

41. Property Acquisitions. Property acquisition may not be worth what we paid due to uncertainties in evaluating recoverable reserves and other expected benefits, as well as potential liabilities. Successful property acquisitions require an assessment of a number of factors beyond our control. These factors include exploration potential, future oil and natural gas prices, operating costs, and potential environmental and other liabilities. These assessments are not precise and their accuracy is inherently uncertain.

In connection with our acquisitions, we perform a customary review of the acquired properties that will not necessarily reveal all existing or potential problems. In addition, our review may not allow us to fully assess the potential deficiencies of the properties. We do not inspect every well, and even when we inspect a well we may not discover structural, subsurface, or environmental problems that may exist or arise. We may not be entitled to contractual indemnification for pre-closing

liabilities, including environmental liabilities. Normally, we acquire interests in properties on as “as is” basis with limited remedies for breaches of representations and warranties.

In addition, significant acquisitions can change the nature of our operations and business if the acquired properties have substantially different operating and geological characteristics or are in different geographic locations than our existing properties. To the extent acquired properties are substantially different than our existing properties, our ability to efficiently realize the expected economic benefits of such acquisitions may be limited.

Integrating acquired properties, including leases, drilling prospects and/or producing properties and businesses involves a number of other special risks, including the risk that management may be distracted from normal business concerns by the need to integrate operations and systems as well as retain and assimilate additional employees. Therefore, we may not be able to realize all of the anticipated benefits of our acquisitions of leases, prospects and properties and the same effect could be experienced by in our sponsored Joint Ventures.

RISKS ASSOCIATED WITH TAX MATTERS

1. General Considerations. Although participation in the Venture is intended to appeal primarily from an economic standpoint, albeit with risk, with the hope of finding oil and/or gas in commercial quantities, favorable federal income tax treatment available with respect to oil and gas drilling and production has a material effect on the desirability of participating in an oil and gas drilling program for certain taxpayers. Any deductions for federal income tax purposes available to the Venturer resulting from his participation in the Venture and the year in which such deductions are taken may have a material effect upon the economic result afforded him.

   The benefit to a particular Venturer of various deductions will depend on the nature and extent of other income, deductions and credits of that Venturer. For this reason, each prospective Venturer should consult with his personal tax advisor. Continuation of certain tax treatment presently available cannot be assured, and the tax benefits related to drilling and production could, at any time, retroactively as well as prospectively, be modified or eliminated by legislative, judicial or administrative action. Such changes could deprive the Venture and its Venturers of certain tax benefits they might otherwise receive and may or may not be retroactive with respect to transactions occurring prior to the effective date thereof. See "Tax Considerations - Possible Changes in Federal Tax Laws."

2. Tax Classification of the Venture. The availability of the tax benefits of participating in the Venture depends upon the classification of the Venture as a "venture" rather than an association taxable as a corporation for federal income tax purposes. Counsel for the Venture believes that, under current law and if the question were litigated, it is more probable than not that the Venture would be treated as a partnership for federal income tax purposes and not as an association taxable as a corporation. This conclusion is not binding on the service and is conditioned on the maintenance of certain conditions. Should the Venture be treated as "an association taxable as a corporation" for federal income tax purposes, (a) income, gains, losses, deductions and credits of the Venture would not flow through to the Venturers, (b) the taxable income of the Venture would be subject to the federal income tax imposed on corporations, and (c) distributions would be treated as corporate distributions to the Venturers and could be taxable as dividends. See "Tax Considerations."

3. No Tax Ruling. No rulings have been sought from the IRS with respect to any of the tax matters discussed in this Private Placement Memorandum, and many of these matters involve developing areas of the law, the application of which is not free from doubt. Instead, the Issuer relies on opinion of counsel and a historical personal knowledge of beneficial tax treatment of such investments. Potential investors are cautioned that history and an opinion of counsel are not binding on either the IRS or the courts, and any of the conclusions set forth may be subject to change as a result of changes in law. Therefore, there can be no assurance that deductions claimed by the Joint Venture and allocated to the Participants may not be successfully challenged by the IRS. Any adjustments which are ultimately sustained by the courts will significantly affect the economic value of this investment. **EACH PROSPECTIVE INVESTOR IS URGED TO CAREFULLY REVIEW THE MATERIAL SET FORTH UNDER THE HEADING ‘TAX ASPECTS’ WITH HIS OWN LEGAL, TAX, INSURANCE AND FINANCIAL ADVISORS BEFORE MAKING A DECISION TO INVEST.**

4. Allocations for Income Tax Purposes. The Venture intends to allocate among the Venturers their allocable share of income, gain, loss, deduction and credit in accordance with the terms of the Venture Agreement. Such allocable shares shall include all of the Venture's intangible drilling and development costs (Intangible Costs) arising from initial operations that are paid from the Venturers' capital contributions. While the Venture intends to make such allocations, no assurance can be given that the Internal Revenue Service will not challenge the allocations of federal income tax items and assert that they are properly allocable among the Venturers in some other manner. See "Tax Considerations - Allocations."

5. Depletion Allowance. Percentage depletion allowable by reason of the Independent Producer Exemption will be available to the Venturers who qualify as independent producers (other than those who owned a pre-October 12, 1990, interest in proven property acquired by the Venture.) Since each Venturer must individually determine his eligibility for the Independent Producer Exemption, there can be no assurance that percentage depletion will be available to any particular Venturer. See "Tax Considerations - Depletion."

6. Passive Activity Limitations. It is expected that the Venture will initially incur tax losses from initial operations (primarily from deductions of intangible costs). The availability of tax losses generated to the Venturers by the Venturers by the Venture to offset the Venturers' income from other sources depends on

   - the classification of the Venture's property as a working interest as defined by the passive loss limitations added by the Tax Reform Act of 1986, and
   - the determination that the Venture does not have an effect on the Venturers' liability that is substantially equivalent to a limited partnership.

   There can be no assurance that the Internal Revenue Service will not challenge the Venture's conclusions with regard to these determinations. If losses generated by the Venture are reclassified as passive, such losses would not be available to deduct against the Venturers' income from other sources. See "Tax Considerations - Limitations on Passive Activity Losses."

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7. Prepayment of Certain Costs. The Managing Venturer expects to expend initial Venture capital in the current calendar tax year to obtain deductions for intangible costs in the current year. Should drilling actually commence after March 31 in the following year, the Venturers would be precluded from deducting their capital contributions (attributable to drilling) in the current year. Likewise, for ventures funded in the coming next year, the Managing Venturer expects to expend initial venture capital in that specific year. Should drilling actually commence after March 31 of the coming next year, the Venturers would be precluded from deducting their capital contributions (attributable to drilling) in that specific year. Counsel to the Venture cannot predict when drilling for the Venture will commence. See "Tax Considerations - Prepayment of Certain Costs."

8. Taxable Income. To the extent Venturers are able to deduct losses generated by the Venture, the basis of each Venturer's Interest will be reduced. Amounts realized by a Venturer on the sale of his Venture Interest may produce taxable gain that may be ordinary income to some extent. Thus, the tax deductions afforded in the early years may only defer to later years a Venturer's overall federal income tax liability. See "Tax Considerations."

9. Tax Preference Items and Recapture of Intangible Costs and Depletion. Certain Intangible Costs and depletion are tax preference items and are also subject to recapture as ordinary income on disposition by the Venture of oil and gas properties at a gain, or upon disposition by a Venturer of an Interest in the Venture at a gain. See "Tax Considerations - Tax Preference Income: Alternative Minimum Tax."

10. Internal Revenue Audit. If the Internal Revenue Service (“Service”) audits the Venture, there can be no assurance that the Service will not challenge certain deductions allocated to the Venturers. See "Tax Considerations - Audit of Tax Returns."

11. State and Local Tax Aspects. Certain states and localities in which Venturers may reside or where the Venture conducts business may levy income taxes for which such Venturers may be liable in respect to their share of Venture income, and it may be necessary for such Venturers to file income tax returns with such states or localities to report such income.

12. Earned but Undistributed Income. The Venturers have no right to demand distribution of Venture income. Therefore, each Venturer may incur tax liability with respect to income earned by the Venture and may have to pay taxes on the Venturer’s allocable share of such income regardless of whether such income is actually distributed by the Venture.

13. No Passive Income. Although losses attributable to the program of the Joint Venture will not be limited pursuant to passive loss rules, the income from the program, provided the program is successful and results in a commercial well(s), will not be available to offset losses from other passive activities.

14. Loss of IDC Deduction. The Managing Joint Venturer has, and expects to exercise, the right to begin drilling of the well(s) before all Units of Joint Venture working interest have been subscribed and paid for. INVESTORS WHO PURCHASE UNITS AFTER THE DRILLING BEGINS MAY NOT BE ENTITLED TO ELECT TO DEDUCT AS INTANGIBLE DRILLING COSTS THEIR PROPORTIONATE SHARE OF SUCH COST INCURRED BEFORE THEIR PURCHASE OF UNITS. Furthermore, on audit, the IRS may take the position that such investors may not deduct as IDC their share of costs attributable to drilling performed after their investment. Each prospective Participant should carefully review the more detailed discussion contained in the “Tax Considerations” section of this memorandum.

15. Leasehold Cost. A value equal to the actual acquisition and booking costs of the lease(s) has been attributed to the lease(s) pursuant to the Operating Agreement. The IRS could take the position that the value so allocated is not appropriate and that a greater amount should be allocated to the leasehold cost. Should the IRS take such position and be sustained, the intangible drilling and development costs to which investors would otherwise be entitled would be reduced.

16. Possible Disallowance of Credits and Deductions. Participants will receive annual information based on the Managing Joint Venturer’s interpretation of data compiled from the books and records of the Joint Venture. Although the Managing Joint Venturer may consult with independent public accountants and with tax counselors to the extent deemed necessary in compiling and delivering information to the purchasers of Units, the amount of deductions and credits reported for purchasers’ individual returns based on such information submitted by the Managing Joint Venturer may vary from the amounts which may be ultimately allowed by the IRS or a reviewing court. (See “Tax Considerations.”)

17. Possible Penalty for Non-Disclosure. The Managing Joint Venturer, after consultation with its tax advisors, will attempt to aid investors in making appropriate disclosures on their individual returns. However, such responsibility is ultimately that of the taxpayer and the taxpayer’s tax advisors. Should the IRS disagree with the disclosure made or the adequacy thereof and be sustained, an investor could be subject to penalties. (See “Tax Considerations.”)

18. Management Fees. The payment of management fees by the Venture for services rendered thereto will be deductible only to the extent such payments are ordinary and necessary business expenses and are reasonable in amount (Internal Revenue Code Sections 162 and 707). See "Tax Considerations "- "Management Fees."

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COMPETITION, MARKETS AND REGULATION

Competition

The oil and gas industry is highly competitive. The Venture will encounter frequent and intense competition from both major oil companies and other independent operators in its effort to secure drilling rigs and equipment necessary in the drilling and completion of wells. Many of such competitors have financial and technical resources and personnel staffing much larger than those available to this Joint Venture.

Markets

The ability of the Joint Venture to market oil and gas found and produced, if any, will depend on numerous factors beyond its control, the effect of which factors cannot be accurately predicted or anticipated. These factors include the availability of other domestic and foreign production, the marketing of competitive fuels, the proximity and capacity of pipelines, fluctuations in supply and demand, the availability of a ready market and the effect of federal and state regulation of production. There is no assurance that the Joint Venture will be able to market any oil or gas found by the Joint Venture at favorable prices, if at all.

Regulation

The volume of production from oil and gas wells is set by state regulatory agencies through the establishment of allowable rates of production and by limitations placed upon the number of days during each month that a well can produce. Additional state regulations require permits before wells are spudded, control well spacing, protect against waste, aid in the conservation of natural gas and oil and guard against adverse environmental consequences.

Regulatory requirements, which are comparable, and in some cases, more restrictive than those described above, will be encountered in all jurisdictions in which drilling is to be done. It is anticipated that various local, state and federal environmental control agencies will have increasing impact on oil and gas operations. All necessary permits for all operations will be secured, or caused to be secured, by the Managing Joint Venturer.

Possible Legislation

No prediction can be made as to possible government action or additional legislation that might be proposed, if any, affecting the competitive status of an oil and gas producer, restricting the prices at which a producer may sell its oil and gas, or market demand for oil and gas, nor can it be predicted which proposals, including those presently under consideration, if any, might be enacted, nor when any such proposals, if enacted, might become effective.

A WYOMING LIMITED LIABILITY COMPANY

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

PART 5

TAX CONSIDERATIONS & GLOSSARY

Tax Considerations

The full implications of federal, state and local laws that may affect the tax consequences of participating in the Venture are too complex and numerous to describe in this Memorandum. Therefore, each prospective Venturer should satisfy himself as to the federal and state income and other tax consequences of participating in the Venture by obtaining advice from his own tax counsel, particularly with respect to any tax proposals that may at some future date be enacted into law.

The discussion below is a general description of some of the federal income tax aspects of participation in the Venture described herein. This summary, while not exhaustive, includes a discussion of the material tax issues involving a reasonable possibility of challenge by the Internal Revenue Service (“Service” or “IRS”). The discussion is directed primarily toward individual taxpayers who are citizens of the United States.

PERSONS WHO ARE NOT UNITED STATES CITIZENS, TAX-EXEMPT ENTITIES, CORPORATE ENTITIES IN GENERAL AND CORPORATE ENTITIES THAT ARE A SUBJECT TO SPECIALIZED RULES, (E.G., S CORPORATIONS OR INSURANCE COMPANIES), AND TRUSTS ARE CAUTIONED TO CONSULT THEIR TAX ADVISORS BEFORE PARTICIPATING IN THE VENTURE. THE SUMMARY ALSO INCLUDES A DISCUSSION OF SOME OF THE PROVISIONS OF THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982 (“TEFRA”), THE TAX REFORM ACT OF 1984 (“TRA 1984”), THE TAX REFORM ACT OF 1986 (“TRA 1986”), THE OMNIBUS BUDGET RECONCILIATION ACT OF 1989 (“OBRA 1989”), AND THE REVENUE RECONCILIATION ACT OF 1990 (“RRA 1990”) AND 1993 (“RRA 1993”).

Some of the federal income tax aspects applicable to this Venture are unsettled and not free from doubt. Moreover, in determining the deductibility of certain expenditures made by the Venture, there are many factual and legal questions involved, including but not limited to the proper characterization of income and expense, the reasonableness of amounts involved, the purpose of the expenditures and the period or periods to which the expenditures are properly attributable. Although this summary has been reviewed by Counsel to the Venture, Venturers should not read this summary as a prediction of a favorable outcome of the tax issues concerning which no favorable prediction is made.

The material tax benefits of participating in the Venture will be the deductions attributable to intangible drilling and development costs (intangible costs), accelerated cost recovery on equipment and other tangible property and, if production is achieved, depletion. Assuming Venture Operations are conducted as proposed herein, Counsel for the Venture believes that, in the aggregate, the material tax benefits contemplated in this Memorandum more likely than not will be realized by a Venturer as set forth below. Venturers, however, must not construe this statement as an indication that all tax benefits described in this summary will likely be realized. In addition, this conclusion concerning the realization of the material tax benefits is based on the facts existing as of the date of this Memorandum concerning the operation of the Venture, and certain representations of the Managing Venturer, and is subject to the discussion below. Final disallowance of any such deduction would adversely affect the Venturers. There can be no assurances that some of the deductions taken by the Venture will not be challenged and disallowed in whole or in part or permitted as deductions only in a subsequent taxable year of the Venture.

Prospective Venturers should be aware that the Venture initially expects to report tax losses from operations primarily resulting from the payment and deduction of Intangible Costs. As discussed below, the Venturers could thereafter recognize substantial taxable income if the Venture drills a producing well. Intangible costs and depletion, to the extent they reduced the basis of the property, are subject to recapture at ordinary income tax rates on the sale or disposition of a Venture Interest or on the sale or disposition of the Prospect by the Venture. To the extent allowed, the deductions afforded in the early years of the Venture could operate to defer to the year of such sale or disposition, and not eliminate, a Venturer’s overall federal income tax liability. Any gain from the sale or disposition of a Venture Interest will be taxed at ordinary rates to the extent attributable to unrealized receivables (which term includes recapture of depreciation, depletion and intangible costs). Therefore, the tax benefit any particular prospective Venturer may derive from participating in the Venture will depend, in part, on the value of such a tax referral to the Venturer.

While the Venture must file a federal income tax return, the Venture is not required to pay any federal income tax. Instead, each Venturer reports on his individual federal income tax return his distributive share (as determined by the Joint Venture Agreement) of income, gains, losses, deductions and credits of the Venture, irrespective of any actual cash distributions made to such Venturer during his taxable year. Subject to the passive activity loss limitations discussed below, a Venturer may offset his allocable share of Venture losses in any taxable year against the Venturer’s income from other sources to the extent of the tax basis of the Venturer’s Interest in the Venture. A Venturer’s deductions will further be limited to the amount he has “at risk” with respect to the activities of the Venture.

Tax Status of the Joint Venture

INTERNAL REVENUE CODE ELECTION

THIS VENTURE IS NOT INTENDED TO CREATE, AND SHALL NOT BE CONSTRUED TO CREATE, A RELATIONSHIP OF PARTNERSHIP OR AN ASSOCIATION FOR PROFIT BETWEEN OR AMONG THE PARTIES HERETO. NOTWITHSTANDING ANY PROVISION HEREIN THAT THE RIGHTS AND LIABILITIES HEREUNDER ARE SEVERAL AND NOT JOINT OR COLLECTIVE, OR THAT THIS AGREEMENT AND OPERATIONS HEREUNDER SHALL NOT CONSTITUTE A PARTNERSHIP. IF, FOR FEDERAL INCOME TAX PURPOSES, THIS AGREEMENT AND THE OPERATIONS HEREUNDER ARE REGARDED AS A PARTNERSHIP, EACH PARTY HEREBY AFFECTED ELECTS TO BE EXCLUDED FROM THE APPLICATION OF ALL OF THE PROVISIONS OF SUBCHAPTER K, CHAPTER 1, SUBTITLE A OF THE INTERNAL REVENUE CODE OF 1954, AS PERMITTED AND AUTHORIZED BY SECTION 761 OF THE CODE AND THE REGULATIONS PROMULGATED THEREUNDER. OPERATOR IS AUTHORIZED AND DIRECTED TO EXECUTE ON BEHALF OF EACH PARTY HEREBY AFFECTED SUCH EVIDENCE OF THIS ELECTION AS MAY BE REQUIRED BY THE SECRETARY OF THE TREASURY OF THE UNITED STATES OR THE FEDERAL INTERNAL REVENUE SERVICE, INCLUDING SPECIFICALLY, BUT NOT BY WAY OF LIMITATION, ALL OF THE RETURNS, STATEMENTS, AND THE DATA REQUIRED BY FEDERAL REGULATIONS 1.761. SHOULD THERE BE ANY REQUIREMENT THAT EACH PARTY HEREBY AFFECTED GIVE FURTHER EVIDENCE OF THIS ELECTION, EACH SUCH PARTY SHALL EXECUTE SUCH DOCUMENTS AND FURNISH SUCH OTHER EVIDENCE AS MAY BE REQUIRED BY THE FEDERAL INTERNAL REVENUE SERVICE OR AS MAY BE NECESSARY TO EVIDENCE THIS ELECTION. NO SUCH PARTY SHALL GIVE ANY NOTICES OR TAKE ANY OTHER ACTION INCONSISTENT WITH THE ELECTION MADE HEREBY. IF ANY PRESENT OR FUTURE INCOME TAX LAWS OF THE STATE OR STATES IN WHICH THE CONTRACT AREA IS LOCATED OR ANY FUTURE INCOME TAX LAWS OF THE UNITED STATES CONTAIN PROVISIONS SIMILAR TO THOSE IN SUBCHAPTER K, CHAPTER 1, SUBTITLE A, OF THE INTERNAL REVENUE CODE OF 1954, UNDER WHICH AN ELECTION SIMILAR TO THAT PROVIDED BY SECTION 761 OF THE CODE IS PERMITTED, EACH PARTY HEREBY AFFECTED SHALL MAKE SUCH ELECTION AS MAY BE

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PERMITTED OR REQUIRED BY SUCH LAWS. IN MAKING THE FOREGOING ELECTION, EACH SUCH PARTY STATES THAT THE INCOME DERIVED BY SUCH PARTY FROM OPERATIONS HEREUNDER CAN BE ADEQUATELY DETERMINED WITHOUT THE COMPUTATION OF PARTNERSHIP TAXABLE INCOME.

The Venture has not requested, and does not intend to request, a ruling from the service that will be treated as a partnership for the federal income tax purposes. As set forth below, however, counsel for the Venture believes that if the question were litigated it is more likely than not that for federal income tax purposes the Venture would be determined to be a partnership and not an association taxable as a corporation. Such treatment for federal income tax purposes depends on the Venture's organization as well as its actual operation.

According to Treasury Regulation Section 301.7701-2, a determination of whether a partnership is to be treated as a partnership or an association taxable as a corporation depends on whether and to what extent there exists the four corporate characteristics of continuity of life, limited liability, free transferability of Interests and centralization of management. A partnership will not be classified as an association taxable as a corporation, according to the regulations, if it lacks at least two of the four corporate characteristics and if it has no other corporate characteristics that are significant in determining its classification. Based on the present federal income tax law, counsel for the Venture believes that if the question were litigated it is more probable than not that it would be determined that the Venture will not have continuity of life, limited liability, centralization of management or free transferability of Interests and will therefore be treated as a Venture for federal income tax purposes and not as an association taxable as a corporation. This conclusion is subject to continuing satisfaction at all times during the existence of the Venture of the following conditions, among others:

- The organization of the Venture will be in accordance with the laws governing Texas Joint Ventures, including the Texas Uniform Partnership Act and the Agreement;
- The operation of the Venture will be in accordance with the Texas Uniform Partnership Act and the Agreement; and
- The Units held by the Managing Venturer and its affiliates, in the aggregate, will not exceed 20% of all outstanding Units of the Venture.

This conclusion is also based on existing Treasury regulations and court decisions, including Phillip G. Larson, 66 T.C. 159 (1976), acq., and Zuckman v. United States, 524 F.2d 729 (Ct. C1. 1975).

While it is anticipated that the Venture will be treated as a Venture for federal income tax purposes, such conclusion is not binding on the service or the courts and is limited to an interpretation of current statutes, regulations and judicial decisions. No assurance can be given that administrative or judicial decisions will not be rendered in the future that would modify such conclusion.

The Managing Venturer represents that condition (a) is true. The Managing Venturer has represented that it will observe conditions (b) and (c).

The Venture should not have continuity of life because under the Agreement the insolvency, bankruptcy, dissolution, removal or resignation of either any Venturer or the Managing Venturer will cause dissolution of the Venture. According to Treasury Regulation Section 301.7701-2(b), if the types of events listed above cause dissolution of a venture, continuity of life does not exist notwithstanding the prior agreement of the remaining Venturers to reconstitute the Venture.

The Venture should not have free transferability of Interests because:

1. the Managing Venturer may not sell, transfer or assign its Managing Venturer's Interest in the Venture without the consent of 51% of the Venturers;
2. the Venturers (other than the Managing Venturer and its affiliates) may not sell, transfer or assign their Interest in the Venture without first offering that Interest to the Managing Venturer is extended to the other Venturers; and
3. assignees of the Venturers (excluding purchasers of Units from the Managing Venturer and its affiliates) will not be entitled to exercise or receive any rights, powers or benefits of a Venturer other than the right to distributions and allocations of net cash flow, net proceeds, federal income tax items and amount realized (all as defined in the Agreement) unless such assignee has been approved and accepted by a vote of 51% of the Venturers in the exercise of their sole and absolute discretion.

Treasury Regulation Section 301.7701-2(e) states that an organization will have the characteristics of free transferability of Interests only if those members owning substantially all of the Interests in the organization have the power, without the consent of other members to substitute for themselves in the same organization a person who is not a member of the organization. The characteristic of free transferability of Interests will not exist if each member can assign only his right to share in profits without the consent of other members but cannot assign his right to participate in the management of the organization. The Units held by the Managing Venturer has represented that the Managing Venturer and its affiliates will not acquire or hold Units in excess of 20% of the total Units outstanding. Therefore, at least 80% of all the Interests in the Venture, and thus substantially all of such Interests, would lack the corporate characteristic of free transferability of Interests.

Pursuant to Treasury Regulation Section 301.7701-2(c) (1), the corporate characteristic of centralization of management exists if any person (or group composed of less than all members of the organization) has the continuing exclusive authority to make the management decisions necessary to conduct the business for which the organization was formed. Under the provisions of the Agreement, the Venturers have delegated broad management powers to the Managing Venturer with respect to the day-to-day Operations. However, Treasury Regulation Section 301.7701-2(c)(4) provides that because of the mutual agency relationship existing between members of a general partnership subject to a statute corresponding to the Uniform partnership Act, a general partnership cannot achieve centralization of management. This is because under state law each Venturer has the power (as opposed to the contractual right) to bind the Venture in dealing with third-party creditors without notice of the delegation of authority to the Managing Venturer. Accordingly, the Venture should not be viewed as possessing the corporate characteristic centralization of management.

An organization has the corporate characteristic of limited liability if, under local law, no member is personally liable for the debts of the organization. Treasury Regulation Section 301.7701-2(d)(1) specifically provides that in "the case of a general partnership subject to a statute corresponding to the Uniform Partnership Act, personal liability exists with respect to each general partner." Inasmuch as the Venture has been organized in accordance with the laws governing Joint Ventures and the Texas Uniform Partnership Act (the "Act"), so long as the Venture is operated in conformity with the Act and the Agreement, the corporate characteristic of limited liability should not exist.

If the Venture were classified as an association for any taxable year, the Venture would be taxed as a corporation, the taxable income of the Venture for such year would be subject to federal income tax at corporate tax rates, the Venturers would be treated as shareholders and distributions by the Venture, if and when made, would be taxable to the Venturers as dividends or otherwise treated as corporate distributions. In such event, there would be no flow through of items of Venture income, deduction, gain or loss to the Partners, with the result that most of the tax benefits mentioned below would not be available to the Venturers.

TRUSTS TAXED AS CORPORATIONS

Any trust participating in the Venture, as a result of its participation, may be treated for federal income tax purposes as an association taxable as a corporation. As such, all income would be taxed at corporate rates at the corporate level, whether or not such income was distributed to the beneficiaries. Treasury regulations indicate that trusts created by beneficiaries as a device to carry on a profit-making business that normally would have been carried on through a more traditional business organization may be taxed as a corporation or partnership under the Code. Such a characterization would depend in part on a factual determination of whether the particular trust had associates and an objective to carry on business and divide gains therefrom. (See Treasury Regulation Sections 301.7701-4(b) and 301.7701-2(a)(2).)

It is possible that a trust's ownership of a Venture Interest may itself, or in combination with other factors, cause the trust to be considered engaged in a trade or business and be taxable as an association. At least two cases have held that limited partners may be considered engaged in the trade or business in which the partnership itself is engaged. (See Don Roy. Ltd. v. United States, 301 F.2d 200 (9th Cir. 1962); George A. Butler, 36 T.C. 1097 (1961).) The determination of when one is engaged in a trade or business is in part a question of fact. The Venture, however, will be engaged in a trade or business if it is operated in the manner presently contemplated.

INTANGIBLE COSTS

The Venture will allocate to the Venturers their proportionate share of intangible drilling and development costs ("Intangible Costs"). Assuming a proper election by the Venture, each Venturer will be entitled to deduct his share of the Intangible Costs that have been properly allocated to the Venturers under the Agreement assuming such costs are properly classified as Intangible Costs and are not non-deductible capital costs or some other costs that are not currently deductible. The Agreement obligates the Managing Venturer to cause the Venture to elect to deduct those expenses or costs that may be deducted pursuant to Code section 2638 and the Treasury regulations issued, or to be issued, relating to the deduction of Intangible Costs.

This election to expense Intangible Costs will only apply to expenses incurred incident to and necessary for the drilling of wells and the preparation of wells for production of oil and gas. For purposes of this election to expense, the Third Circuit Court of Appeals and the Service have defined a "well" as a shaft drilled in search of hydrocarbons, which is designed and drilled to be capable, on encountering hydrocarbons and on appropriate completion of the shaft by the Operator, of conducting or aiding in the condition of hydrocarbons to the surface. This definition of "well" excludes shafts, such as core drilling, that because of design or manner in which they are drilled are incapable of conducting or aiding in the conduction of hydrocarbons to the surface. Such shafts are capable of solely yielding geological information. However, if an appropriately drilled shaft is drilled in search of hydrocarbons, it is a well regardless of whether there is intent to produce hydrocarbons. (See Sun Co. v. Commissioner, 677 F.2d 294 (3d Cir. 1982); Rev. Rule. 88-10, 1988-31.R.B.53.) The Venture intends to drill shafts that meet this definition of "well" and that will be eligible for the election to expense. However, the Venturers will not be able to expense the costs of any shaft drilled by the Venture that do not satisfy this definition.

The Venture will enter into the Operating Agreement with the Managing Venturer, in its individual capacity, with respect to services to be performed in connection with the organization of the Venture and drilling, testing and, if attempted, the completion of the Prospect Wells. Payment of the drilling and completion costs will entitle the Venture, as an owner of the Working Interest, to have such Prospect Well on the Prospect drilled, tested and, if attempted, completed.

It is possible that the costs allocable to drilling, testing and completing the Prospect Wells will exceed the cost paid to the Managing Venturer of drilling, testing and completing the Prospect Wells and may exceed rates charged by third parties for similar wells in the locality. Although the Tax Court recognized in Brountas v. Commissioner, 73 T.C.491 (1979), that a markup over estimated cost is regularly charged by operators or drilling contractors for certain turnkey contracts, and although the Managing Venturer believes that the rates allocable to drilling, testing and completing the Prospect Wells is at or competitive with rates charge by third parties for similar wells in the locality, there is a risk that a portion of the costs paid to the Managing Venturer by the Venture and treated as deductible Intangible Costs could be reclassified as acreage acquisition costs, tangible costs, or some other costs that are not currently deductible. If any such positions of the Service were tangible costs, or some other costs that are not currently deductible. If any such position of the Service were sustained, the deductions attributable to that portion of the costs could be disallowed, reduced or delayed, and the tax liability of the Venturers would be increased. The issue as to the allocation of the costs charged by the Managing Venturer between deductible Intangible Costs, deductible other costs, nondeductible tangible costs and other nondeductible capital costs and the reasonableness thereof are factual and to a certain extent predicated upon future events. For that reason, Counsel to the Venture cannot predict the outcome of a challenge with regard to this matter. Nevertheless, Counsel to the Venture is of the opinion that if the question were litigated, it is more likely than not that a portion of the rates paid to the Managing Venturer would be determined to be deductible as Intangible Costs.

If an oil or gas property of the Venture or an Interest in the Venture is sold at a gain, amounts deducted for Intangible Costs must be recaptured on such disposition. Therefore, gain would be ordinary income to the extent Intangible Costs have been deducted if, but for the deduction, they would have been reflected in the adjusted basis of the property. Moreover, in certain circumstances, Intangible Costs deductions will be considered items of tax preference. See "Tax Preference Income: Alternative Minimum Tax." Finally, integrated producers must capitalize 30% of otherwise deductible Intangible Costs. This 30% amount may be amortized over a five year period.

FARMOUT AND FARMIN AGREEMENTS

Although the Venture has no present plans to enter into a farmout on behalf of the Venture, the Agreement authorized the Venture to enter into a farmout under the certain circumstances. A farmout allows the holder of an oil and gas working interest ("Farmor") to shift the initial wells dry hole risk to another party through a sharing arrangement. In a typical transaction the Farmor might assign all (or a portion) of its working interest in a drill site to the assignee ("Farmee") in exchange for the Farmee's agreement to bear all costs

of the obligation well on the drill site. Such agreement generally also provides that (1) the Farmee earns an interest in the Farmor's additional acreage surrounding the drill site, (2) the Farmee is entitled to payout on the obligation well, and (3) after payout, a portion of the drill site working interest reverts to the Farmor.

Historically, for federal tax purposes, the Farmee has deducted 100% of the Intangible Costs incurred in drilling the obligation well and has treated 100% of the capital expenses as expenditures subject to depreciation. The Service has taken the position in Revenue Ruling 77-176, 1977-1 C.B. 77, that although the Farmee is entitled to deduct the Intangible Costs actually paid or incurred in drilling and completing the obligation well, the transferred portion of the working interest in the Farmor's additional acreage surrounding the drill site constitutes compensation in the form of property to the Farmee for undertaking the development project on the drill site. Consequently, the fair market value of such working interest, determined as of the date of its transfer to the Farmee, is includable in the Farmee's gross income in the year the well is completed or when the working interest in the additional acreage is transferred to the Farmee, whichever is earlier. With respect to the fraction of the working interest in the acreage exclusive of the drill site transferred by the Farmor to the Farmee, the Farmor is to be treated as having sold such interest for its fair market value on the date of transfer and having paid the cash proceeds to the Farmee as additional compensation to the Farmee for undertaking the development project on the drill site. This treatment may result in taxable income to the Farmor, a factor generally not present under prior tax treatment of these types of transactions.

If the Venture enters into a farmout, the Managing Venturer will attempt to minimize the effect of Revenue Ruling 77-176 in negotiating any farmout or farming transactions on behalf of the Venture. However, to the extent any such transaction produces taxable income under the ruling; the Venturers' tax liability attributable to such transaction may exceed cash distributed from the Venture. In addition, the fair market value of such property is a factual question and may be adjusted by the Service to produce additional tax liabilities for the Venturers.

DEPLETION

Code section 611 allows as a deduction against income received from the oil or gas produced each year a reasonable allowance for depletion. The depletion deduction is the greater of percentage depletion at the applicable rate, if available, or cost depletion. Cost depletion allows the recovery of capitalized costs (such as bonus, other lease acquisition costs, exploratory charges, legal fees and certain other capitalized, non-depreciable costs) of a producing property over its life by an annual deduction computed on the basis of the actual oil and gas sold each year in relation to estimated recoverable oil and gas. Percentage depletion, if applicable, is an annual statutory allowance equal to a percentage of the gross income from the depletable property (but in no event exceeding 100% of the taxable income from the property before allowance for depletion) computed without regard to the costs associated with the property. Deductions resulting from percentage depletion can therefore exceed total costs associated with acquisition of the property. However, on sale of the property, the portion of the gain that represents Intangible Costs and depletion that reduced the basis of the property will be recaptured as ordinary income. In addition, "excess percentage depletion" constitutes an item of "tax preference income" as hereinafter described. See "Tax Preference Income: Alternative Minimum Tax." The available of percentage depletion, under the provisions of Code section 613A, is now largely dependent on the personal tax situation of each individual Participant. ACCORDINGLY, EACH PROSPECTIVE PARTICIPANT SHOULD CONSULT WITH HIS PERSONAL TAX ADVISOR CONCERNING THE AVAILABILITY TO HIM OF PERCENTAGE DEPLETION.

Except for certain natural gas production, percentage depletion is generally available only with respect to a limited amount of domestic crude oil or domestic natural gas production of each taxpayer, under the so-called "independent producer exemption." The first 1,000 barrels per day of a taxpayer's domestic oil production or the first 6,000,000 cubic feet per day of a taxpayer's domestic gas production may qualify for the percentage depletion allowance under the "independent producer exemption." The applicable rate of percentage depletion on oil and gas production under the "independent producer exemption" is 15%. Varying percentage depletion rates will apply to marginal properties. The rate will increase one percentage point for each whole dollar by which the reference price of a barrel of crude oil is below $20, but the rate can't exceed 25%. The reference price is the average annual decontrolled wellhead price of crude oil as estimated by the Secretary of the Treasury. It is determined on a calendar year basis. The reference price for the previous year is determined on a calendar year basis. THE REFERENCE PRICE FOR THE PREVIOUS YEAR DETERMINES THE RATE FOR THE CURRENT YEAR. FOR EXAMPLE, 1991'S REFERENCE PRICE WAS $16.50 ($3.50 UNDER $20.00) SO 1992'S PERCENTAGE DEPLETION RATE ON MARGINAL PROPERTIES WAS 18%. 1992'S REFERENCE PRICE WAS $15.98. IT IS TO BE ANNOUNCED EACH YEAR BY APRIL 1ST. 1990'S REFERENCE PRICE WAS $20.03. THE DEPLETION DEDUCTION UNDER THE "INDEPENDENT PRODUCER EXEMPTION" MAY NOT EXCEED 65% OF THE TAXPAYER'S TAXABLE INCOME FOR THE YEAR, WITHOUT REGARD TO CERTAIN DEDUCTIONS AND SUBJECT TO A CARRY-OVER OF THE UNUSED PORTION OF THE DEDUCTION. FOR A TRUST, THE 65% LIMITATION IS COMPUTED WITHOUT A DEDUCTION FOR THE DISTRIBUTIONS TO BENEFICIARIES DURING THE TAXABLE YEAR.

The "independent producer exemption" is not available to a taxpayer (a) who refines more than 50,000 barrels of oil on any one day in a taxable year; or (b) who directly or through certain related persons sells oil or gas or any product derived therefrom (i) through a retail outlet operated by him or certain related persons, or (ii) to any person who occupies a retail outlet that is owned and controlled by the taxpayer or certain related persons, provided that the gross receipts from such sales exceed $5,000,000.

The Venture will not compute the depletion allowance. Instead, each Venturer must separately compute his own depletion allowance with respect to his allowable share of Venture property and reduce the adjusted basis of his Venture Interest (but not below zero) by the amount of such depletion deduction to the extent such deduction does not exceed the basis allocated to that Venturer oil and gas property with respect to which the deduction is claimed. Each potential Venturer is urged to consult his tax counsel with respect to the availability to him of the percentage depletion allowance. Many uncertainties exist with respect to the interpretation of these provisions of the Code.

PREPAYMENT OF CERTAIN COSTS

If all Units are subscribed prior to October 30, in the current year, the Managing Venturer expects to expend Initial Venture Capital during the current year to obtain deductions for Intangible Costs in this calendar year. However, if the Venture pays for drilling, testing or completion in the current year but all or a portion of the drilling, testing or completion does not take place until the following year, the deduction for Intangible Costs in the current year would be limited to that portion of the payments represented by actual drilling, testing or completion activities in current year unless such activities are commenced within 90 days after the close of the taxable year (March 31, of the subsequent year), the prepayment is not a deposit, there is a business purpose for the prepayment and the deduction does not materially distort income.

DEPRECIATION

The cost of casing, tubing, tanks, pumping units and other types of tangible property and equipment cannot be deducted currently, but must be capitalized and depreciated or amortized pursuant to applicable provisions of the Code. Under the accelerated cost recovery system ("MACRS") it is likely the cost of most of the tangible personal property to be acquired by the Venture will be depreciated over either a five year recovery period (available for property with a class life of more than four years but less than ten years) or a seven year recovery period (available for property that has a class life of ten or more years but less than sixteen years). This property would be depreciated on the 200% declining balance method switching to the straight line method for the first taxable year the straight line method would yield a larger allowance. It is likely that the Venture will have a taxable year of less than 12 months. WEIR 1986 indicates that, in the case of a taxable year of less than 12 months, property is to be treated as being placed in service for half the number of months in such taxable year. (See Conference Report to Accompany HR 3838, Rep. No. 99-841, 99th Cong., 2d Sess. at II-46 (September 16, 1986) (Statement of the Managers).) Consequently, first year depreciation will be computed as if the property was placed in service at the midpoint of the taxable year. Finally, any depreciation allowable on such tangible property and equipment may also be subject to recapture as ordinary income on transfer of the property or Venture Interest.

LEASEHOLD COST AND ABANDONMENT

The cost of acquiring oil and gas lease interests, or other similar oil and gas property interests, is a capital expenditure that may not be deducted in the year paid or incurred. However, if a lease is proved to be worthless by drilling or abandonment, the cost of that lease constitutes a loss and is deductible for federal income tax purposes. The federal income tax deduction for the loss, however, must be taken by the Venturers, individually, rather than by the Venture and allocated to the Venturers. The deduction for such loss is taken in the year in which the lease becomes worthless or is abandoned.

VENTURE ORGANIZATION EXPENSES

Expenses connected with the organization and capitalization of the Venture, known as syndication fees, are not deductible by the Venturers or the Venture and are not eligible for the 60-month amortization period accorded to organizational expenses. Syndication fees include expenditures connected with the initial capitalization of the Venture, such as sales commissions, some professional fees, selling expenses and printing costs. Under Treasury regulations, such syndication expenses are not deductible. Such expenses are instead capitalized, thereby reducing the gain, if any, which would otherwise be recognized on the liquidation of the Venture.

Other expenses incident to the organization of the Venture and chargeable to a capital account may be amortized over the ascertainable life of the Venture. If a proper election is made by the Venture, these expenses may be deducted through amortization over a period of not less than 60 months. If the Venture is liquidated within the 60-month period, the Venture should be able to deduct as a loss the balance of the deferred expenses.

All Organizational Costs incurred in connection with the organization and capitalization of the Venture, except for commissions, will be paid by the Managing Venturer out of its Management Fee. The Managing Venturer intends to allocate a portion of its Management Fee attributable to Organizational Costs to non-amortizable syndication expenses and a portion to amortization organization expenses. There can be no assurance that the Service will not take the position that some of the expenses treated by the Venture as amortizable organization expenses or deductible Intangible Costs are non-amortizable syndication expenses and that lay such claim by the Service would not be sustained by the courts if litigated. Further, no assurance can be given that amounts allocated by the Venture to amortizable organization expense should instead be capitalized as part of the cost of the Prospect. If the Service were successful in this contention, the Venturers would not be able to amortize amounts otherwise allocable to amortizable organization expenses.

MANAGEMENT FEES

Management fees paid by the Venture will be deductible only to the extent such fees are ordinary and necessary business expenses and are reasonable in amount. (See code sections 162 and 707.) The Managing Venturer will determine whether all or only part of the amounts paid for the management fee for Initial Operations or management fee for assessments, if any, paid by the Venture are properly deductible under the Code in the year paid. The issue as to the allocation of such management fees between deductible ordinary and necessary business expenses, organization and Venture costs, and other costs required to be capitalized, if any, and the reasonableness thereof, are inherently factual and, to a certain extent, predicated upon future events. For that reason, Counsel to the Venture cannot predict the outcome of a challenge with regard to these matters. There can be no assurance that the Service will not attempt to disallow, in whole or in part, a deduction for management fees that the Managing Venturer determines are properly deductible and that, if litigated, any such position by the Service would not be sustained by the courts, at least as to a portion of such fees. There is a substantial risk that any portion of the management fees treated as a deductible payment could be reclassified in whole or in part as a syndication fee, an organization expense, a lease acquisition cost, a payment for services to be performed over the life of the Venture or for some other cost that is not currently deductible. If any such position of the Service were sustained, the deductions attributable to the payment of the management fees would be disallowed, reduced or delayed, and the tax liability of the Venturers of the Venture would be increased.

ORGANIZATION AND ADMINISTRATIVE EXPENSES

Under the terms of this Memorandum and the Agreement, the Managing Venturer will be reimbursed for Organization and Administrative Expenses incurred in the course of conducting the business of the Venture. Under the Code, the reimbursements will be deductible only if they constitute ordinary and necessary business expenses. The Managing Venturer will cause the Venture to deduct the reimbursement for Organization and Administrative Expenses as an ordinary and necessary business expense. Because of the factual questions involved in determining what constitutes ordinary and necessary business expenses, there can be no assurance that the Service will not challenge the deduction.

TAX BASIS IN VENTURE INTEREST

The tax basis of a Venturer in its Venture Interest is important for several reasons including, but not limited to, determining: (1) the current deductibility of a Venturer's distributive share of Venture losses; (2) income tax consequences of distributions; and (3) gain or loss on the sale of a Venture Interest. A Venturer's adjusted basis in its Interest in the Venture will be its capital contribution to the Venture increased by: (a) its distributive share of Venture income and gain (including tax-exempt income); and (b) its share of liabilities of the Venture for federal income tax purposes; and decreased (but not below zero) by: (I) distributions from the Venture to

the Venturer; (ii) its distributive share of Venture losses; (iii) its share of any reduction in the Venture's liabilities to the extent such liability was included in its basis; (iv) its share of non-deductible expenses of the Venture that are not properly chargeable to a capital account; and (v) the amount of the Venturer's deduction for depletion attributable to Venture oil or gas property to the extent such deduction does not exceed the basis of such property allocated to that Venturer.

Code section 613Ac (7)(D) requires each individual Venturer, rather than the Venture, to compute depletion and gain or loss on the sale, exchange or abandonment of oil or gas property. Proposed regulations issued under Code section 705, however, provide for an adjustment to the basis of a Venturer's Venture Interest for gain recognized on the Venture's disposition of oil or gas property.

TREATMENT OF CASH DISTRIBUTIONS FROM THE VENTURE

A Venturer generally will not recognize gain or loss for federal income tax purposes when he receives a cash distribution from the Venture in respect of, and not in liquidation of, his Venture Interest so long as it is not in exchange for his Interest in "unrealized receivables" (which include potential recapture of depletion, intangible costs and MACRS deductions) or "inventory items" that have substantially appreciated in value. A Venturer will recognize gain on cash distributions (including any reduction in Venture indebtedness for which no Venturer is personally liable) that exceed the adjusted basis in his Venture Interest immediately prior to such distribution. (See also "At Risk Recapture of Losses" below.)

TAX ON SELF-EMPLOYMENT INCOME

Individuals are required to pay a tax on their income from self-employment that is from carrying on a trade or business as a sole proprietor or as a partner. The tax is designed to afford social security coverage to self-employed individuals. The tax is levied as part of the estimated tax liability of self-employed persons. The self-employment tax is imposed on "self-employment income," which is based on "net earnings from self-employment." Net earnings from self-employment include a Joint Venturer's distributive share (whether or not distributed) of income or loss from any reader or business carried on by his Venture.

SALES OF VENTURE PROPERTY

Under the Code, if property used in a trade or business, including a working interest in oil or gas property, is sold and if the seller is not a dealer in such property, gain on such property held more than one year will be a "Section 1231 gain," subject however to recapture of MACRS, depletion and intangible costs (which recapture is taxed as ordinary income). Section 1231 gain passes through to the Venturer's and Venturer must combine his share of Venture Section 1231 gain with his personal Section 1231 gains and losses. Except as otherwise provided in the rules relating to" non-recaptured net Section 1231 losses, the excess of Section 1231 gains over Section 1231 lost, constitutes long-term capital gain. However, net Section 1231 gain will be ordinary income to the extent it does not exceed the "non-recaptured net Section 1231 losses." Non-recaptured net Section 1231 losses will include all net Section 1231 losses claimed for the five most recent preceding taxable years to the extent they have not previously been recaptured (i.e., converted into ordinary income).

Section 1231 gains and losses characterized as capital gains and losses are combined with all the taxpayer's other capital gains and losses. A non-corporate taxpayer's net capital gain (i.e., the excess of net long-term capital gain over net short-term capital loss) is currently subject to tax at a maximum tax rate of 28%. A non-corporate taxpayer may deduct losses from sales or exchanges of capital assets to the extent of his gains from such sales or exchanges plus the lesser of (I) $3,000 or (ii) the excess of such losses over such gains. See also "Tax Preference Income: Alternative Minimum Tax."

SALES OF INTEREST IN THE VENTURE

If a Venturer sells his Interest in the Venture pursuant to the provisions of the Agreement, he will recognize taxable gain or loss on the sale measured by the difference between the amount realized by him on such sale and his adjusted tax basis in his Venture Interest. The amount realized by such Venturer will include his allocable share of Venture debt, if any, as well as the amounts paid to him as a result of the sale. If the Venture Interest has been held by the selling Venturer for more than one year, the realized and recognized gain or loss on the sale will be taxed as long-term capital gains or loss, except to the extent the sale price is attributable to unrealized receivables (which includes MACRS, depletion and Intangible Cost recapture) or substantially appreciated inventory. The portion of the sale price attributable to those items will be taxed to the selling Venturer as ordinary income.

LIQUIDATION OF THE VENTURE

On expiration of its term or as otherwise provided in the Agreement, the Venture will dissolve and, if not reconstituted, after payment of its liabilities, distribute its property or proceeds from the sale of its property to the Venturers in complete liquidation. The Venture will not recognize gain or loss as a result of the liquidating distribution. Each Venturer will recognize gain or loss as a result of the Venturer's sale of its assets. Assuming each item of Venture property is distributed to the Venturers on a pro rata basis, each Venturer will recognize gain to the extent any money distributed exceeds the adjusted basis of such Venturer's Interest in the Venture immediately before the distribution. A Venturer will recognize loss on the liquidating distribution if no property other than cash, unrealized receivables (which include MACRS, depletion and Intangible Cost recapture) and inventory are distributed to a Venturer. Such Venturer will recognize such loss only to the extent the adjusted basis of such Venturer's Interest in the Venture exceed the sum of the cash, the basis of unrealized receivables (which include MACRS, depletion and Intangible Cost recapture) and the basis of inventory distributed. The basis of property distributed to each Venturer (other than cash) will be an amount equal to the adjusted basis of such Venturer's Interest in the Venture described herein reflect only the general rules for such a liquidating distribution. On actual liquidation of the Venture, various exceptions to these rules may alter the tax consequences described above.

TERMINATION OF THE VENTURE

Under Code section 708(b)(1)(B), a venture will terminate for tax purposes if 50% or more of the Interests in the venture's capital and profits are sold or exchanged within a single twelve-month period. To prevent this occurrence, the Agreement provides that a Venturer may not transfer his Venture Interest unless he presents to the Managing Venturer an opinion of counsel satisfactory Managing Venturer to the effect that such transfer does not cause the Venture to terminate within the meaning of Code section 708(b)(1)(B). However, it is possible that there could be transfers of Venture Interests in breach of this contractual provision.

Treasury Regulation section 1.708-1(b)(1)(ii) provides that neither the liquidation of a Venture Interest nor the contribution of property to a venture constitutes a "sale or exchange" within the meaning of Code section 708. Consequently, the abandonment of a

Venturer's Interest in the Venture because of his failure to contribute his Completion Assessment or the reduction of a Venturer's relative Interest in the Venture because of his failure to contribute Optional Additional Assessments should not constitute a "sale or exchange" within the meaning of Code section 708. Nevertheless, if within a short time before or after such reduction, the reduced Venturer received distribution from the Venture and another Venturer made a contribution to the Venture, the Service may take the position, under principles set forth in Treasury Regulation sections 1.708-1(b)(1)(ii) and 1.731-1(c)(3), that such reduction constituted a sale or exchange of such reduces Venturer's Interest in the Venture. If within a twelve-month period 50% or more of the Interests of the Venturers in the Venture were shifted, under such circumstances, the Venture may be deemed to have terminated within the meaning of Code section 708. A termination of the Venture could cause a Venturer to recognize gain upon the deemed distribution of Venture assets and property to the Venturers in connection with such termination.

ACTIVITIES ENGAGED IN FOR PROFIT

Code section 183 provides that if an activity is not "engaged in for profit," the only amounts deductible with respect to that activity are: (1) those expenses that would be deductible whether or not incurred in connection with an activity engaged in for profit, (e.g., certain interest and taxes); and (2) those expenses otherwise deductible had the activity been engaged in for profit, but only to the extent of the income from the activity, reduced by otherwise allowable non-business deductions. Although Code section 183(a) refers to an activity, refers to an activity engages in by an individual, it also applies to the activities of a partner in a partnership. (See Revenue Ruling 77-320, 1977-2C.B. 78; Edward B. Hager 76 T.C. 759(1981).) Moreover, in determining whether Code section 183 applies to a partnership, the Tax Court has determined that the question is whether the Commissioner, 88 T.C. 464(1987) and Brannen v. Commissioner, 78 T.C. 471 (1982). However, it is possible that the Service might take the position that Code section 183 will also apply to an individual partner of a partnership or a Joint Venturer in a Joint Venture if that Venturer lacks the proper profit objective, notwithstanding the existence of such objective at the partnership or Joint Venture level. If it is determined the Venture or a Venturer is not engaged in an activity for profit, a substantial portion of the deductions arising from Venture operations could be disallowed. The issue of whether an activity is engaged in for profit is primarily a question of fact. The resolution of this issue may be based in part on the intent of the Venturers, as evidenced by objective factors.

THEREFORE, NO ONE SHOULD PARTICIPATE IN THE VENTURE UNLESS HIS OBJECTIVE IS TO SECURE AN ECONOMIC PROFIT SEPARATE AND APART FROM ANY TAX BENEFITS THAT MAY FLOW FROM THE VENTURE. Because of the factual nature of this issue, Counsel to the Venture cannot predict the outcome of a challenge under Code 183.

ALLOCATIONS

Under the Code section 704, allocations of all Venture items of income, gain, loss, deduction and credit must have "substantial economic effect" to be recognized for federal income tax purposes. Regulations issued under Code section 704(b) provide that an allocation will give substantial economic effect must be substantial.

With respect to the second test, the regulations provide that generally the economic effect of an allocation is substantial if there is a reasonable possibility that the allocation (or allocation) will affect substantially the dollar amounts to be received by the partners from the partnership, independent of tax consequences. However, the regulations provide that the economic effect of an allocation (or allocations) is not substantial if at the time the allocation becomes part of the partnership agreement: (I) the after-tax economic consequences of at least one partner may, in present value terms, be enhances compared to such consequences if the allocation (or allocations) were not contained in the partnership agreement; and (ii) if there is a strong likelihood that the after tax economic consequences of no partner will in present value terms, be substantially diminished compared to such consequences if the allocation (or allocations) were not contained in the partnership agreement.

According to the regulations, an allocation will have economic effect if the partner to whom the allocation is made receives the economic consequences of no partner will, in present value terms, be substantially diminished compared to such consequences if the allocation (or allocations) were not contained in the partnership agreement.

According to the regulations, an allocation will have economic effect if the partner to whom the allocation is made receives the economic benefit or bears the economic burden or risk associated with the allocation. The regulations state that, in general, an allocation will have economic effect if throughout the term of the partnership the partnership agreement:

1. provides for the determination and maintenance of the partners' capital accounts in accordance with the rules set forth in the regulations;
2. requires that on liquidation of the partnership (or any partners' interest in the partnership), liquidating distributions must in all cases be made by the later of the end of the taxable year in which the liquidation occurs or 90 days after the liquidation, in accordance with the positive capital account balances of the partners; and
3. either obligates a partner with a deficit in his capital account following the liquidation of his interest in the partnership to restore such deficit or contain a "qualified income offset" pursuant to which a partner that unexpectedly receives an allocation, adjustment or distribution described in Treasury Regulation 1.704-1(b)(2)(ii)(d)(4), (5) or (6) will be allocated income and gain in an amount and manner sufficient to eliminate any deficit capital account balance of such partner as quickly as possible.

If a partnership agreement contains a qualified income offset instead of a deficit restoration clause (as does the Partnership Agreement) the allocation will have economic effect only to the extent it does not create or increase a deficit capital account balance.

In each case, capital account balances must be determined after taking into account all adjustments for the partnerships taxable year in which the liquidation occurs (other than the adjustments made pursuant to (2) or (3) above). The courts have also used a capital account analysis to determine whether an allocation should be recognized for federal income tax purposes (i.e., <u>Allison v. United States</u>, 701 F.2d 933 (Fed. Cir. 1983)); <u>Goldfine v. Commissioner</u>, 80 T.C. 843 (1983); <u>Holladay v. Commissioner</u>, 72, T.C. 571 (1979), aff'd, 649 F.2d 1176 (5th Cir. 1981); <u>Orrich v. Commissioner</u>, 55 T.C. 395 (1970).

The regulations set forth special rules regarding allocations with respect to oil or gas property and corresponding adjustments to capital accounts. Code sections 613A(c)(7)(D) provides for the allocation of partnership depletion basis to the partners as of the date the partnership acquires the property, so that each partner may separately determine his depletion deduction with respect to the property and gain or loss on the disposition of such property. Consequently, these items are not partnership items and would not be

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reflected in the partners' capital accounts. The regulations set forth rules for determining "simulated" depletion and gain or loss on the sale of partnership oil or gas properties for purposes of adjusting the partners' capital accounts. The agreement provides for the calculation of these "simulated" amounts and allocates them in the same proportions the Venturers were allocated adjusted basis with respect to Venture oil and gas property. The application of these rules on liquidation of the Venture appears to be in conflict with the general rule that liquidating distributions must be made on the basis of capital account balances. In an attempt to comply with all of the rules set forth in the regulations, the Agreement initially provides for the distribution of oil or gas property in kind or of the cash realized from the sale thereof to the Venturers in the same proportions the Venturers were allocated basis in such depletion property, with corresponding adjustments to Capital Accounts. Then, after all allocations and the corresponding adjustments to Capital Accounts as provided in the Agreement, the remaining Venture property or cash realized from the sale thereof will be distributed to the Venturers in accordance with their Capital Account balances (the computation of which is defined in the Agreement).

Code section 613A(c)(7)(D) provides that a partnership must allocate to each partner as of the date of acquisition of an oil or gas property his proportionate share of the adjusted basis of the property as determined in accordance with his interest in capital or income. Code section 613A(c)(7)(D) and the proposed regulations issued thereunder provide that a partner's proportionate share of the adjusted basis of partnership property shall be determined in accordance with his interest in partnership capital. However, a partner's share of the adjusted basis of partnership property may be determined in accordance with his interest in the partnership if the partnership agreement so provides, unless either:

a. written provision has been made for the share of any partnership income to be reduces for any purpose other than merely to reflect the admission of a new partner, or
b. at the time of allocation any partner expects his income interest to be reduces pursuant to an understanding with another partner or partners.

Under the regulations issued pursuant to Code section 704(b) allocations of partnership basis of oil or gas properties will be recognized as being in accordance with the partners interests in partnership capital under Code section 613A(c)(7)(D) provided:

(i) such allocations do not give rise to capital account adjustments under Treasury Regulation section 1.704-1(b)(2)(iv)(k) the economic effects of which are insubstantial, and

c. all other allocations and capital account adjustments under the partnership agreement are recognized under Treasury Regulation section 1.704-1(b)(4)(v).

Otherwise, such adjusted basis must be allocated among the partners pursuant to Code section 613A(c)(7)(D) in accordance with the partners actual interests in partnership capital or income. The agreement allocates basis depletion properties in the proportion the Venturers share Net Cash Flow, Net Proceeds and Federal Income Tax Items (as defined in the Agreement) as of the date of acquisition of such oil or gas property. While the question is primarily one of fact, Counsel to the Venture believes it is more likely than not that this allocation of basis will be recognized as being in accordance with the Venturers' interest in Venture capital or income under Code section 613A(c)(7)(D).

If less than all the Venturers participate in a Subsequent Operation, The Managing Venturer may admit additional Venturers to obtain sufficient funds to undertake the Subsequent Operation, subject to an appropriate Vote of the Venturers. If the Subsequent Operation is undertaken on a newly acquired oil and gas property, the basis of property will be allocated among the Venturers (including any additional Venturers) participating in the Subsequent Operation. If, on the other hand, the Subsequent Operation is undertaken on the property previously acquired by the Venture, it is possible that the additional Venturer will not be permitted to claim either cost or percentage depletion with respect to any income for the wells drilled in the Subsequent Operation. Percentage depletion may not be available to the additional Venturers if after Initial Operations the property constitutes proven property. Venturers only claim cost depletion to the extent of their basis in the Venture's oil and gas properties. (See "Tax Considerations - Depletion.") If the Subsequent Operation is conducted on the basis in that property that had previously been allocated to the Venturers that did not participate in the Subsequent Operation. However, there is no clear authority for such a reallocation. The Venture was required to allocate the basis of each oil and gas property on the date it acquired that property, and the Code contains no provision for reallocating that basis to newly admitted Venturers. Consequently, no assurance can be given that the Venture will be permitted to reallocate the basis of any oil and gas property. Finally, because it is likely that any oil and gas property acquired by the Venture will have a low original cost to the Venture, the amount of cost depletion that can be claimed with respect to production from any such property be nominal.

In Hamilton v. United States, 687 F 2nd 408 (Ct. Cl. 1982), the limited partners contributed 95% of the capital of the partnership and were allocated 95% of the income, expenses and losses until they reach payout. After payout, all allocations shifted to 60% for the limited partners and 40% for the general partners. If the partnership was liquidated prior to payout, the general partners would receive 40% of the partnership assets subject to the right of the limited partner to recover a share of their investment in the form of a net profits interest. The Service argued that the sharing arrangement set up by the partnership agreement was a 60:40 partnership with the limited partners making a nonrecourse loan of 35% of the partnership capital to the general partners. The Service argued that throughout the term of the partnership, the allocations of all partnership federal income tax items should have been made in accordance with this 60:40 split. The court rejected this "loan" argument holding that it was contrary to the economic reality of the partnership agreement. The court noted that the key factor behind any analysis of the validity of a partnership allocation is that the allocation must reflect the true economic substance of the partners' agreement.

The regulation under Code section 704(b) set forth an example of a real estate limited partnership in which partnership net taxable income and net taxable loss would be allocated 99% to the limited partner until cumulative net taxable income allocated for all taxable years is equal to the cumulative net taxable loss previously allocated to the partners. The example concludes that since the partnership agreement contains provisions that met the three requirements for economic effect cited above, the allocations in the Agreement had economic effect. Counsel to the Venture believes that if the Service challenged the allocations in the Agreement on the basis of the argument set forth in Hamilton, it is more likely than not that the allocations would be upheld as written in the Agreement.

The allocations of Federal Income Tax Items to the Venturers made in the Agreement should satisfy the "substantiality" portion of the test in the regulations because the economic consequences of the allocations should be equivalent to the tax consequences of such allocations. Likewise the allocation of Federal Income Tax Items to the Venturers made in the Agreement should have "economic effect" since the Agreement contains the three requirements for economic effect listed above.

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ELECTION TO ADJUST TAX BASIS OF VENTURE PROPERTY

As a result of the tax accounting complexities inherent in, and the substantial expense that would be attendant to, making the election to adjust the tax basis of Venture property provided by Code sections 734,743, and 754, the Managing Venturer does not presently intend to make such election on behalf of the Venture. The absence of any such effective election and of the power to compel the making of such an election may, in many circumstances; result in a reduction in value of a Venturer's Interest to any potential transferee and may be considered an additional impediment to the transferability of Venture Interests.

REPAYMENT OF LOANS

Each Venturer will be subject to federal income tax on his distributive share of the net taxable income of the Venture, whether or not such income is actually distributed to him. Advances against production received by the Venture (such as a loan or an advance secured by a specific share of future production), if any, will be treated as loans to the Venture and will not be recognized as income by the Venture on receipt. Proceeds from production used to pay such advances or other loans will be ordinary income, subject to depletion, to the Venture in the year the production is realized. The principal portion of repayments will not be deductible by the Venture will be entitled to a deduction of interest, if any, paid on the advances or loans. During repayment of such advances or loans, the taxable income of the Venturers from the property subject to the advance or loan may be greater than the net cash proceeds therefrom distributed to them. Therefore, taxes will be payable on revenues used to repay the principal amount of the advance or loan, as well as on remaining Venture revenues available for distribution, whether or not actually distributed.

LIMITATIONS ON PASSIVE ACTIVITY LOSSES

TRA 1986 imposes new limitations on taxpayers' ability to deduct losses from passive activities against the taxpayers' other income. On February 19, 1988, the Departments of the Treasury promulgated the first installment of its extensive Temporary and Proposed Regulations on Passive Activity Losses and Credits (the "Passive Loss Regulations"). In general, a taxpayer may not deduct losses from a passive activity against income from wages and salaries (or other so called "active" income) or against income from interest, dividends and royalties ("portfolio income"). However, a taxpayer may deduct against such income losses from activities in which the taxpayer materially participates (subject to other limitations in the Code). The passive activity loss rules apply to individuals, estates, trusts, closely held C corporations (50% of the value of which is owned by five or fewer individuals), and "personal service corporations." An activity will be classified as "passive" if the activity is a rental activity or the conduct of a trade or business in which the taxpayer does not "materially participate." A taxpayer materially participates in an activity if the taxpayer is involved in the operations of the activity on regular, continuous, and substantial basis. A taxpayer is not treated as materially participating in an activity if his interest in that activity is held as a limited partner in a limited partnership.

In computing a taxpayer's passive activity loss limitation, the taxpayer must determine his aggregate deductions and losses from all passive activities for the taxable year and offset them against this aggregate income and gains from passive activities during the taxable year. Similarly, the taxpayer must aggregate all credits earned during the taxable year from passive activities and offset them against the tax liability allocable to all passive activities during the taxable year. Although a taxpayer is permitted to offset losses from one passive activity against income and gains from another passive activity, the taxpayer may not offset his losses from passive activities against his wages, salary, or other income derived from the active conduct of a business, nor against income from interest, dividends, or royalties not derived in the ordinary course of a trade or business, or against the gain from the sale of property producing such income.

Should a taxpayer have net losses from passive activities and net credits from passive activities, both net losses and credits may be carried forward indefinitely and deducted against any future net income and tax liability, respectively, from passive activities. Any unused losses are held in suspense until the taxpayer disposes of his entire interest in the passive activities. Any unused losses are held in suspense until the taxpayer disposes of his entire interest in the passive activity, the taxpayer is generally permitted to deduct the suspended passive losses against the taxpayer's other income or gain (after first offsetting them against gain recognized on the disposition and against net income for the taxable year from all passive activities). Suspended credits, however, must continue to be carried forward until used to offset tax on income from other passive activities. If the disposition is because of the taxpayer's death, the suspended losses can only be used to the extent they exceed the amount by which the property's basis is increased as a result of the taxpayer's death. If a disposition is by means of an installment sale, the suspended losses may only be recognized in any taxable year to the extent of the percentage of the total gain on the sale that is recognized during that taxable year.

Material participation, however, is not all cases determinative as to whether an activity is a "passive activity." Under the "working interest exception," working interests in oil and gas properties are not treated as passive activities (regardless of whether the taxpayer materially participates) if the taxpayer owns the interest directly or through an entity that does not limit his liability with respect to the activity. Two elements must be met before a taxpayer qualifies for the working interest exception to the passive activity loss rules, so that losses will not be treated as losses from a passive activity. First, the property generating the losses must constitute a "working interest" as defined by the passive loss rules. Second, the interest must not be held through an entity that limits the liability of the taxpayer with regard to the activity.

With respect to the first part of the test, the Passive Loss Regulations indicate that a "working interest" does not include non-operating mineral interests such as royalty interests, production payments, or net profits interests. The Report of the Committee on Finance, United States Senate, to Accompany H.R. 3838, S. Rep. No. 99-313, 99th Cong., 2d Session 744,745 (1986) ("Senate Finance Committee Report"), indicated that a "working interest" generally has characteristics such as "responsibility for signing authorizations for expenditures with respect to the activity, receiving periodic drilling and completion reports, receiving periodic reports regarding the amount of oil extracted, possession of voting rights proportionate to the right to continue activities if the present Operator decides to discontinue operations, a proportionate share of tort liability with respect to the property (e.g., if a well catches fire), and some responsibility to share in further costs with respect to the property in the event that a decision is made to spend more than the amounts already contributed. Nevertheless, "the fact that a taxpayer is entitled to decline, or does decline, to make additional contributions does not contradict the taxpayer's possession of a working interest. In addition, the fact that tort liability may be insured against does not contradict such taxpayer's possession of a working interest."

Under the Agreement, the Venturers will receive periodic reports regarding drilling and completion and regarding the amount of oil extracted. The Venture may conduct further activities on the Lease after the Venture or the Operator discontinues its Initial Operations on the property. The Venturers will possess voting rights proportionate to their interests in the Venture. The question of whether the

Venturers own a "working interest" as defined by the passive loss rules is in part one of fact. While it is possible that the Service might take a contrary position and that, if litigated, a court might sustain such a position, Counsel for the Venture believes that, if challenged, the Venture property would be held to be a "working interest" as defined by the passive loss rules.

The second part of the test requires that the "working interest" not be held directly or indirectly through an entity that limits the taxpayer's liability with respect to the activity. The Senate Finance Committee Report indicates that an interest owned through a limited partnership or through a form of ownership that is substantially equivalent in its effect on liability to a limited partnership interest will not qualify for the working interest exception. Although the Venture or the Operator intends to obtain insurance to protect against various liabilities, to the extent the insurance coverage obtained by the Venture fails to cover a particular risk or is insufficient to pay the entire amount of a particular claim or to the extent the insurer is financially insolvent or otherwise unable to pay a particular claim, the Venturers will bear the ultimate liability for losses with respect to the Venture. In addition, The Passive Loss Regulations provide that the presence of insurance is not taken into account in determining whether the taxpayer holds a working interest through an entity that limits the taxpayer's liability. Although it is possible that the Service might take a contrary position and that, if litigated, a court might sustain such position, Counsel for the Venture believes that, if challenged, the court might sustain such position, Counsel for the Venture believes that, if challenged, the interests in the Venture held by the Venturers would not be deemed substantially equivalent in their effect on liability to a limited partnership interest. Each prospective Venturer would be aware, however, that even if the Venture itself is not an entity that limits the liability of the Venturer with respect to the activity, no person will be deemed to materially participate in the Venture's activities (and losses allocated to that individual will be deemed losses from a passive activity) if such person owns his individual interest in the Venture through an entity, such as a limited partnership or an S Corporation, that limits the liability of that individual with respect to the Venture.

To the extent the Service were successful in contending either that the Venturers do not own oil or gas working interest as defined in the passive loss rules or that the form in which the Venturers own the Venture property has an effect on the Venturer's liability similar to that of a limited partnership, a Venturer's share of any losses, generated by the Venture would constitute passive losses, which the Venturer could deduct only to the extent of such Venturer's passive income.

AT-RISK LIMITATION ON DEDUCTIONS FOR EXPENSES

The "at-risk" limitation provision of Code section 465 restricts the amount of loss a Participant can deduct in connection with activities conducted in "exploring for, or exploiting oil and gas resources." Under this rule, all non-corporate taxpayers and certain corporate taxpayers that sustain a loss in connection with oil and gas activities may deduct such loss only to the extent of the amount "at risk" in such activities at the end of a taxable year. This limitation applies to each activity engaged in and not on an aggregate basis for all activities. For the purpose of initially computing the amount of such limitation, the amount "at risk" for each taxpayer is limited to: (1) the amount of money contributed to the activity, (2) the adjusted basis of other property contributed to the activity, and (3) any amount borrowed with respect to the activity for which the taxpayer is personally liable for repayment or with respect to which he has pledged property (other than property used in the activity) as security for the repayment of the amount borrowed from any person other than a person who has an interest in the activity or who is a related party (as defined), limited however, to the net fair market value of his interest in such pledged property. "Loss" is defined as the excess of allowable deductions for a taxable year from an activity over the amount of income actually received or accrued by the taxpayer during such year from the activity.

The amount the taxpayer has "at risk" may not include the amount of any loss against which the taxpayer is protected through non-recourse financing, guarantees, stop loss agreements or other similar arrangements. The amount of any such loss disallowed in any taxable year shall be carried over to the first succeeding taxable year. Further, a taxpayer's "at risk" amount in subsequent taxable years with respect to the activity involved shall be reduced by that portion of the loss allowable as a deduction.

AT-RISK RECAPTURE OF LOSSES

The "at-risk" rules also provide that a Venturer must recognize income to the extent his "at-risk" basis is reduced below zero (limited to loss amounts previously allowed to the Venturer over any amounts previously recaptured). Distributions to a Venturer, changes in the amount of recourse indebtedness attributable to a Venturer or the commencement of guarantees or similar arrangements may reduce a Venturer's amount "at-risk." A Venturer may be allowed a deduction for the recaptured amounts included in taxable income if he increases his amount "at-risk" in a subsequent taxable year.

TAX PREFERENCE INCOME: ALTERNATIVE MINIMUM TAX

Individuals, corporations, trusts and estates are subject to an "alternative minimum tax" on certain tax preference items. Treasury Regulation section 1.58-2(b) (pursuant to the regulatory authority granted in Code section 702(a)(7)) requires that a partner, in computing his individual tax preference items, take into account separately those income and deduction items of a partnership that enter into his computation of tax preference items. The Venture will generate tax preference items attributable to its current deduction of Intangible Costs to the extent of the amount by which the individual Venturer's "excess intangible drilling costs" for the year exceeds 65% of his net income from his oil and gas properties for that year. "Excess intangible drilling costs" are defined as the excess of the allowable intangible drilling costs paid or incurred in connection with productive oil and gas wells, over the portion of those costs, if any, that would have been allowable for the year if capitalized and (1) amortized on the basis of a 10-year life, beginning with the month in which production from such well begins, or (2) recovered through cost depletion. For taxpayers other than integrated oil companies, the preference applies only to the extent that, had it applied fully, it would have increased alternative minimum taxable income by an amount that exceeds 30% (40% for taxable years beginning after '93) of the alternative minimum taxable income for the taxable year determined without the intangible drilling cost preference and without the alternative tax net operating loss deduction. Intangible Costs with respect to the drilling of a nonproductive well are not subject to the above computation of tax preference items. A Venturer in the Venture may also realize tax preference items for any taxable year attributable to percentage depletion in excess of depletable basis (determined without regard to the depletion deduction for the taxable year).

In the case of a married individual filing a separate return, the tentative minimum tax for the tax year is equal to 26% of the "taxable excess" that doesn't exceed $87,500, plus 28% of the taxable excess that does exceed $87,500. The alternative minimum tax for individuals is a flat 21% (24% for taxable years beginning on or after January 1, 1991) of "alternative minimum taxable income" in excess of the exemption amount. Alternative minimum taxable income is defined as adjusted gross income, plus tax preference items such as excess Intangible Costs, less specially computed net operating loss and itemized deduction amounts. For property other than Section 1250 property and property the taxpayer had elected to depreciate on the straight line method, a taxpayer may reduce his

alternative minimum taxable income only for depreciation computed based on the 150% (rather than the 200%) declining balance method. In general, the net operating loss deduction must be reduced by tax preference items in computing the alternative minimum taxable income. For tax years beginning after December 30, 1990, alternative minimum taxable income is reduced by a special energy deduction. The special energy deduction is an amount equal to the lesser of an “alternative tax energy preference deduction” or forty percent (40%) of alternative minimum taxable income (determined without regard to the special energy deduction or the alternative minimum tax operating loss deduction.) The alternative tax energy preference deduction is an amount equal to the sum of (i) in the case of the Intangible Cost preference, an amount equal to 75 percent of the Intangible Cost preference attributable to qualified exploratory costs plus 15 percent of the excess of the Intangible Cost preference over that portion of the Intangible Cost preference attributable to qualified exploratory costs, plus (ii) 50 percent of the marginal production depletion preference. This special energy deduction in computing alternative minimum taxable income is phased out as the price of crude oil exceeds $28 per barrel. The ‘93 Act provides that, in the case of married couples filing joint returns or surviving spouses, the exemption amount is $45,000; for unmarried individuals, who aren’t surviving spouses, the exemption amount is $33,750; for married individuals filing separate returns, estates and trusts, the exemption amount is $22,500. (Code Sec. 55(d) (1) as amended by ‘93 Act 13203 (b)). Married individuals filing separately must add to alternative minimum taxable income the lesser of (a) 25% of the excess of alternative minimum taxable income over $165,000 or (b) $22,500. (Code Sec. 55(d)(3) as amended by ‘93 Act 13203(c)(1)). The alternative minimum tax exemption amount is presently $40,000 for a joint return or surviving spouse, $30,000 for an unmarried individual other than a surviving spouse, and $20,000 for married individuals filing separate returns, estates or trusts. In addition, a taxpayer must reduce his exemption amount by 25% of the amount by which his alternative minimum taxable income exceeds $150,000 ($112,500 for single persons who are not surviving spouses and $75,000 for married persons filing separate returns, estates and trusts). An individual is required to pay the alternative minimum tax only if the amount of such tax exceeds his “regular tax,” as defined.

Venturers may individually elect to amortize their allocable shares of the Venture’s Intangible Costs over a five-year period beginning with the year the expenditure is made. If this election is made, there will be no preference items on these amounts. However, such amount will still be treated as Intangible Costs for purposes of the recapture rules.

PARTICIPATION BY IRAS, EMPLOYEE BENEFIT PLANS AND SIMILAR TAX EXEMPT ORGANIZATIONS

IRAs and employee benefit plans including trusts formed as part of such plans and certain charitable and other organizations described in Code section 501(c) are exempt from federal income tax. However, such entities are subject to tax on unrelated business taxable income. Unrelated business taxable income is gross income derived by an exempt organization from any unrelated trade or business regularly carried on by it or by a partnership of which it is a member. Specific deductions directly connected with the carrying on of such trade or businesses, computed with modifications, including a $1,000 deduction, are allowed. Since the Venture will carry on a trade or business, a tax-exempt Venturer may be considered to be regularly carrying on the trade or business of the Venture and any Venture income allocated to a tax-exempt Venturer may be unrelated business taxable income to such Venturer, unless such income is specially exempt from such classification.

The receipt of unrelated business taxable income by a tax-exempt entity generally has no effect on that entity’s tax-exempt status or on the exemption from tax of its other income. However, for certain types of tax-exempt entities, the receipt of any unrelated business income may have extremely adverse consequences.

ACCORDINGLY, EACH PROSPECTIVE TAX-EXEMPT VENTURER IS URGED TO CONSULT ITS OWN ADVISOR REGARDING THE POSSIBLE CONSEQUENCES OF PARTICIPATING IN THE VENTURE.

FOREIGN PARTICIPANTS

The Venture expects most Venturers will be United States residents. However, the federal income taxation of non-resident alien individuals, foreign corporations and other foreign entities (hereinafter referred to collectively as “foreign participants”) is a highly complex matter that may be affected by applicable tax treaties and other considerations.

Under Code section 875, a non-resident alien individual or foreign corporation is deemed engaged in a trade or business within the United States if the partnership of which such foreign participant is a member is so engaged. In general, if foreign participants participate in the Venture, all items of Venture income included in their distributive shares, including gains on the sale or other disposition of Venture properties, will be subject to United States taxation as income that is effectively connected with a United States trade or business (“effectively connected income”). Consequently, such Venturers will be required to file United States income tax returns and will be subject to United States tax on their distributive shares of net business income from the Venture at the same rates applicable to a United States citizen, resident or corporation. In determining a Venturer’s distributive share of net business income from the Venturer, such investor would be permitted the same deductions allowed to a United States citizen, resident or corporation.

Partnerships and Joint Ventures that have “effectively connected taxable income” must now pay withholding tax on the income allocable to foreign partners at an amount equal to the foreign partners’ income allocation times the highest applicable tax rate (currently 31% for non-corporate partners). The amount withheld is generally treated as a distribution to the foreign partner and is credited against the foreign participant’s United States income tax liability.

Although there is little direct authority on this issue, it is likely that a non-resident alien individual would be subject to United States estate tax on the value of his venture interest if he owns such venture interest at the time of his death. However, a non-resident alien who transfers a venture interest by gift would not, in most cases, be subject to United States gift tax. Finally, certain transfers would cause a non-resident alien to become liable for the generation-skipping transfer tax.

The above rules on United States taxation are subject to modification by applicable income and estate tax treaties. THEREFORE, FOREIGN PARTICIPANTS ARE URGED TO CONSULT THEIR OWN TAX ADVISORS WITH RESPECT TO PARTICIPATING IN THE VENTURE AND THE EFFECT OF THE TAX LAWS OF OTHER JURISDICTIONS IN WHICH THEY ARE SUBJECT TO TAXATION WITH RESPECT TO SUCH PARTICIPATION.

STATE AND LOCAL INCOME TAXES

Certain states or localities where the Venture may engage in business or where the Partners may reside may levy income taxes for which the Venturers may be liable with respect to their shares of the Venture income, and it may be necessary for each Venturer to tile state or local income tax returns to report income in such jurisdictions. Neither the Managing Venturer nor Counsel to the Venture has reached any conclusions or rendered an opinion on matters of state or local income tax law.

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STATE INCOME TAX CONSEQUENCES

You should also consider the state income tax consequences of the acquisition, ownership and disposition of the Joint Venture Units of Interest. State income tax law may differ substantially from the corresponding federal law, and this discussion does not purport to describe any aspect of the income tax laws of any state. Therefore, you should consult your own tax advisors with respect to the various state tax consequences of an investment in the Joint Venture Units of Interest.

TAX SHELTER REGISTRATION

TRA 1984 added a provision requiring the registration of "tax shelters" with the Service. For this purpose, a "tax shelter" is an investment with a "tax shelter ratio" greater than 2 to 1 as of the close of any of the first five years ending after the date on which the investment is offered for sale. An investment meeting this ratio test must be registered with the Service if the investment must be registered with a state or federal securities commission, or is a substantial investment. A substantial investment is defined as any investment for which the aggregate amount that may be offered for sale exceeds $250,000 and five or more investors are expected.

The "tax shelter ratio" means, with respect to any year, the ratio that the aggregate amount of deductions and 350% of the credits potentially available to any investor for all periods up to and including the close of such year bears to the "investment base" as of the close of such year. As applied to the Venture, "investment base" would mean the amount of money contributed to the Venture by a Venturer as of the close of such year. Temporary and proposed regulations issued pursuant to this provision clearly state that for purposes of determining the "tax shelter ratio," gross deductions are not offset by gross income. Consequently, the definition of "tax shelter" is broad and will encompass many investments that are not marketed or customarily designated as tax shelters.

EACH PROSPECTIVE INVESTOR SHOULD BE AWARE THAT IT IS NEITHER A SIGNIFICANT NOR AN INTENDED FEATURE OF ANY INVESTMENT IN THIS JOINT VENTURE THAT FOR FEDERAL OR STATE INCOME TAX PURPOSES (1) DEDUCTIONS IN EXCESS OF INCOME FROM THE INVESTMENT WILL BE AVAILABLE IN ANY YEAR TO OFFSET TAXES ON INCOME FROM OTHER SOURCES IN THAT YEAR OR (2) CREDITS IN EXCESS OF THE TAX ATTRIBUTABLE TO THE INCOME FROM THE INVESTMENT WILL BE AVAILABLE IN ANY TAX YEAR TO OFFSET TAXES ON INCOME FROM OTHER SOURCES IN THAT YEAR.

ACCORDINGLY, THE JOINT VENTURE SHOULD NOT CONSTITUTE A 'TAX SHELTER' WITHIN THE MEANING OF TREASURY CIRCULAR 242 (31 CFR $10.33) AND FORMAL OPINION 346 OF THE AMERICAN BAR ASSOCIATION.

THIS SUMMARY OF FEDERAL INCOME TAX CONSEQUENCES DOES NOT COMPLY WITH THE REQUIREMENTS FOR 'TAX SHELTER OPINIONS' UNDER TREASURY CIRCULAR 242 AND AFA OPINION 346. THIS DISCUSSION OF FEDERAL INCOME TAX CONSEQUENCES IS INTENDED TO CONSTITUTE MERELY A SUMMARY OF MAJOR INCOME TAX QUESTIONS RELATIVE TO THE PROPOSED JOINT VENTURE.

The Managing Venturer does not believe that participating in the Venture necessarily constitutes an investment in "securities" for purposes of applicable federal and state securities law. Nevertheless, the Managing Venturer has estimated the aggregate amount of deductions and credits that may be generated by Venture activities and has concluded that the "tax shelter ratio," if deemed applicable, is not reasonably expected to exceed 2 to 1 for any Venturer as of the close of any one of the first five years of the Venture. Therefore, the Venture has not been registered with the Service.

AUDIT OF TAX RETURNS

In light of the announced emphasis by the Service on audits of tax shelter investment programs, the tax returns of the Venture may be audited and such audit may result in adjustments. Any adjustment of the Venture's tax return would at a minimum result in a corresponding adjustment of the federal income tax liability of individual Venturers, and may result in a full audit of their individual tax returns (thereby resulting in adjustments to non-Venture, as well as Venture, income and deductions). In addition, an initial audit of a single Venturer's individual tax return could result in the audit of the Venture tax return, thereby possibly triggering the consequences just indicated to all Venturers in the Venture.

It should be observed that TEFRA introduced substantial changes in the procedural aspects of audit and litigation regarding items of partnership (and for these purposes Joint Venture) income, gain, loss, deduction, and credit. Under TEFRA, the tax treatment of such items will be determined at the partnership level in a unified partnership proceeding. Partners (other than partners with less than a 1% interest in the profits of a partnership with more than 100 partners), referred to as "Notice Partners," would be notified at the beginning of the partnership audit proceeding and as to the final partnership administrative adjustment (FPAA). One general partner of a partnership will be designated as the "Tax Matters Partner." On settlement with any partner prior to mailing a notice of the FPAA to the Tax Matters Partner, the Service will be required to offer consistent settlement terms with any other partner who requests such settlement terms before the expiration of 150 days after such mailing of the FPAA to the

TAX MATTERS PARTNER

Only the partnership, through the Tax Matters Partner, will have a right to contest the Service's determination in court within 90 days following the notice of FPAA. If the Tax Matters Partner does not file a petition for judicial review, any other Notice Partner would have a right to file such petition, within 60 days following such 90 day period. However, only one proceeding may go forward on behalf of the partnership, which would be the first action filed in the Tax Court, or, if no petition is filed with the Tax Court, the first action filed by a partner in either a United States District Court or the United States Claims Court. All other actions would be dismissed. However, each partner with an interest in the outcome would be allowed to participate in the action. The court acquiring jurisdiction of the proceedings will have jurisdiction to determine all items of the partnership taxable year to which the FPAA relates and the proper allocation of such items among the partners. TEFRA also provides a procedure for any partner to file a request for administrative adjustment of partnership items. The Tax Matters Partner may file a petition for review with respect to any part of the requested adjustment that is disallowed, in which case other partners would be treated as parties to the action. Suits by individual partners, other than the Tax Matters Partner, would also be allowed with respect to certain disallowed items in requests for administrative adjustment filed by such partners, with certain limitations. The Tax Matters Partner is required to keep the partners informed of all administrative and judicial proceedings.

Under TEFRA, the period of time in which assessments of deficiencies and claims for refunds may be made with respect to federal income taxes attributable to "partnership items" is three years from the date of filing of the partnership return or, if later, the last date prescribed for filing such return determined without extensions. The period may be extended with respect to any partner by agreement with such partner, or for all partners by agreement with the Tax Matters Partner. A "partnership item" is any item required to be taken

into account for the partnership's taxable year under any provision of subtitle A of the code to the extent regulations provide that such item is more appropriately determined at the partnership level. Additionally, assessments may be made at any time against partners who sign or actively participate in a fraudulent return. Also, as to other partners affected by such return the period of assessment is extended from three to six years. The period of limitations is also six years in any case in which there is an omission from gross income of any amount properly includable that exceeds 25% of the amount of the gross income stated in the return. If no partnership return is filed, assessments may be made at any time.

PENALTY FOR SUBSTANTIAL UNDERSTATEMENTS

Code section 6662, in part, imposes an accuracy-related penalty of 30% of the amount of any underpayment attributable to (I) negligence or intentional disregard of rules or regulations; and (ii) "substantial understatements" of income tax. A "substantial understatement" is defined as a reported liability that understates the amount of tax owed by the greater of 10% or $5,000 ($10,000 for corporations other than S corporations and personal holding companies). An understatement is reduced by that portion of the understatement attributable to an item (other than a "tax shelter" item) if there is "substantial authority" for the taxpayer's treatment of such item on his return or if the taxpayer's return (including the partnership return in the case of a partnership item) adequately discloses the facts relating to the item's tax treatment. The regulations issued under Code section 6661 (now included in Section 6662) provide that the "substantial authority" standard requires stronger support than a mere "reasonable basis" for taking the position but the treatment need not be "more likely than not" the proper treatment. Under the regulations, there is substantial authority for the tax treatment of an item only if the weight of the authorities supporting the treatment is substantial in relation to the weight of authorities supporting contrary positions.

With respect to an item attributable to a "tax shelter," however, a more stringent standard applies for the reduction of understatements attributable thereto. A "tax shelter" is defined as a partnership or other entity or any other plan or arrangement the principal purpose of which is to avoid or evade tax. The regulations provide that the principal purpose of an entity, plan or arrangement merely claims tax benefits provided by the Code, such as claiming MACRS deductions, percentage depletion, or deductions attributable to the payment of Intangible Costs. An item will be considered a tax shelter item if such item is directly or indirectly attributable to the principal purpose of a tax shelter to avoid or evade federal income tax. The regulation gives as an example a partnership established to acquire and overvalue property for the purpose of claiming investment tax credit; the investment tax credit with respect to the property would be a tax shelter item. With respect to an item attributable to a tax shelter, in addition to having "substantial authority" for his position, the taxpayer must reasonably believe that the treatment claimed by him was "more than likely than not" the proper treatment for such an item. EACH PROSPECTIVE VENTURER SHOULD CONSULT HIS PERSONAL TAX ADVISOR WITH RESPECT TO THE SUBSTANTIAL UNDERSTATEMENT PENALTY.

REPORTS

The Venture will annually compute its taxable income or loss for the appropriate taxable period, and in computing such taxable income or loss, it will deduct Intangible Costs, MACRS and other deductible costs to the extent allowable under applicable federal income tax laws and regulations. Each Venturer will compute his depletion deduction individually. Each Venturer will be furnished a copy of the Venturer's Joint Interest Statement for his use in the preparation of his individual income tax return, and each Venturer will include in his individual federal income tax return his distributive share of the Venture taxable income (whether or not distributed) or loss, as computed on the federal income tax return of the Venture.

Under TEFRA, each Venturer is required to treat Venture items on his return consistently with the treatment on the Venture return unless the Venturer files a statement with the Service identifying the inconsistency. If a Venturer fails to satisfy these requirements the Service may assess any deficiency attributable to any computational adjustment required to make the treatment consistent with the Venture return without commencement of a Venture proceeding or notification to the Venturer that the inconsistent item will be treated as a non-Venture item.

Under TRA 1984, if a Venturer sells an Interest in the Venture, the selling Venturer must promptly notify the Venture of such transfer. The Venture is required to file a return for the year of the sale setting forth the name and address of the selling Venturer and the transferee. By regulation the Secretary of the Treasury may require other information and establish rules regarding the time and manner for filing this return. The Venture must also furnish the information shown on the return to the person's names therein. A penalty may be imposed for failure to give notice, file the return or furnish information in a timely manner.

VENTURERS REQUIRED TO MAINTAIN INFORMATION

Venturers are required to maintain the records concerning their share of the basis of oil and gas properties and the related depletion allowances. The Venture will allocate the adjusted basis of each oil and gas property to the Venturers as set forth in the Agreement, and provide a report of such allocation to each Venturer, who then must keep his own records.

POSSIBLE CHANGES IN FEDERAL TAX LAWS

The statutes and regulations with respect to all of the foregoing tax matters are subject to continual change by Congress or the Department of Treasury. Similarly, interpretations of these statutes and regulations may be modified or affected by judicial decision or the Department of Treasury. Any such change may have an effect on the discussion set forth above.

Furthermore, in recent years there have been a number of other proposals made in Congress by government agencies and the executive branch of the federal government for changes in federal income tax laws. In addition, the Service has proposed and is still considering changes in regulations and procedures, and numerous private interest groups have lobbied for regulatory and legislative changes in federal income taxation. Many of such proposals would, if adopted, have the overall effect of reducing the tax benefits presently associated with participating in partnerships such as the Venture.

It is likely that further proposals will be forthcoming or that previous proposals will be revived in some form in the future. It is impossible to predict with any degree of certainty what past proposals may be revived or what new proposals may be forthcoming, the likelihood of adoption of any such proposals, the likely effect of any such proposals upon the income tax treatment presently associated with oil and gas ventures, investments, or the Venture, or the effective date of any legislation which may derive from any such past or future proposals.

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CONSULTATION WITH PERSONAL TAX ADVISORS

THE FOREGOING ANALYSIS IS NOT INTENDED AS A SUBSTITUTE FOR CAREFUL TAX PLANNING. EACH PROSPECTIVE VENTURER SHOULD CONSULT WITH HIS OWN PERSONAL TAX ADVISOR CONCERNING (I) THE APPLICABILITY TO AND EFFECT ON HIM OF THE UNITED STATES INCOME TAX LAWS AND THEIR ADMINISTRATION, AND (II) THE APPLICABILITY TO AND EFFECT ON HIM OF STATE, LOCAL AND FOREIGN TAX LAWS AND THEIR ADMINISTRATION.

IRS CIRCULAR 230 DISCLOSURE

TO ENSURE COMPLIANCE WITH U.S. TREASURY REGULATIONS GOVERNING TAX PRACTICE, WE INFORM YOU THAT ANY U. S. FEDERAL TAX ADVICE CONTAINED IN THIS COMMUNICATION, INCLUDING ANY APPENDICES, IS NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED, FOR THE PURPOSE OF (I) AVOIDING ANY PENALTIES UNDER U. S. FEDERAL TAX LAW, OR (II) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TRANSACTION OR MATTER ADDRESSED HEREIN.

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Glossary

Certain terms as used herein have special meanings within this Confidential Private Placement Memorandum which are set forth below, and other terms of general use in the industry are defined below for your reference.

2-D SEISMIC or 2-D DATA. Seismic data that is acquired and processed to yield a two-dimensional cross-section of the subsurface.

3-D SEISMIC or 3-D DATA. Seismic data that is acquired and processed to yield a three-dimensional picture of the subsurface.

AFFILIATE with respect to the Managing Venturer shall mean (i) any person or entity directly or indirectly owning, controlling or holding, with power to vote, ten percent (10%) or more of the outstanding voting securities of the Managing Venturer; (ii) any entity, ten percent (10%) or more of which outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the Managing Venturer; (iii) any person or entity directly or indirectly controlling, controlled by or under common control of the Managing Venturer; (iv) any officer, director or partner of the Managing Venturer; and (v) if the Managing Venturer is an officer, director, or partner, any company for which the Managing Venturer acts in any such capacity, For the purpose of this Memorandum and accompanying documentation, any partnership of which Signal Oil llc. is a general partner, and any joint venture in which Signal Oil llc. is a venturer, is an Affiliate of Signal Oil llc..

AGREEMENT or **JOINT VENTURE AGREEMENT.** The Joint Venture Agreement between Signal Oil llc. as the Managing Venturer, and the Venturers, pursuant to which the Venture has been formed, a copy of which is attached hereto as Exhibit "B", together with all amendments thereto.

ACT. The Texas Uniform Partnership Act, as from time to time amended.

ADDITIONAL ASSESSMENT CONTRIBUTIONS. With respect to any participating Venturer, the sum of the additional assessments paid by such Participating Venturer on his own behalf plus the additional assessments paid by such participating Venturer on behalf of a non-participating Venturer.

ADDITIONAL ASSESSMENTS. Assessments of Venturers requested by the Joint Venture to fund Subsequent Operations.

AGREEMENT or **JOINT VENTURE AGREEMENT.** This Agreement between Signal Oil llc. as the Managing Venturer, and the Venturers, together with all amendments hereto.

AMOUNT REALIZED. The amount realized by the Joint Venture for federal income tax purposes on a sale of a Joint Venture oil and gas property.

AUTHORITY FOR EXPENDITURE (AFE). An AFE is a budgeting and approval form used during the planning process for a well about to be drilled (and for other projects). It includes an estimate of costs to be incurred during the IDC (intangible drilling cost) category and in the tangible equipment category.

BACK-IN AFTER PAYOUT. The working interest retained by Signal Oil llc. and other parties if applicable, in aggregate, after the Venturers have attained payout of their initial investment. The Venturers' working interest percentage at payout will be proportionately reduced by that specific percentage hereinabove delineated to accommodate Signal Oil llc.'s back-in interest. (See Reversionary Interest)

Bbl. One stock tank barrel, or 42 U.S. gallons liquid volume, used in reference to oil or other liquid hydrocarbons.

Bcf. Billion cubic feet, used in reference to natural gas.

BCFE. Billion cubic feet of gas equivalent. Gas equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

BOE. Barrels of oil equivalent. Oil equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

CAPITAL ACCOUNTS of the Venturers shall be determined and maintained in accordance with the rules of Treasury Regulation section 1.704-1(b)(2)(iv) and, to the extent consistent therewith, each Venturer's Capital Account shall be increased by:

d. the amount of money contributed by such Venturer to the Joint Venture;
e. the fair market value of any property contributed by such Venturer to the Joint Venture (net of any liabilities securing such contributed property that the Joint Venture is considered to assume or take, subject to under Code section 752).
f. allocations to such Venturer of income or gain (including tax exempt income) pursuant to Article VIII but excluding any income or gain described in Treasury Regulation section 1.704-1(b)(4)(I);
g. the amount of Joint Venture liabilities assumed by such Venturer or that are secured by any Joint Venture property distributed to such Venturer other than the liabilities referred to in paragraph (f) below; and each Venturer's Capital Account shall be decreased by:
h. the amount of any money distributed to such Venturer by the Joint Venture;
i. the fair market value of any property distributed to such Venturer by the Joint Venture (net of any liabilities securing such distributed property that such Venturer is considered to assume or take subject to pursuant to Code section 752).
j. the amount of losses, costs and expenses allocated to such Venturer under Article VIII;

CAPITALIZATION PERIOD. The period of time during which Venturers shall be accepted from the Effective Date of the Joint Venture (See Effective Date of Joint Venture, herein, and/or Joint Venture Agreement), for a period of 180 days therefrom, unless extended by the Managing Venturer for a period of not more than one-hundred eighty (180) days, with a maximum of two (2) extension periods; provided, however, that the Managing Venturer, in its sole and absolute discretion, may terminate the Capitalization Period at any time prior to such date.

CODE. The Internal Revenue Code of 1986, as from time to time amended and any federal legislation that may be substituted therefore.

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COMPLETION ASSESSMENTS. Proportionate assessments of the Venturers, in an amount hereinabove specified (See Investment Summary) per Unit called for by the Venture to fund the completion of Venture well; the amount hereinabove specified per Unit requested by the Managing Venturer to fund, among other things, the Completion aspects of Initial Operations; the nonpayment of which will constitute an election to withdraw from the Joint Venture with respect to such nonpaying Venturer's Units and interest in the Joint Venture.

COMPLETION. In the context of the Venture, completion shall mean the cleaning out of a well after reaching a specified depth, and/or conducting those processes or operations which the Managing Venturer decides to employ in a good faith effort to make a well capable of producing oil and/or gas in commercial quantities or determine that it will not produce oil and/or gas in commercial quantities. Such effort shall not require an obligation by the Managing Venturer or the Venture to attempt a completion in more than one potentially productive horizon or geological formation.

DEVELOPMENT WELL. A well drilled within the proved area of an oil or gas reservoir to the depth of a stratigraphic horizon known to be productive.

DRY HOLE. A well which the Managing Venturer or the Venturers by vote determine is not capable of producing oil and/or gas in commercial quantities. A well may qualify as a dry hole either before or after completion. If a well is deemed a dry hole before completion, the Turnkey Contract will provide for the plugging and abandonment of the well, as stipulated by the appropriate regulatory agency(ies). If the well is deemed a dry hole or unproducible after the attempted completion, the venture provides that the expenses associated with plugging and abandonment be offset by the salvage value, if any, of the tangible equipment installed on or pertinent to the venture well. Any excess salvage value will be distributed to the joint venture participants in proportion to their interests and will constitute the final business for that venture well.

EFFECTIVE NOTICE also see (NOTICE).

1. For a venturer or third party to "notice" the managing joint venturer or the operator of record would require delivery through the postal service or other means into the care, custody and control of the Registered Agent for the Corporation, or pertinent entity.
2. For the managing joint venturer or operator to notice a joint venturer would require the deposit into the Post Office or other official depository, in a postpaid wrapper, properly addressed to the Venturer at the last known address recorded on the Venture's records, substantiated by the affidavit of any person having knowledge of such fact, shall constitute notice to a joint venturer.

EXPENSES AND COSTS. All of the costs and expenses of the Venture, including but not limited to the following, each of which shall have the special meaning set forth opposite each such term:

1. **ORGANIZATIONAL COSTS.** The aggregate of (i) expenses for printing and mailing material used in connection with the applications for participation in the Venture and/or collection of assessments; (ii) allocable salaries and expenses of employees of the Managing Venturer assisting with the organization and formation of the Venture and/or the initial capitalization and/or collection of assessments; (iii) charges of depositories in connection with the Units; (iv) attorneys' and accountants' fees in connection with the organization and formation of the Venture and the preparation of this Memorandum and/or the collection of assessments; (v) "General and administrative Expenses" of Signal Oil llc. during the Capitalization Period; and (vi) any and all other expenses incurred by the Venture or the Managing Venturer in connection with the formation of the Venture, the applications for participation in the Venture, and the collection of assessments, if any.
2. **OPERATING EXPENSES.** The customary expenses of operations of oil and/or gas wells, and producing and marketing the oil and/or gas therefrom, including but not limited to the costs of reworking or workover or similar expenses relating to any well, but excluding Drilling Completion Costs or the depletion, depreciation or amortization thereon, or the expenses for recompletion in or deepening to another productive zone.
3. **GENERAL AND ADMINISTRATIVE EXPENSES.** All customary and routine legal, accounting, geological, engineering, travel, office rent, telephone, compensation to officers and employees, and other incidental expenses of the Managing Venturer necessary to the conduct of Venture Operations.

EXPLORATORY WELL. A well drilled to find and produce oil or gas in an unproved area, to find a new reservoir in a field previously found to be productive of oil or gas in another reservoir, or to extend a known reservoir beyond its known horizon.

FARMOUT. An agreement whereby the Venture would agree to assign its interest in a specific leasehold or working interest owned by it to other parties while retaining some part of its original interest (such as an overriding royalty interest, oil and/or gas payment, offset acreage, or other type of interest) subject to the drilling of one or more specified wells or other performances by the other parties as a condition of the assignment.

An assignment of an interest in a drilling location and related acreage conditioned upon the drilling of a well on that location.

FEE LAND. The most extensive interest that can be owned in land, including surface and mineral (including oil and gas) rights.

FEDERAL INCOME TAX ITEMS. Profits, Losses, Gain from Capital Transactions and Loss from Capital Transactions.

FIELD. An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature or stratigraphic condition.

FINDING COST. Expressed in dollars per BOE or MCFE. Finding costs are calculated by dividing the amount of total capital expenditures for oil and gas activities, including the effect of asset retirement obligations, by the amount of estimated net proved reserves added through discoveries, extensions, infill drilling, acquisitions, and revisions of previous estimates during the same period.

FORMATION. A succession of sedimentary beds that were deposited under the same general geologic conditions.

GAIN FROM CAPITAL TRANSACTIONS. Income or gain or the Joint Venture as determined for federal income tax purposes as a result of the sale, exchange, or refinancing of all or a portion of the Joint Venture's property other than depletable property.

GROSS ACRE. An acre in which a working interest is owned.

GROSS WELL. A well in which a working interest is owned.

HOLDER OF RECORD. The person in whose name any Unit is registered on the books and records of the Joint Venture.

HORIZONTAL WELLS. Wells drilled at angles greater than 70 degrees from vertical.

HYDRAULIC FRACTURING. A procedure to stimulate production by forcing a mixture of fluid and proppant_ (usually sand) into the formation under high pressure. This creates artificial fractures in the reservoir rock, which increases permeability and porosity.

INITIAL OPERATIONS. All activities commenced in connection with the acquisition of the Venture's interest in the lease and the drilling, testing and Completion of the Prospect Well, and the production of oil and/or gas therefrom. More specifically, any Joint Venture activity related to (i) acquiring the Prospect; (ii) drilling any well on the Prospect; (iii) testing, completing, equipping, reworking, deepening, recompleting, capping or plugging any well on a Prospect; (iv) installing, pumping, producing, processing, gathering and/or transporting facilities to produce, process, gather, and/or transport any oil or gas produced from any well on the Prospect; or (v) conducting any activity incident to the foregoing as may be deemed necessary by the Venturers in furtherance of a Joint Venture purpose.

INITIAL PRODUCTION or **I.P**. The early production of an oil or gas well, recorded after the testing operations, and the recovery of oil or other fluids used to acidize, fracture, and/or stimulate the target formation have been completed. The I.P. is used as a potential indicator of the maximum ability of a well to produce upon completion, without subsequent reservoir damage; provided, however, that, historically, the actual sustained production of oil or gas realized from a well is usually less, on an ongoing basis, than Initial Production; and, provided, further, that there can be no assurance that the actual production to be realized from a well on an ongoing basis following the conclusion of all completion activities with respect thereto will be equal to Initial Production.

INITIAL JOINT VENTURE CAPITAL. The total capital contribution to the Joint Venture actually paid by the Managing Venturer and Venturers as represented by Units, including Completion assessments, but excluding Additional Assessments.

LANDOWNERS'S ROYALTY INTEREST. An interest in production or the proceeds therefrom, to be received free and clear of all costs of drilling, development, operation, or maintenance, reserved by a landowner and/or mineral owner (if the mineral rights have been severed from the surface or upon the creation of an oil and gas lease.

LEASE. The oil, gas or mineral leases representing the percentage of the Working Interest in the Prospect Well acquired by Signal Oil llc. pursuant to an assignment in substantially the form of a typical oil and gas lease. The lease(s) more specifically referred to in the Memorandum.

LEASE OPERATING EXPENSE(S) (LOE). Those costs and expenses related to the ongoing producing operations on the lease which are invoiced to the venture working interest owner’s account(s) after the turnkey phases of drilling and testing and completing and equipping the venture property. Such expenses include, but are not limited to, ad valorem taxes in various forms (county, school, hospital district, college district, etc.), operating overhead, field pumper, water disposal, chemicals and chemical treating, repairs and maintenance of the equipment and property, additional operations conducted on the well (subject to the joint venture agreement and AAPL operating agreement), field supervision, field expenses, and insurance charges. Such expenses are invoiced monthly and typically are expensed tax items, with the exception of significant tangible equipment which is amortized and depreciable.

LIQUIDATOR. The Liquidating Trustee(s) designated in Section 9.3 hereof to handle the liquidation of the Joint Venture.

LOSSES. Each item of loss, deduction and credit of the Joint Venture as determined for federal income tax purposes but excluding Loss from Capital Transactions.

LOSS FROM CAPITAL TRANSACTIONS. Any loss of the Joint Venture as determined for federal income tax purposes as a result of the sale, exchange or refinancing of all or a portion of the Joint Venture's property other than depletable property.

MANAGING VENTURER. Refers to Signal Oil llc. (or its successor or replacement) when acting in the capacity of the Managing Venturer of the Venture.

MBbl. One thousand barrels of oil or other liquid hydrocarbons.

MEMORANDUM. The Confidential Private Placement Memorandum or Confidential Memorandum.

MMBbL. One million barrels of oil or other liquid hydrocarbons.

MBOE. One thousand barrels,of oil equivalent. Oil equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

MMBOE. One million barrels of oil equivalent. Oil equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

Mcf. One thousand cubic feet, used in reference to natural gas.

MCFE. One thousand cubic feet of gas equivalent. Gas equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

MMcf. One million cubic feet, used in reference to natural gas.

MMCFE. One million cubic feet of gas equivalent. Gas equivalents are determined using the ratio of six Mcf of gas (including gas liquids) to one Bbl of oil.

MMBtu. One million British Thermal Units. A British Thermal Unit is the amount of heat required to raise the temperature of a one-pound mass of water by one-degree Fahrenheit.

NET ACRES OR NET WELLS. The sum of our fractional working interests owned in gross acres or gross wells.

NET CASH FLOW. Monies available from the operation of the Joint Venture without deduction for depreciation but after deducting monies used to pay or establish a reserve for all other expenses, debt payments, improvements and repairs related to the Operation and administration of the Joint Venture.

NET PROCEEDS. The amount realized by the Joint Venture on the disposition of a Joint Venture property, less all fees, costs or expenses paid or to be paid with respect thereto and the amount of indebtedness (if any) of the Joint Venture paid or to be paid from such monies. Further, this shall mean Proceeds reduced by the Venture's adjusted basis in such oil and gas property for capital accounts, as determined under Section 8.2.2 of the Agreement.

NON-PARTICIPATING VENTURER. Any Venturer who fails to contribute completion assessments or additional assessments.

NOTICE, (also see, EFFECTIVE NOTICE):

1. For a venturer or third party to “notice” the managing joint venturer or the operator of record would require delivery through the postal service or other means into the care, custody and control of the Registered Agent for the LLC,Corporation, or pertinent entity.
2. For the managing joint venturer or operator to “notice” a joint venturer would require the deposit into the Post Office or other official depository, in a postpaid wrapper, properly addressed to the Venturer at the last known address recorded on the Venture’s records, substantiated by the affidavit of any person having knowledge of such fact, shall constitute notice to a joint venturer.

NYMEX. New York Mercantile Exchange.

OPERATIONS. Any Joint Venture activity related to (i) acquiring the Prospect Well site through options, leases or purchase, the acquisition of geologic data and geophysical data and research; (ii) drilling any well on the Prospect; (iii) testing, completing, equipping, reworking, deepening, recompleting, capping or plugging any well on the Prospect; (iv) installing pumping, production, processing, gathering and/or transporting facilities to produce, process, gather, and/or transport any oil or gas produced from any well on the Prospect; (v) conducting any secondary recovery operation on or with respect to the Prospect; or (vi) conducting any activity incident to the foregoing as may be deemed necessary by the Venturers in furtherance of a Joint Venture purpose.

OPTIONAL ADDITIONAL ASSESSMENTS. Assessments of the Venturers requested by the Venture fund Subsequent Operations, the payment of which shall be wholly voluntary.

OVERRIDING ROYALTY INTEREST. An interest in the oil and gas produced pursuant to a specified oil and gas lease or leases, or the proceeds from the sale thereof, carved out of the Working Interest granted by the landowners and/or mineral owners in said lease(s), to be received free and clear of all costs of drilling, development, operations or maintenance. This interest, abbreviated as ORRI is typically attributed to Petroleum Landmen and Geologists who are instrumental in acquiring or developing the prospect for the Venture. Overriding royalty interests are also held by oil companies who sub-lease or farm-out mineral acreage they hold, to other companies. In aggregate, the typical lease burden, including all royalty and overriding royalty, commonly amounts to 25-30%.

PAYOUT. The recovery, from production revenues, of the costs of drilling, completing, equipping, and operating the venture well(s) as well as all the costs associated with the offering, organizational costs, legal, general and administrative costs, leasehold (proportionate), geophysical, damages and other costs affiliated with acquisition, offering, drilling and completion of the prospect to the point of initial commercial production. In its most basic form, payout consists of the recovery from production revenues, all costs associated with conducting the ventures business equal to the dollar amount invested by the joint venture participant or in aggregate.

PARTICIPATING VENTURER. Any Venturer, including the Managing Venturer, electing pursuant to the provisions of Section 2.10 to contribute additional assessments with respect to any particular Subsequent Operation, and/or any additional Venturers admitted to the Joint Venture to contribute additional assessments with respect to any particular Subsequent Operation on behalf of a Non-Participating Venturer.

PROFITS. Each item of income and gain of the Joint Venture, as determined for federal income tax purposes, but excluding Gain from Capital Transactions.

PROCEEDS. The amount realized by the Venture on the disposition of oil and/or gas.

PRODUCTION DECLINE. The characteristic of wells in most formations, similar to certain wells in other parts of the country, to decline over time in production from a variety of factors, some of which may be corrected or ameliorated. Over the effective producing life of a given well, production levels are expected to decline in accordance with published industry data.

PROPORTIONATE SHARE. With respect to the Venturers, that share described in Article VIII of the Joint Venture Agreement.

PROSPECT. The oil, gas and mineral leasehold estate or estates, or undivided interest therein, and other contract rights and interests in oil, gas and minerals on which the drill site is proposed to be acquired pursuant to an assignment of the Lease. Nothing herein shall prevent another venture or other entity organized by the Managing Venturer or any of its Affiliates from acquiring a prospect which, subsequent to such acquisition, is determined to be in the same geological reservoir as any Prospect owned by the Venture.

PROSPECT WELL. The initial test well(s) proposed to be drilled and/or tested and, if appropriate, completed on the Prospect as a part of Initial Operations. In the case of a producing property purchase, the prospect well(s) may mean the proposed producing well(s) to be acquired.

PV-10 VALUE. The present value of estimated future gross revenue to be generated from the production of estimated net proved reserves, net of estimated production and future development costs, using prices and costs in effect as of the date indicated (unless such prices or costs are subject to change pursuant to contractual provisions), without giving effect to non-property related expenses such as general and administrative expenses, debt service and future income tax expenses or to depreciation, depletion, and amortization, discounted using an annual discount rate of 10 percent. While this measure does not include the effect of income taxes as it would in the use of the standardized measure calculation, it does provide an indicative representation of the relative value of the one company on a comparative basis to other companies, or producing properties and from period to period.

PRODUCTIVE WELL. A well that is producing oil or gas or that is capable of commercial production.

PROVED DEVELOPED RESERVES. Reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

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PROVED RESERVES. The estimated quantities of oil, gas and gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.

PROVED UNDEVELOPED RESERVES. Reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion.

REVERSIONARY INTEREST shall mean, as used in the oilfield, a legal term to denote an interest that develops after the occurrence of certain events or facts, such a payout of the well or venture.

ROYALTY INTEREST. A share of gross production of oil and gas, free of all costs of production. Abbreviated RI, this interest is typically attributed to the owner of record (usually multiple owners) of the minerals (sic) which have been leased for development through drilling. For many years, the most typical leases stipulated royalties of 12.5% or one eighth, whereas since the late 1970's and most particularly on high value tracts, royalty interests are now most commonly 20% to 30%.

SUBSEQUENT OPERATIONS. Activities not part of initial operations, which the Venturer deems necessary to develop the Prospect subsequent to the drilling, testing and Completion of the Prospect Well.

SUBSTITUTE VENTURER. Any person not previously a Venturer who purchases Units from a Venturer in accordance with the terms of this Agreement. After admission, all Substitute Venturers shall have all the rights of a Venturer.

TURNKEY COMPLETION CONTRACT. If completion is attempted on the Prospect Well, the agreement to be entered into by and between either the Managing Joint Venturer or the operator of record, in its individual capacity, and the Venture providing for the obligation of the Managing Venturer to bear the completion costs of completing the Prospect Well at a fixed or turnkey price.

TURNKEY DRILLING CONTRACT. The agreement to be entered into by and between the Managing Joint Venturer or the Operator of Record, in its individual capacity, and the Venture providing for the obligation of the Managing Venturer to bear the Drilling Costs of drilling and testing the Prospect Well at a fixed or turnkey price. The Managing Joint Venturer is obligated only to drill and test to a predetermined depth subject to certain conditions and is obligated to complete only one potential pay zone under the typical turn-key contract. Operations in addition to those specified under the Turn-Key contract are subject to additional charges to the joint venture which may be through operating cost charges or additional assessments for subsequent operations.

TURNKEY PRICE. The amount to be paid by the Venture to Signal Oil llc. to perform the Turnkey Drilling Contract (the Turnkey Drilling Price) and, if advisable, to perform the Turnkey Completion Contract (the Turnkey Completion Price).

UNITS. Interests in the Joint Venture initially authorized under the Joint Venture Agreement and allocated to the Venturers as shown on the books and records of the Venture on the date of the event for which such Units are to be computed.

UNDEVELOPED ACREAGE. Lease acreage on which wells have not been drilled or completed to a point that would permit the production of commercial quantities of oil and gas, regardless of whether such acreage contains estimated net proved reserves.

VENTURE or **JOINT VENTURE.** This Joint Venture formed under Texas law and governed by this Agreement and the Texas Uniform Partnership Act. The Joint Venture will not commence Initial Operations until the Capitalization Period is closed.

VENTURE WELLS. The wells proposed to be drilled, tested and, if appropriate, completed on the Prospect as a part of Operations.

VENTURERS. All persons or entities which are a party to the Joint Venture Agreement and participating in Units who are accepted as Venturers pursuant to the Joint Venture Agreement. The term "Venturer" shall mean any of the Venturers and includes the Managing Venturer unless the context requires otherwise. The term "SUBSTITUTE VENTURER" shall mean any person not previously a Venturer who purchases Units from a Venturer in accordance with the terms of the Joint Venture Agreement. All Venturers shall have the status of general partners. After admission, all Substitute Venturers shall have all of the rights of a Venturer.

VENTURERS' INITIAL CAPITAL. The total capital contribution to the Venture actually paid by the Venturers, including completion assessments but excluding optional additional assessments.

VOTE. The right of the Venturers, subject to all limitations set forth below and elsewhere in this Agreement, to decide any matter than may be submitted for decision by the Venturers in accordance with the express written terms of this Agreement or under the provisions of the Act. Each Venturer, including the Managing Venturer, shall be entitled to cast one vote for every one-half Unit held of record by him on the date when notice is given of the matter to be voted on or consented to by the Venturers. Except as otherwise expressly provided in this Agreement.

A Vote of the Venturers owning a majority equal to 51% of the Units shall be sufficient to pass and approve any matter submitted to a Vote of the Venturers. Whenever a Vote of the Venturers is required or permitted, a written consent to the action to be taken signed by the Venturers holding the required percentage may be used in lieu of holding a formal meeting at which a Vote is taken. The rights of the Venturers to require or be permitted to vote on any matter shall be subject to and conditioned upon the requirements set forth in Section 4.11 hereof. Proxy voting and/or split interest votes are expressly prohibited, under the agreements.

WORKING INTEREST. The joint venture interest in the oil and gas leasehold estates (the Prospect Well) which is subject to some proportion of the expense of drilling, development, operation, or maintenance. The operating interest that gives the owner the right to drill, produce, and conduct operating activities on the property and to share in the production, sales, and costs.

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