

O'Neill Andrew J  
 Form 4  
 April 04, 2018

**FORM 4**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
 Washington, D.C. 20549**

OMB APPROVAL

OMB Number: 3235-0287  
 Expires: January 31, 2005  
 Estimated average burden hours per response... 0.5

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. See Instruction 1(b).

**STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES**

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person \*  
 O'Neill Andrew J

2. Issuer Name and Ticker or Trading Symbol  
 CENTRAL SECURITIES CORP  
 [CET]

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

(Last) (First) (Middle)

3. Date of Earliest Transaction (Month/Day/Year)  
 04/02/2018

\_\_\_ Director \_\_\_ 10% Owner  
 Officer (give title below) \_\_\_ Other (specify below)  
 Vice President

C/O CENTRAL SECURITIES CORPORATION, 630 FIFTH AVENUE SUITE 820

(Street)

4. If Amendment, Date Original Filed(Month/Day/Year)

6. Individual or Joint/Group Filing(Check Applicable Line)  
 Form filed by One Reporting Person  
 \_\_\_ Form filed by More than One Reporting Person

NEW YORK, NY 10111

(City) (State) (Zip)

**Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned**

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)	
				(A) or (D)	Price			
				Code	V	Amount		
Common Stock	04/02/2018		P	A	1,129	\$ 26.41	D	
Common Stock					844		I	By child

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

**Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.**

SEC 1474 (9-02)

Edgar Filing: O'Neill Andrew J - Form 4

**Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned**  
(e.g., puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and Amount of Underlying Securities (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Nu Deriv Secur Bene Own Follo Repo Trans (Instr
						Date Exercisable	Expiration Date	Title	Amount or Number of Shares
						Code	V	(A)	(D)

## Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
O'Neill Andrew J C/O CENTRAL SECURITIES CORPORATION 630 FIFTH AVENUE SUITE 820 NEW YORK, NY 10111			Vice President	

## Signatures

/s/Andrew J. O'Neill 04/04/2018

\_\_Signature of Reporting Person Date

## Explanation of Responses:

\* If the form is filed by more than one reporting person, see Instruction 4(b)(v).

\*\* Intentional misstatements or omissions of facts constitute Federal Criminal Violations. See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, see Instruction 6 for procedure. Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. ; font-size:12pt">

### Item 6.

#### Indemnification of Directors and Officers.

Oppenheimer Holdings Inc. is obligated by its bylaws to indemnify its directors and officers and the directors and officers of its subsidiaries to the maximum extent permitted by the Canada Business Corporations Act. Oppenheimer Holdings Inc. has entered into indemnity agreements with each of its directors providing for such indemnities. In addition, Oppenheimer Holdings Inc. carries liability insurance for its directors and officers and the directors and

officers of its subsidiaries.

**Item 7.**

**Exemption from Registration Claimed.**

Not applicable.

**Item 8.**

**Exhibits.**

All exhibits are filed herewith unless otherwise indicated. For a list of the exhibits required by this item, see the Index to Exhibits immediately following the signature pages.

**Item 9.**

**Undertakings.**

(a)

The registrant hereby undertakes:

(1)

To file, during any period in which offers or sales are being made, a post-effective amendment to this Registration Statement:

(i)

To include any prospectus required by Section 10(a)(3) of the Securities Act;

(ii)

To reflect in the prospectus any facts or events arising after the effective date of the Registration Statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represents a fundamental change in the information set forth in the Registration Statement; and

(iii)

To include any material information with respect to the plan of distribution not previously disclosed in the Registration Statement or any material change to such information in the Registration Statement;

provided, however, that paragraphs (a)(1)(i) and (a)(1)(ii) do not apply if the information required to be included in a post-effective amendment by those paragraphs is contained in periodic reports filed with or furnished to the Securities and Exchange Commission by the registrant pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 that are incorporated by reference in this Registration Statement.

(2)

That, for the purpose of determining any liability under the Securities Act, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

(3)

Explanation of Responses:

To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

(a)

The registrant hereby undertakes that, for purposes of determining any liability under the Securities Act of 1933, each filing of the registrant's annual report pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 that is incorporated by reference in the Registration Statement shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

(b)

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or controlling persons of the registrant pursuant to any arrangement, provision or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of such issue.

**SIGNATURES**

Pursuant to the requirements of the Securities Act of 1933, as amended, the Company certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-8 and has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of New York, State of New York, on this 29th day of October, 2007.

OPPENHEIMER HOLDINGS INC.

(Registrant)

By: /s/ E. K. Roberts

E. K. Roberts,

President, Treasurer,

Chief Financial Officer

**POWER OF ATTORNEY**

Each person whose signature appears below hereby constitutes and appoints Elaine K. Roberts his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any or all amendments or supplements to this Registration Statement and to file the same with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent full power and authority to do and perform each and every act and thing necessary or appropriate to be done with respect to this Registration Statement or any amendments or supplements hereto in the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement has been signed by the following persons in the capacities and on the dates indicated.

Explanation of Responses:

Signature

Title

Date

/s/ A. G. Lowenthal

Chairman of the Board,

October 25, 2007

A. G. Lowenthal

Chief Executive Officer,

Director

/s/ E. K. Roberts

President, Treasurer,

October 25, 2007

E. K. Roberts

Chief Financial Officer,

Director

Signature

Title

Date

/s/A. W. Oughtred

Secretary, Director

October 25, 2007

A. W. Oughtred

/s/J. L. Bitove

Director

October 25, 2007

J.L. Bitove

/s/R. Crystal

Director

October 25, 2007

R. Crystal

/s/K. W. McArthur

Director

October 25, 2007

K. W. McArthur

/s/B. Winberg

Director

Explanation of Responses:

October 25, 2007

B. Winberg

## INDEX TO EXHIBITS

Exhibits designated by an asterisk have been heretofore filed by the Company pursuant to Section 13 or 15(d) of the Exchange Act and are hereby incorporated by reference to the pertinent filing.

<u>Exhibit No.</u>	<u>Description of Exhibit</u>	<u>Sequentially Numbered Page</u>
4(a)	Articles of Incorporation of Oppenheimer Holdings Inc. (previously filed as an exhibit to Form 10-Q for the quarterly period ended June 30, 2005).	*
4(b)	By-Laws (previously filed as an exhibit to Form 10-Q for the quarterly period ended June 30, 2005).	*
10	Oppenheimer Holdings Inc. 2006 Equity Incentive Plan	
5	Opinion of Borden Ladner Gervais LLP.	
23.1	Consent of PricewaterhouseCoopers LLP.	
23.2	Consent of Borden Ladner Gervais LLP.	
24	Power of Attorney (included on the signature pages of the registration statement)	

Voting Authority

---

Edgar Filing: O'Neill Andrew J - Form 4

Dispositive Authority

Name and Address	Total Amount of Beneficial Ownership	Percent of Class
		Sole
		Shared
		Sole
		Shared
Barclays Global Investors and affiliates 45 Fremont Street San Francisco, CA 94105 2,330,750 0 2,586,883 0 2,586,883 6.2%	440,493	
Neuberger Berman Inc. 605 Third Ave. NY, NY 10158-3698	1,526,547	
	0	
	2,688,974	
	2,688,974	
	6.4	
	%	
Royce & Associates LLC 1414 Avenue of the Americas New York, NY 10019	2,708,010	
	0	
	2,708,010	
	0	
	2,708,010	
	6.5	
	%	
State Farm Mutual Automobile Insurance One State Farm Plaza		

## Edgar Filing: O'Neill Andrew J - Form 4

Bloomington, IL 61710

2,194,205

9,346

2,194,205

9,346

2,203,551

5.3  
%

### OTHER MATTERS

#### Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires Cimarex's directors and executive officers, and persons who own more than 10% of its common stock, to file reports of ownership of, and transactions in, Cimarex common stock with the SEC. The reports by such persons are published on Cimarex's website at <http://www.cimarex.com>. Based on a review of such reports, and on written representations from our reporting persons, Cimarex believes that all reports were timely filed in 2004, except forms reporting the exchange by Messrs. Helmerich, Sullivan and Teague of 1,829 shares of restricted stock for a like number of deferred compensation units were not timely filed.

#### Incorporation by Reference

To the extent that this joint proxy statement/prospectus is incorporated by reference into any other filing by Cimarex under the Securities Act of 1933 or the Securities Exchange Act of 1934, the sections of this joint proxy statement/prospectus entitled "Governance Committee Report on Executive Compensation," and "Report of the Audit Committee" and "Stock Price Performance" will not be deemed incorporated, unless specifically provided otherwise in such filing.

#### Other Matters

There are no other matters that the Board of Directors intends to present, or has reason to believe others will present, at the Cimarex annual meeting. If other matters come before the annual meeting, the persons named in the accompanying form of proxy will vote in accordance with their best judgment with respect to such matters.

II-14

---

**Complaint and Reporting Procedures**

Cimarex has established complaint and reporting procedures, which are posted on Cimarex's website at *www.cimarex.com*. Any person, whether or not an employee, who has a concern about the conduct of Cimarex or any of its people, including accounting, internal accounting controls or auditing issues, may, in a confidential or anonymous manner, communicate that concern by calling Cimarex's confidential hotline, 1-866-519-1898. Any interested party, whether or not an employee, who wishes to communicate directly with the presiding non-management director or with Cimarex's non-management directors as a group, also may call the confidential hotline. The hotline is available 24 hours a day, seven days a week and is completely confidential. Comments will be typed verbatim and will be delivered to a representative with authority to investigate the concern.

II-15

---

**CHAPTER III THE STOCKHOLDER MEETINGS, VOTING AND OTHER INFORMATION**

**THE CIMAREX ANNUAL MEETING**

Cimarex is furnishing this joint proxy statement/prospectus to its common stockholders in connection with the solicitation of proxies by the Cimarex board of directors for use at the annual meeting of its stockholders. This joint proxy statement/prospectus and form of proxy will be mailed to Cimarex stockholders on approximately May 6, 2005.

**The board of directors of Cimarex, by unanimous vote of the directors present at their meeting:**

**has determined that the merger agreement and the transactions contemplated thereby, including the merger, are fair to, and in the best interests of, Cimarex and its stockholders;**

**has approved and adopted the merger agreement and approved the merger and the other transactions contemplated thereby;**

**recommends that the stockholders of Cimarex vote "FOR" approval of the issuance of shares of Cimarex common stock in connection with the merger;**

**recommends that the stockholders of Cimarex vote "FOR" approval of the proposed amendments to the Cimarex charter and the Cimarex incentive plan that are described below;**

**recommends that stockholders of Cimarex vote "FOR" each of the named nominees for director; and**

**recommends that stockholders of Cimarex vote "FOR" the ratification of KPMG LLP as Cimarex's independent auditors for the year ending December 31, 2005.**

**Date; Place and Time**

The Cimarex annual meeting is scheduled to be held in the Central City Room at the Brown Palace Hotel, 321 17<sup>th</sup> Street, Denver, Colorado 80202, on June 6, 2005, at 10:30 a.m. local time.

**Purpose of the Annual Meeting**

The purpose of the Cimarex annual meeting is to consider and vote upon:

the issuance of shares of Cimarex common stock in connection with the merger agreement, dated as of January 25, 2005, as amended on February 18, 2005 and April 20, 2005, by and among Cimarex, Magnum Hunter and Merger Sub, a wholly owned subsidiary of Cimarex, under which Merger Sub will be merged with and into Magnum Hunter;

a proposal to amend the Cimarex charter to increase the number of authorized shares of common stock from 100 million shares to 200 million shares;

a proposal to amend the Cimarex charter to increase the maximum size of the board of directors from nine to ten directors;

## Edgar Filing: O'Neill Andrew J - Form 4

a proposal to amend the Cimarex incentive plan to increase the number of shares authorized for issuance under the plan from seven million shares to 12.7 million shares and make other changes to the Cimarex incentive plan as discussed under the caption "Chapter I The Merger Other Merger-Related Proposals to Be Presented at the Cimarex Annual Meeting Proposal to Amend the Cimarex Incentive Plan" on page I-137;

a proposal to elect three directors to serve until the 2008 annual meeting; and

a proposal to ratify the audit committee's appointment of KPMG LLP as Cimarex's independent auditors for the year ending December 31, 2005; and

III-1

---

## Edgar Filing: O'Neill Andrew J - Form 4

to the extent permitted under the merger agreement, such other matters as may be appropriate for consideration at the annual meeting.

Approval of the proposal to issue Cimarex common stock in the merger is a condition to the closing of the merger. Approval of the proposals to amend the Cimarex charter and the Cimarex incentive plan is not a condition to the closing of the merger. Neither of the proposed amendments to the Cimarex charter will be effected unless the merger takes place. The proposed amendment to the Cimarex incentive plan will be effected whether or not the merger closes.

### **Record Date; Stock Entitled to Vote; Quorum**

Cimarex stockholders of record as of the close of business on April 29, 2005, the record date for the annual meeting, are entitled to receive notice of and to vote at the annual meeting. Cimarex's common stock is the only class of voting securities of Cimarex. On the record date, there were 41,786,219 shares of Cimarex common stock outstanding and entitled to vote at the annual meeting.

Each share of common stock you own as of the April 29, 2005 record date entitles you to one vote. The number of shares you own is shown on your proxy card beneath and to the right of your name.

In order to conduct business at the annual meeting, Cimarex must have a quorum. This means that greater than 50% of the outstanding shares of common stock as of the close of business on the April 29, 2005 record date must be represented in person or by proxy at the annual meeting. Abstentions and broker non-votes are counted as present for establishing a quorum. Broker non-votes occur when a broker returns a proxy but does not have authority to vote on a particular proposal. If a quorum is not present at the meeting, a vote for adjournment will be taken among the stockholders present or represented by proxy. If a majority of the stockholders present or represented by proxy vote for adjournment, it is Cimarex's intention to adjourn the annual meeting until a later date and to vote proxies at the adjourned meeting.

### **Vote Required**

The affirmative vote of a majority of the votes cast in person or by proxy and entitled to vote at the Cimarex annual meeting is required to approve the issuance of shares of Cimarex common stock in connection with the merger and the proposed amendment to the Cimarex incentive plan. The affirmative vote of a majority of the outstanding shares of Cimarex common stock as of the record date of the Cimarex annual meeting is required to approve each of the proposed amendments to the Cimarex charter. Directors will be elected by a plurality of the votes. A "plurality" means that the three director nominees receiving the most "FOR" votes will be elected as Class III directors. The affirmative vote of a majority of the shares present and entitled to vote, in person or by proxy, at the annual meeting is required to ratify the audit committee's appointment of KPMG LLP as Cimarex's independent auditors for 2005.

Abstentions may be specified with respect to the proposal by properly marking the "ABSTAIN" box on the proxy for that proposal or by making the same election by telephone or Internet voting. Abstentions, broker non-votes and failures to vote will not affect the outcome of the vote on the proposals to issue shares in the merger, amend the Cimarex incentive plan or ratify the appointment of KPMG LLP as independent auditors for 2005, since they will not be counted as votes either for or against these proposals. Abstentions, broker non-votes and failures to vote will count as votes against each of the proposals to amend the Cimarex charter. Neither abstentions nor broker non-votes will have an effect on the votes for or against the election of a director.

## Edgar Filing: O'Neill Andrew J - Form 4

Continental Stock Transfer & Trust Company, New York, New York, Cimarex's stock transfer agent, will receive proxies and ballots, tabulate the vote, determine whether a quorum exists and serve as inspector of election at the annual meeting.

### Share Ownership of Cimarex Directors, Executive Officers and Significant Stockholders

At the close of business on the record date and excluding shares underlying options and restricted stock, Cimarex's directors and executive officers and their affiliates may be deemed to be the beneficial owners of, and have the power to vote, 1,393,190 shares of Cimarex common stock, representing approximately 3.3% of the then outstanding shares of Cimarex common stock entitled to vote at the Cimarex annual meeting. Cimarex believes that each of its directors and executive officers intends to vote "FOR" the approval of the issuance of shares of Cimarex common stock in the merger, "FOR" each proposed amendment to the Cimarex charter, "FOR" the proposed amendment to the Cimarex incentive plan, "FOR" the election of each of the named nominees for director and "FOR" the ratification of the appointment of KPMG LLP as independent auditors for 2005.

### Voting of Proxies

Cimarex provides several options for Cimarex stockholders to cast their vote. You may attend the meeting and vote in person or you can vote in any one of the following three ways:

by telephone by following the instructions on either the enclosed proxy card or voting instruction form; or

on the Internet by following the instructions on the enclosed proxy card; or

by signing and returning the proxy card in the enclosed postage paid envelope.

Shares of Cimarex common stock represented by properly executed proxies received before the annual meeting will be voted at the annual meeting in the manner specified on the proxies. Physical proxies that are properly executed and timely submitted but which do not contain specific voting instructions will be voted "FOR" each of the proposals presented at the Cimarex annual meeting.

Cimarex stockholders whose shares are held in "street name" (i.e., in the name of a broker, bank or other record holder) must either direct the record holder of their shares as to how to vote their shares or obtain a proxy from the record holder to vote at the annual meeting. If you do not provide voting instructions (commonly referred to as "broker non-votes"), your shares will be counted for purposes of determining the presence or absence of a quorum for the transaction of business, but will not be voted in favor of any of the proposals presented at the Cimarex annual meeting. Broker non-votes will be considered as abstentions and will not affect the outcome of the vote to approve the issuance of Cimarex common stock in the merger, or the proposed amendment to the Cimarex incentive plan or the ratification of KPMG LLP as independent auditors for 2005, since they will not be counted as votes either for or against the proposal. Broker non-votes will be counted as votes against each proposed amendment to the Cimarex charter. Broker non-votes will have no effect on the votes for or against the election of a director.

Cimarex stockholders may receive more than one proxy or voting card depending on how they hold their shares. If you hold shares through someone else, such as a stockbroker, you may receive material from them asking how you want to vote your shares. Please vote each proxy you receive.

If you are a participant in the Cimarex Energy Co. 401(k) Plan, you will receive a proxy card for the Cimarex shares you own through the 401(k) Plan. That proxy card will serve as a voting instruction card for the trustee of the 401(k) Plan, and your 401(k) Plan shares will be voted as you instruct. If you do not sign and return your voting instruction card to indicate your instructions, the 401(k) Plan trustee will vote your 401(k) Plan shares in the same proportion as the shares voted by other plan participants.

### **Revoking Your Proxy**

Cimarex recommends you vote by proxy even if you plan to attend the meeting. You may always change your vote at the meeting. If you hold shares through a bank, broker or other nominee and would like to attend the annual meeting and vote in person, you will need to bring an account statement as of the close of business on April 29, 2005. Alternatively, you may contact the person in whose name your shares are registered and obtain a proxy and bring it to the annual meeting.

Cimarex stockholders may revoke their proxy before it is voted by submitting a new proxy with a later date (either by telephone, on the Internet, or by returning a new proxy card), by voting in person at the meeting, or by notifying Cimarex's Assistant Corporate Secretary in writing at 1700 Lincoln Street, Suite 1800, Denver, Colorado 80203-4518.

Attending the annual meeting will not by itself revoke your proxy. To do so, you must vote in person at the meeting. If you have instructed your broker to vote your shares, you must follow your broker's directions in order to change your vote.

### **Expenses of Solicitation**

Cimarex will bear all costs of the solicitation of proxies, including the costs of printing and mailing this joint proxy statement/prospectus to Cimarex stockholders and reimbursements to brokerage firms and others for their expenses in forwarding proxy materials. In addition to solicitation by mail, solicitation of proxies may be made by certain officers and regular employees of Cimarex by mail, telephone or in person. Cimarex also has retained Georgeson Shareholder Communications, Inc. to aid in the solicitation of brokers, banks, intermediaries, and other institutional holders in the United States for a fee not to exceed \$15,000 plus out-of-pocket expenses.

### **Miscellaneous**

If a quorum is not present at the time the Cimarex annual meeting is convened, or if for any other reason Cimarex believes that additional time should be allowed for the solicitation of proxies, Cimarex may adjourn the annual meeting with or without a vote of the stockholders. If Cimarex proposes to adjourn the annual meeting by a vote of the stockholders, the persons named in the enclosed form of proxy will vote all shares of Cimarex common stock for which they have voting authority in favor of an adjournment. Proxies voted against the proposal related to the issuance of Cimarex common stock in the merger will not be voted in favor of any adjournment of the annual meeting for the purpose of soliciting additional proxies.

Cimarex does not expect that any matter not referred to in this joint proxy statement/prospectus will be presented for action at the Cimarex annual meeting. If any other matters are properly brought before the annual meeting, the persons named in the proxies will have discretion to vote on those matters according to their best judgment. The grant of a proxy will also confer discretionary authority on the persons named in the proxy as proxy appointees to vote in accordance with their best judgment on matters incidental to the conduct of the annual meeting.

### **THE MAGNUM HUNTER SPECIAL MEETING**

Magnum Hunter is furnishing this joint proxy statement/prospectus to its common stockholders in connection with the solicitation of proxies by the Magnum Hunter board of directors for use at the special meeting of its stockholders. Magnum Hunter is also furnishing this joint proxy statement/prospectus to the holders of its Series A preferred stock to provide them with notice of the meeting as required by Nevada law. This joint proxy statement/prospectus will be mailed to Magnum Hunter common stockholders and Series A preferred stockholders, and the form of proxy will be mailed to Magnum Hunter common stockholders, on approximately May 6, 2005.

**The board of directors of Magnum Hunter unanimously:**

**has determined that the merger agreement, the merger, in accordance with the terms of the merger agreement, and the other transactions contemplated thereby are fair to, and in the best interests of, Magnum Hunter and its stockholders;**

**has approved and adopted the merger agreement and approved the merger and the other transactions contemplated thereby; and**

**recommends that the stockholders of Magnum Hunter vote "FOR" approval of the merger agreement and the merger.**

**Date; Place and Time**

The Magnum Hunter special meeting is scheduled to be held at the Four Seasons Resort and Club, 4150 North MacArthur Blvd., Irving, Texas 75038, on June 6, 2005, at 10:00 a.m. local time.

**Purpose of the Special Meeting**

The purpose of the special meeting is to consider and vote upon the merger agreement, dated as of January 25, 2005, as amended on February 18, 2005 and April 20, 2005, by and among Cimarex, Magnum Hunter and Merger Sub, a wholly owned subsidiary of Cimarex, under which Merger Sub will be merged with and into Magnum Hunter, and, to the extent permitted under the merger agreement, such other matters as may be appropriate for consideration at the special meeting. Approval of this proposal is a condition to the closing of the merger.

**Record Date; Stock Entitled to Vote; Quorum**

Holders of Magnum Hunter's common stock at the close of business on April 15, 2005, the record date for the special meeting, are entitled to receive notice of and to vote at the special meeting. Magnum Hunter's common stock will be the only class of securities of Magnum Hunter entitled to vote on the proposal. On the record date, approximately 95,187,747 shares of common stock were issued and outstanding and entitled to vote at the special meeting. Holders of Magnum Hunter's Series A preferred stock at the close of business on April 15, 2005, the record date for the special meeting, are entitled to receive notice of the special meeting but are not entitled to vote at the special meeting. Although Magnum Hunter's Series A preferred stock does not have voting rights with respect to the proposal, Nevada law requires Magnum Hunter to give the Series A preferred stockholders notice of the special meeting. Because all shares of Magnum Hunter's 1996 Series A convertible preferred stock are currently held by a wholly owned subsidiary of Magnum Hunter, they are not considered "outstanding" and are not entitled to vote on the proposal.

Owners of record of Magnum Hunter common stock on the record date are each entitled to one vote per share with respect to the approval of the merger agreement.

A quorum of Magnum Hunter stockholders is necessary to have a valid meeting of stockholders. The presence at the Magnum Hunter special meeting, in person or by proxy, of the holders of one-third of the outstanding shares of Magnum Hunter common stock will constitute a quorum. Abstentions and broker non-votes count as present for purposes of establishing a quorum. An abstention occurs when a stockholder attends a meeting, either in person or by proxy, but abstains from voting. A broker non-vote occurs on an item when a broker is not permitted to vote on that item without instructions from the beneficial owner of the shares and no instructions are given.

### **Vote Required**

The affirmative vote of the holders of at least a majority of the shares of Magnum Hunter common stock issued and outstanding and entitled to vote at the Magnum Hunter special meeting is required to approve the merger agreement and the merger. Abstentions may be specified with respect to the proposal by properly marking the "ABSTAIN" box on the proxy for that proposal. Abstentions, broker non-votes and failures to vote will have the effect of votes cast against the proposal.

### **Share Ownership of Magnum Hunter Directors, Executive Officers and Significant Stockholders**

At the close of business on the record date and excluding shares underlying options, Magnum Hunter's directors and executive officers and their affiliates may be deemed to be the beneficial owners of, and have the power to vote, 6,080,496 shares of Magnum Hunter common stock, representing approximately 6.3% of the then outstanding shares of Magnum Hunter common stock entitled to vote at the Magnum Hunter special meeting. Magnum Hunter believes that each of its directors and executive officers intends to vote "FOR" the approval of the merger agreement and the merger.

On the date the merger agreement was executed, Gary C. Evans, Magnum Hunter's former President and Chief Executive Officer, and Jacquelyn Evelyn Enterprises, Inc. a related stockholder, entered into a voting agreement with Cimarex. As of March 31, 2005, these stockholders beneficially owned and were entitled to vote, in the aggregate, 3,943,794 shares of Magnum Hunter common stock, which represented approximately 4.1% of the shares of Magnum Hunter common stock outstanding on that date. Under the voting agreement, these stockholders have agreed, among other things, to vote all of their shares of Magnum Hunter common stock in favor of the merger agreement, against any action or agreement that they would reasonably expect to result in a material breach of any covenant, representation, warranty or other obligation of Magnum Hunter under the merger agreement and against any other takeover proposal. The voting agreement is attached as *Annex E* to this joint proxy statement/prospectus.

### **Voting of Proxies**

Magnum Hunter stockholders may cast their vote by attending the meeting and voting in person or by signing and returning the proxy card in the enclosed postage paid envelope.

Shares of Magnum Hunter common stock represented by properly executed proxies received before the special meeting will be voted at the special meeting in the manner specified on the proxies. Physical proxies that are properly executed and timely submitted but which do not contain specific voting instructions will be voted "FOR" the proposal presented at the Magnum Hunter special meeting.

Magnum Hunter stockholders whose shares are held in "street name" (i.e., in the name of a broker, bank or other record holder) must either direct the record holder of their shares as to how to vote their shares or obtain a proxy from the record holder to vote at the special meeting. If you do not provide voting instructions (commonly referred to as "broker non-votes"), your shares will be counted for purposes of determining the presence or absence of a quorum for the transaction of business, but will not be voted in favor of the proposal presented at the Magnum Hunter special meeting. Broker non-votes will be counted as votes against the approval of the merger agreement and the transactions contemplated thereby.

Magnum Hunter stockholders may receive more than one proxy or voting card depending on how they hold their shares. If you hold shares through someone else, such as a stockbroker, you may receive material from them asking how you want to vote your shares. Please vote each proxy you receive.

If you are a participant in the Magnum Hunter Resources, Inc. 401(k) Employee Stock Ownership Plan, the trustee of the plan's related trust will vote all shares of Magnum Hunter common stock held in trust, though you as a participant may direct the trustee regarding how to vote any shares allocated

to your plan account. You will receive voting instructions from the trustee as to how to exercise your voting rights under the plan. If you do not exercise your right to vote the shares allocated to your plan account, the trustee will vote those shares in accordance with the terms of the plan and trust. Unallocated shares held by the trustee also will be voted by the trustee in accordance with the terms of the plan and trust.

If you are a participant in the Magnum Hunter, Inc. 2003 Bonus Deferral Plan, you will receive a proxy card for the Magnum Hunter shares that are credited to your bookkeeping account. That proxy card will serve as a voting instruction card for the Plan committee and those shares will be voted as you instruct. If you do not sign and return your voting instruction card to the Plan committee, the Plan committee will direct the manner in which your shares are voted.

### **Revoking Your Proxy**

Magnum Hunter recommends you vote by proxy even if you plan to attend the meeting. You may always change your vote at the meeting. If you hold shares through a bank, broker or other nominee and would like to attend the special meeting and vote in person, you will need to bring an account statement as of the close of business on April 15, 2005. Alternatively, you may contact the person in whose name your shares are registered and obtain a proxy and bring it to the special meeting.

Magnum Hunter stockholders may revoke their proxy before it is voted by submitting a new proxy card with a later date, by voting in person at the meeting, or by notifying Magnum Hunter's Secretary at 600 East Las Colinas Blvd., Suite 1100, Irving, Texas 75039.

Attending the special meeting will not by itself revoke your proxy. To do so, you must vote in person at the meeting. If you have instructed your broker to vote your shares, you must follow your broker's directions in order to change your vote.

### **Expenses of Solicitation**

Cimarex will bear the costs of printing this joint proxy statement/prospectus and Magnum Hunter will bear the costs of mailing this joint proxy statement/prospectus to Magnum Hunter stockholders and the costs of soliciting proxies from Magnum Hunter stockholders, including reimbursements to brokerage firms and others for their expenses in forwarding proxy materials. In addition to solicitation by mail, solicitation of proxies may be made by certain officers and regular employees of Magnum Hunter by mail, telephone or in person. Magnum Hunter also has retained Georgeson Shareholder Communications, Inc. to aid in the solicitation of brokers, banks, intermediaries, and other institutional holders in the United States for a fee not to exceed \$11,000 plus out-of-pocket expenses.

### **Miscellaneous**

If a quorum is not present at the time the Magnum Hunter special meeting is convened, or if for any other reason Magnum Hunter believes that additional time should be allowed for the solicitation of proxies, Magnum Hunter may adjourn the special meeting with or without a vote of the stockholders. If Magnum Hunter proposes to adjourn the special meeting by a vote of the stockholders, the persons named in the enclosed form of proxy will vote all shares of Magnum Hunter common stock for which they have voting authority in favor of an adjournment.

Magnum Hunter does not expect that any matter not referred to in this joint proxy statement/prospectus will be presented for action at the Magnum Hunter special meeting. If any other matters are properly brought before the special meeting, the persons named in the proxies will have discretion to vote on those matters according to their best judgment. The grant of a proxy will also confer discretionary authority on the persons named in the proxy as proxy appointees to vote in accordance with their best judgment on matters incidental to the conduct of the special meeting. Proxies voted against the proposal related to the merger will not be voted in favor of any adjournment of the special meeting for the purpose of soliciting additional proxies.

**Holders of Magnum Hunter common stock and Magnum Hunter Series A preferred stock should not send their stock certificates at this time. If the merger is completed, a separate letter of transmittal will be mailed to you, which will enable you to receive the appropriate consideration.**

### LEGAL MATTERS

The validity of the issuance of the shares of Cimarex's common stock to be issued to Magnum Hunter stockholders in the merger will be passed upon for Cimarex by Holme Roberts & Owen LLP, Denver, Colorado.

Certain United States federal income tax consequences of the merger will be passed upon for Cimarex by Holme Roberts & Owen LLP, Denver, Colorado and for Magnum Hunter by Thompson & Knight L.L.P., Dallas, Texas.

### EXPERTS

The consolidated financial statements of Cimarex as of December 31, 2004 and 2003, and for each of the years in the three-year period ended December 31, 2004, and management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2004 have been incorporated by reference herein in reliance upon the reports of KPMG LLP, independent registered public accounting firm, incorporated by reference herein, and upon authority of said firm as experts in accounting and auditing. Their reports refer to the adoption of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations," as of January 1, 2003.

The consolidated financial statements and related financial statement schedule included in this joint proxy statement/prospectus have been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report appearing herein (which report expresses an unqualified opinion on the financial statements and financial statement schedule and includes an explanatory paragraph relating to changes in methods of accounting for asset retirement obligations and employee stock based compensation in 2003 as required by Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" and Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure, an Amendment to FASB Statement No. 123") and have been so included in reliance upon the reports of such firm given upon their authority as experts in auditing and accounting.

Ryder Scott Company, L.P., independent petroleum engineers, has reviewed Cimarex's proved reserve estimates associated with approximately 80 percent of the discounted future net cash flows before income taxes for the years ended December 31, 2004 and 2003. Estimated quantities of Cimarex's oil and gas reserves and the net present value of such reserves have been included and incorporated by reference in this joint proxy statement/prospectus in reliance on the authority of said firms as experts in petroleum engineering.

The estimated reserve evaluations and related calculations for Magnum Hunter of DeGolyer and MacNaughton and Cawley, Gillespie & Associates, Inc., each independent petroleum engineering consultants, included in this joint proxy statement/prospectus have been so included in reliance on the authority of said firms as experts in petroleum engineering.

### INDEPENDENT ACCOUNTANTS

Representatives of KPMG LLP, current independent accountants of Cimarex, are expected to be present at the Cimarex annual meeting and will be available to respond to appropriate questions.

Representatives of Deloitte & Touche LLP, current independent accountants of Magnum Hunter, are expected to be present at the Magnum Hunter special meeting and will be available to respond to appropriate questions.

### CIMAREX 2006 ANNUAL STOCKHOLDERS MEETING AND STOCKHOLDER PROPOSALS

Any stockholder wishing to submit a proposal for the vote of the stockholders at Cimarex's 2006 annual meeting must submit such proposal or proposals in writing to Cimarex no later than December 21, 2005. Proposals should be sent to the attention of the Assistant Corporate Secretary at 1700 Lincoln Street, Suite 1800, Denver, Colorado 80203. Cimarex is not required to include in its proxy statement a form of proxy or stockholder proposal that is received after that date or otherwise fails to meet the requirements for stockholder proposals established by regulations of the Securities and Exchange Commission.

As required by Cimarex's By-laws, a stockholder must give timely notice of a nomination for election as a director. A notice is timely if received no earlier than February 10, 2006 and no later than February 20, 2006. The advance notice must be delivered to the attention of the Assistant Corporate Secretary at 1700 Lincoln Street, Suite 1800, Denver, Colorado 80203, and must comply with the requirements of Cimarex's By-Laws.

### MAGNUM HUNTER 2005 ANNUAL STOCKHOLDERS MEETING AND STOCKHOLDER PROPOSALS

Magnum Hunter will hold an annual meeting in 2005 only if the merger has not already been completed. In order to be included in the proxy statement for the 2005 annual meeting of Magnum Hunter's stockholders, stockholder proposals must have been received by Magnum Hunter by January 31, 2005, in order to be considered for inclusion in Magnum Hunter's proxy statement and form of proxy relating to that meeting.

### WHERE YOU CAN FIND MORE INFORMATION

Cimarex and Magnum Hunter file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's public reference rooms in Washington, D.C., New York, New York and Chicago, Illinois. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our SEC filings are also available to the public at the SEC's website at <http://www.sec.gov>. Copies of documents filed by Cimarex and Magnum Hunter with the SEC are also available at the offices of The New York Stock Exchange, 20 Broad Street New York, New York 10005.

Cimarex has filed a registration statement on Form S-4 with the SEC under the Securities Act to register the Cimarex common stock to be issued in connection with the merger. This joint proxy statement/prospectus constitutes the prospectus of Cimarex filed as part of the registration statement. This joint proxy statement/prospectus does not contain all of the information that Cimarex stockholders and Magnum Hunter stockholders can find in the registration statement or the exhibits to the registration statement because certain parts of the registration statement are omitted in accordance with the rules and regulations of the SEC. The registration statement and its exhibits contain important information about Cimarex and Magnum Hunter and their respective business, financial condition and results of operations and are available for inspection and copying as indicated above.

## Edgar Filing: O'Neill Andrew J - Form 4

The SEC allows us to "incorporate by reference" into this joint proxy statement/prospectus documents filed with the SEC by Cimarex. This means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be a part of this joint proxy statement/prospectus, and later information that Cimarex files with the Securities and Exchange Commission will update and supersede that information. We incorporate by reference the documents listed below and any documents filed by Cimarex under Section 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of this joint proxy statement/prospectus and before the date of the Cimarex annual meeting and the Magnum Hunter special meeting, excluding any information furnished under Item 7.01 or Item 2.02 of any current report on Form 8-K:

<u>Cimarex's Filings (SEC File No. 001-31446)</u>	<u>Periods</u>
Annual Report on Form 10-K Current Reports on Form 8-K	Year ended December 31, 2004 Filed on January 26, January 28, February 23, March 14, March 18 and April 8, 2005
The description of Cimarex's common stock and preferred stock contained in Amendment No. 1 to Cimarex's Registration Statement on Form 10	Filed on September 23, 2002

Cimarex also incorporates by reference additional documents that may be filed with the SEC under Section 13(a), 13(c), 14 or 15(d) of the Exchange Act between the date of this joint proxy statement/prospectus and the date of the Cimarex annual meeting and the Magnum Hunter special meeting. These include periodic reports, such as Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, as well as proxy statements, excluding any information furnished under Item 7.01 or Item 2.02 of any current report on Form 8-K.

If you are a Cimarex stockholder, Cimarex may have sent you some of the documents incorporated by reference, but you can obtain any of them through Cimarex, the SEC or the SEC's Internet web site as described above. Documents incorporated by reference are available from the companies without charge, excluding all exhibits, except that if the companies have specifically incorporated by reference an exhibit in this joint proxy statement/prospectus, the exhibit will also be provided without charge. Stockholders may obtain documents incorporated by reference in this joint proxy statement/prospectus by requesting them in writing or by telephone from Cimarex at the following address:

Cimarex Energy Co.  
1700 Lincoln Street, Suite 1800  
Denver, Colorado 80203-4518  
Attn: Mary Kay Rohrer, Assistant Corporate  
Secretary  
(303) 295-3995

**Your request must be received no later than five business days before the Cimarex annual meeting or the Magnum Hunter special meeting, as applicable, in order to obtain timely delivery of any materials that you request.**

This joint proxy statement/prospectus does not constitute an offer to sell, or a solicitation of an offer to purchase, the securities offered by this joint proxy statement/prospectus, or the solicitation of a proxy, in any jurisdiction to or from any person to whom or from whom it is unlawful to make such offer, solicitation of an offer or proxy solicitation in such jurisdiction. Neither the delivery of this joint proxy statement/prospectus nor any distribution of securities under this joint proxy statement/prospectus shall, under any circumstances, create any implication that there has been no change in the information set forth or incorporated into this joint proxy statement/prospectus by reference or in the affairs of

Cimarex or Magnum Hunter since the date of this joint proxy statement/prospectus. The information contained in this joint proxy statement/prospectus with respect to Cimarex was provided by Cimarex and the information contained in this joint proxy statement/prospectus with respect to Magnum Hunter was provided by Magnum Hunter.

**You should rely only on the information contained in or incorporated by reference into this joint proxy statement/prospectus to vote on the approval of the merger agreement. Neither Cimarex, Magnum Hunter nor Merger Sub has authorized anyone to provide you with information that is different from what is contained in this joint proxy statement/prospectus. This joint proxy statement/prospectus is dated as of the date set forth on the cover page. You should not assume that the information contained in this joint proxy statement/prospectus is accurate as of any date other than this date and neither the mailing of this joint proxy statement/prospectus to stockholders nor the delivery of shares of Cimarex's common stock in the merger shall create any implications to the contrary.**

III-11

---

**CHAPTER IV MAGNUM HUNTER BUSINESS &  
FINANCIAL INFORMATION**

**SELECTED HISTORICAL FINANCIAL DATA**

The selected historical financial data sets forth Magnum Hunter's summary historical consolidated financial data as of and for the years ended December 31, 2004, 2003, 2002, 2001 and 2000, and was derived from the audited consolidated financial statements and notes thereto for those years. The selected historical financial data is qualified in its entirety by, and should be read in conjunction with, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and the notes thereto included elsewhere in this joint proxy statement/prospectus. For additional information relating to Magnum Hunter's operations, see "Business" and "Properties." Certain reclassifications have been made to the selected historical financial data of the prior years, as well as to certain quarterly financial data, to conform with the current presentation. All data is in thousands, except per share data.

	2004	2003	2002	2001	2000
<b>Income Statement Data:</b>					
Operating revenues	\$ 493,726	\$ 325,014	\$ 265,869	\$ 152,806	\$ 127,510
Operating costs and expenses(a)	(287,793)	(232,316)	(197,000)	(104,755)	(77,181)
Operating profit	205,933	92,698	68,869	48,051	50,329
Provision for impairment of investment(b)			(621)	(7,123)	
Costs associated with early retirement of debt(c)	(12,250)	(6,716)	(1,000)	(490)	
Cumulative effect on prior years of a change in accounting principle, net of tax(d)		399			
Net Income	103,573	26,117	15,522	13,516	22,260
Dividends applicable to preferred shares(e)					(9,708)
Income applicable to common shares	103,573	\$ 26,117	\$ 15,522	\$ 13,516	\$ 12,552
Income per common share before cumulative effect of a change in accounting principle					
Basic(e)	\$ 1.35	\$ 0.38	\$ 0.25	\$ 0.39	\$ 0.60
Diluted(e)	\$ 1.31	\$ 0.38	\$ 0.25	\$ 0.36	\$ 0.51
Income (loss) per common share after cumulative effect of a change in accounting principle					
Basic(e)	\$ 1.35	\$ 0.39	\$ 0.25	\$ 0.39	\$ 0.60
Diluted(e)	\$ 1.31	\$ 0.39	\$ 0.25	\$ 0.36	\$ 0.51
<b>Other Data:</b>					
Proceeds from sale of assets	\$ 22,902	\$ 17,123	\$ 95,988	\$ 1,124	\$ 43,770
Capital expenditures(f)	\$ 540,010	\$ 175,535	\$ 141,046	\$ 204,370	\$ 60,830

(a) Includes in 2001 a provision for loss of \$3.2 million related to the Enron bankruptcy.

(b) Includes in 2002 and 2001 a provision for \$621 thousand and \$2.1 million, respectively, for the impairment of available-for-sale equity securities deemed by Magnum Hunter's management to have suffered an other than temporary impairment. The impairment was determined using a quoted market price at December 31, 2001 of \$0.86 per share. Magnum Hunter had previously reported losses in accumulated other comprehensive income of \$507 thousand (\$466 thousand net of income tax benefit) through December 31, 2001. Also included in 2001 was an impairment

## Edgar Filing: O'Neill Andrew J - Form 4

provision of \$5.0 million due to the bankruptcy of a privately held company in which Magnum Hunter owned a minority interest and had invested \$4.5 million in equity securities and \$453 thousand in secured loans.

- (c) Includes in 2004 the cost of retirement of \$105 million in principal of Magnum Hunter's 9.6% Senior Notes due March 15, 2012. Includes in 2003 the cost of retirement of \$129.5 million in principal of Magnum Hunter's 10% Senior Notes due June 1, 2007. Includes in 2002 the costs associated with the amendment of Magnum Hunter's Facility in connection with the Prize merger. Includes in 2001 the cost of retirement of \$10.5 million of Magnum Hunter's 10% Senior Notes.
- (d) Includes in 2003 the cumulative effect on prior years of a change in accounting principle due to the adoption of SFAS No. 143 relating to asset retirement obligations. The cumulative effect was a gain of \$399 thousand, net of income tax expense of \$244 thousand.
- (e) Includes the effect in the year 2000 of the payment of a \$5.5 million fee upon redemption of \$25.0 million (liquidation value) of Magnum Hunter's 1999 Series A 8% convertible preferred stock. The fee was treated as a dividend, reducing income per common share, basic and diluted, by \$0.26 per share and \$0.17 per share, respectively, for the year 2000.
- (f) Capital expenditures include cash expended for acquisitions plus normal additions to oil and natural gas properties and other fixed assets. It does not include the cost of property acquired through the issuance of common stock and does not include cash adjustments for liabilities assumed in the New Mexico property acquisition during 2004.

	2004	2003	2002	2001	2000
<b>Balance Sheet Data:</b>					
Property, plant and equipment, net	\$ 1,496,912	\$ 1,095,883	\$ 1,001,609	\$ 419,837	\$ 260,532
Total assets	1,702,501	1,265,892	1,169,656	454,385	315,612
Total debt(a)	645,500	597,500	570,837	288,583	191,139
Total stockholders' equity	\$ 679,813	\$ 389,676	\$ 350,196	\$ 117,974	\$ 93,416

- (a) Consists of current notes payable and long-term debt, including current maturities of long-term debt, and excluding production payment liabilities of \$12 thousand, \$114 thousand, \$203 thousand, \$359 thousand as of December 31, 2003, 2002, 2001 and 2000, respectively. As of December 31, 2002 and 2000, \$7.0 million and \$20.6 million, respectively, of the debt was non-recourse to Magnum Hunter.

	2004	2003	2002	2001	2000
<b>Cash Flow Data:</b>					
Cash flow from operating activities	\$ 300,610	\$ 162,638	\$ 83,403	\$ 104,074	\$ 49,466
Cash flows from investing activities	(513,939)	(159,675)	(89,420)	(203,989)	(20,008)
Cash flows from financing activities	\$ 214,978	\$ 12,661	\$ 6,331	\$ 102,661	\$ (31,014)

IV-2

Edgar Filing: O'Neill Andrew J - Form 4

The following tables set forth unaudited summary financial results on a quarterly basis for the two most recent years. All data is in thousands, except per share data.

<b>2004</b>				
	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Revenues	\$ 100,378	\$ 110,036	\$ 128,460	\$ 154,852
Depreciation, depletion, amortization and accretion	25,480	27,645	35,226	38,828
Operating Profit	40,608	44,963	52,255	68,107
Cost of early debt retirement			(12,250)	
Net Income	19,262	23,230	18,964	42,117
Income per common share, basic	0.28	0.34	0.22	0.49
Income per common share, diluted	\$ 0.28	\$ 0.33	\$ 0.22	\$ 0.47

<b>2003</b>				
	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Revenues	\$ 80,054	\$ 78,438	\$ 82,575	\$ 83,947
Depreciation, depletion, amortization and accretion	21,524	24,978	26,682	26,430
Operating Profit	25,914	21,444	21,153	24,187
Cost of early debt retirement	(1,855)	(2,211)	(19)	(2,631)
Cumulative effect of accounting change	399			
Net Income	7,990	4,170	6,669	7,288
Income per common share, basic	0.12	0.06	0.10	0.11
Income per common share, diluted	\$ 0.12	\$ 0.06	\$ 0.10	\$ 0.11

IV-3

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
RESULTS OF OPERATIONS**

**Executive Summary**

Magnum Hunter Resources, Inc. is well positioned over the next several years to continue its growth trajectory in reserves, production and its financial performance due principally to its large in-house inventory of drilling opportunities both onshore and offshore in the Gulf of Mexico. Magnum Hunter has a proved reserve base of 1.0 Tcfe predominantly located in the southwestern United States onshore, where annual production decline rates are typically less than other regions of the country. Magnum Hunter's management believes Magnum Hunter has over a five-year inventory of over 900 onshore development drilling locations and workover opportunities and 245 OCS Blocks in the Gulf of Mexico. This significant inventory of new drilling prospects enhances its capability in meeting its annual goal of replacing reserves and production in any given year.

Magnum Hunter's drilling success has continued to exceed 90% over the last four years. All of its 2004 growth in reserves and production was from a combination of drill bit growth and successful acquisitions. Magnum Hunter acquired 465 producing oil and gas wells from Encana Corporation during August 2004. The purchase also included approximately 44,000 net acres of undeveloped properties. The majority of these properties are located in Lea and Eddy counties of Southeast New Mexico. Magnum Hunter also acquired 170 producing wells in the Permian Basin of West Texas during October 2004. Magnum Hunter drilled a total of 175 wells in 2004 and completed 167 of them for an overall 95% success rate. Offshore drilling totals for the year included 33 of 39 offshore wells drilled successfully. Since Magnum Hunter's initial entry into the Gulf of Mexico in 1999, it has completed 111 of 134 wells, for an 83% overall rate of success.

Magnum Hunter's proved reserves increased from 838 Bcfe at the end of 2003 to 1.0 Tcfe at the end of 2004. Its proved reserves are predominantly long-life, stable, onshore reserves with 59% located in the Permian Basin region, 25% in the Mid-continent region, 8% on the Texas Gulf Coast and 8% from its offshore properties in the Gulf of Mexico. There has been a lot of discussion in the market, as well as at Magnum Hunter's board level, concerning the quality of proved reserves reported by publicly traded oil and gas companies. Fortunately, Magnum Hunter has been very pro-active in this area. Magnum Hunter believes its petroleum engineers have used a very conservative approach in booking proved reserves and therefore its risk in this area has been significantly mitigated. Magnum Hunter's management believes it has always used the most rigorous level of external reserve evaluation by DeGolyer & MacNaughton, referred to as D&M, and Cawley Gillespie, which are its third party engineering firms, and they evaluate 100% of Magnum Hunter's proved reserves.

Over the last several years, Magnum Hunter has continued a significant divestiture program of properties deemed to be more expensive to operate, environmentally sensitive, and having minimal, if any, upside exploration or development potential. Total proceeds received from this group of non-core assets sold over the last two years was \$45.2 million, including the sale of Magnum Hunter's ownership interest in NGTS and TEL Offshore Trust. The net proceeds received from these assets sales have been used to reduce its overall indebtedness and to fund the capital expenditure program centered around activities in southeastern New Mexico and the Gulf of Mexico.

Magnum Hunter has been working over the last several years to continue a program of reducing overall indebtedness and improving its interest expense per Mcfe produced. Actions taken during 2004 to redeem a portion of its \$300 million of outstanding High Yield Bonds that bear interest of 9.6% in combination with the new equity placement of \$169.3 million of common stock. Additionally, Magnum Hunter's overall debt-to-book capitalization has continued to decrease from a high of 82% at December 31, 1999 to a current level of approximately 49%. It is the goal of Magnum Hunter management to reach a debt-to-capitalization level of 40% to 45% or better by year-end 2005.

Magnum Hunter's capital expenditure budget for 2005 is currently estimated to be \$250 million. While oil field service costs have continued to be at the lower end of previous cycles, it is beginning to see significant increases in certain sectors of the business such as oil field pipe and tubulars. Magnum Hunter anticipates experiencing price increases in other areas of the oil field. By operating the majority of its properties, it is in a unique position to better control the timing of its capital expenditure program and these expenses.

The Southeast New Mexico properties consist of approximately 1,110 wells in Chaves, Lea, and Eddy Counties, of which 71% are operated by Gruy. Several of the fields in Lea County produce from the Yates, Seven Rivers, Queen and other formations at depths generally shallower than 3,000 feet. The average net production for the Southeast New Mexico properties for December 2004 was 1,915 Bbl/d and 42,784 Mcf/d.

Magnum Hunter has been actively drilling increased density wells in the Morrow formation at approximately 11,500 feet. It participated in 34 Morrow wells in 2004 and has 23 operated wells planned for 2005. D&M has identified 93 proved undeveloped locations for the Morrow, with net reserves of 64.8 BCFe.

Several of the Morrow wells have identified proved developed non-producing areas in the Atoka and Strawn formations. The Encana acquisition that closed in 2004 greatly increased Magnum Hunter's upside potential in Southeast New Mexico.

Due to an unusual period within the energy industry wherein interest rates are low, oil field service costs are relatively low, and commodity prices for both oil and natural gas are at record highs, an opportunity for unforeseen expansion in Magnum Hunter's profit margins has occurred. Magnum Hunter does not anticipate any significant reductions in the price of crude oil and natural gas over the next several years due to tight supplies and increased demand here in North America and worldwide. Management of Magnum Hunter believes it is properly positioned during this period with its existing portfolio of assets and a significantly improved financial condition, to continue to report record financial results over the next several years.

#### **Recent Announcement To Be Acquired by Cimarex Energy**

On January 26, 2005, Magnum Hunter and Cimarex announced that their respective boards of directors had approved an agreement and plan of merger that provides for the acquisition of Magnum Hunter by Cimarex. Closing is anticipated before the end of the second quarter in 2005, subject to customary regulatory approvals.

Under the terms of the proposed agreement, Magnum Hunter shareholders will receive 0.415 shares of Cimarex common stock for each share of Magnum Hunter common stock that they own. The merger is expected to be non-taxable to the shareholders of both companies. In addition to the merger consideration and prior to closing, Magnum Hunter intends to distribute its ownership interest in TEL Offshore Trust to its common stockholders as a special dividend.

Cimarex Energy Co., headquartered in Denver, CO, is an independent oil and gas exploration and production company with operations focused in the Mid-Continent and Gulf Coast areas of the U.S. Its principal operations offices are located in Tulsa, New Orleans and Houston.

#### **Results of Operations**

The following discussion and analysis should be read in conjunction with Magnum Hunter's consolidated financial statements and the notes associated with them contained elsewhere in this joint proxy statement/prospectus. This discussion should not be construed to imply that the results discussed herein will necessarily continue into the future or that any conclusion reached herein will necessarily be indicative of actual operating results in the future. Such discussion represents only the best present

## Edgar Filing: O'Neill Andrew J - Form 4

assessment by management of Magnum Hunter. Throughout this joint proxy statement/prospectus, there are statements that are classified as "forward-looking." Please refer to the "Cautionary Statement Concerning Forward-Looking Statements" for an explanation of these types of assertions.

Magnum Hunter's results of operations are significantly affected by its ability to maintain or increase oil and natural gas production through exploration and exploitation activities. Fluctuations in oil and gas prices also significantly affect its results of operations.

Successful merger and acquisition activities also have a large impact on Magnum Hunter's results of operations by increasing proved reserves in its core areas which allows greater exploration and production potential paired with existing operation and production expertise in these areas.

On July 30, 2004, Magnum Hunter purchased oil and gas properties located in the state of New Mexico, primarily in Lea and Eddy counties for \$239.1 million, subject to certain purchase price adjustments. The properties include both proved producing oil and gas wells and proved undeveloped leasehold mineral interests. The effective date of the acquisition was May 1, 2004. Magnum Hunter purchased additional properties related to this acquisition during September 2004 for a purchase price of \$1.4 million, net of certain purchase price adjustments. It also recorded additional asset retirement obligations of \$1.5 million as a result of the acquisition. Pro forma information related to this acquisition has not been presented, as the effect was not material to Magnum Hunter's historical results of operations.

On August 30, 2004, Magnum Hunter entered into an agreement to purchase approximately 170 producing wells located in the Permian Basin of West Texas for \$40 million, net of certain purchase price adjustments. Closing occurred on October 29, 2004 and had an effective date of September 1, 2004. Pro forma information related to this acquisition has not been presented, as the effect was not material to Magnum Hunter's historical results of operations.

On November 19, 2003, Magnum Hunter acquired an 80% controlling ownership interest in Metrix, an internet-based field marketing service company, through the settlement of outstanding litigation in its favor as well as the conversion of its \$325 thousand loan to Metrix into equity of that company. As a result of the settlement, Magnum Hunter has fully consolidated Metrix, effective December 1, 2003. Prior to this acquisition, Magnum Hunter accounted for its approximate 32% ownership interest in Metrix as an equity investment. No goodwill was recorded on this acquisition. Pro forma information related to this acquisition has not been presented, as the effect was not material to Magnum Hunter's historical results of operations.

On March 15, 2002, Magnum Hunter completed its merger with Prize Energy Corp., referred to as Prize, a publicly traded oil and gas production company engaged primarily in the acquisition, enhancement, and exploitation of producing oil and gas properties. For operating and financial reporting purposes, the effective date of the merger was March 1, 2002. As such, the results of operations for 2002 includes ten months of operating contributions from Prize. The transaction has been accounted for as a purchase of Prize by Magnum Hunter in accordance with the provisions of SFAS No. 141. Under the terms of the merger, Magnum Hunter distributed 2.5 shares of common stock plus \$5.20 in cash for each Prize share outstanding. The following summary, prepared on a pro forma basis, presents the results of operations for the year ended December 31, 2002 as if the

acquisition occurred as of the beginning of the year. The pro forma information includes the effects of adjustments for interest expense, depreciation, depletion and amortization, and income taxes:

	<b>2002</b>	
	<b>(Unaudited)</b>	
	<b>(in thousands, except for per share amounts)</b>	
Revenue	\$	292,872
Total Operating Costs and Expenses		(219,575)
Operating Profit		73,297
Interest Expense and Other		(60,202)
Income before Tax		13,095
Benefit for Income Tax		892
Net Income	\$	13,987
Net Income Per Common Share		
Basic	\$	0.20
Diluted	\$	0.20

Subsequent to the Prize merger, Magnum Hunter sold non-strategic proved producing oil and gas reserves for total proceeds of approximately \$136 million, net of purchase price adjustments. Substantially all of the properties sold were acquired in the Prize merger, and the proceeds have been used to reduce Magnum Hunter's overall indebtedness and fund its capital expenditure program. The impact of these non-strategic divestitures are described below in results of operations.

On July 29, 2003, Magnum Hunter exercised its option to sell its 30% interest in NGTS, LLC, referred to as NGTS. Magnum Hunter reduced the carrying value of its investment by approximately \$791 thousand and recorded a charge to equity in earnings of affiliate in that amount to state its investment at its estimated fair value. The sale closed on September 30, 2003, and Magnum Hunter received proceeds of \$5.2 million on that date, which were used to repay indebtedness. No gain or loss was recorded on the sale.

Magnum Hunter's results of operations have been significantly affected by its past success in acquiring oil and gas properties at or near the bottom of the commodity price cycles and its ability to maintain or increase oil and natural gas production through its exploration and exploitation activities. Fluctuations in oil and gas prices and commodity hedging activities have also significantly affected the results of operations.

## Edgar Filing: O'Neill Andrew J - Form 4

The following table sets forth certain information with respect to Magnum Hunter's business segments:

	Years Ended		
	2004	2003	2002
<b>Exploration and Production Operations</b>			
<b>Production:</b>			
Oil (MBbls)	4,080	3,893	3,875
Gas (MMcf)	55,961	49,695	47,683
Oil and gas (MMcfe)	80,442	73,052	70,933
Equivalent daily rate (MMcfe/day)	219.8	200.1	194.3
<b>Average sale prices (after hedging):</b>			
Oil (per Bbl)	\$ 34.27	\$ 26.42	\$ 24.04
Gas (per Mcf)	5.41	3.66	3.10
Oil and gas (per Mcfe)	5.50	3.90	3.40
Hedging losses (thousands)	(44,990)	(73,833)	(3,229)
Effect of hedging losses (per Mcfe)	(0.56)	(1.01)	(0.05)
<b>Lease operating expense (per Mcfe):</b>			
Lifting costs	0.76	0.77	0.72
Production tax and other costs	0.54	0.45	0.40
Gross margin (per Mcfe)(a)	4.21	2.68	2.28
Depreciation, depletion, amortization and accretion (per Mcfe)	1.54	1.32	1.17
Segment profit (thousands)	\$ 215,196	\$ 99,809	\$ 78,288
<b>Gas Gathering, Marketing and Processing Operations</b>			
<b>Throughput volumes (Mcf per day)</b>			
Gathering	17,157	15,823	15,535
Processing	25,639	24,947	22,811
<b>Gross margin (in thousands)(a)</b>			
Gathering (per Mcf throughput)	\$ 0.17	\$ 0.14	\$ 0.13
Processing (per Mcf throughput)	1.21	\$ 0.99	\$ 0.55
Segment profit (thousands)	\$ 10,425	\$ 7,624	\$ 3,643
<b>Oil Field Management Services</b>			
Segment profit (thousands)	\$ 2,262	\$ 1,045	\$ 1,115

(a) Excludes depletion, depreciation, amortization and accretion.

### Period to Period Comparisons

#### *For the Years Ended December 31, 2004 and 2003*

Magnum Hunter reported record net income of \$103.6 million for the year ended December 31, 2004 as compared to net income of \$26.1 million for the same period in 2003, an increase of 297%, reflecting solid performance growth in all of its business segments in 2004. Total operating revenues increased 52% to \$493.7 million in 2004 from \$325.0 million in 2003. A 41% increase in the price received for oil and gas sold (on a thousand cubic feet equivalent, or Mcfe, basis), combined with a 10% increase in oil and gas production (on a million cubic feet equivalent, or MMcfe, basis) in its exploration and production segment, as well as a 19% increase in revenues in its gas gathering, marketing and processing segment due to product price increases, and a 76% increase in oil field services revenues due to the acquisition of Metrix, were

primarily responsible for the growth in

IV-8

---

## Edgar Filing: O'Neill Andrew J - Form 4

revenues. Total operating costs and expenses increased 24% to \$287.8 million in 2004 from \$232.3 million in 2003, principally due to higher depreciation, depletion, amortization and accretion expense, lease operating expense, gas gathering, marketing and processing expense, and general administrative expense. Operating profit increased 122% to \$205.9 million in 2004 from \$92.7 million in 2003, due primarily to a 116% increase in Magnum Hunter's exploration and production segment profit from \$99.8 million in 2003 to \$215.2 million in 2004, a 37% increase in its gas gathering, marketing and processing segment profit from \$7.6 million in 2003 to \$10.4 million in 2004, and a 116% increase in its oil field management services segment profit from \$1 million in 2003 to \$2.3 million in 2004. Income before income tax and cumulative effect of a change in accounting principle increased 289% to \$159.3 million in 2004 from \$40.9 million in 2003, due to the growth in Magnum Hunter's business segment performance discussed in detail below. Magnum Hunter recorded income tax expense of \$55.8 million for 2004 (\$53.8 million deferred), versus an income tax expense of \$15.2 million for 2003 (\$15.5 million deferred), due to the growth in pre-tax income. The 2003 period includes a gain of \$399 thousand, net of income tax, for the cumulative effect on prior years of a change in accounting principle due to the adoption of SFAS No. 143 relating to asset retirement obligations. Basic and diluted earnings per share in 2004 were \$1.35 and \$1.31 versus basic and diluted earnings per share of \$0.39 in the 2003 period. Diluted shares outstanding increased 17% in the 2004 period compared to the 2003 period, primarily as a result of exercise of employee stock options and warrants, a secondary offering of 17.3 million shares of Magnum Hunter common stock, and the 49% increase in the average market price of Magnum Hunter common stock in 2004 compared to 2003. The 236% gain in diluted earnings per share in 2004 compared to 2003 was primarily the result of the increase in net income.

### *Exploration and Production Operations*

For the year ended December 31, 2004, Magnum Hunter reported oil production of 4.1 million barrels and natural gas production of 56 billion cubic feet, which represents a 5% increase in oil produced from the 3.9 million barrels reported in 2003, and a 13% increase in natural gas produced from the 49.7 billion cubic feet reported in 2003. Magnum Hunter's reported equivalent daily rate of production on a million cubic feet per day basis (MMcfe per day) increased 10% to 219.8 MMcfe per day in the 2004 period from 200.1 MMcfe per day in the 2003 period. These increases were primarily the result of the New Mexico and West Texas property acquisitions and the success of Magnum Hunter's drilling program offsetting both normal production declines and the effect of the sale of non-strategic oil and gas properties subsequent to the Prize merger. Approximately 2.7% of the production growth was from acquisitions and approximately 7.5% of the production growth was from its drilling program.

Oil revenues increased 36% to \$139.8 million in the 2004 period compared to \$102.8 million in the 2003 period. The oil price received, after hedging effects, was \$34.27 per Bbl in the 2004 period compared to \$26.42 per Bbl in the 2003 period, an increase of 30%. Gas revenues increased 67% to \$302.9 million in the 2004 period versus \$181.7 million in the 2003 period. The gas price received, after hedging effects, was \$5.41 per Mcf in the 2004 period compared to \$3.66 per Mcf for the same period in 2003, an increase of 48%. Total oil and gas sales increased 56% to \$443.4 million in 2004 from \$284.9 million in 2003, including the effect of hedging losses. Magnum Hunter reported a loss of \$45 million from hedging activities in 2004 versus a loss of \$73.8 million in 2003, a decrease of 39% due to the expiration of less favorably priced hedges in 2004. These losses are included in Magnum Hunter's reported oil and gas sales.

From time to time, Magnum Hunter enters into various commodity hedging contracts in order to reduce its exposure to the possibility of declining oil and gas prices which provide a basic level of cash flow to fund capital expenditures. During the 2004 period, hedging decreased the average price Magnum Hunter received for oil by \$5.35 per Bbl and decreased the average price received for gas by \$0.41 per Mcf. During the 2004 period, Magnum Hunter had approximately 86.7 Mmcf per day of gas

hedged through cost-less collars with a weighted average floor price of \$3.92 per Mmbtu and a weighted average ceiling price of \$5.90 per Mmbtu. Approximately 57% of 2004 natural gas production was hedged. On the crude side, Magnum Hunter had approximately 5,865 Bbls per day hedged through cost-less collars with a weighted average floor price of \$23.87 per Bbl and a weighted average ceiling price of \$29.85 per Bbl. Approximately 53% of 2004 crude oil production was hedged.

Lease operating expense consists of lifting costs and production taxes and other costs. For the 2004 period, lifting costs were \$60.9 million versus \$56.3 million in the 2003 period, an increase of 8%. Production taxes and other costs were \$43.7 million in the 2004 period versus \$32.8 million in the 2003 period, an increase of 33%. The increase in lifting costs was primarily due to the property acquisitions and to Magnum Hunter's successful drilling program which increased the number of producing wells. The increase in production tax and other costs was primarily due to higher oil and gas prices and to higher volumes of oil and gas sold. For the 2004 period, lifting costs, on a unit of production basis, were \$0.76 per Mcfe as compared to \$0.77 per Mcfe in the 2003 period, a decrease of 1%. Production taxes and other costs were \$0.54 per Mcfe in the 2004 period compared to \$0.45 per Mcfe in the 2003 period, an increase of 20%. The increase in production taxes and other costs per Mcfe was caused by an increase in production taxes of \$0.04 per Mcfe due to higher commodity prices received during the 2004 period, higher insurance costs of \$0.02 per Mcfe, and higher overhead costs of \$0.03 per Mcfe.

Magnum Hunter's gross margin realized from exploration and production operations (oil and gas revenues less lease operating expenses) for the 2004 period was \$338.8 million, or \$4.21 per Mcfe, compared to \$195.9 million, or \$2.68 per Mcfe in the 2003 period, an increase of 57% on a per unit of production basis. The gross margin increase is the result of a 41% increase in revenue per Mcfe produced, offset by a 7% increase in lease operating expense per Mcfe produced.

Depreciation, depletion, amortization and accretion of oil and gas properties was approximately \$123.6 million in the 2004 period versus approximately \$96.1 million in the 2003 period. The 2004 period included accretion expense related to asset retirement obligations (due to the adoption in January 2003 of SFAS No. 143) of \$2.9 million versus \$2.5 million in 2003. On a unit of production basis, depreciation and depletion expense (excluding accretion expense) was \$1.50 per Mcfe produced in the 2004 period versus \$1.28 per Mcfe produced in the 2003 period. This 17% increase in the equivalent unit cost was due to the effect of Magnum Hunter's New Mexico property acquisition, an increase in development costs and shorter reserve life properties associated with activities in the Gulf of Mexico, and the transfer of \$32.7 million of costs from unproved properties to the full cost pool. The costs which were transferred related to unproved property costs associated with properties which were sold or proved during 2004, as well as costs associated with leases which expired during the year. Accretion expense was \$0.04 per Mcfe in 2004 versus \$0.03 in 2003. Total depreciation, depletion, amortization and accretion for this segment was \$1.54 per Mcfe in 2004 versus \$1.32 per Mcfe in 2003.

Segment profit for exploration and production operations was \$215.2 million for the 2004 period versus approximately \$99.8 million for the 2003 period, an increase of 116%, due to property acquisitions, the success of Magnum Hunter's drilling program, and higher realized crude oil and natural gas prices.

#### *Gathering, Marketing and Processing Operations*

For the year ended December 31, 2004, Magnum Hunter's gathering system throughput was 17.2 MMcf per day versus 15.8 MMcf per day for the same period in 2003, an increase of 8% due to the construction and operation of two new gathering systems.

Gas processing throughput was 25.6 MMcf per day in 2004 versus 24.9 MMcf per day in 2003, an increase of 3% due to a combination of less downtime for unfavorable economics in 2004 and successful drilling behind the plants.

## Edgar Filing: O'Neill Andrew J - Form 4

Revenues from gathering, marketing and processing increased 19% to \$41.9 million in 2004 versus \$35.3 million in 2003, primarily due to higher realized prices for natural gas and natural gas liquids. Operating costs for this segment increased 15% to \$29.1 million in 2004 from \$25.4 million in 2003 due primarily to higher costs of gas purchased. The gross margin realized from gathering, marketing and processing for 2004 was \$12.8 million versus \$9.9 million in 2003, an increase of 29%. The gathering margin was \$0.17 per Mcf gathered in 2004 versus \$0.14 per Mcf in 2003 due to an increase in gathering fees and gas marketing margins. The processing margin was \$1.21 per Mcf in 2004 compared to \$0.99 per Mcf in 2003 due to more favorable processing economics.

Depreciation expense for gas gathering, marketing and processing operations was \$2.4 million for the 2004 period versus \$2.3 million for the 2003 period, an increase of 2% due to the new gathering systems.

Segment profit for gas gathering, marketing and processing operations was \$10.4 million in the 2004 period versus \$7.6 million for the 2003 period, an increase of 37%, due to higher gathering and processing throughput and improved processing economics at Magnum Hunter's natural gas processing plants.

### *Oil Field Management Services Operation*

In December 2003 Magnum Hunter increased its equity ownership in Metrix to 80% and began to fully consolidate its results of operations with Magnum Hunter's oil field management services segment. The 2004 operating results for this segment contains twelve months of Metrix operations versus one month in 2003. Revenues from oil field management services were \$8.4 million in the 2004 period versus \$4.8 million in the 2003 period due to higher management and operations services fees charged to third parties. The higher fees were primarily due to a full year of consolidated operations of Metrix in 2004. Operating costs increased to \$5.0 million in 2004 from \$3.1 million in 2003 due to higher costs for labor and overhead and the inclusion of a full year of consolidated Metrix operations in 2004. The gross margin for this segment in 2004 increased to \$3.4 million from \$1.6 million in 2003, an increase of 106%, primarily due to Metrix.

Depreciation expense was \$1.1 million in the 2004 period versus \$604 thousand in the 2003 period, an increase of 88%, due to Metrix. Segment profit was \$2.3 million in 2004 versus \$1 million in 2003, an increase of 116%, due to Metrix.

### *Depreciation, Depletion, Amortization and Accretion*

Total depreciation, depletion, amortization and accretion expense was \$127.2 million in the 2004 period versus \$99.6 million in the 2003 period, an increase of 28%, primarily due to increased oil and gas production and increased depletion and accretion rates per unit produced in Magnum Hunter's exploration and production segment.

### *General and Administrative Expenses*

General and administrative expenses for 2004 increased 44% to \$22.1 million from \$15.3 million in 2003. The principal reasons for this increase were higher legal, accounting and other fees of \$2.5 million, Metrix expenses (due to 12 months of Metrix consolidated in 2004 versus one month in 2003) of \$2.1 million, and employee salaries and benefit costs of \$2.2 million. The number of full-time employees at fiscal year-end 2004 and 2003 was 262 and 222, respectively. Fees and expenses, other than employee costs, associated with Sarbanes Oxley compliance were \$1 million in 2004 versus \$62 thousand in 2003.

## Edgar Filing: O'Neill Andrew J - Form 4

### *Other Income and Expenses*

Magnum Hunter recorded a gain on sale of assets other than oil and gas properties of \$288 thousand in 2004 versus \$171 thousand in 2003.

Magnum Hunter recorded no equity in earnings of affiliate in 2004 versus equity in loss of affiliate of \$162 thousand in 2003, principally due to the acquisition of 80% control of Metrix in December 2003. Other income was \$2.6 million for 2004 versus \$889 thousand in 2003, a 191% increase, due to a settlement of a lawsuit in favor of Magnum Hunter. Magnum Hunter recognized a \$1.1 million gain in other non-cash hedging adjustments in 2004 versus a gain of \$1.5 million in 2003. In the 2004 period, \$792 thousand of the hedging gain relates to the amortization of commodity hedge liabilities acquired in the Prize merger, while \$332 thousand of the gain was due to recording hedge ineffectiveness. In the 2003 period, \$1.3 million of the hedging gain relates to the amortization of commodity hedge liabilities acquired in the Prize merger, while \$186 thousand of the gain was due to recording hedge ineffectiveness.

Magnum Hunter incurred costs associated with early retirement of debt of \$12.3 million in 2004 versus \$6.7 million in 2003. The 2004 period debt retirement costs were associated with the \$105 million principal value redemption of its 9.6% Senior Notes at 109.6% of par. The 2003 period costs were associated with the \$30 million, \$50 million, and \$60 million redemptions in principal value of Magnum Hunter's 10% Senior Notes at 105% of par, 103.333% of par, and 103.333% of par in January, June and December 2003, respectively, as well as a subsidiary's August 2003 purchase of \$381 thousand in principal value of its 10% Senior Notes at 103.75% of par. Of the \$140 million in principal value of 10% Senior Notes redeemed in 2003, a subsidiary received \$10.9 million in principal value.

Interest expense was \$38.1 million for 2004 versus \$47.3 million for 2003, a decrease of 19%, primarily the result of interest saved on the early redemption of Magnum Hunter's 10% and 9.6% Senior Notes and lower interest rate hedging costs. During the 2004 period, the average interest rate on Magnum Hunter's Senior Credit Facility, referred to as the Facility, was 3.54% versus 3.4% in 2003, an increase of 4%. The weighted average daily balance of the Facility increased 2% to \$217.8 million in 2004 from \$213.7 million in 2003. In addition, Magnum Hunter incurred no interest rate hedge expense in the 2004 period versus \$961 thousand in the 2003 period. The interest rate hedge expired in August 2003.

Magnum Hunter recorded income tax expense of \$55.8 million in 2004 (\$53.8 million of which was deferred), versus an income tax expense of \$15.2 million in 2003 (\$15.5 million of which was deferred). The variance in the effective tax rate from the statutory rate of 35% in 2004 was primarily due to state income taxes. Magnum Hunter reduced its blended state income tax rate from 2.875% to 1.2% due to a change in estimate of the amount of income from its offshore properties and properties held by a limited partnership which are not subject to state income taxes. This change in estimate, when applied to its deferred state income tax liability, resulted in a reduction of deferred state income tax expense of \$4.8 million in 2004. Magnum Hunter also increased its valuation allowance for utilization of its state net operating loss carryforwards, resulting in additional state tax expense of \$2 million in 2004.

### ***For the Years Ended December 31, 2003 and 2002***

Magnum Hunter reported net income of \$26.1 million for the year ended December 31, 2003 as compared to net income of \$15.5 million for the same period in 2002, an increase of 68%, reflecting the solid performance of both its exploration and production segment and its gathering, marketing and processing segment. Total operating revenues increased 22% to \$325.0 million in 2003 from \$265.9 million in 2002. A 15% increase in the price received for oil and gas sold (on a thousand cubic feet equivalent, or Mcfe, basis), combined with a 3% increase in oil and gas production (on a million cubic feet equivalent, or MMcfe, basis) in its exploration and production segment, as well as a 70%

## Edgar Filing: O'Neill Andrew J - Form 4

increase in revenues in its gas gathering, marketing and processing segment due to the Prize merger and product price increases, were primarily responsible for the improvement in revenues. The production increase in Magnum Hunter's exploration and production segment was impacted by the merger with Prize, the success of its drilling program, and the sale of non-strategic oil and gas properties. Total operating costs and expenses increased 18% to \$232.3 million in 2003 from \$197.0 million in 2002, principally due to higher depreciation, depletion, amortization and accretion expense, lease operating expense, gas gathering, marketing and processing expense, and general administrative expense due to the merger with Prize. Operating profit increased 35% to \$92.7 million in 2003 from \$68.9 million in 2002, due primarily to a 27% increase in its exploration and production segment profit from \$78.3 million in 2002 to \$99.8 million in 2003 and a 109% increase in its gas gathering, marketing and processing segment profit from \$3.6 million in 2002 to \$7.6 million in 2003. Segment profit for Magnum Hunter's oil field management service segment declined approximately 6% from \$1.1 million in 2002 to \$1 million in 2003 due to higher depreciation expense. Net income before income tax and cumulative effect of a change in accounting principle increased 194% to \$40.9 million in 2003 from \$13.9 million in 2002, primarily due to the Prize merger and the increase in crude oil, natural gas, and natural gas liquids prices in the 2003 period compared to the 2002 period. Additionally, the 2003 period included costs associated with early retirement of debt of \$6.7 million from the redemption of its 10% Senior Notes, discussed in further detail below in " Other Income and Expenses." Magnum Hunter recorded income tax expense of \$15.2 million for 2003, of which \$15.5 million was deferred tax expense, versus a deferred tax benefit of \$1.6 million for 2002. The 2002 period income tax benefit resulted from the elimination of the \$7.1 million valuation allowance that had been carried against deferred tax assets derived from net operating loss carryovers generated by Magnum Hunter in prior years. As a result of the Prize merger, Magnum Hunter believes that this tax asset can be fully realized. Additionally, the 2003 period includes the cumulative effect on prior years of a change in accounting principle due to the adoption of SFAS No. 143 relating to asset retirement obligations. The cumulative effect was a gain of \$399 thousand, net of income tax expense of \$244 thousand, or \$0.01 per share, both basic and diluted. Basic and diluted earnings per share in 2003 were \$0.39 versus basic and diluted earnings per share of \$0.25 in the 2002 period. Basic and diluted shares outstanding increased 8% in the 2003 period compared to the 2002 period, primarily as a result of new shares issued in the Prize merger. The 56% gain in diluted earnings per share in 2003 compared to 2002 was primarily the result of the increase in net income.

### *Exploration and Production Operations*

For the year ended December 31, 2003, Magnum Hunter reported oil production of approximately 3.9 million barrels and natural gas production of approximately 49.7 billion cubic feet, which represents no change in oil produced and an increase of 4% in natural gas produced from the 47.7 billion cubic feet reported in the 2002 period. Magnum Hunter's reported equivalent daily rate of production on a million cubic feet per day basis (MMcfe per day) increased 3% to 200.1 MMcfe per day in the 2003 period from 194.3 MMcfe per day in the 2002 period. These increases were primarily the result of the Prize merger and the success of its drilling program offsetting both normal production declines and the effect of the sale of non-strategic oil and gas properties subsequent to the Prize merger. The impact of these non-strategic property sales on reported production was a decrease of 27.1 Mmcfe per day in the 2003 period compared to the 2002 period. Removing the effect of sold properties from both the 2003 and 2002 periods, Magnum Hunter's daily equivalent production grew 15.9% from 2002 to 2003.

Oil revenues increased 10% to \$102.8 million in the 2003 period compared to \$93.2 million in the 2002 period. The oil price received, after hedging effects, was \$26.42 per Bbl in the 2003 period compared to \$24.04 per Bbl in the 2002 period, an increase of 10%. Gas revenues increased 23% to \$181.7 million in the 2003 period versus \$147.8 million in the 2002 period. The gas price received, after hedging effects, was \$3.66 per Mcf in the 2003 period compared to \$3.10 per Mcf for the same period in 2002, an increase of 18%. Magnum Hunter also recorded \$398 thousand in oil and gas sales in the

2003 period from business interruption insurance proceeds resulting from claims filed in 2002 due to Hurricane Lili. Total oil and gas sales increased 18% to \$284.9 million in 2003 from \$241 million in 2002.

From time to time, Magnum Hunter enters into various commodity hedging contracts in order to reduce its exposure to the possibility of declining oil and gas prices which provide a basic level of cash flow to fund capital expenditures. During the 2003 period, hedging decreased the average price Magnum Hunter received for oil by \$3.20 per Bbl and decreased the average price received for gas by \$1.23 per Mcf. During the 2003 period, Magnum Hunter had approximately 35.0 Mmcf per day of gas hedged through fixed price swaps with a weighted average price of \$3.10 per Mmbtu and approximately 55.0 Mmcf per day of gas hedged through cost-less collars with a weighted average floor price of \$2.91 per Mmbtu and a weighted average ceiling price of \$3.97 per Mmbtu. Approximately 60% of 2003 natural gas production was hedged. On the crude side, Magnum Hunter had approximately 1,000 Bbls per day hedged through fixed price swaps with a weighted average price of \$21.25 per barrel and approximately 6,000 Bbls per day hedged through cost-less collars with a weighted average floor price of \$23.00 per Bbl and a weighted average ceiling price of \$27.00 per Bbl. Approximately 66% of 2003 crude oil production was hedged.

Lease operating expense consists of lifting costs and production taxes and other costs. For the 2003 period, lifting costs were \$56.3 million versus \$51.6 million in the 2002 period, an increase of 9%. Production taxes and other costs were \$32.8 million in the 2003 period versus \$28.2 million in the 2002 period, an increase of 16%. Both increases were primarily attributable to the Prize merger. For the 2003 period, lifting costs, on a unit of production basis, were \$0.77 per Mcfe as compared to \$0.72 per Mcfe in the 2002 period, an increase of 7%. The increase in lifting costs per Mcfe produced in the 2003 period was due to higher power and fuel costs and increased remedial and workover expense. The increased workover expense is due to remedial work on older properties acquired in the Prize merger as well as discretionary workovers done to enhance current production. Production taxes and other costs were \$0.45 per Mcfe produced in the 2003 period compared to \$0.40 per Mcfe produced in the 2002 period, an increase of 13%. The increase in production taxes per Mcfe produced was caused by an increase in crude oil and natural gas prices received during the 2003 period.

Magnum Hunter's gross margin realized from exploration and production operations (oil and gas revenues less lease operating expenses) for the 2003 period was \$195.9 million, or \$2.68 per Mcfe, compared to \$161.2 million, or \$2.28 per Mcfe in the 2002 period, an increase of 18% on a per unit of production basis. The gross margin increase is the result of a 15% increase in revenue per Mcfe produced, offset by a 9% increase in lease operating expense per Mcfe produced.

Depreciation, depletion, amortization and accretion of oil and gas properties was \$96.1 million in the 2003 period versus \$83 million in the 2002 period. The 2003 period included accretion expense related to asset retirement obligations (due to the adoption in January 2003 of SFAS No. 143) of \$2.5 million versus none in 2002. On a unit of production basis, depreciation and depletion expense (excluding accretion expense) was \$1.28 per Mcfe produced in the 2003 period versus \$1.17 per Mcfe produced in the 2002 period. This 10% increase in the equivalent unit cost was due primarily to an increase in development costs and shorter reserve life properties associated with activities in the Gulf of Mexico as well as the transfer of \$75.0 million of costs from unproved properties to the full cost pool. The costs which were transferred related to unproved property costs associated with properties which were sold or proved during 2003, as well as costs associated with leases which expired during the year. Accretion expense was \$0.03 per Mcfe in 2003 versus none in 2002. Total depreciation, depletion, amortization and accretion for this segment was \$1.32 per Mcfe in 2003 versus \$1.17 per Mcfe in 2002.

Segment profit for exploration and production operations was \$99.8 million for the 2003 period versus \$78.3 million for the 2002 period, an increase of 27%, principally due to properties acquired in

the Prize merger, the success of Magnum Hunter's drilling program, and higher realized crude oil and natural gas prices.

*Gathering, Marketing and Processing Operations*

For the year ended December 31, 2003, Magnum Hunter's gathering system throughput was 15.8 MMcf per day versus 15.5 MMcf per day for the same period in 2002, an increase of 2% due to successful drilling behind the system. Gas processing throughput was 24.9 MMcf per day in 2003 versus 22.8 MMcf per day in 2002, an increase of 9%, due primarily to the effect of the Prize merger.

Revenues from gathering, marketing and processing increased 70% to \$35.3 million in 2003 versus \$20.8 million in 2002, primarily due to higher realized prices for natural gas and natural gas liquids. The gross margin realized from gathering, marketing and processing for 2003 was \$9.9 million versus \$5.7 million in 2002, an increase of 74%. The gathering margin was \$0.14 per Mcf gathered in 2003 versus \$0.13 per Mcf in 2002 due to an increase in gathering fees. The processing margin was \$0.99 per Mcf in 2003 compared to \$0.55 per Mcf in 2002 due to more favorable processing economics.

Depreciation expense for gas gathering, marketing and processing operations was \$2.3 million for the 2003 period versus \$2.1 million for the 2002 period, due to the Prize merger.

Segment profit for gas gathering, marketing and processing operations was \$7.6 million in the 2003 period versus \$3.6 million for the 2002 period, an increase of 109%, principally due to higher throughput and improved processing economics at Magnum Hunter's natural gas processing plants.

*Oil Field Management Services Operations*

Revenues from oil field management services were \$4.8 million in the 2003 period versus \$4.1 million in the 2002 period due to higher management and operations services fees charged to third parties. Operating costs increased to \$3.1 million in 2003 from \$2.5 million in 2002 due to higher costs for labor and overhead. The gross margin for this segment in 2003 compared to 2002 was unchanged at \$1.6 million.

Depreciation expense was \$604 thousand in the 2003 period versus \$507 thousand in the 2002 period, an increase of 19%, due to capital additions. Segment profit was \$1 million in 2003 versus \$1.1 million in 2002, a decrease of 6%, due to the increase in depreciation expense.

*Depreciation, Depletion, Amortization and Accretion*

Total depreciation, depletion, amortization and accretion expense was \$99.6 million in the 2003 period versus \$86.5 million in the 2002 period, an increase of 15%, primarily as a result of increased production and increased depletion and accretion rates in Magnum Hunter's exploration and production segment.

*General and Administrative Expenses*

General and administrative expenses for 2003 increased 15% to \$15.3 million from \$13.3 million in 2002. The principal reason for this increase was the \$3.0 million cost of expensing employee stock options recorded in the 2003 period as a result of the adoption of SFAS No. 123 in June 2003, with an effective date of January 1, 2003. The number of full-time employees at fiscal year-end 2003 and 2002 was 222 and 221 respectively.

*Other Income and Expenses*

Magnum Hunter recorded a gain on sale of assets other than oil and gas properties of \$171 thousand in 2003 versus \$61 thousand in 2002. Magnum Hunter recorded equity in loss of affiliate

of \$162 thousand in 2003 versus equity in earnings of affiliate of \$792 thousand in 2002, principally due to the reduction of the carrying value of its investment in NGTS by \$791 thousand to state it at its estimated fair value prior to sale, as well as its equity in losses generated by Metrix prior to Magnum Hunter's acquisition of 80% control of Metrix in December 2003. Other income was \$889 thousand for 2003 versus \$452 thousand in 2002, a 97% increase, due to an increase in interest income. In 2002, Magnum Hunter recorded an impairment of \$621 thousand on an investment in a company that declared bankruptcy. Magnum Hunter recognized a \$1.5 million gain in other non-cash hedging adjustments in 2003 versus a loss of \$6.6 million in 2002. In the 2003 period, \$1.3 million of the hedging gain relates to the amortization of commodity hedge liabilities acquired in the Prize merger, while \$186 thousand of the gain was due to recording hedge ineffectiveness. In the 2002 period, a loss of \$6.1 million relates to the amortization of commodity hedge assets acquired in the Prize merger, and a loss of \$500 thousand was due to recording hedge ineffectiveness.

Magnum Hunter incurred costs associated with early retirement of debt of \$6.7 million in 2003 versus \$1 million in 2002. The 2003 period costs were associated with the \$30 million, \$50 million, and \$60 million redemptions in principal value of its 10% Senior Notes at 105% of par, 103.333% of par, and 103.333% of par in January, June and December 2003, respectively, as well as a subsidiary's August 2003 purchase of \$381 thousand in principal value of Magnum Hunter's 10% Senior Notes at 103.75% of par. Of the \$140 million in principal value of 10% Senior Notes redeemed in 2003, a subsidiary received \$10.9 million in principal value. The 2002 period debt retirement costs of \$1 million were associated with the amendment of the Facility in connection with the Prize merger.

Interest expense was \$47.3 million for 2003 versus \$47.9 million for 2002, a decrease of 1%, primarily as a result of lower interest rates on the Facility, lower interest rate hedging costs, and interest saved on the early redemption of Magnum Hunter's 10% Senior Notes. During the 2003 period, the average interest rate on the Facility was 3.4% versus 4.0% in 2002, a decline of 15%. The weighted average daily balance of the Facility increased 17% to \$213.7 million in 2003 from \$182.9 million in 2002. By December 31, 2003, the level of the Facility had been reduced to \$165 million through sales of non-strategic oil and gas properties and the issuance in December 2003 of \$125 million of floating rate convertible senior notes, referred to as Convertible Notes, which have a floating interest rate based on three-month LIBOR (initially set at 1.17%). In addition, Magnum Hunter incurred interest rate hedge expense of \$961 thousand in the 2003 period versus \$1.2 million in the 2002 period. The interest rate hedge expired in August 2003.

Magnum Hunter recorded income tax expense of \$15.2 million in 2003 (\$15.5 million of which was deferred), versus a deferred income tax benefit of \$1.6 million in 2002. The 2002 period benefited from the release of the \$7.1 million valuation allowance on previously reserved deferred tax assets as a result of the increased likelihood (due to the Prize merger) that the tax assets generated from prior net operating losses will be realized in the future. The 2002 period was also impacted by a \$2.3 million deferred tax provision from the adjustment of goodwill due to sales of non-strategic oil and gas properties. The effective tax rate for 2003 and 2002 was 37.2% and (11.4%), respectively. The variance in the effective tax rate from the statutory rate of 35% was due to state income taxes in the 2003 period and the release of the valuation allowance on Magnum Hunter's previously reserved deferred tax assets in the 2002 period.

### **Liquidity and Capital Resources**

Magnum Hunter's liquidity is primarily dependent upon its ability to generate cash flow from operations and from external sources such as commercial banks or the bond market. One of the most significant items that can impact Magnum Hunter's internally generated funds and availability under the Facility is commodity prices. Should oil and gas prices decline significantly, Magnum Hunter's cash flow would be negatively impacted. If commodity prices declined and were perceived by its lenders to be more than temporary, the amount available under the Facility would be reduced. Reductions in

Magnum Hunter's borrowing capacity could cause it to have to pay down its bank debt, reduce its drilling activities and possibly sell oil and gas properties.

Increases in interest rates could also negatively impact Magnum Hunter's liquidity, as more cash flow would have to be directed toward the payment of interest. Because Magnum Hunter is leveraged, interest expense is a significant financial obligation.

Magnum Hunter attempts to mitigate the impact of decreases in commodity prices and increases in interest rates by the use of hedging contracts; however, it does not hedge all of its commodity price or interest rate risks. Instead, Magnum Hunter management judges the likelihood of changes in commodity prices and interest rates and considers other factors such as the amount of debt and estimated cash flow under various scenarios. Hedges are then considered and entered into as deemed appropriate.

**CASH FLOW AND WORKING CAPITAL.** Net cash provided by operating activities was \$300.6 million, \$162.6 million, and \$83.4 million in 2004, 2003, and 2002, respectively. Magnum Hunter's operating cash flow for 2004 increased over that for 2003, primarily due to substantially higher operating profits realized by its business segments when adjusted for non-cash items. Please see the period to period comparisons for further explanations on the causes and amounts of the increases in its earnings. In the 2004 period, Magnum Hunter made income tax payments (net of current year refunds) of \$2.4 million.

Magnum Hunter's net working capital position at December 31, 2004 was a deficit of \$5.2 million. At this date, it had \$202.5 million available under the Facility. A large factor in Magnum Hunter's negative working capital was \$14.0 million in current derivative liabilities it had recorded on its 2005 hedging program due to continued increases in commodities prices over its hedged prices. This liability is partially offset by \$5.0 million in deferred tax assets which will be released as its 2005 hedges are settled. If actual commodities prices realized on its production remain higher than its hedged prices, Magnum Hunter's resulting higher proceeds from oil and gas sales will offset any actual amounts paid out on this liability.

Magnum Hunter's 2003 operating cash flow was higher than its 2002 operating cash flow also due to higher profits realized by its business segments when adjusted for non-cash items. Please refer to the period to period comparisons for further explanations on the causes and amounts of the increases in earnings. Magnum Hunter also benefited from \$8.1 million in refunds (net of 2003 payments) as well as the return of \$6.5 million in margin deposits it had posted on commodity hedge positions.

Magnum Hunter's net working capital position at December 31, 2003 was also a deficit of \$5.2 million. At this date it had \$87.5 million available under the Facility. Again, a large factor in its negative working capital was \$21.9 million in current derivative liabilities it had recorded on its 2004 hedging program due to continued increases in commodities prices over its hedged prices for 2004 production. The amounts paid out on these liabilities were offset by higher cash received for the related production in 2004. This liability was also offset by \$8.3 million of current deferred tax assets which were released as the positions were settled.

**INVESTING ACTIVITIES.** Net cash used in investing activities was \$513.9 million, \$159.7 million, and \$89.4 million in 2004, 2003, and 2002, respectively. During July 2004, Magnum Hunter paid \$234.2 million, net of certain purchase price adjustments, for its acquisition of New Mexico properties. In 2004, the main source of its investing was \$303.1 million spent for capital expenditures which are discussed in the section immediately following the liquidity and capital resources discussions. During 2004, Magnum Hunter also received \$22.9 million from the sales of non-strategic oil and gas properties.

In 2003, the main source of Magnum Hunter's investing was \$175.5 million spent for capital expenditures. During 2003, Magnum Hunter also received \$17.1 million from the sales of non-strategic

oil and gas properties as well as \$5.2 million from the sale of its 30% interest in NGTS. Magnum Hunter spent \$6.1 million to purchase land which it currently has available for sale and \$1.5 million to purchase land to be held for geothermal development.

During 2002, Magnum Hunter spent \$141.0 million on capital expenditures as well as \$41.1 million to complete the Prize merger. These expenditures were partially offset by \$96.0 million received on sales of non-strategic oil and gas properties acquired in the Prize merger.

**FINANCING ACTIVITIES.** Net cash provided by financing activities was \$215 million, \$12.7 million, and \$6.3 million in 2004, 2003, and 2002, respectively. During 2004, Magnum Hunter received \$169.3 million from the issuance of common stock pursuant to its secondary offering of common stock. Magnum Hunter also received \$10.4 million from the issuance of stock pursuant to its employee stock option plans. Magnum Hunter loaned \$2.3 million to its KSOP to purchase approximately 225 thousand shares of its common stock to be available for purchase by participants at future dates. KSOP participants paid Magnum Hunter \$807 thousand to purchase approximately 134 thousand unallocated KSOP shares of its common stock and Magnum Hunter forgave KSOP debt of \$1.3 million by contributing approximately 223 thousand unallocated shares of its common stock to participants as its 2004 employer retirement plan contribution. At December 31, 2004, the KSOP had a loan balance of \$6.2 million. This loan carries no interest and is due December 31, 2005. Magnum Hunter paid \$115.1 million to redeem \$105 million in principal of its 9.6% Senior Notes at 109.6% of par, borrowed approximately \$466 million under the Facility, and made repayments on its debt of \$313 million. Magnum Hunter also paid fees related to its financing activities of \$1.0 million.

During 2003, Magnum Hunter received \$4.7 million from the issuance of common stock and treasury stock pursuant to employee stock option and warrant exercises, and paid down debt of \$486.3 million. Magnum Hunter paid \$134.4 million to redeem the outstanding \$129.5 million in principal of its 10% Senior Notes and borrowed approximately \$517.4 million under the Facility. Magnum Hunter also received \$125 million from the issuance of Convertible Notes and paid fees related to financing activities of \$4.4 million. During 2003, Magnum Hunter also spent \$7.4 million to repurchase approximately 1.3 million shares of its common stock. Magnum Hunter loaned \$2.7 million to its KSOP to purchase approximately 486 thousand shares of its common stock and forgave KSOP debt of \$1.1 million by contributing approximately 172 thousand shares of its common stock to participants. KSOP participants paid Magnum Hunter \$380 thousand to purchase approximately 59 thousand unallocated shares of its common stock.

During 2002, Magnum Hunter received \$300 million from the issuance of its 9.6% Senior Notes due 2012 and paid down debt of \$30 million. Magnum Hunter paid off \$246.8 million of long-term debt acquired in the Prize merger. During 2002, Magnum Hunter also spent \$18.0 million to repurchase approximately 2.7 million shares of its common stock. Magnum Hunter loaned \$3.7 million to its KSOP to purchase approximately 532 thousand shares of its common stock and forgave KSOP debt of \$1.3 million by releasing approximately 244 thousand shares of its common stock to participants. Magnum Hunter also received \$3.6 million from the exercise of employee stock options.

**CAPITAL RESOURCES.** Cash flow from operations and borrowings under the Facility are its major sources of liquidity. From time to time, it may also sell investments and oil and gas properties to increase its liquidity. In addition, Magnum Hunter also may use other sources of capital, such as issuances of additional debt or equity securities to fund acquisitions or other specific needs. In the past, Magnum Hunter has accessed both public and private capital markets to obtain capital for specific activities as well as general corporate purposes. Magnum Hunter currently has \$23.2 million available remaining under its current shelf registration with the Securities and Exchange Commission.

On May 1, 2002, Magnum Hunter's Board of Directors announced an expansion of its existing stock repurchase program originally established in June 2001. Under the program, Magnum Hunter or its affiliates are authorized to repurchase up to two million shares of Magnum Hunter common stock.

## Edgar Filing: O'Neill Andrew J - Form 4

On October 17, 2002, Magnum Hunter's Board of Directors approved a new three million share repurchase program. Approximately 4.2 million shares have been repurchased through these programs, and approximately 818 thousand remain available for repurchase.

On December 5, 2001, Magnum Hunter announced a distribution of one warrant for every five shares of its common stock owned on January 10, 2002. These warrants were distributed on March 21, 2002. Each new warrant entitles the holder to purchase one share of common stock at \$15. The warrants will expire three years from the date of distribution unless extended by the Board of Directors.

On January 15, 2002, Magnum Hunter entered into a sale-leaseback transaction on three newly constructed offshore production platforms and associated pipelines. Magnum Hunter received a total of \$11.2 million in new funding which was used for general corporate purposes, including a voluntary reduction under the Facility. The production platforms are being leased from a syndicate group of lenders over a term of three to five years at a cost of funds based on LIBOR, yielding a weighted average rate of 5.58% per annum at December 31, 2004. This transaction was accounted for as a capital lease.

On March 15, 2002, Magnum Hunter amended and restated the Facility in conjunction with the merger with Prize. The amended Facility provided for total borrowings of \$500 million, up from \$225 million, and raised the borrowing base limit from \$160 million to \$300 million. Additionally, Magnum Hunter amended and extended the expiration date of the Facility to March 2005. After March 15, 2002, the Facility was used i) to fund the cash component of the Prize merger, ii) to pay certain costs associated with the merger, and iii) for general corporate purposes. In connection with certain oil and gas property divestitures, the borrowing base was reduced to \$250 million on September 3, 2002.

During 2003, Magnum Hunter amended the Facility in May and October to ultimately increase the borrowing base to \$350 million, up \$100 million from its previous \$250 million borrowing base. Magnum Hunter also extended the expiration date of the Facility to May 2, 2006. The increased borrowing base was used to fund the redemptions of its 10% Senior Notes which were completed prior to the issuance of its Convertible Notes in December 2003. Magnum Hunter also used the increased borrowing base to fund the costs of issuing its Convertible Notes. Upon the issuance of its Convertible Notes, Magnum Hunter repaid approximately \$144 million of its borrowings on this Facility, and the borrowing base was reduced \$95 million to \$255 million.

On April 30, 2004, Magnum Hunter amended the Facility to receive a more favorable rate structure and to increase the borrowing base to \$275 million. Magnum Hunter also extended the maturity date by one year, resulting in a new maturity date of May 2, 2007. On July 15, 2004, Magnum Hunter amended the Facility again to increase the borrowing base to \$480 million upon the consummation of its New Mexico property acquisition, an increase of \$205 million, and to allow it to use proceeds from its secondary common stock offering to redeem and retire up to \$105 million in principal value of its 9.6% Senior Notes at 109.6% of par. On October 18, 2004, Magnum Hunter amended the Facility to increase the borrowing base by \$45 million, from \$480 million to \$525 million and to increase its maximum borrowings from \$500 million to \$750 million. The level of the borrowing base is dependent on the valuation by the lenders of the assets pledged, primarily oil and gas reserves. At December 31, 2004, Magnum Hunter had \$202.5 million of available credit under the Facility.

The Facility includes covenants, the most restrictive of which requires maintenance of a funded debt to EBITDA ratio and an interest coverage ratio, as defined in the loan agreement. Magnum Hunter was not in compliance with the funded debt to EBITDA ratio required under the covenants at March 31, 2002. The lender provided it with a waiver as of that date, and it negotiated a less restrictive funded debt to EBITDA ratio for the next four successive quarters until March 31, 2003. Magnum Hunter was in compliance with the covenants for the remainder of 2002 and has been in compliance

with the revised covenants for all of 2003 and 2004. Magnum Hunter expects to be able to comply with these covenants in the future.

On a semi-annual basis, Magnum Hunter's borrowing base under the Facility is redetermined by the financial institutions who have committed to it based on their review of its proved oil and gas reserves and other assets. If the outstanding balance on the Facility exceeds the redetermined borrowing base, Magnum Hunter must repay the excess over a six-month period. The last redetermination date had an effective date of June 30, 2004 and was completed on October 15, 2004. This redetermination increased Magnum Hunter's borrowing base by \$45 million up to \$525 million, and the maximum borrowings were increased from \$500 million to \$750 million. Magnum Hunter's next redetermination date will have an effective date of December 31, 2004 and will have a completion date of no later than May 9, 2005.

On March 15, 2002, Magnum Hunter completed a private placement of \$300 million of Senior Notes, referred to as the Private Placement, due 2012 that are unsecured. The Senior Notes bear an annual interest rate of 9.6% due semi-annually, commencing September 15, 2002. Magnum Hunter redeemed \$105 million in principal of these notes on August 27, 2004 at a redemption price of 109.6% of par. Magnum Hunter paid the holders of these redeemed notes \$115.1 million plus accrued and unpaid interest of \$4.5 million. Magnum Hunter recorded \$12.3 million in costs associated with this redemption comprised of \$10.1 million in premiums and \$2.2 million in unamortized deferred financing fees that were written off.

With the funds provided by the new Facility in 2002 and the Private Placement of the 9.6% Senior Notes, Magnum Hunter repaid indebtedness on its old Facility of \$155.7 million, retired the long-term debt acquired in the Prize merger for \$246.8 million, funded the cash component of the merger for \$70.9 million (\$41.1 million net of cash acquired), and paid approximately \$12.2 million for fees and expenses related to the merger. In connection with the Prize merger, Magnum Hunter issued 34,062,963 shares of its common stock to Prize shareholders, increasing its total shares outstanding by 96%.

During 2003, Magnum Hunter paid \$145.2 million to redeem the \$140 million in principal of its 10% Senior Notes. This redemption was funded by borrowings under the Facility as well as the issuance of \$125 million in Convertible Notes during December 2003. Magnum Hunter paid approximately \$5.2 million in premiums to redeem the 10% Senior Notes. Of the notes redeemed, a subsidiary received approximately \$10.9 million in principal and received premiums of approximately \$273 thousand.

During December of 2003, Magnum Hunter issued \$125 million in face value of Convertible Notes. These Convertible Notes bear interest equal to the three-month LIBOR, to be adjusted quarterly. The initial rate set on issuance of the Convertible Notes was 1.17%, and the current rate is 2.49%. The Convertible Notes are convertible into a combination of cash and Magnum Hunter common stock upon certain events. The initial conversion price is \$12.19, subject to adjustment under certain conditions. The Convertible Notes are due December 2023, but can be put by the holders on December 15, 2008, 2013, and 2018. Magnum Hunter has the right to call these Convertible Notes at any time after December 22, 2008. The proceeds from these Convertible Notes were used to repay borrowings under the Facility.

Holders may surrender Convertible Notes for conversion into cash and shares of Magnum Hunter common stock prior to the Convertible Notes' maturity date in the following circumstances: i) during any calendar quarter commencing after the issuance of the Convertible Notes, if Magnum Hunter's common stock price for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the calendar quarter preceding the quarter in which the conversion occurs is more than 110% of the conversion price per share of its common stock in effect on that 30<sup>th</sup> trading day; ii) if Magnum Hunter has called the particular Convertible Notes for redemption and the

redemption has not yet occurred; iii) during the five trading day period after any five consecutive trading day period in which the trading price of \$1,000 principal amount of the Convertible Notes for each day of such five-day period was less than 95% of the product of the closing sale price of Magnum Hunter common stock on that day multiplied by 82.0345, referred to as the Conversion Rate; or iv) upon the occurrence of specified corporate transactions.

Upon the occurrence of the circumstances described above, holders may convert any outstanding notes into cash and shares of Magnum Hunter common stock at an initial conversion price per share of \$12.19. Subject to certain exceptions, at the time notes are tendered for conversion, the value, referred to as the Conversion Value, of the cash and shares of Magnum Hunter common stock, if any, to be received by a holder converting \$1,000 principal amount of the notes will be determined by multiplying the Conversion Rate by the ten-day average closing stock price of Magnum Hunter common stock. Magnum Hunter will deliver the Conversion Value to holders as follows: i) an amount in cash, referred to as the Principal Return, equal to the lesser of (a) the Conversion Value and (b) the principal amount of the notes to be converted and, if the Conversion Value is greater than the Principal Return, ii) an amount in shares equal to the Conversion Value less the Principal Return, referred to as the Net Share Amount. The number of Net Shares to be paid will be determined by dividing the Net Share Amount by the ten day average closing stock price of Magnum Hunter common stock.

Metrix has a \$500 thousand revolving credit facility with a lender. This facility matures on December 16, 2005 and is governed by a borrowing base. Magnum Hunter is a guarantor to this facility. As of December 31, 2004, there were no borrowings outstanding under this facility.

Magnum Hunter's internally generated cash flows, results of operations, and financing of its operations are substantially dependent on oil and gas prices. To the extent that oil and gas prices decline, its earnings and cash flows may be adversely affected regardless of its commodity hedging programs. Magnum Hunter believes that its cash flows from operations, existing working capital, and availability under the Facility will be sufficient to meet interest payments and fund capital expenditures during 2005.

**CAPITAL EXPENDITURES.** For the year ended December 31, 2004, Magnum Hunter's total capital expenditures for property, plant and equipment, were \$540 million. The following summarizes its capital expenditures by cost component (in thousands):

	<b>Oil and Gas Properties</b>	<b>Other Property</b>	<b>Total</b>
	<u>          </u>	<u>          </u>	<u>          </u>
Acquisition costs:			
Unproved acquisitions	19,515		19,515
Proved acquisitions	297,957		297,957
Other property acquisitions		3,311	3,311
Development costs	166,484		166,484
Exploratory costs	52,743		52,743
	<u>          </u>	<u>          </u>	<u>          </u>
Total	536,699	3,311	540,010
	<u>          </u>	<u>          </u>	<u>          </u>

For the year 2005, Magnum Hunter has budgeted approximately \$250 million for exploration and development activities. Magnum Hunter anticipates that the 2005 capital expenditure budget will be funded by cash flow from operations and Facility utilization. Magnum Hunter is not contractually obligated to proceed with any of its material budgeted capital expenditures. The amount and allocation of future capital expenditures will depend on a number of factors that are not entirely within its control or ability to forecast, including drilling results, oilfield costs, and changes in oil and gas prices. As a result, actual capital expenditures may vary significantly from current expectations.

In the normal course of business, Magnum Hunter reviews opportunities for the possible acquisition of oil and gas reserves and activities related thereto. When potential acquisition opportunities are deemed consistent with its growth strategy, bids or offers in amounts and with terms acceptable to Magnum Hunter may be submitted. It is uncertain whether any such bids or offers which Magnum Hunter may submit from time to time, will be acceptable to the sellers. In the event of a future significant acquisition, Magnum Hunter may require additional financing in connection therewith. Magnum Hunter does not budget for acquisition expenditures.

The following summarizes the oil and gas properties acquired in the Prize merger (in millions):

<b>Oil &amp; Gas Properties</b>				
	<b>Unproved</b>	<b>Proved</b>	<b>Other Property</b>	<b>Total</b>
Acquisition Costs	\$ 140,312	\$ 453,834	\$ 22,826	\$ 616,972

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS. Magnum Hunter has the following contractual obligations as of December 31, 2004:

<b>Payments Due by Period</b>					
<b>Total</b>	<b>Less than 1 Year</b>	<b>1-3 Years</b>	<b>4-5 Years</b>	<b>After 5 Years</b>	
(in thousands)					
<b>Contractual Obligations:</b>					
Long-Term Debt	640,000		320,000		320,000
Fixed-Rate Interest Payments	140,400	18,720	37,440	37,440	46,800
Capital Leases	5,500	2,458	3,042		
Commodity Derivatives	20,027	14,046	5,981		
Operating Leases	6,532	2,381	2,079	1,310	762
<b>Total Contractual Obligations</b>	<b>812,459</b>	<b>37,605</b>	<b>368,542</b>	<b>38,750</b>	<b>367,562</b>

Magnum Hunter has no off balance sheet arrangements, variable interest entities, or financing partnerships. In the past it has provided trade guarantees on behalf of its formerly 30% owned affiliate, NGTS. The last of these guarantees expired in July 2003. Further, Magnum Hunter has sold its 30% ownership interest in NGTS, and, therefore, no longer maintains any equity interest in this affiliate. On February 18, 2005, Magnum Hunter's 40% owned subsidiary, Apple Tree Holdings, LLC entered into a \$20.6 million construction loan agreement, referred to as the Construction Loan. The Construction Loan provides financing for the construction of a processing plant, natural gas lateral, carbon dioxide line and related infrastructure in Huerfano County, Colorado. The Construction Loan bears interest at either LIBOR plus 2.25% or a base rate plus 1.25% and will mature no later than July 31, 2006. Magnum Hunter has provided a guaranty to the lender for this Construction Loan. In return for its guaranty, Magnum Hunter received an up-front cash payment as well as a 55% distribution of cash flows from the entity until certain financial tests are met. In the event that the Construction Loan goes into default and Magnum Hunter has to pay on the guaranty, Magnum Hunter will have recourse against the project and related subsidiaries.

Magnum Hunter's 2005 capital expenditure budget is \$250 million. Based on its reserve report, future development costs are estimated to be \$351 million for its proved reserves and \$206.8 million for its probable reserves.

In relation to its hedging programs, Magnum Hunter could have significant cash payments related to current derivative positions. Based on current pricing, Magnum Hunter will make payments of \$14.0 million during 2005 and \$6.0 million during 2006 related to its hedging program. These payment estimates are based on December 31, 2004 commodity prices, and will vary in the future. Please see

Item 7A and Note 12 to the Consolidated Financial Statements for additional information related to Magnum Hunter's derivatives and market risk.

Magnum Hunter makes significant interest payments each year on its debt. During 2004, Magnum Hunter paid \$49.7 million in interest and recorded a liability for \$5.8 million for 2004 interest which would be paid during 2005. At December 31, 2004, Magnum Hunter had \$195 million fixed rate debt and \$450.5 million in variable rate debt; interest payments are made at least semi-annually under all of its debt agreements. Magnum Hunter expects debt levels in the future to decrease over time, unless it completes a significant acquisition. With respect to the variable rate debt, Magnum Hunter is exposed to interest rate risk. Please see Item 7A and Note 5 to the Consolidated Financial Statements for additional information about its debt.

Magnum Hunter currently has \$113.8 million in federal and state income tax net operating loss carryforwards, which, for the most part, prevent it from paying income taxes. These losses will expire, if unused, in years 2012 through 2023. Approximately \$51.4 million of these losses are limited to \$7.8 million per year. Magnum Hunter expects it will be able to continue to offset any federal taxes due with these losses for the foreseeable future. Magnum Hunter provided a \$2 million valuation allowance for utilization of state net operating loss carryforwards in 2004.

In relation to its oil and gas properties, Magnum Hunter has substantial retirement obligations. Magnum Hunter estimates that it will have obligations of \$41.3 million in plugging and abandonment costs related to its current properties. While Magnum Hunter does not anticipate material payments in relation to its plugging obligations until 2017 and beyond, the timing of these costs is not subject to its control. Please see Note 3 to the Consolidated Financial Statements for additional information on Magnum Hunter's asset retirement obligations.

**RECENT TRENDS.** The following is a discussion of recent trends Magnum Hunter considers important and its assessment of the impact of these trends on its business plan.

*Commodity prices.* Magnum Hunter believes that natural gas prices (NYMEX index) will average between \$4.00 and \$7.00 per MCF over the next several years and will likely remain volatile. Magnum Hunter based its 2005 capital and operating budgets on prices of approximately \$6.22 per Mcf. Crude oil prices have increased significantly, but in Magnum Hunter's view are much more variable due to worldwide political and economic factors. For 2005 budgeting purposes, Magnum Hunter has assumed crude prices will average approximately \$45.60 per Bbl (NYMEX index). Its production mix is largely natural gas, and therefore its gross margins are largely driven by natural gas prices.

*Interest rates.* Magnum Hunter has experienced an unusually low interest rate environment for the past several years. Magnum Hunter expects interest rates to increase moderately over the next several years. By December 31, 2005, it expects that approximately 39% of its debt will be fixed at 9.6% through at least 2007 and potentially 2012, with the remaining 61% to be variable rate debt.

*Depreciation, depletion, amortization and accretion (DD&A).* Magnum Hunter's exploration and production segment DD&A rate has increased an annual average of 15% per year since 1999. This increase is primarily attributable to its increased capital expenditures in the offshore Gulf of Mexico region where, typically for its industry, finding and development costs per unit are higher than its average finding and development costs per unit have been historically onshore and its significant New Mexico property acquisition. Magnum Hunter expects to continue to spend a significant percentage of its total capital expenditures budget on offshore Gulf of Mexico projects due to economic parameters experienced in that region. Assuming similar results in its drilling activities and reserve recognition to what it has been achieving, Magnum Hunter would expect its DD&A rate to continue to increase.

*Magnum Hunter management's assessment of the impact of these trends on its business plan.* Magnum Hunter has concentrated its capital budget in areas where it expect to realize the highest

financial benefits, including rate of return and return on capital deployed. As such, it has dedicated significant portions of its capital expenditure budget to the offshore Gulf of Mexico region and onshore in the Southeast New Mexico area over the past several years.

Magnum Hunter has significant exploration, development and exploitation opportunities both onshore and offshore. Magnum Hunter management continues to monitor commodity prices, finding and development costs and interest rates, among other factors, to determine both the total dollars to be spent and the allocation of these dollars among alternative projects within the capital budget. Even if DD&A rates and interest rates continue to increase, and commodity price increases in turn offset these expenses, then Magnum Hunter would expect to continue its current business plan. Magnum Hunter believes it has significant flexibility in the management of its cash flows.

### **Critical Accounting Policies and Other**

Magnum Hunter's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The reported financial results and disclosures were determined using significant accounting policies, practices and estimates as described below. Magnum Hunter believes the reported financial results are reliable and that the ultimate actual results will not differ significantly from those reported.

#### *Oil and Gas Properties*

Magnum Hunter uses the full cost method of accounting for its investment in oil and gas properties. Under the full cost method of accounting, all costs of acquisition, exploration and development of oil and gas proved reserves, including directly related overhead costs, are capitalized into a "full-cost pool" on a country-by-country basis as incurred. Internal costs that directly relate to acquisition, exploration and development activities totaled \$1.3 million for the years ended December 31, 2004 and 2003. The balance of capitalized costs included in oil and gas properties for the years ended December 31, 2004 and 2003 were \$6.5 million and \$5.2 million, respectively. Magnum Hunter's management believes that the basis it uses to determine the amount of internal costs capitalized is appropriate.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves and estimated dismantlement and abandonment costs, net of salvage values, are amortized on the unit-of-production method using estimates of proved reserves. Costs directly associated with the acquisition and evaluation of unproved properties are excluded from the amortization base until the related properties are evaluated. Such unproved properties are assessed for impairment quarterly and any provision for impairment is transferred to the full-cost amortization base. Sales of oil and gas properties, including consideration received from sales or transfers of properties in connection with partnerships, joint venture operations or drilling arrangements, are credited to the full-cost pool unless the sale would have a significant effect on the amortization rate. Abandonment of properties is accounted for as an adjustment to capitalized costs with no loss recognized.

Costs are transferred into the amortization base on an ongoing basis as the projects are evaluated and proved reserves are established or impairment determined. Pending determination of proved reserves attributable to the above costs, Magnum Hunter cannot assess the future impact on the amortization rate.

The capitalized costs are subject to a "ceiling test," which generally limits such costs less accumulated amortization and related deferred income taxes to the aggregate of the estimated present value of future net revenues from proved reserves discounted at ten percent (PV-10) based on current economic and operating conditions less income tax effects related to the differences between the book and tax basis of the oil and gas properties. The ceiling test is performed on a quarterly basis. Magnum Hunter experienced no impairment in 2004, 2003, or 2002.

All costs relating to production activities are charged to expense as incurred.

In accordance with SFAS 143, "Accounting for Asset Retirement Obligations," Magnum Hunter carries a liability for any legal retirement obligations on its oil and gas properties. The associated asset retirement costs are capitalized as part of the full-cost pool and depleted on the unit of production basis.

For purposes of the ceiling test, Magnum Hunter removes the discounted present value included in its future development costs on its reserve report for which it has already booked an obligation under SFAS 143. For purposes of its depletion calculation, Magnum Hunter includes in future development costs the estimated plugging and abandonment costs, net of estimated salvage values, for proved undeveloped wells. For purposes of both of these calculations, Magnum Hunter does not include plugging and abandonment costs in its future development costs on developed proportions for which it has booked an obligation under SFAS 143.

Reserve engineering is a subjective process that is dependent on the quality of available data and on engineering and geological interpretation and judgment. Reserve estimates are subject to change over time as additional information becomes available.

#### ***Revenue Recognition***

Revenues are recognized when title to the product transfers to purchasers. Magnum Hunter follows the "sales method" of accounting for revenue for oil and natural gas production, so that it recognizes sales revenue on all production sold to purchasers, regardless of whether the sales are proportionate to its ownership in the property. In these instances when Magnum Hunter's sales are not proportionate to its interests, a receivable or liability is recognized only to the extent that Magnum Hunter has an imbalance on a specific property greater than the expected remaining proved reserves. Current revenues are accrued based on Magnum Hunter's expectation of actual deliveries and actual prices received. Plant revenues are recognized as product is sold, and its gathering fees are recognized as the gathering services are performed. Revenues for Magnum Hunter's oilfield management services segment are recognized as services are performed and equipment is delivered.

#### ***Derivative Instruments***

Magnum Hunter's product price and interest hedging activities are described in Note 12 to the consolidated financial statements. Periodically Magnum Hunter enters into derivative instruments such as futures, swaps and options contracts to reduce the adverse effects of fluctuations in natural gas and crude oil prices. Under Magnum Hunter's risk management policy, at inception, commodity hedge positions may not exceed 75% of natural gas and 90% of crude oil current forecasted (18 months) commodity production. For forecasted non-current (greater than 18 months) commodity production, at inception, commodity hedge positions for natural gas and crude oil may not exceed 75% of forecasted production for each product. Magnum Hunter also utilizes, from time to time, financial derivative instruments to hedge the risk associated with interest on its outstanding debt. Generally, the cash settlement of all derivative instruments is recognized as income or expense in the period in which the hedged transaction is recognized.

All freestanding financial derivative instruments, including certain derivative instruments embedded in other contracts if certain criteria are met, are recognized at estimated fair value on Magnum Hunter's balance sheet. Magnum Hunter determines its fair values based on market values obtained from its counterparties. Derivative instruments that are not designated as hedges must be adjusted to fair value through net income. Changes in the fair value of derivative instruments that are fair value hedges are offset against changes in the fair value of the hedged items, and are recognized in net income. Changes in the fair value of derivative instruments that are cash-flow hedges are recognized in other comprehensive income until such time as the hedged items are recognized in net income.

Ineffective portions of a derivative instrument's change in fair value are immediately recognized in net income.

### ***Goodwill***

As a result of its merger with Prize, Magnum Hunter currently has \$56.5 million of goodwill recorded on its books. Under SFAS No. 142, Magnum Hunter will not amortize any of the goodwill acquired in the merger. All goodwill has been allocated to the Exploration and Production reporting unit. Magnum Hunter tests its goodwill for impairment on an annual basis or whenever indicators of impairment exist. Magnum Hunter performed its annual impairment test at December 31, 2004, and determined that no impairment existed. The annual impairment test requires management to make significant estimates and judgments. If impairment is determined to exist, Magnum Hunter will measure its impairment based on a comparison of the carrying value of goodwill to the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the Exploration and Production reporting unit to all of the assets and liabilities of that unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. If the carrying amount of goodwill exceeds the implied fair value of that goodwill, impairment will be recognized in the income statement.

### ***Stock Compensation***

At December 31, 2004, Magnum Hunter had four stock-based employee compensation plans, which are described more fully in Note 13 of the Consolidated Financial Statements. Magnum Hunter accounts for its employee stock option plans under SFAS No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure, an Amendment to FASB Statement No. 123," in December 2002. SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation and amends the disclosure requirements of SFAS No. 123. On June 1, 2003, and effective January 1, 2003, Magnum Hunter began expensing the fair market value of stock options newly granted, modified or settled pursuant to SFAS No. 123, "Accounting for Stock-Based Compensation," and as allowed under the prospective method of SFAS No. 148. The fair value of each option granted after December 31, 2002, is estimated on the grant date, using the Black-Scholes option-pricing model. For the years ended December 31, 2003 and 2004, Magnum Hunter recorded stock compensation expense of \$3.0 million and \$768 thousand, respectively, which is reflected in its general and administrative expenses. For options granted prior to January 1, 2003, Magnum Hunter continues to use the intrinsic method under APB No. 25, "Accounting for Stock Issued to Employees and Related Interpretations," whereby no compensation expense is recognized for stock options granted with an exercise price equal to the market value of Magnum Hunter stock on the grant date. Magnum Hunter's future accounting for stock-based compensation will be impacted by the issuance of SFAS No. 123(R). Please see " Recently Issued Statements" discussion below for additional information.

## Edgar Filing: O'Neill Andrew J - Form 4

If Magnum Hunter had recorded stock option expense under the fair value provisions of SFAS No. 123 for all prior and current grants, its net income and earnings per share ("EPS") would have been as shown in the below pro forma tables (in thousands):

	Year Ended December 31,		
	2004	2003	2002
Net income, as reported	\$ 103,573	\$ 26,117	\$ 15,522
Total Stock-based employee compensation expense included in reported net income, net of income taxes of \$278 and \$1,144, respectively	490	1,873	
Deduct: Total stock-based employee compensation determined under fair value-based method for all awards, net of income taxes of \$1,871, \$2,896, and \$1,962 respectively	(3,298)	(4,751)	(3,219)
<b>Pro forma net income</b>	<b>\$ 100,765</b>	<b>\$ 23,239</b>	<b>\$ 12,303</b>
<b>Earnings per share:</b>			
Basic as reported	\$ 1.35	\$ 0.39	\$ 0.25
Basic pro forma	\$ 1.31	\$ 0.35	\$ 0.20
Diluted as reported	\$ 1.31	\$ 0.39	\$ 0.25
Diluted pro forma	\$ 1.28	\$ 0.34	\$ 0.20

Magnum Hunter estimated the fair value of each stock based grant (options and warrants) using the Black-Scholes option pricing method while using the following weighted average assumptions:

	2004(a)	2003(b)	2002
Risk-free interest rate	3.38%	1.58%	3.68%
Expected life	4.1 years	2.1 years	7.4 years
Expected volatility	40.7%	46.3%	49.5%
Dividend yield			
Weighted average fair value of options granted	\$ 3.81	\$ 3.03	\$ 3.17

- (a) Magnum Hunter granted 1,403,000 options during 2004, which had a reduced term of four years. Prior grants have ten-year terms.
- (b) Magnum Hunter granted 999,260 options during 2003, which had a reduced term of three years. Prior grants have ten-year terms.

### *Income Taxes*

Magnum Hunter files a consolidated federal income tax return. Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due, if any, plus net deferred taxes related primarily to differences between the basis of assets and liabilities for financial and income tax reporting. Deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets include

## Edgar Filing: O'Neill Andrew J - Form 4

recognition of operating losses that are available to offset future taxable income and tax credits that are available to offset future income taxes. Valuation allowances are recognized to limit recognition of deferred tax assets where appropriate. Such allowances may be reversed when circumstances provide evidence that the deferred tax assets will more

IV-27

---

likely than not be realized. Magnum Hunter recorded an allowance on certain state operating losses of \$2.0 million during 2004.

#### ***Asset Retirement Obligations***

SFAS No. 143, "Accounting for Asset Retirement Obligations," became effective beginning January 1, 2003. SFAS No. 143 requires the recognition of a fair value liability for any retirement obligation associated with long-lived assets in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over the asset's useful life. See Note 3 of the Consolidated Financial Statements for additional information on Magnum Hunter's asset retirement obligations. Upon adoption of SFAS No. 143, Magnum Hunter recorded an addition to oil and gas properties of \$25.4 million, an asset retirement obligation of \$30.4 million, a reduction of accumulated depletion of \$5.6 million, and a pre-tax gain of \$643 thousand. The retirement obligation requires management to make significant estimates and judgments regarding Magnum Hunter's expected plugging costs and retirement dates.

#### ***Recently Issued Statements***

The Financial Accounting Standards Board ("FASB") has issued FASB Staff Position ("FSP") No. 142-2, "Application of FASB Statement 142, Goodwill and Other Intangible Assets, to Oil-and-Gas Producing Entities after evaluating an issue involving the classification of mineral rights. In June 2001, FASB issued Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations," which requires the purchase method of accounting for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method. In July 2001, the FASB also issued SFAS No. 142, "Goodwill and Other Intangible Assets," which discontinues the practice of amortizing goodwill and indefinite lived intangible assets and initiates an annual review of impairment. Intangible assets with a determinable useful life will continue to be amortized over that period. The amortization provisions apply to goodwill and intangible assets acquired after June 30, 2001. SFAS No. 141 and 142 clarify that more assets should be distinguished and classified between tangible and intangible. Magnum Hunter did not change or reclassify contractual mineral rights included in proved and unproved oil and gas properties on its balance sheet upon adoption of SFAS No. 142. Magnum Hunter believes the treatment of such mineral rights as tangible assets under the full cost method of accounting for oil and gas properties is appropriate. An issue was raised regarding whether these mineral rights should be classified as tangible or intangible assets. FSP No. 142-2 addressed this issue and supports Magnum Hunter's current accounting treatment of mineral rights and will not impact its financial statements. This FSP is effective for reporting periods beginning after September 2, 2004.

FASB issued FSP FAS 129-1, "Disclosure Requirements Under FASB Statement No. 129, *Disclosure of Information About Capital Structure*," in April 2004. This FSP provides additional guidance on the disclosure requirements of contingently convertible securities. Magnum Hunter made the required disclosures related to the terms of its Convertible Notes in its Annual Report on Form 10-K and has provided explanations in Note 6 of its Form 10-K about the dilutive effects of these notes on its earnings per share, referred to as EPS.

FASB's Emerging Issues Task Force ("EITF") has issued an Abstract for EITF Issue No. 04-8, "The Effect of Contingently Convertible Debt on Diluted Earnings per Share," which addresses the issue of when the dilutive effects of contingently convertible debt instruments should be included in diluted earnings per share. This guidance requires companies to include the dilutive effect of convertible debt securities in diluted earnings per share regardless of whether or not the contingent conversion features have been triggered. The principal of Magnum Hunter's Convertible Notes must be settled in cash, with the conversion spread settled in stock. This EITF is effective for periods ending after December 15, 2004. Magnum Hunter has accordingly included approximately 94 thousand

potential shares to be issued for its Convertible Notes in its earnings per share computations for the year ending 2004 based on the spread between its average market price during the year and the conversion price on these notes. Magnum Hunter did not include any potential dilution for the 2003 period because the conversion price did not exceed its average market price during that period.

The SEC Staff Accounting Bulletin ("SAB") 106 was released in September 2004. SAB 106 expresses the SEC staff's views on the interaction of SFAS No. 143 and the full cost method and provides guidance on computing the full cost ceiling as well as depreciation, depletion, and amortization. The SAB also requires additional disclosures regarding how the application of SFAS No. 143 has affected the ceiling test and depreciation, depletion and amortization. This guidance is effective for the first fiscal quarter beginning after its publication. Magnum Hunter implemented this guidance for its ceiling test and depletion calculations during the fourth quarter of 2004 and experienced no significant impact.

FASB issued SFAS No. 123(R), "Share-Based Payment," during December 2004. Under this revised guidance, all share-based equity and liability instruments will be recorded as compensation expense based on their fair values, and all liability instruments will be remeasured each reporting period. This guidance will be effective as of the beginning of the first annual or interim reporting period that begins after June 15, 2005, which would cause Magnum Hunter to adopt this statement July 1, 2005. Magnum Hunter currently accounts for its stock-based compensation under the prospective method, under which it only records compensation expense on awards granted after 2003. Upon adoption of this statement, Magnum Hunter will apply the modified prospective method to its equity instruments under which compensation expense will also be recorded on the unvested portions of awards granted prior to 2003. At this time, Magnum Hunter estimates the impact of these prior years' grants on 2005 earnings to be an additional pre-tax expense of \$1.2 million.

FASB also issued SFAS No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29," during December 2004. SFAS No. 153 amends APB Opinion No. 29 by eliminating the exception from fair value measurement prescribed in that statement and replaces it with an exception for exchanges that have no significant impact on future cash flows. This statement is effective for exchanges that take place in fiscal periods beginning after June 15, 2005. Magnum Hunter does not expect this statement to have an impact on its future financials.

#### *Off Balance Sheet Arrangements*

In the past, Magnum Hunter has provided trade guarantees on behalf of an unconsolidated affiliate, which has since been sold. The last of these guarantees expired in July 2003. Further, Magnum Hunter sold its 30% ownership interest in NGTS and, therefore, no longer maintains any equity interest in this former affiliate. On February 18, 2005 Magnum Hunter's 40% owned subsidiary, Apple Tree Holdings, LLC entered into a \$20.6 million construction loan agreement, referred to as Construction Loan. The Construction Loan provides financing for the construction of a processing plant, natural gas lateral, carbon dioxide line and related infrastructure in Huerfano County, Colorado. The Construction Loan bears interest at either LIBOR plus 2.25% or a base rate plus 1.25% and will mature no later than July 31, 2006. Magnum Hunter has provided a guaranty to the lender for this Construction Loan. In return for its guaranty, Magnum Hunter received an up-front cash payment as well as 55% distribution of cash flows from the entity until certain financial tests are met.

Magnum Hunter had equity and debt investments in a privately held entity which declared bankruptcy on March 4, 2002, and for which it recorded an impairment charge against earnings of \$5.0 million at December 31, 2001. Magnum Hunter is not responsible for any debts of this entity. Magnum Hunter had an investment in available-for-sale securities of another entity of \$2.8 million at December 31, 2001. Because of the deteriorating financial condition of this entity, Magnum Hunter recorded an other than temporary impairment of \$2.1 million as a charge against earnings at

December 31, 2001, and it recorded an additional impairment for the remaining carrying value of this asset at June 30, 2002. Magnum Hunter is not responsible for any debts of this entity.

*Other*

At March 1, 2005, Magnum Hunter had approximately 43% of its natural gas production and approximately 17% of its crude oil production hedged through December 31, 2005. In addition, Magnum Hunter had approximately 11% of its natural gas production and 8% of its crude oil production hedged for the calendar year 2006. Unless Magnum Hunter enters into additional hedging transactions, the remainder of its hydrocarbon volumes will be sold at market prices. Future commodity price declines will negatively impact future income and cash flow to the extent of any production sold at market prices. These declines could ultimately affect the quantity of proved oil and gas reserves and cost center ceiling values. These results, individually or collectively, could result in bank debt default and/or debt acceleration, restrict Magnum Hunter's ability to attract qualified personnel or cause further industry consolidation. There is no requirement from any of Magnum Hunter's lenders to hedge its products.

Magnum Hunter's domestic operations are concentrated in the southwestern and mid-continent regions of the United States and shallow water region of the Gulf of Mexico offshore Texas and Louisiana. Magnum Hunter currently has no operations outside of the United States of America. Magnum Hunter currently has 27 wells that individually produce a net 1.5 MMcf per day or greater, but these are not concentrated in any one field. Magnum Hunter has no individual fields in which disruptions could materially reduce its financial results.

**Quantitative and Qualitative Disclosures About Market Risk**

Magnum Hunter's operations are exposed to market risks primarily as a result of changes in commodity prices and interest rates. Magnum Hunter does not use derivative financial instruments for speculative or trading purposes.

*Energy Swap Agreements*

Magnum Hunter produces, purchases, and sells crude oil, natural gas, condensate, and natural gas liquids. As a result, Magnum Hunter's financial results can be significantly impacted as these commodity prices fluctuate widely in response to changing market forces. Magnum Hunter has previously engaged in oil and gas hedging activities and intend to continue to consider various hedging arrangements to realize commodity prices which it considers favorable and to reduce volatility. Magnum Hunter engages in futures contracts with certain of its oil and gas production through various contracts, referred to as Swap Agreements. The primary objective of these activities is to protect against significant decreases in price during the term of the hedge.

The Swap Agreements provide for separate contracts tied to the New York Mercantile Exchange, referred to as NYMEX, light sweet crude oil futures and Henry Hub natural gas futures, and to the Inside FERC natural gas index price postings, referred to as Index. Magnum Hunter has combined contracts which have agreed upon price floors and ceilings, referred to as Costless Collars. When the Index price exceeds the contract ceiling, Magnum Hunter pays the spread between the ceiling and the Index price applied to the related contract volumes. When the contract floor exceeds the Index, Magnum Hunter receives the spread between the contract floor and the Index price applied to the related contract volumes.

To the extent Magnum Hunter receives the spread between the contract floor and the Index price applied to related contract volumes, it has a credit risk in the event of nonperformance of the counterparty to the agreement. Magnum Hunter does not anticipate any material impact to its results of operations as a result of nonperformance by these counterparties.

## Edgar Filing: O'Neill Andrew J - Form 4

Magnum Hunter has no margin deposits with any counter-parties as of December 31, 2004 related to hedge transactions. Magnum Hunter does not intend to enter into any new hedging contracts with institutions that require margin deposits.

At December 31, 2004, Magnum Hunter had open contracts with the following terms:

Commodity	Type	Volume/Day	Duration	Wtd. Avg. Price
Natural Gas	Collar	60,000 MMBTU	Jan 05 - Dec 05	\$4.21 - \$6.85
Natural Gas	Swap	20,000 MMBTU	Jan 05 - Dec 05	\$6.25
Natural Gas	Collar	20,000 MMBTU	Jan 06 - Dec 06	\$5.25 - \$6.30
Crude Oil	Swap	1,000 BBL	Jan 05 - Dec 05	\$34.90
Crude Oil	Collar	1,000 BBL	Jan 05 - Dec 05	\$35.00 - \$55.00
Crude Oil	Collar	1,000 BBL	Jan 06 - Dec 06	\$30.00 - \$35.85

Based on future market prices at December 31, 2004, the fair value of open contracts to Magnum Hunter was a net liability of \$19.8 million. If future market prices were to increase 10% from those in effect at December 31, 2004, the fair value of Magnum Hunter's open contracts would be a liability of \$39.1 million. If future market prices were to decline 10% from those at December 31, 2004, the fair value of Magnum Hunter's open contracts would be a liability of \$6.5 million.

At inception, commodity hedge positions may not exceed 75% of natural gas and 90% of crude oil forecasted current (18 months) commodity production. For non-current (greater than 18 months) commodity production, at inception, commodity hedge positions for natural gas and crude oil may not exceed 75% of forecasted production for each product. Unhedged portions of Magnum Hunter's natural gas and crude oil production will be subject to market price fluctuations.

### *Fixed and Variable Debt*

Magnum Hunter uses fixed and variable debt to partially finance budgeted expenditures. These agreements expose Magnum Hunter to market risk related to changes in interest rates.

The following table presents the carrying and fair value of Magnum Hunter's debt along with average interest rates. Fair values are calculated as the net present value of the expected cash flows of the financial instruments, except for the 9.6% Senior Notes and the Convertible Notes, which are valued at their last traded value before December 31, 2004.

Expected Maturity Dates	2005	2006 - 2007	2012	2023	Total	Fair Value
(in thousands)						
<b>Variable Rate Debt:</b>						
Bank Debt(a)	\$	\$ 320,000	\$	\$	\$ 320,000	\$ 320,000
Convertible Notes(b)	\$	\$	\$	\$ 125,000	\$ 125,000	\$ 151,719
Capital Lease Obligations(c)	\$ 2,458	\$ 3,042	\$	\$	\$ 5,500	\$ 5,500
<b>Fixed Rate Debt:</b>						
9.6% Senior Notes	\$	\$	\$ 195,000	\$	\$ 195,000	\$ 221,325

(a) The weighted average interest rate on the bank debt with recourse at December 31, 2004 was 3.92%.

(b) The interest rate on the Convertible Notes at December 31, 2004 was 2.49%. The rate on these Convertible Notes is equal to the three month LIBOR, adjusted quarterly. A holder of these notes has the right to require Magnum Hunter to repurchase all or a portion of the notes on December 15, 2008, 2013, and 2018. The repurchase price will be equal to the face value of the notes plus accrued and unpaid interest up to the date of repurchase.

(c) The weighted average interest rate on capital lease obligations at December 31, 2004 was 5.58%.



**BUSINESS**

Additional information regarding Magnum Hunter and its business can be found in "Chapter I The Merger The Companies Magnum Hunter."

**Properties**

Magnum Hunter's major properties are located in four core areas: (i) the Mid-Continent region, (ii) the Permian Basin, (iii) the Gulf Coast region and (iv) the Gulf of Mexico.

***Mid-Continent Region***

Magnum Hunter's Mid-Continent operations include assets principally located in the Ardmore Basin in south central Oklahoma/Texas Panhandle and in Southwestern Arkansas. The majority of these properties were acquired from Burlington Resources, Spirit 76, Vastar and Prize. Approximately 72% of the estimated reserves are natural gas and 28% are oil and natural gas liquids located on approximately 263,216 net mineral leasehold acres in twenty-seven counties in Oklahoma, eleven counties in Texas and two counties in Arkansas. As of December 31, 2004, DeGolyer and MacNaughton, referred to as D&M, and Cawley, Gillespie & Associates, Inc., referred to as Cawley Gillespie, independent reservoir engineers, have estimated the Mid-Continent properties proved reserves at 12.1 MMBbl of oil and natural gas liquids and 182.8 Bcf of natural gas, or, on a natural gas equivalent basis, 255.6 Bcfe. Total net daily production from the Mid-Continent properties for the month of December 2004 was 34.9 MMcf/d for natural gas and 1,273 Bbl/d of oil and natural gas liquids or 42.5 MMcfe/d. Magnum Hunter's wholly-owned subsidiary, Gruy Petroleum Management Co., referred to as Gruy, is the operator of approximately 85% of the wells located in the Mid-Continent Region. Additional Mid-Continent development drilling, recompletion activities and improvements to existing waterflood operations focus on the Walnut Bend Field, the Red Deer Creek Field, the Madill Field and the Eola-Robberson Field.

*Panoma.* The Panoma properties currently consist of approximately 544 natural gas wells in the East Panhandle and South Erick Fields along a corridor 66 miles long and 20 miles wide stretching from Beckham County, Oklahoma to Gray County, Texas. All wells are less than 2,300 feet deep and produce natural gas from the Granite Wash and/or Brown Dolomite formations. For the month of December 2004, net natural gas sales were approximately 9.0 MMcf/d, which excludes liquids processed from this natural gas stream through Magnum Hunter's gas processing facility located adjacent to these fields, known as the McLean Plant. Development continues with increased density drilling in the West Panhandle.

*Eola-Robberson.* The Eola-Robberson Field is located in Garvin County, Oklahoma and has been producing since 1920. It is productive in multiple reservoirs from the fractured Devonian Klippe at 6,400 feet to the Basal Oil Creek at 11,800 feet. The field has primarily been developed within two units, the Eola North Fault Block Unit and the South Eola Bromide Sand Unit. The waterfloods for this field were discontinued in 1992, with the South Eola Bromide Sand Unit being disbanded in 2003. The wellbores are being recompleted into bypassed oil pockets in the Bromide, McLish and Oil Creek and the fractured gas reservoirs such as the Sycamore, Woodford, Hunton and Viola. Magnum Hunter has an interest in 66 producing wells, with working interests varying from 8% to 100%. Magnum Hunter operates all but 14 of these wells. For the month of December 2004, net production from the field averaged 6,399 Mcf/d and 380 Bbl/d.

*Cumberland.* The Cumberland Field is located in Bryan and Marshall Counties, Oklahoma. It was discovered in 1940 and is productive in multiple reservoirs from the Goddard down to the Arbuckle formation. Depths range from 2,000 feet to 6,800 feet. Initially, the field produced oil from the Bromide, McLish and Oil Creek formations. These zones were unitized in 1964 for waterflood

operations, which continue today. The "Shallow Gas" zones include the Sycamore, Woodford, Hunton, and Viola. These formations are predominantly gas productive and are produced commingled. Development drilling plans exist for four additional proved undeveloped locations to exploit the shallow gas on 160 acre spacing and one proved undeveloped location in the Oil Creek formation. The shallowest zone in the field is the Goddard, which is a channel sand. Magnum Hunter has an interest in 74 active wells, with working interests varying from 17% to 100%. Magnum Hunter operates all but 10 of these wells. For the month of December 2004, net production from the field averaged 6,061 Mcf/d and 144 Bbl/d.

*Walnut Bend.* The Walnut Bend Field is located in Cooke County, Texas. The field was discovered in the late 1930's and produces oil and gas from numerous intervals ranging in depth from 2,000 feet in the Montgomery sands to over 7,000 feet in the Ellenburger carbonate. There are currently 107 active producing wells and 31 active injection wells. Magnum Hunter's working interest ownership in the wells is approximately 91%. For the month of December 2004, net production from the wells averaged 86 Mcf/d and 568 Bbl/d. Current activities in the field include a recompletion program on both active and inactive wellbores as identified by a two-year geological study. This will include the initiation of numerous small waterflood projects.

*Madill.* The Madill Field is located in Marshall County in Southern Oklahoma. The first production from this field occurred in 1906 and produces primarily gas from various shallow reservoirs, such as the Sycamore, Woodford, Viola and Bromide at depths ranging from 3,750 feet to 5,700 feet. There are currently 57 active producing wells. Magnum Hunter's working interest ownership in the wells varies from 41% to 100%. For the month of December 2004, net production from the wells averaged 1,202 Mcf/d and 56 Bbl/d.

*Red Deer Creek.* The Red Deer Creek Field and the adjoining Shriekey West Field are located in Roberts County, Texas in the Texas Panhandle. Initial production was established in 1958 in the Lower Albany Dolomite and subsequent successful completions were made in the Wolfcamp, Granite Wash, and Morrow. Producing depths range from 4,100 ft. to 11,000 ft. There are currently 27 active wellbores with working interest ownerships ranging from 53% to 100%. During 2004, these fields benefited from 11 recompletions in the Granite Wash. The Red Deer Creek Field has been re-spaced to 40 acres and a drilling program is slated to begin in 2005 with the Granite Wash as its target. For the month of December 2004, net production from these wells averaged 2,632 Mcf/d and 25 Bbl/d.

#### ***Permian Basin***

Magnum Hunter's Permian Basin operations include assets located in West Texas and Southeastern New Mexico with an interest in 3,840 wells located in 240 different fields. Magnum Hunter's wholly-owned subsidiary, Gruy Petroleum, is the operator of approximately 77% of the producing wells. Management believes the Permian Basin properties will continue to provide significant opportunities for exploitation of oil and natural gas through development drilling, workovers, recompletions, and optimization of enhanced oil recovery projects. As of December 31, 2004, the Permian Basin properties had proved reserves of 48.9 MMBbl of oil and 299.5 Bcf of natural gas, or on a natural gas equivalent basis, 592.8 Bcfe. Total net daily production from the Permian Basin properties for the month of December 2004 was approximately 60,269 Mcf/d of natural gas and 7,451 Bbls/d of oil or 104.9 MMcfe/d.

In evaluating the Permian Basin properties, Magnum Hunter has identified 509 drilling locations including developmental production and injection wells. The top valued fields in the Permian Basin are Spraberry, Westbrook, Warwink, Howard Glasscock, Jo-Mill, Kermit, Keystone, Willo, P&P and the Southeast New Mexico area.

## Edgar Filing: O'Neill Andrew J - Form 4

*Spraberry.* The Spraberry field is located in Irion, Glasscock and Reagan Counties, Texas. Magnum Hunter owns interest in 309 oil and gas wells. Gruy Petroleum operates 98% of the wells in this field. The NG Tex acquisition in 2004 added several operated wells to Magnum Hunter's existing position in the Spraberry trend. For the month of December 2004, Magnum Hunter's net production in this field averaged 344 Bbl/d and 2,685 Mcf/d. The wells in this field produce from the Spraberry formation at approximately 6,000 feet D&M has identified 88 infill PUD locations with net reserves of 30.7 Bcfe. Magnum Hunter has several wells budgeted for 2005 in this trend.

*Westbrook.* The Westbrook field is located in Mitchell County, Texas and produces from the Clearfork formation at a depth of approximately 3,200 feet. Gruy operates the Southwest Westbrook Unit and Morrison G lease and Magnum Hunter owns an 89% and 100% working interest, respectively. Magnum Hunter also owns a small working interest in the Enervest operated North Westbrook Unit. As of December 31, 2004, there were 122 active wells in these three leases. For the month of December 2004, net production from the wells averaged 823 Bbl/d. The initial wells in this area were drilled in the 1920's and waterflood operations began in the 1960's. Magnum Hunter is actively drilling infill wells and optimizing waterflood operations in the Southwest Westbrook Unit.

*Warwink.* The Warwink field is located in Ward and Winkler Counties, Texas. Magnum Hunter owns interests in 52 wells producing from the Cherry Canyon formation at depths from 4,800 to 7,400 feet. Magnum Hunter's working interest ownership in these wells varies from 71% to 85% and all wells are operated by Gruy. For the month of December 2004, Magnum Hunter's net production from these wells averaged 324 Bbl/d and 1,003 Mcf/d. The wells in this field have multiple stacked Cherry Canyon sands that can be produced together. Several behind pipe zones have been identified and Magnum Hunter is actively adding these zones in the existing wells.

*Howard Glasscock.* The Howard Glasscock field is located on the border of Howard and Glasscock Counties, Texas. Magnum Hunter owns an interest in 175 wells, of which 93% are operated by Gruy. Magnum Hunter acquired additional interests in 2002 on two properties, regaining operations and increasing the working interest from 50% to 100%. Magnum Hunter's working interest in the other wells in this area range from 5% to 100%. For the month of December 2004, Magnum Hunter's net production from these wells averaged 640 Bbl/d for oil, and 109 Mcf/d for gas. The properties in the Howard Glasscock field consist of multiple waterfloods in the San Andres, Glorieta and Clearfork formations. Magnum Hunter also owns interests in leases that have been identified as future waterflood candidates.

*Jo-Mill.* The Jo-Mill field is located in Borden County, Texas and produces in the Sprayberry formation at approximately 7,100 to 7,500 feet. Magnum Hunter owns a non-operated working interest that ranges from 5% to 33% in three different waterflood units. Magnum Hunter's net production from these three units averaged 671 Bbl/d and 243 Mcf/d in December of 2004. These fields were unitized between 1963 and 1973 and were initially waterflooded on a peripheral pattern with 80 acre spacing. From the mid 70's to the 90's, multiple infill wells were drilled to convert the floods to a line drive pattern on 40 acre spacing. In 2000, ChevronTexaco started drilling 20 acre infill wells in their operated Jo-Mill Unit. D&M has assigned net proved undeveloped reserves of 8,392 MMcfe to an additional 120 locations in the ChevronTexaco operated Jo-Mill Unit.

*Kermit.* The Kermit field is located in the heart of Winkler County, Texas. Magnum Hunter owns interests in 191 oil and gas wells with a working interest varying from 21% to 100%. Gruy operates 89% of the wells in this field. The average December 2004 net production from these wells was 169 Bbl/d and 3,521 Mcf/d. The wells in this field produce from several different horizons, including the Ellenburger, McKee, Fusselman, Devonian, Clearfork, Holt, Colby and Yates. The majority of the wells Magnum Hunter has an interest in are currently producing from the Yates gas cap.

## Edgar Filing: O'Neill Andrew J - Form 4

*Keystone.* The Keystone field is located in Winkler County, Texas. Magnum Hunter owns an interest in 248 oil and gas wells of which 99.9% are operated by Gruy. These wells produced an average of 296 Bbl/d and 406 Mcf/d net in December 2004. Magnum Hunter owns 100% working interests in the East Keystone Unit where waterflood operations commenced in June of 2002. This unit is flooding the San Andres and Holt formations on a 20 acre 5 spot pattern. Initial waterflood response has been seen in most parts of the field.

*Willo.* The Willo field is located in Crockett and Val Verde Counties, Texas. Magnum Hunter owns an interest in 17 oil and gas wells producing from the Ellenburger, Strawn and Canyon/Wolfcamp formations. Magnum Hunter's working interest ranges from 23% to 100% in this field with 82% of the wells operated by Gruy. Magnum Hunter's average net production for December 2004 for these wells was 2,129 Mcf/d. The most prolific zone in this field is the Ellenburger dolomite at an average depth of 14,000 feet. This zone accounts for 94% of the 8.9 MMcfe net proved developed producing reserves assigned to this field by D&M. Proved undeveloped reserves of 17.0 MMcfe net for four additional Ellenburger wells have been identified by D&M.

*P&P.* The P&P field is located in Crane County, Texas producing from the Devonian at a depth of 5,500 feet. This field was unitized as the River Bend Devonian Unit for waterflood operations in 2000. Water injection was started in September of 2000 and the unit has experienced an increase in net oil production from 160 Bbl/d in April of 2001 to 350 Bbl/d in December of 2004. Magnum Hunter owns a 47% working interest in 20 wells and all are operated by Gruy. This field is located adjacent to the Gruy operated Abell Devonian Unit that has been under waterflood operations in the Devonian since 1961. Proved undeveloped reserves were assigned by D&M to the River Bend Devonian Unit in contemplation of a carbon dioxide injection project that is anticipated to follow waterflood operations.

*Southeast New Mexico.* The Southeast New Mexico properties consist of approximately 1,100 wells in Chaves, Lea, and Eddy Counties, of which 71% are operated by Gruy. Several of Magnum Hunter's fields in Lea County produce from the Yates, Seven Rivers, Queen and other formations at depths generally shallower than 3,000 feet. The average net production for the Southeast New Mexico properties for December 2004 was 1,915 Bbl/d and 42,784 Mcf/d. Magnum Hunter has been actively drilling increased density wells in the Morrow formation at approximately 11,500 feet. Magnum Hunter participated in 34 Morrow wells in 2004 and has 23 operated wells planned for 2005. D&M has identified 93 proved undeveloped locations for the Morrow, with net reserves of 64.8 BCFe. Several of the Morrow wells have identified proved developed non-producing areas in the Atoka and Strawn formations. The Encana acquisition that closed in 2004 greatly increased Magnum Hunter's upside potential in S. E. New Mexico.

### *Gulf Coast*

Magnum Hunter owns an interest in 360 wells in the Gulf Coast region, of which Gruy is the operator of approximately 71% of the wells. Magnum Hunter has received an engineering evaluation from D&M on the net reserves in the Gulf Coast. According to D&M, as of December 31, 2004, the Gulf Coast properties had proved reserves of 2.0 MMBbl of oil and 63.7 Bcf of natural gas, or on a natural gas equivalent basis, 75.6 Bcfe. Approximately 84% of the estimated reserves are natural gas and 16% are oil. Total net daily production from the Gulf Coast properties for the month of December 2004 was approximately 20.1 MMcf/d of natural gas and 566 Bbls/d of oil. The principal fields in the onshore Gulf Coast region are Brazil, Buchel, Provident City, Alta Loma and Word, North.

*Buchel.* Magnum Hunter operates eight producing wells and one salt water disposal well in this Dewitt County, Texas field. Magnum Hunter has an 87.5% working interest in two of the wells and own a 100% working interest in the remaining wells. The producing interval in the Buchel field is the lower cretaceous Edwards formation at approximately 14,000 feet. Production averaged 1,567 Mcf/d and

## Edgar Filing: O'Neill Andrew J - Form 4

17 Bbl/d in December 2004 net to Magnum Hunter's interest. Net proved reserves for this field were 10.4 Bcfe as of December 31, 2004.

*Provident City.* Magnum Hunter owns varying working interests, between 2% and 100%, in 15 wells in this field located in Lavaca County, Texas. Five of the wells are Magnum Hunter operated. Production is primarily from the Wilcox formation at 8,500 feet to 17,500 feet. Production attributable to Magnum Hunter's interest averaged 1,747 Mcf/d and 9 Bbl/d in December 2004. As of December 31, 2004, the net proved reserves assigned to this field were 5.2 Bcfe.

*Alta Loma.* Magnum Hunter owns a 41% and a 48% working interest in two producing wells in this field. In addition, Magnum Hunter also owns and operates a salt water disposal well. This field is located in Galveston County, Texas and produces from the Frio formation at approximately 12,500 feet. Production attributable to Magnum Hunter's interest averaged 1,925 Mcf/d and 130 Bbl/d in December 2004. As of December 31, 2004, the net proved reserves assigned to this field were 6.5 Bcfe.

*Brazil.* Magnum Hunter owns varying working interests, between 30% and 50%, in eight producing wells in this field located in McMullen County, Texas. Six of the wells are Magnum Hunter operated. Production is primarily from the Wilcox formation at 9,000 feet to 13,000 feet. Production attributable to Magnum Hunter's interest averaged 8,505 Mcfd and 21 Bbl/d in December 2004. Magnum Hunter drilled and completed three new wells in this area in 2004 and is in the process of drilling a fourth. As of December 31, 2004, the net proved reserves assigned to this field were 7.5 Bcfe.

*Word, North.* Magnum Hunter owns varying working interests, between 4% and 100%, in 21 wells in this field located in Lavaca County, Texas. Eighteen of the wells are operated by Magnum Hunter. Production is from the Edwards formation at approximately 14,000 feet and averaged 1,121 Mcf/d and 17 Bbl/d in December 2004 net to Magnum Hunter's interest. Net proved reserves for this field were 9.5 Bcfe as of December 31, 2004.

### *Gulf of Mexico*

Magnum Hunter's initial entry into the Gulf of Mexico occurred March 27, 1998 when it acquired approximately 40% beneficial ownership interest in TEL Offshore Trust. One year later in May 1999, Magnum Hunter began participating as a working interest owner in new exploratory drilling on the shallow water shelf. Magnum Hunter currently owns an interest in 245 blocks in the Gulf of Mexico ranging from 12.5% to 100%. Proved reserves have been assigned in 55 blocks encompassing 85 gross wells (29.7 net wells). Magnum Hunter operates 16 of these wells (10.1 net wells). According to D&M, as of December 31, 2004, the Gulf of Mexico properties had proved reserves of 3.1 MMBbl of oil and 64.1 Bcf of natural gas (82.6 Bcfe). Approximately 78% of the estimated reserves are natural gas and the remaining 22% is oil. Total net daily production from the Gulf of Mexico properties for the month of December 2004 was 53.4 MMcf/d of natural gas and 2,121 Bbls/d of oil. At December 31, 2004, Magnum Hunter had nine additional discoveries that commenced production in 2005.

*Ship Shoal 358.* Magnum Hunter owns varying working interests, between 15% and 39.2%, in four wells operated by ATP Oil & Gas. Production is from Upper Pliocene sands at approximately eight to nine thousand feet. The wells are located in Federal waters south of Terrebonne Parish, Louisiana in a water depth of 420 feet. Production from the first well was initiated in March 2004. Subsequent wells were put on production as they were completed. Production from all the wells attributable to Magnum Hunter's interest averaged 3,397 Mcfd and 270 Bbls/d in December 2004. As of December 31, 2004, the net proved reserves for Ship Shoal 358 were 5.1 Bcfe.

*Vermilion 241.* Magnum Hunter's interest in Vermilion 241 consists of a 50% working interest in one well operated by Remington Oil & Gas. Production is from the Bul 1 Sand at approximately 11,000 feet. The field is located in 115 feet of water on Federal leases south of Vermilion Parish,

## Edgar Filing: O'Neill Andrew J - Form 4

Louisiana. First production was established in July 2004 and averaged 1,850 Mcfd and 56 Bbls/d in December 2004, net to Magnum Hunter's interests. The net proved reserves attributable to this well were 3.7 Bcfe as of December 31, 2004.

*West Cameron 458 Area.* This area encompasses West Cameron blocks 457 and 458. Magnum Hunter owns a 40% working interest in one subsea completion and four additional wells drilled from the platform located in Block 458. Remington Oil & Gas operates the field which is located in 117 feet of water on Federal leases south of Cameron Parish, Louisiana. The initial well started production in July 2004 with the last well coming on in October 2004. Production is from the Lentic 1 and Basal Nebraskan zones ranging in depths from 7,400 feet to 12,000 feet. Net to Magnum Hunter's interest, production averaged 7,227 Mcfd and 2 Bbls/d in December 2004. Net proved reserves for the West Cameron 458 Area were 3.8 Bcfe as of December 31, 2004.

*Main Pass 107.* Main Pass 107 is operated by Kerr McGee and is located on Federal leases in 52 feet of water east of Plaquemines Parish, Louisiana. Magnum Hunter's ownership consists of a 50% working interest in one well producing from the Tex W 1 at approximately 11,400 feet. The well also has numerous behind pipe recompletion opportunities in zones up to 9,800 feet. First production was established in January 2003. In December 2004, production for the well averaged 1,776 Mcfd and 114 Bbls/d net to Magnum Hunter's interest. As of December 31, 2004, the net proved reserves attributable to this well were 6.0 Bcfe.

*Eugene Island 302.* Magnum Hunter's interest in Eugene Island 302 consists of a 30% working interest in two producing wells and one shut in well operated by Remington Oil & Gas. Current production is from the Basal Nebraskan zone at approximately 9,000 to 10,000 feet. The field is located in 220 feet of water on Federal leases south of St. Mary Parish, Louisiana. Initial production was established in May 2002. Production attributable to Magnum Hunter's interest averaged 391 Mcfd and 329 Bbls/d in December 2004. Net proved reserves for this field were 3.2 Bcfe as of December 31, 2004.

*Main Pass 178 Area.* This area is comprised of Main Pass blocks 163, 164 and 178 and is located in Federal waters east of Plaquemines Parish, Louisiana in water depths of 124 feet to 150 feet. Magnum Hunter owns a 100% working interest and operates four existing wells from two platforms; and added an additional well and platform in 2003, in which it owns a 60% working interest. First production for the area was established in December 2001. These wells produce from various sands of Lower Pliocene to Middle Miocene age, at depths ranging from 4,800 feet to 12,000. A sidetrack well to the Main Pass 178 A-1 well is planned to be drilled in 2005. Magnum Hunter will retain a 60% interest in this well. Production to Magnum Hunter's interest averaged 975 Mcfd and 29 Bbls/d in December 2004. Net proved reserves for the Main Pass 178 Area were 7.9 Bcfe as of December 31, 2004.

*South Timbalier 265 Area.* This area encompasses South Timbalier blocks 250, 264 and 265 and is located in Federal waters south of Terrebonne Parish, Louisiana in water depths of 185 feet to 225 feet. Magnum Hunter operates eight producing wells and seven shut in wells from five platforms with interests ranging from 40% to 100%. Magnum Hunter initially acquired its interest in South Timbalier 265 through a like-kind property exchange with Kerr McGee in August 2000. Additional interests in the area were acquired from El Paso in March 2001. The wells produce from various sands ranging in depth from 4,800 feet to 16,000 feet. Magnum Hunter drilled the South Timbalier 250 A-3 well in 2004 which came on production in January 2005 at an average rate of 2,100 Mcfd net to Magnum Hunter's interest. Production for the area averaged 1,287 Mcfd and 124 Bbls/d in December 2004 prior to this well coming on line. As of December 31, 2004, the net proved reserves for the South Timbalier 265 Area were 7.5 Bcfe.

### ***Gas Processing Plants***

***McLean Plant.*** In January 1997, Magnum Hunter complemented its Panoma acquisition by purchasing a 50% ownership interest in the McLean Gas Plant and a related 22 mile products pipeline. This plant is a modern cryogenic plant utilizing approximately 2,000 horsepower of high speed compression and a gas processing capacity of approximately 23 MMcf/d. For the month of December 2004, throughput of the plant averaged 6.5 MMcf/d with processed liquids of 426 Bbl/d. The McLean Gas plant keeps 100% of the liquids recovered through the plant and pays the producer a value per Btu for the shrink and residue allocable to each producer's production less a gathering fee, plant and compression fuel and system loss.

***Madill Plant.*** In December 1999, Magnum Hunter acquired the Madill Gas Processing Plant and associated gathering system assets from Dynegy Midstream Services, Limited Partnership, a wholly-owned subsidiary of Dynegy Inc. The gas processing plant and associated facilities are located in Marshall and Bryan Counties, Oklahoma, and were acquired in conjunction with Magnum Hunter's 50% partner, Carrera Gas Gathering Co., L.L.C., of Tulsa, Oklahoma, who acquired the other 50% of the gas plant and associated assets. The acquisition includes over 130 miles of gas gathering pipelines. This modern cryogenic plant has 3,350 horsepower of high speed compression and has gas processing capacity of approximately 18 MMcf/d. For the month of December 2004, throughput of the plant averaged 7.9 MMcf/d of natural gas with processed liquids of 483 Bbl/d. The Madill Gas Plant processes natural gas under contracts that are primarily percent of proceeds, referred to as POP, based contracts. The contracts' percentages vary depending on volume and producer.

***Walker Creek Plant.*** In conjunction with the Vastar acquisition, Magnum Hunter acquired an approximate 59% ownership interest and became the operator of the Walker Creek Plant and associated gathering system. In 2000, Magnum Hunter sold a 44.2% interest in the Walker Creek Plant to Mallard Hunter L.P., of which Magnum Hunter is the general partner. This facility is located in southwest Arkansas in Lafayette and Columbia counties. This propane refrigeration plant utilizes 3,160 horsepower of leased compression and has a gas processing capacity of 12 Mmcf/d. For the month of December 2004, throughput of the plant net to Magnum Hunter's interest averaged 131 Mcf/d with processed liquids of 7 Bbl/d. The Walker Creek Plant is run for the sole benefit of the Walker Creek Unit. No third party production is delivered into the facility. All residue and NGL proceeds and plant costs are allocated to the Walker Creek Unit.

***Elmore City Processing Plant.*** Magnum Hunter acquired a 100% ownership interest in the Elmore City Plant in the Prize merger. This gas processing facility and associated gathering system assets are located in Garvin County, Oklahoma. These facilities include over 25 miles of gathering pipelines and an NGL extraction plant consisting of a cryogenic unit and approximately 7,000 horsepower of various types of compressors. The plant's 2004 throughput averaged 10.4 MMcf/d with a total throughput capacity of approximately 35 MMcf/d. For the month of December 2004, throughput of the plant averaged 9.8 MMcf/d with processed liquids of 845 Bbl/d. The Elmore City Plant processes natural gas under contracts that are solely POP contracts. The plant receives on average approximately 20% of the residue and 40% to 45% of the recovered liquids attributable to a producer's gas delivered into the system.

### **Oil and Gas Reserves**

#### ***General***

All information set forth in this joint proxy statement/prospectus regarding estimated proved reserves and related estimated future net cash flows for Magnum Hunter's oil and gas interests is taken from reports prepared by DeGolyer and MacNaughton of Dallas, Texas and Cawley Gillespie & Associates, Inc. of Fort Worth, Texas, both independent petroleum engineers with respect to Magnum

## Edgar Filing: O'Neill Andrew J - Form 4

Hunter's interests at December 31, 2004, December 31, 2003 and December 31, 2002 (using oil and gas prices in effect on each respective date).

The estimates of these independent petroleum engineers were based upon their review of production histories and other geological, economic, ownership and engineering data Magnum Hunter provided. Magnum Hunter bears complete responsibility and liability for its reserve estimates.

Net cash flows is defined as net revenues, after deducting production and ad valorem taxes, future capital costs and operating expenses, but before deducting federal income taxes. Estimates have been made using constant oil and gas prices and operating costs, at December 31, 2004, or as otherwise indicated.

The estimates of future net cash flows from proved reserves are made using oil and gas sales prices in effect as of the dates of such estimates and are held constant throughout the life of the properties. Magnum Hunter's estimates of proved reserves and future net cash flows were estimated using the following weighted average prices, before deduction of production taxes:

	Prices Used in Reserve Reports at December 31,		
	2004	2003	2002
Gas (per Mcf)	\$ 5.66	\$ 5.24	\$ 4.23
Oil (per Bbl)	\$ 41.66	\$ 31.33	\$ 29.99
NGL	\$ 29.93	\$ 22.96	\$ 17.80

All reserves are evaluated at contract temperature and pressure which can affect the measurement of gas reserves. Operating costs, development costs and certain production related and ad valorem taxes were deducted in arriving at the estimated future net cash flows. No provision was made for income taxes. The estimates following this section set forth reserves considered to be economically recoverable under normal operating methods and existing conditions at the prices and operating costs prevailing at the dates indicated above.

Proved reserves are estimates of oil and gas to be recovered in the future. Reservoir engineering is a subjective process of estimating the sizes of underground accumulations of oil and gas that cannot be measured in an exact way. The accuracy of any reserve estimates is a function of the quality of available data and of engineering and geological interpretation and judgment. Reserve reports of other engineers might differ from the reports contained herein. Results of drilling, testing, and production subsequent to the date of the estimate may justify revision of such estimate. Future prices received for the sale of oil and gas will likely be different from those used in preparing these reports. The amounts and timing of future operating and development costs may also differ from those used. Accordingly, reserve estimates are often different from the quantities of oil and gas that are ultimately recovered.

Except for the effect of changes in oil and gas prices, no major discovery or other favorable or adverse event is believed to have caused a significant change in these estimates of Magnum Hunter's proved reserves since December 31, 2004. No estimates of proved reserves of oil and gas have been filed by Magnum Hunter with, or included in any report to, any United States authority or agency (other than the Securities and Exchange Commission) since January 1, 2001.

### *Magnum Hunter Reserves*

The following tables set forth Magnum Hunter's estimated proved reserves of oil and gas on an actual basis at December 31, 2004, 2003 and 2002. These proved reserves were determined in accordance with Regulation S-X, Rule 4-10(a) (2) (3) (4), which are the only applicable definitions of proved oil and gas reserves.

## Estimated Proved Oil and Natural Gas Reserves(a)

	At December 31,		
	2004	2003	2002
<b>Net gas reserves (Mcf):</b>			
Proved developed	442,630,521	368,530,450	362,325,297
Proved undeveloped	167,487,550	125,522,024	96,318,346
<b>Total proved gas reserves</b>	<b>610,118,071</b>	<b>494,052,474</b>	<b>458,643,643</b>
<b>Net oil reserves (Bbl):</b> (including condensate)			
Proved developed	42,441,787	38,260,657	40,786,302
Proved undeveloped	17,302,268	13,920,319	13,885,296
<b>Total proved oil reserves</b>	<b>59,744,055</b>	<b>52,180,976</b>	<b>54,671,598</b>
<b>Net NGL reserves (Bbl)</b> (including condensate)			
Proved developed	5,566,810	4,728,119	7,726,147
Proved undeveloped	770,280	488,364	684,241
<b>Total proved NGL reserves</b>	<b>6,337,090</b>	<b>5,216,483</b>	<b>8,410,388</b>
<b>Total Proved Reserves (Mcf)</b>	<b>1,006,604,941</b>	<b>838,437,228</b>	<b>837,135,559</b>

(a) Based upon reserve reports at December 31, 2004, 2003 and 2002 prepared by D&M and Cawley Gillespie.

The following tables set forth the estimated proved reserves of oil and gas included in the previous tables which are claimed exclusively through Magnum Hunter's gas plant ownership.

**Estimated Proved Oil and Natural Gas Reserves(a)  
(Through Gas Plant Ownership)**

	At December 31,		
	2004	2003	2002
<b>Net gas reserves (Mcf):</b>			
Proved developed	9,418,512	9,162,200	8,030,900
Proved undeveloped	350,349	351,100	328,400
<b>Total proved gas reserves</b>	<b>9,768,861</b>	<b>9,513,300</b>	<b>8,359,300</b>
<b>Net oil reserves (Bbl):</b> (including condensate)			
Proved developed	126,598	166,800	121,600
Proved undeveloped	9,298	30,400	5,600
<b>Total proved oil reserves</b>	<b>135,896</b>	<b>197,200</b>	<b>127,200</b>
<b>Net NGL reserves (Bbl)</b> (including condensate)			
Proved developed	4,398,390	3,637,100	4,179,700
Proved undeveloped	550,016	452,600	349,100
<b>Total proved NGL reserves</b>	<b>4,948,406</b>	<b>4,089,700</b>	<b>4,528,800</b>
<b>Total Proved Reserves (Mcf)</b>	<b>40,274,673</b>	<b>35,234,700</b>	<b>36,295,300</b>

(a)

Based upon reserve reports at December 31, 2004, 2003 and 2002 prepared by D&M.

**Significant Properties**

On December 31, 2004, 100% of Magnum Hunter's proved reserves on a Bcfe basis were located in the Mid-Continent region, the Permian Basin, the Gulf Coast region and the Gulf of Mexico. On such date, Magnum Hunter's properties included working interests in 5,455 gross (3,641 net) productive oil and gas wells.

The following table sets forth summary information with respect to Magnum Hunter's estimated proved reserves of oil and gas at December 31, 2004.

	Proved Reserves			
	Oil (Bbl)	Gas (Mcf)	NGL (Bbl)	Natural Gas Equivalent (Mcf)
Mid-Continent region(a)	5,793,128	182,819,743	6,337,090	255,601,051
Permian Basin-New Mexico region(a)	8,247,951	184,159,914		233,647,620
Permian Basin-Texas region	40,630,590	115,364,687		359,148,227
Gulf Coast region(a)	1,984,696	63,696,822		75,604,998
Gulf of Mexico(a)	3,087,690	64,076,905		82,603,045

Explanation of Responses:

Edgar Filing: O'Neill Andrew J - Form 4

Proved Reserves

---

Total	59,744,055	610,118,071	6,337,090	1,006,604,941
-------	------------	-------------	-----------	---------------

---

(a)

Based on reserve reports at December 31, 2004 prepared by D&M and Cawley Gillespie.

IV-41

---

**Oil and Gas Production, Prices and Costs**

The following table shows the approximate net production attributable to Magnum Hunters' oil and gas interests, the average sales price and the average production expense attributable to Magnum Hunter's oil and gas production for the periods indicated. Production and sales information relating to properties acquired or disposed of is reflected in this table only since or up to the closing date of their respective acquisition or sale and may affect the comparability of the data between the periods presented.

	Year Ended December 31,		
	2004	2003	2002
<b>Oil and gas production:</b>			
Oil (Mbbbl)	4,080	3,893	3,875
Gas (MMcf)	55,961	49,695	47,683
Natural Gas Equivalent (MMcfe)	80,442	73,052	70,933
<b>Average sales price(a):</b>			
<b>Before Hedge Contracts:</b>			
Oil (per Bbl)	\$ 39.62	\$ 29.62	\$ 25.18
Gas (per Mcf)	5.82	4.89	3.07
Natural Gas Equivalents (per Mcfe)	6.06	4.91	3.45
<b>After Hedge Contracts:</b>			
Oil (per Bbl)	\$ 34.27	\$ 26.42	\$ 24.04
Gas (per Mcf)	5.41	3.66	3.10
Natural Gas Equivalent (per Mcfe)	5.50	3.90	3.40
Oil and gas production lifting costs (per Mcfe)	\$ 0.76	\$ 0.77	\$ 0.72
Production taxes and other costs (per Mcfe)(b)	\$ 0.54	\$ 0.45	\$ 0.40

(a) Before deduction of production taxes and net of hedging results.

(b) Includes ad valorem taxes, insurance, bonds, company overhead and net profits interest.

**Drilling Activity**

The following table sets forth the results of Magnum Hunter's drilling activities during the three fiscal years ended December 31, 2004, 2003 and 2002.

Year	Type of Well	Gross Wells(a)			Net Wells(b)		
		Total	Producing(c)	Dry(d)	Total	Producing(c)	Dry(d)
2004	Exploratory						
	Texas	2	2	0	0.21	0.21	0
	Oklahoma	1	1	0	0.04	0.04	0
	New Mexico	1	1	0	0.23	0.23	0
	Offshore Gulf of Mexico	32	26	6	12.10	9.86	2.24
	Development						
	Texas	89	89	0	35.19	35.19	0
	Oklahoma	9	7	2	1.21	0.97	0.24
	New Mexico	34	34	0	16.09	16.09	0
	Offshore Gulf of Mexico	7	7	0	2.35	2.35	0
2003	Exploratory						
	Texas	2	1	1	0.6	0.33	0.27
	Oklahoma	0	0	0	0	0	0
	New Mexico	2	2	0	0.35	0.35	0
	Offshore Gulf of Mexico	21	14	7	8.86	6.51	2.35
	Development						
	Texas	64	63	1	27.29	26.41	0.88
	Oklahoma	4	4	0	0.35	0.35	0
	New Mexico	25	25	0	12.62	12.62	0
	Offshore Gulf of Mexico	6	6	0	1.03	1.03	0
2002	Exploratory						
	Texas	2	1	1	1.3	1	0.3
	Oklahoma	0	0	0	0	0	0
	New Mexico	6	6	0	2.05	2.05	0
	Offshore Gulf of Mexico and Other	21	16	5	6.24	4.82	1.42
	Development						
	Texas	62	61	1	23.01	22.01	1
	Oklahoma	3	2	1	0.26	0.13	0.13
	New Mexico	16	16	0	5.20	5.20	0
	Offshore Gulf of Mexico and Other	14	14	0	2.8	2.8	0

- (a) The number of gross wells is the total number of wells in which a working interest is owned.
- (b) The number of net wells is the sum of fractional working interests owned in gross wells expressed as whole numbers and fractions thereof.
- (c) A producing well is an exploratory or development well found to be capable of producing either oil or gas in sufficient quantities to justify completion as an oil or gas well.
- (d) A dry well is an exploratory or development well that is not a producing well.

**Oil and Gas Wells**

The following table sets forth the number of oil and natural gas wells in which Magnum Hunter had a working interest at December 31, 2004. All of these wells are located in the United States.

Location	Productive Wells As of December 31, 2004					
	Gross(a)			Net(b)		
	Oil	Gas	Total	Oil	Gas	Total
Texas	2,295	1,228	3,523	1,644.85	867.24	2,512.09
New Mexico	421	629	1,050	292.73	378.84	671.57
Oklahoma	196	484	680	151.39	247.82	399.21
Louisiana	8	8	16	4.96	4.51	9.47
Arkansas	59	1	60	2.80	0.00	2.80
Offshore Gulf of Mexico	9	102	111	1.13	39.83	40.96
Other	1	14	15	0.06	4.87	4.93
<b>Total</b>	<b>2,989</b>	<b>2,466</b>	<b>5,455</b>	<b>2,097.92</b>	<b>1,543.11</b>	<b>3,641.03</b>

- (a) The number of gross wells is the total number of wells in which a working interest is owned. Well counts include wells with multiple completions. Fluid injection wells for waterflood and other enhanced recovery projects are not included as gross wells.
- (b) The number of net wells is the sum of fractional working interests owned in gross wells expressed as whole numbers and fractions thereof.

**Oil and Gas Acreage**

The following table summarizes Magnum Hunter's developed and undeveloped leasehold acreage at December 31, 2004:

	Developed		Undeveloped	
	Gross(a)	Net(b)	Gross(a)	Net(b)
Arizona			920,217	920,217
Kansas	10,377	6,873	480	480
Louisiana	472	283		
New Mexico	190,108	77,429	1,698,877	1,635,409
Oklahoma	168,149	105,098	22,042	12,873
Texas	351,694	200,588	136,585	85,897
Utah	8,063	8,063	87,106	87,106
Wyoming	25,775	25,555	2,720	2,720
Offshore Gulf of Mexico	292,903	111,368	829,877	491,375
Other	8,087	3,045	6,772	4,178
<b>Total</b>	<b>1,055,628</b>	<b>538,302</b>	<b>3,704,676</b>	<b>3,240,255</b>

- (a) The number of gross acres is the total number of acres in which a working interest is owned.

## Edgar Filing: O'Neill Andrew J - Form 4

- (b) The number of net acres is the sum of fractional working interests owned in gross acres expressed as whole numbers and fractions thereof.

Substantially all of Magnum Hunter's interests are leasehold working interests or overriding royalty interests (as opposed to mineral or fee interests) under standard onshore oil and gas leases. As is customary in the industry, Magnum Hunter generally acquire oil and gas acreage without any warranty of title except as to claims made by, through or under the transferor. Although Magnum Hunter has

IV-44

---

title examined by a landman or title attorney prior to acquisition of mineral acreage in those cases in which the economic significance of the acreage justifies the cost, there can be no assurance that losses will not result from title defects or from defects in the assignment of leasehold rights. In certain instances, title opinions may not be obtained if, in Magnum Hunter's judgment, it would be uneconomical or impractical to do so. Magnum Hunter anticipates no material expirations on any of its leased acreage over the next three years.

## **Development and Exploration Activities**

### *Overview*

Magnum Hunter seeks to minimize its overhead and capital expenditures by subcontracting the drilling, re-drilling and workover of wells to independent drilling contractors and by outsourcing other services. Magnum Hunter typically compensates its drilling subcontractors on a turnkey (fixed price), footage or day-rate basis depending on its assessment of risk and cost considerations on each individual project.

### *Development Drilling*

Magnum Hunter's development strategy focuses on maximizing the value and productivity of its oil and gas asset base through development drilling and enhanced recovery projects. Magnum Hunter has budgeted approximately \$96.8 million for exploitation and development activities for 2005 with \$67.4 million of such budget allocated to its proved undeveloped reserves. Magnum Hunter has identified 976 development drilling locations and workover opportunities on its properties to which proved reserves have been attributed. In exploiting its producing properties, Magnum Hunter relies upon its in-house technical staff of petroleum engineering and geological professionals and utilize the services of outside consultants on a selective basis.

*Mid-Continent Region.* A total of 194 development drilling locations and workover opportunities have been identified in the Mid-Continent Region. Increased density drilling will continue to enhance the value of the Panoma Prospect. Approximately 92 drilling locations have been identified as proven, many of which were reclassified as proven in late 2003 when Magnum Hunter received regulatory approval to reclassify its westernmost Panoma acreage. Spacing for those units was changed from 640 acres to 160 acres per well.

Additional Mid-Continent development opportunities center around recompletion opportunities in the Eola-Robberson, North Madill, Cumberland and Walnut Bend Fields. All of these fields are large, multi-pay fields with a large well count. Approximately 116 recompletion opportunities have been identified in those four fields.

*Permian Basin Properties.* Magnum Hunter has maintained a continuous two-rig drilling program in Southeast New Mexico for over two years. A third operated rig was added in September of 2004 with the closing of the Encana acquisition. Target reservoirs are Morrow, Atoka and Strawn at depths down to 13,000 feet. The majority of the wells drilled have been increased density wells. Primary fields drilled in 2004 and scheduled for 2005 are White City and South Carlsbad in Eddy County and the Quail Ridge in Lea County. A total of 23 operated wells are budgeted for 2005. Magnum Hunter's working interest ranges from 24% to 100%, with an average in the 70% range. Most of the drilling through February 2005 has been on acreage acquired in the Burlington, Mallon and Encana acquisitions. Magnum Hunter recently entered into two separate agreements with ConocoPhillips which allows Magnum Hunter to participate in wells drilled on ConocoPhillips acreage in the High Lonesome area. Additional similar farmouts are in the various stages with other large producers in the general area.

Additional development drilling in the Permian Basin centers around increased density drilling in the Westbrook Field in Mitchell County, Texas, where Magnum Hunter drilled 11 wells in 2004. Over 100 Spraberry and Canyon locations were identified with the NG Tex acquisition that was closed in 2004. Several well sidetrack recompletions are planned for the Brunson Ranch Field in Loving County, Texas with one budgeted for 2005. Also numerous proven undeveloped locations have been identified in Lea County, New Mexico targeting the shallow intervals down to approximately 3,000 feet.

### **Exploratory Drilling**

Magnum Hunter spent \$52.7 million of its \$540 million 2004 capital expenditures on exploratory drilling and related land and geophysical costs. Thirty-two offshore exploratory wells were drilled in 2004, of which 26 were completed as producing wells providing Magnum Hunter with a 81% success rate. Magnum Hunter entered the Gulf of Mexico as a working interest owner in new exploratory drilling on the shallow water shelf in May 1999. This program has yielded 82 completions in 104 attempts by the end of 2004, and as the proved reserves associated with these new wells are developed, they have been adding significant cash flow. Production from Magnum Hunter's producing blocks was approximately 66.1 MMcfe/d net to Magnum Hunter as of December 2004. Nine new wells scheduled to commence production in the first half of 2005 should add to these levels. Magnum Hunter currently owns an interest ranging from 12.5% to 100% in 245 offshore blocks and expect to add to the number of OCS blocks in 2005. An aggressive drilling program will continue in 2005.

The onshore exploration program remains active. One of the Morrow tests drilled in New Mexico was a true exploratory test in which Magnum Hunter held a 100% working interest. The well found gas in the Morrow, as well as from the Strawn zone. Magnum Hunter participated in additional exploration in West Texas on successful projects with Oxy Oil and Gas and EOG Resources.

### **Gathering and Processing of Gas**

Hunter Gas Gathering, Inc., a wholly-owned subsidiary of Magnum Hunter, owns five gas gathering systems located in Oklahoma, New Mexico, Texas and Arkansas, none of which are subject to regulation by the Federal Energy Regulatory Commission, referred to as FERC, and has ownership interests in four gas processing plants. Gruy operates all of the gas gathering systems and two of the gas processing plants.

Generally, the gathering systems transport the natural gas from wells to a common point where it is dehydrated prior to redelivery to downstream pipelines. In managing its gas gathering systems, Magnum Hunter has emphasized operating efficiency and overhead management and introduced a program in certain areas which ties throughput costs to volume transported rather than to compression capacity. Magnum Hunter believes that its focus on volume-based pricing reduces the potential financial impact of a decline in actual throughput. Since most of the compression costs are not fixed, but are tied to volumes transported, the compression operator has an incentive to ensure compression is appropriately sized to gain compression efficiency and to minimize compressor downtime so that as much volume is being transported as possible. The lower the volume transported, the lower the fee to the compression operator, and in some situations, the compression operator incurs a penalty.

The Panoma system, the largest of Magnum Hunter's gas gathering systems, consists of approximately 455 miles of pipeline. The main trunk lines run east to west for approximately 66 miles with the east end starting in Beckham County, Oklahoma and the west end starting in Gray County, Texas. For the year ending December 31, 2004, gas throughput for the Panoma gas gathering system averaged 15.2 MMcf/d. The Panoma gas gathering system is connected to a third party header system which provides access to multiple major interstate and intrastate pipelines in the area serving Midwestern, Western and Oklahoma markets. Magnum Hunter operates approximately 523 of the

approximately 610 wells connected to the Panama system, and is actively seeking to add new wells to this system through acquisition, development or arrangements with third party producers.

Effective January 1997, Magnum Hunter purchased a 50% ownership interest in the McLean Gas Plant, a gas processing facility located adjacent to its Panama gas gathering system. The purchase also included a 22 mile products pipeline between the McLean Gas Plant and the Koch Pipeline at Lefors, Texas and all gas and product purchase and sales agreements related to the plant. The McLean Gas Plant is a modern cryogenic gas processing plant with a throughput capacity of 23.0 MMcf/d. For the year ending December 31, 2004, throughput net to Hunter Gas Gathering, was approximately 7.01 MMcf/d with processed liquids of 468 Bbl/d. Magnum Hunter acquired its 50% ownership interest in the plant from Carrera Gas Company, L.L.C., referred to as Carrera, of Tulsa, Oklahoma, which owns the remaining 50% of the plant and is plant operator.

Magnum Hunter acquired a 100% ownership interest in the Elmore City Plant in the Prize merger. This gas processing facility and associated gathering system assets are located in Garvin County, Oklahoma. The facilities include over 25 miles of gathering pipelines and an NGL extraction plant consisting of a cryogenic unit and approximately 7,000 horsepower of various types of compression. For the year ending December 31, 2004, the plant's 2004 throughput averaged 10.4 MMcf/d with 942 Bbls/d of processed liquids. The plant has a total throughput capacity of approximately 35 MMcf/d.

In December 1999, Magnum Hunter acquired the Madill Gas Processing Plant and associated gathering system assets from Dynege Midstream Services, Limited Partnership, a wholly-owned subsidiary of Dynege Inc. The gas processing plant and associated facilities are located in Marshall and Bryan Counties, Oklahoma and were acquired in conjunction with its 50% partner, Carrera. The acquisition includes over 130 miles of gas gathering pipelines. This modern cryogenic plant has 3,350 horsepower of high-speed compression and has gas processing capacity of approximately 18 MMcf/d. For the year ending December 31, 2004, throughput of the plant, net to Hunter Gas Gathering, averaged 8.03 MMcf/d of natural gas with processed liquids of 493 Bbls/d.

In conjunction with the Vastar acquisition, Magnum Hunter acquired approximately 59% ownership interest and became the operator of the Walker Creek Plant and associated gathering system. In 2000, Magnum Hunter sold a 44.2% interest in the Walker Creek Plant to Mallard Hunter L.P., of which Magnum Hunter is the general partner. This facility is located in southwest Arkansas in Lafayette and Columbia counties. This propane refrigeration plant utilizes 3,160 horsepower leased compression and has a gas processing capacity of 12 MMcf/d. The Walker Creek Plant is run for the sole benefit of the Walker Creek Unit. There is not any third party production delivering into the facility nor is the facility set up as a separate business unit. All residue and NGL proceeds and plant costs are allocated to the Walker Creek Unit. For the year ending December 31, 2004, throughput of the plant, net to Magnum Hunter's interest, averaged 0.157 MMcf/d with processed liquids of 8 Bbls/d.

In the second half of 2004, Hunter Gas Gathering began construction of the White City Gathering System, located 5 miles southeast of the White City Penn Field in Eddy County New Mexico. The system will initially service a 12-section area under development by Magnum Hunter's production company, Magnum Hunter Production, Inc. in an area previously lacking any pipeline infrastructure for getting gas to markets. This system was put into service in October 2004 and development of this area is progressing with three wells connected and flowing and others in stages of drilling or completion. There are 32 potential locations identified for service by the White City System. There is no processing expected in this area due to the dry nature of the gas. The system is currently connected to one downstream gatherer with the potential for two interconnects to move gas into the interstate markets. For the month of December 2004, throughput on the system was 1.9 MMcf/d.

The Baker Gas Gathering System was constructed and put into service in August 2004. Hunter Gas Gathering is the operator of the system and owns a 50% interest with Rutherford Oil Corporation owning the remaining interest. It consists of approximately 19,500 feet of 8" pipeline located in

McMullen County, Texas and provides an outlet for multiple wells to Houston Pipe Line's 16" line to the South. Initial production from each well is estimated in the range of 8-15 MMcf/d with 3 wells connected and flowing. For the month of December 2004, throughput on the system, net to Hunter Gas Gathering, averaged 3.3 MMcf/d.

### **Marketing of Production**

Magnum Hunter markets all of its gas production as well as gas it purchases from third parties to gas marketing firms or end-users either on (i) the spot market under contracts of less than one year at prevailing spot market prices (approximately 75% of Magnum Hunter's volume) or (ii) at market responsive prices under multi-year contracts (approximately 25% of Magnum Hunter's volume). Marketing gas for Magnum Hunter's own account exposes it to the attendant commodities risk which Magnum Hunter attempts to mitigate through various financial hedges. Magnum Hunter normally sells its own oil under month-to-month contracts with a variety of crude oil purchasers. Oil is usually sold for Magnum Hunter's own account through the services of Enmark Services, a marketing agent in Dallas, Texas. While Magnum Hunter has historically been able to sell oil above posted prices, it is also exposed to the commodities risk inherent in short-term contracts which it attempts to mitigate through various financial hedges. For a discussion of Magnum Hunter's hedging activities, see "Chapter IV Magnum Hunter Business and Financial Information Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Hedging Activity" and Note 12 to Magnum Hunter's consolidated financial statements included elsewhere in this joint proxy statement/prospectus.

The market for oil and natural gas Magnum Hunter produces depends on factors beyond its control, including the extent of domestic production and imports of oil and natural gas, the proximity and capacity of natural gas pipelines and other transportation facilities, weather, demand for oil and natural gas, the marketing of competitive fuels and the effects of state and federal regulation. The oil and natural gas industry also competes with other industries in supplying the energy and fuel requirements of industrial, commercial and individual consumers.

### **Petroleum Management and Consulting Services**

Magnum Hunter acquired Gruy in December 1995. Gruy, which conducts operations for both Magnum Hunter and third parties, has managed properties for nearly half a century for financial institutions, bankruptcy trustees, estates, individual investors, trusts and independent oil and gas companies. Gruy provides drilling, completion and other well-site services; advice regarding environmental and other regulatory compliance; receipt and disbursement functions, expert witness testimony and other managerial services and petroleum engineering services. Gruy manages, operates and provides consulting services on oil and gas properties, gathering systems and processing plants located in Texas, Oklahoma, Mississippi, Louisiana, New Mexico and Kansas. Gruy is an important component of Magnum Hunter's acquisition program. As the operator of wells for third parties and as a provider of consulting services for the energy industry, Gruy is often uniquely able to identify attractive acquisition opportunities.

Magnum Hunter acquired an 80% controlling interest in Metrix Networks, Inc., referred to as Metrix, in December 2003. Metrix provides equipment and monitoring services to companies in the energy industry.

For additional information on Magnum Hunter's business segments, see Note 15 to Magnum Hunter's consolidated financial statements, included elsewhere in this joint proxy statement/prospectus.

## **Competition**

The oil and gas industry is highly competitive. Magnum Hunter's competitors include major oil companies, other independent oil and gas concerns, and individual producers and operators, many of which have substantially greater financial resources and larger staffs and facilities than those of Magnum Hunter. In addition, Magnum Hunter frequently encounters competition in the acquisition of oil and gas properties, gas gathering systems, gas processing plants and in Magnum Hunter's management and consulting business. The principal means of such competition are the amount and terms of the consideration offered. The principal means of such competition with respect to the sale of oil and gas production are product availability and price. The price at which Magnum Hunter's products may be sold will continue to be affected by a number of factors, including the price of alternate fuels such as oil, natural gas, nuclear power, hydroelectric power and coal, and competition among various gas producers and marketers.

## **Regulations**

### *General Federal and State Regulations*

There have been, and continue to be, numerous federal and state laws and regulations governing the oil and gas industry that are often changed in response to the current political or economic environment. Compliance with this regulatory burden is often difficult and costly and may carry substantial penalties for noncompliance. The following are some specific regulations that may affect Magnum Hunter. Magnum Hunter cannot predict the impact of these or future legislative or regulatory initiatives.

### *Regulation of Natural Gas and Oil Exploration and Production*

Magnum Hunter's operations are subject to various types of regulation at the federal, state and local levels. Such regulation includes requiring permits for drilling wells, maintaining bonding requirements in order to drill or operate wells and regulating the location of wells, the method of drilling and casing wells, the surface use and restoration of properties upon which wells are drilled, the plugging and abandoning of wells and the disposal of fluids used in connection with operations. Magnum Hunter's operations are also subject to various conservation laws and regulations. These include the regulation of the size of drilling and spacing units or proration units and the density of wells which may be drilled in and the unitization or pooling of oil and gas properties. In addition, state conservation laws establish maximum rates of production from oil and gas wells, generally prohibit the venting or flaring of gas and impose certain requirements regarding the ratable production. The effect of these regulations may limit the amount of oil and gas Magnum Hunter can produce from its wells and may limit the number of wells or the locations at which Magnum Hunter can drill. The regulatory burden on the oil and gas industry increases Magnum Hunter's cost of doing business and, consequently, affects its profitability. In as much as such laws and regulations are frequently expanded, amended and reinterpreted, Magnum Hunter is unable to predict the future cost or impact of complying with such regulations.

### *Federal Regulation of Sales Prices and Transportation*

Currently, there are no federal, state or local laws that regulate the price for sales of Magnum Hunter's natural gas, NGLs, crude oil or condensate. However, the rates charged and terms and conditions for the movement of gas in interstate commerce through certain intrastate pipelines and production area hubs are subject to regulation under the Natural Gas Policy Act of 1978, referred to as NGPA. Pipeline and hub construction activities are, to a limited extent, also subject to regulations under the Natural Gas Act of 1938, referred to as NGA. While these controls do not apply directly to Magnum Hunter, their effect on natural gas markets can be significant in terms of competition and cost

of transportation services. Additional proposals and proceedings that might affect the natural gas industry are considered from time to time by Congress, FERC, state regulatory bodies and the courts. Magnum Hunter cannot predict when or if any such proposals might become effective and their effect, if any, on Magnum Hunter's operations. Historically, the natural gas industry has been heavily regulated; therefore, there is no assurance that the less stringent regulatory approach recently pursued by FERC, Congress and the states will continue indefinitely into the future.

### *Gathering Regulations*

State regulation of gathering facilities generally includes various safety, environmental and, in some circumstances, nondiscriminatory take requirements. Such regulation has not generally been applied against gatherers of natural gas, although natural gas gathering may receive greater regulatory scrutiny in the future. Magnum Hunter's operations on federal, state or Indian oil and gas leases are subject to numerous restrictions, including nondiscrimination statutes. Such operations must be conducted pursuant to certain on-site security regulations and other permits and authorizations issued by the Bureau of Land Management, Minerals Management Service and other agencies.

### *Environmental Regulation*

Magnum Hunter's exploration, development, and production of oil and gas, including its operation of saltwater injection and disposal wells, are subject to various federal, state and local environmental laws and regulations. Such laws and regulations can increase the costs of planning, designing, installing and operating oil and gas wells. Magnum Hunter's domestic activities are subject to a variety of environmental laws and regulations, including but not limited to, the Oil Pollution Act of 1990, referred to as OPA, the Clean Water Act, referred to as CWA, the Comprehensive Environmental Response, Compensation and Liability Act, referred to as CERCLA, the Resource Conservation and Recovery Act, referred to as RCRA, the Clean Air Act, referred to as CAA, and the Safe Drinking Water Act, referred to as SDWA, as well as state regulations promulgated under comparable state statutes. Magnum Hunter is also subject to regulations governing the handling, transportation, storage, and disposal of naturally occurring radioactive materials that are found in its oil and gas operations. Civil and criminal fines and penalties may be imposed for non-compliance with these environmental laws and regulations. Additionally, these laws and regulations require the acquisition of permits or other governmental authorizations before undertaking certain activities, limit or prohibit other activities because of protected areas or species, and impose substantial liabilities for cleanup of pollution.

Under the OPA, a release of oil into water or other areas designated by the statute could result in Magnum Hunter being held responsible for the costs of remediating such a release, certain OPA specified damages, and natural resource damages. The extent of that liability could be extensive, as set forth in the statute, depending on the nature of the release. A release of oil in harmful quantities or other materials into water or other specified areas could also result in Magnum Hunter being held responsible under the CWA for the costs of remediation, and civil and criminal fines and penalties.

CERCLA and comparable state statutes, also known as "Superfund" laws, can impose joint and several and retroactive liability, without regard to fault or the legality of the original conduct, on certain classes of persons for the release of a "hazardous substance" into the environment. In practice, cleanup costs are usually allocated among various responsible parties. Potentially liable parties include site owners or operators, past owners or operators under certain conditions, and entities that arrange for the disposal or treatment of, or transport hazardous substances found at the site. Although CERCLA, as amended, currently exempts petroleum, including but not limited to, crude oil, gas and natural gas liquids from the definition of hazardous substance, Magnum Hunter's operations may involve the use or handling of other materials that may be classified as hazardous substances under CERCLA. Furthermore, there can be no assurance that the exemption will be preserved in future amendments of the act, if any.

RCRA and comparable state and local requirements impose standards for the management, including treatment, storage, and disposal of both hazardous and nonhazardous solid wastes. Magnum Hunter generates hazardous and nonhazardous solid waste in connection with its routine operations. From time to time, proposals have been made that would reclassify certain oil and gas wastes, including wastes generated during drilling, production and pipeline operations, as "hazardous wastes" under RCRA which would make such solid wastes subject to much more stringent handling, transportation, storage, disposal, and clean-up requirements. This development could have a significant impact on Magnum Hunter's operating costs. While state laws vary on this issue, state initiatives to further regulate oil and gas wastes could have a similar impact.

Because oil and gas exploration and production, and possibly other activities, have been conducted at some of Magnum Hunter's properties by previous owners and operators, materials from these operations remain on some of the properties and in some instances require remediation. In addition, in certain instances Magnum Hunter has agreed to indemnify sellers of producing properties from which it has acquired reserves against certain liabilities for environmental claims associated with such properties. While Magnum Hunter does not believe that costs to be incurred by it for compliance and remediating previously or currently owned or operated properties will be material, there can be no guarantee that such costs will not result in material expenditures.

Additionally, in the course of Magnum Hunter's routine oil and gas operations, surface spills and leaks, including casing leaks, of oil or other materials occur, and Magnum Hunter incurs costs for waste handling and environmental compliance. Moreover, Magnum Hunter is able to control directly the operations of only those wells for which it acts as the operator. Management believes that Magnum Hunter is in substantial compliance with applicable environmental laws and regulations.

It is not anticipated that Magnum Hunter will be required in the near future to expend amounts that are material in relation to its total capital expenditures program by reason of environmental laws and regulations, but inasmuch as such laws and regulations are frequently changed, Magnum Hunter is unable to predict the ultimate cost of compliance. There can be no assurance that more stringent laws and regulations protecting the environment will not be adopted or that Magnum Hunter will not otherwise incur material expenses in connection with environmental laws and regulations in the future.

#### **Employees**

At December 31, 2004, Magnum Hunter had 262 full-time employees of which 62 were management, 118 were administrative and 82 were field personnel. None of Magnum Hunter's employees are represented by a union. Management considers Magnum Hunter's relations with employees to be very good.

#### **Facilities**

Magnum Hunter occupies approximately 23,386 square feet of office space at 600 East Las Colinas Boulevard, Suite 1100, Irving, Texas, under a lease that expires in November 2005. Magnum Hunter also occupies approximately 19,635 square feet of office space in Grapevine, Texas, under a lease that expires in December 2005. Magnum Hunter own field offices and production yards in Shamrock, Gainesville and Victoria, Texas; Cumberland and Madill, Oklahoma; Carlsbad, New Mexico; and Taylor, Arkansas. Magnum Hunter also leases field production offices in Midland, Kermit and Abilene, Texas; Artesia and Eunice, New Mexico; and Oklahoma City and Woodward, Oklahoma.

#### **Legal Proceedings**

Except as otherwise described in "Chapter I The Merger The Merger Legal Proceedings Related to the Merger," no legal proceedings are pending other than ordinary routine litigation incidental to Magnum Hunter's business, the outcome of which management believes will not have a material adverse effect on Magnum Hunter.

## MANAGEMENT

**Directors of Magnum Hunter**

The following table sets forth the directors of Magnum Hunter and their ages. Magnum Hunter's Bylaws divide the Board of Directors into three (3) classes of directors serving staggered three-year terms, with one class to be elected at each annual meeting. Assuming that the stockholders of Cimarex approve the proposal to amend the Cimarex charter to increase the maximum size of its board of directors from nine to ten directors, one current member of the Magnum Hunter board of directors will be selected by Cimarex before the effective time of the merger to serve on the Cimarex board of directors after the merger.

Name	Age	Title
Jerry Box	66	Chairman of the Board
Gary C. Evans	47	Director
Gerald W. Bolfig	76	Director
Donald A. Erickson	61	Director
Matthew C. Lutz	70	Director
Jody Powers	58	Director
John H. Trescot, Jr.	80	Director
F. Walker Tucei, Jr.	62	Director

*Jerry Box* has served as Chairman of Magnum Hunter since October 2004, and as director since March 1999. From February 1998 to March 1999, he served in the position of president and chief operating officer and as a director of Oryx Energy Company, now owned by Kerr McGee Corporation. From December 1995 to February 1998, he was executive vice president and chief operating officer of Oryx. From December 1994 through November 1995, he served as executive vice president, exploration and production of Oryx. Previously, he served as senior vice president, exploration and production of Oryx. Mr. Box attended Louisiana Tech University, where he received B.S. and M.S. degrees in geology, and is also a graduate of the Program for Management Development at the Harvard University Graduate School of Business Administration. Mr. Box served as an officer in the U.S. Air Force from 1961 to 1966. Mr. Box is a former member of the Policy Committee of the U.S. Department of the Interior's Outer Continental Shelf Advisory Board, past chairman and vice-chairman of the American Petroleum Institute's Exploration Affairs subcommittee, a former president of the Dallas Petroleum Club and a member of the Independent Petroleum Association of America.

*Gary C. Evans* has been a director of Magnum Hunter since December 1995. He also served as President and Chief Executive Officer of Magnum Hunter from December 1995 until April 2005 and Chairman and Chief Executive Officer of all of the Magnum Hunter subsidiaries since their formation or acquisition until April 2005. In 1985, Mr. Evans formed the predecessor company, Hunter Resources, Inc., that was merged into and formed Magnum Hunter some ten years later. From 1981 to 1985, Mr. Evans was associated with the Mercantile Bank of Canada where he held various positions including Vice President and Manager of the Energy Division of the Southwestern United States. From 1978 to 1981, he served in various capacities with National Bank of Commerce (now BancTexas, N.A.) including Credit Manager and Credit Officer. Mr. Evans serves on the Board of Directors of Novavax, Inc., a NASDAQ listed pharmaceutical company. He additionally serves on the board of two private Texas-based companies that Magnum Hunter owns an interest in, including (i) Swanson Consulting Services, Inc., a geological consulting firm and (ii) Metrix Networks, Inc., a company that provides web-enabled automation to the oil and natural gas industry. He also serves as a Trustee of TEL Offshore Trust, a NASDAQ listed oil and gas trust of which Magnum Hunter owns an approximate 29% interest. Mr. Evans also serves on the Board of Advisors of the Maguire Energy Institute at Southern Methodist University.

*Gerald W. Bolfig* has been a director of Magnum Hunter since December 1995. Mr. Bolfig was appointed a director of Hunter Resources, Inc. in August 1993. He is an investor in the oil and gas business and a past officer of one of Hunter's former subsidiaries. From 1962 to 1980, Mr. Bolfig was a partner in Bolfig Food Stores in Waco, Texas. Mr. Bolfig was involved in American Service Company in Atlanta, Georgia from 1964 to 1965, and was active with Cable Advertising Systems, Inc. of Kerrville, Texas from 1978 to 1981. He joined a Hunter subsidiary in the well servicing business in 1981 where he remained active until its divestiture in 1992. Mr. Bolfig is on the board of directors of Capital Marketing Corporation of Hurst, Texas.

*Donald A. Erickson* has served as a Director of Magnum Hunter since February 3, 2004. Mr. Erickson spent nearly 20 years with Ernst & Young, LLC in their corporate finance group. During his career at Ernst & Young, he was the National Director of Valuation and the market leader for the Southwest Region Valuation Practice. Mr. Erickson's responsibilities included the valuation of business interests and intangible assets. Prior to his tenure at Ernst & Young, Mr. Erickson was a Vice President for two national valuation firms and served as an officer in the United States Army. He retired from Ernst & Young in June 2003. Currently, Mr. Erickson is the President of Erickson Partners, LLC, a valuation consulting and financial advisory firm. A 1965 graduate of Santa Clara University, with a B.S.C. degree, Mr. Erickson holds an M.B.A. degree from the University of Oregon. He is a graduate of the Ernst & Young Kellogg Executive Program at Northwestern University. Mr. Erickson is an Accredited Senior Appraiser (ASA) with the American Society of Appraisers and has served as the National Chairman of its Business Valuation Committee.

*Matthew C. Lutz* retired as chairman of Magnum Hunter on September 1, 2001 after having served in that capacity since March 1997, and after having previously served as vice chairman of Magnum Hunter from December 1995 to March 1997. Mr. Lutz also previously served as executive vice president of Magnum Hunter from December 1995 to September 2001. Mr. Lutz held similar positions with Hunter Resources, Inc. from September 1993 until October 1996. From 1984 through 1992, Mr. Lutz was senior vice president of exploration and a director of Enserch Exploration, Inc., with responsibility for its worldwide oil and gas exploration and development program. Prior to joining Enserch, Mr. Lutz spent 28 years with Getty Oil Company. He advanced through several technical, supervisory and managerial positions, which gave him various responsibilities, including exploration, production, lease acquisition, administration and financial planning.

*Jody Powers* has served as a Director of Magnum Hunter since September of 2003. Mr. Powers spent 34 years of his career with Halliburton Company and various subsidiaries with increasing levels of domestic and international management responsibilities, culminating with his retirement in May 2002, holding the executive position of President of Halliburton Energy Services. A 1968 graduate of the University of Houston, Mr. Powers is a current member of the Society of Petroleum Engineers and the 25 Year Club of the Petroleum Industry.

*John H. Trescot, Jr.* has served as a director of Magnum Hunter since June 1997. Mr. Trescot is the principal of AWA Management Corporation, a consulting firm specializing in project evaluation. Mr. Trescot began his professional career as an engineer with Shell Oil Company. Later, Mr. Trescot joined Hudson Pulp & Paper Corp. (now a part of Georgia-Pacific Corp.), where he served 19 years in various positions in woodlands and pulp and paper, advancing to the position of senior vice president for its Southern Operations. Mr. Trescot then became vice president of The Charter Company, a multi-billion dollar corporation with operations in oil, communications and insurance. In 1979, Mr. Trescot became the chief executive officer of JARI, a timber, pulp and mining operation in the Amazon Basin of Brazil. From 1982 through 1989, while he was the chief executive officer of TOT Drilling Corp., TOT drilled many deep wells in West Texas and New Mexico for major and independent oil companies. Mr. Trescot served as an officer in the United States Navy. Mr. Trescot received his BME degree from Clemson University and his M.B.A. from Harvard University.

## Edgar Filing: O'Neill Andrew J - Form 4

*F. Walker Tucei, Jr.* has been elected to Magnum Hunter's Board of Directors effective November 2004. Mr. Tucei retired in 1999 after a distinguished 37-year career with Arthur Andersen, LLP. He was admitted to the firm's partnership in 1972. During his career with Arthur Andersen, LLP, Mr. Tucei served as the New Orleans office Partner-in-Charge of the audit practice from 1975 to 1986. He also served as the New Orleans office Managing Partner from 1986 to 1999 and was responsible for the firm's practice in Louisiana, Mississippi, southern Alabama, and western Florida. During his career with Arthur Andersen, LLP, Mr. Tucei served on various firm related task forces and committees. Mr. Tucei has been involved in numerous civic and non-profit organizations, including serving as President of the Southeast Louisiana Council of the Boy Scouts of America and the World Trade Center of New Orleans. A 1963 graduate of the University of Mississippi with a B.B.A. degree, Mr. Tucei is a Certified Public Accountant (Retired) in Louisiana and Mississippi. He is a member of both the American Institute and Louisiana Society of Certified Public Accountants. Mr. Tucei has served since 2003 as a member of the board, member of the governance and nominating committees and currently serves as chairman of the audit committee for Newpark Resources, Inc. (NYSE:NR). Since 2000 he has also been a member of the Audit Committee for the Archdiocese of New Orleans and currently serves as Chairman of that committee.

### *Audit Committee*

The members of Magnum Hunter's Audit Committee include Gerald W. Bolfing, Donald A. Erickson and F. Walker Tucei, Jr. Each member possesses the required level of financial literacy and at least two members, Donald A. Erickson and F. Walker Tucei, Jr., have been determined by the Board to meet the current standards of the "audit committee financial expert" required by applicable rules and regulations. No member of the Audit Committee has any relationship to Magnum Hunter that may interfere with the exercise of their independence from management and Magnum Hunter.

The Audit Committee selects the independent public accountants, reviews the independence of such accountants, approves the scope of the annual audit, approves the rendering of any material non-audit services by the independent accountants, approves the fee payable to the independent accountants and reviews the audit results. The Audit Committee approves all fees paid to Magnum Hunter's principal accountants.

### Option/SAR Grants in Last Fiscal Year

Name	Individual Grants				Potential realizable value at assumed annual rates of stock price appreciation for option term		Alternative to (f) and (g): grant date value
	Number of securities underlying Options/SARs granted (#) (b)	Percent of total options SARs granted to employees in fiscal year (c)	Exercise or base price(\$/Sh) (d)	Expiration date (e)	5% (\$) (f)	10% (\$) (g)	Grant date present value* \$ (f)*
Jerry Box	7,500	0.5%	10.48	7/1/09			\$ 28,350
Gary C. Evans	250,000	17.4%	10.48	7/1/09			\$ 945,000

\*

The Black-Scholes method was used to determine the value of the option grants.

## Aggregated Option/SAR Exercises in Last Fiscal Year and FY-End Option/SAR Values

Name (a)	Shares acquired on exercise (#) (b)	Value Realized (\$) (c)	Number of securities underlying unexercised options/SARs at fiscal year-end (#)	Value of unexercised in- the money options/SARs at fiscal year-end (\$)
			Exercisable/ unexercisable (d)	Exercisable/ unexercisable (e)
Jerry Box	20,000	84,000	38,100/14,500	\$ 210,896/\$63,090
Gary C. Evans	250,000	1,457,500	818,000/410,000	\$ 4,580,590/\$1,634,600

The following table sets forth information with respect to the equity compensation plans available to Magnum Hunter's directors, officers and employees as of December 31, 2004:

## Equity Compensation Plan

Plan Category	(A)	(B)	(C)
	Number of securities to be issued upon exercise of outstanding options and warrants	Weighted-average exercise price of outstanding options and warrants	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column A).
Equity compensation plans approved by security holders	4,719,562	\$ 7.85	738,674
Equity compensation plans not approved by security holders	1,218,540	\$ 8.01	

For those options which were granted under the plans not approved by Magnum Hunter's security holders, the options were granted by the Board of Directors in such amounts and to such employees whom the Board determined in their sole discretion. Each option grant vested 20% at the date of grant with the balance vesting an additional 20% per year on the anniversary date over the next four years. The exercise price was fair market value at the date of each grant.

*Compensation of Directors*

Magnum Hunter has eight individuals who serve as directors, seven of which have been determined by the Board to be independent. One director receives compensation with respect to his services and in his capacities as an executive officer of Magnum Hunter, and no additional compensation has historically been paid for his services as a director. The other eight directors were not employees at December 31, 2004, and receive no compensation for their services as directors other than as stated below. For fiscal year 2004, independent directors received a \$26,000 retainer and \$24,000 worth of restricted stock for being a board member and received \$1,000 per regular and committee meeting attended. At December 1, 2004, the pay compensation for attending board and committee meetings was increased to \$2,000 per meeting. In addition, for the fiscal year 2004 each independent director was granted stock options to acquire 7,500 shares of Magnum Hunter's common stock at an exercise price of \$10.48 per share. Finally, all chairpersons of Magnum Hunter's board of directors' committees received an annual retainer of \$2,500 for acting as chairman of his respective committee. Upon becoming Chairman of the Board during October 2004, Jerry Box began receiving compensation of \$20,000 per month. This will continue through 2005. For fiscal year 2005, independent directors will receive a \$26,000 retainer and \$24,000 worth of restricted stock for being a board

## Edgar Filing: O'Neill Andrew J - Form 4

member and, in addition, will receive \$2,000 per meeting attended and \$2,000 per committee meeting attended. All chairpersons of Magnum Hunter's board of directors' committees will receive an annual retainer of \$2,500 for acting as chairman of his respective committee. Other than the compensation stated herein, Magnum Hunter has not entered into any arrangement, including consulting contracts, in consideration of the director's service on the board.

### **CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

There are no loans or extensions of credit to directors of Magnum Hunter as of December 31, 2004.

IV-56

---

Edgar Filing: O'Neill Andrew J - Form 4

**Index to Consolidated Financial Statements**

Report of Independent Registered Public Accounting Firm

Financial Statements:

Consolidated Balance Sheets at December 31, 2004 and 2003

Consolidated Statements of Operations For the Years Ended December 31, 2004, 2003 and 2002

Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss) For the Periods Ended December 31, 2004, 2003 and 2002

Consolidated Statements of Cash Flows For the Years Ended December 31, 2004, 2003 and 2002

Notes to Consolidated Financial Statements

Supplemental Information on Oil and Gas Producing Properties (Unaudited)

IV-57

---

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders  
Magnum Hunter Resources, Inc.

We have audited the accompanying consolidated balance sheets of Magnum Hunter Resources, Inc. and Subsidiaries (the "Company") as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2004. Our audits also included the financial statement schedule listed in the Index at Item 15. These consolidated financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and the financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Magnum Hunter Resources, Inc. and Subsidiaries (the "Company") as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, the Company changed its method of accounting for asset retirement obligations in 2003 as required by Statement of Financial Accounting Standard No. 143, "Accounting for Asset Retirement Obligations", and changed its method of accounting for employee stock-based option grants in 2003 by adopting the prospective method specified by Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure, and Amendment to FASB Statement No. 123".

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2004, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 15, 2005 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ Deloitte & Touche LLP

Dallas, Texas  
March 15, 2005

## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(in thousands of dollars)

	December 31, 2004	December 31, 2003
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$ 20,342	\$ 18,693
Restricted cash	212	
Accounts receivable		
Trade, net of allowance of \$4,776 and \$4,331, respectively	85,462	46,716
Notes receivable	1,396	1,996
Due from affiliates	768	
Deferred income taxes, current	5,010	8,263
Deposits	3,198	2,713
Available for sale investments	6,067	7,563
Prepaid drilling costs	9,480	8,770
Other current assets	7,579	5,623
	<b>139,514</b>	<b>100,337</b>
Property, Plant and Equipment		
Oil and gas properties, full-cost method		
Unproved	94,472	110,467
Proved	1,828,839	1,292,388
Pipelines	36,607	34,149
Other property	9,969	7,805
	<b>1,969,887</b>	<b>1,444,809</b>
Accumulated depreciation, depletion, amortization and impairment	(472,975)	(348,926)
	<b>1,496,912</b>	<b>1,095,883</b>
Other assets		
Deferred financing costs and other	9,608	13,205
Goodwill	56,467	56,467
	<b>1,702,501</b>	<b>1,265,892</b>
<b>Total Assets</b>	<b>\$ 1,702,501</b>	<b>\$ 1,265,892</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities		
Trade payables	\$ 65,215	\$ 28,793
Accrued interest	5,764	8,909
Accrued liabilities	15,298	11,228
Due to affiliates	503	1,742
Other current liabilities	8,198	7,060
Revenues payable	10,871	7,860
Suspended revenue payable	22,401	16,049
Derivative liabilities, current	14,046	21,853
Current maturities of long-term debt	2,458	2,009
	<b>144,754</b>	<b>105,503</b>
Long-Term Liabilities		
Long-term debt, less current maturities	643,042	595,503
Asset retirement obligations	40,086	32,489
Derivative liabilities, noncurrent	5,981	1,198
Deferred income taxes payable	188,366	141,000
Other non-current liabilities	459	523
Stockholders' Equity		
Preferred stock \$.001 par value; 10,000,000 shares authorized, 216,000 designated as Series A; 80,000 issued and outstanding, liquidation amount \$0	1	1

Edgar Filing: O'Neill Andrew J - Form 4

	December 31, 2004	December 31, 2003
Common Stock \$.002 par value; 200,000,000 shares authorized, 91,324,168 and 71,977,759 shares issued, respectively	183	144
Additional paid-in capital	615,046	429,446
Accumulated other comprehensive loss	(12,621)	(13,576)
Retained earnings	108,576	5,003
Common stock in deferred compensation plan, at cost (34,416 shares)	(192)	(192)
Unearned common stock in KSOP, at cost (880,083 and 1,012,203 shares, respectively)	(6,215)	(6,110)
	704,778	414,716
Treasury stock, at cost (3,931,614 and 3,942,294 shares, respectively)	(24,965)	(25,040)
Total Stockholders' Equity	679,813	389,676
Total Liabilities and Stockholders' Equity	\$ 1,702,501	\$ 1,265,892

The accompanying notes are an integral part of these consolidated financial statements.

IV-59

## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands of dollars, except for share and per share amounts)

	For the Years Ended December 31,		
	2004	2003	2002
<b>Operating Revenues:</b>			
Oil and gas sales	\$ 443,412	\$ 284,929	\$ 240,964
Gas gathering, marketing and processing	41,900	35,317	20,809
Oil field services	8,414	4,768	4,096
<b>Total Operating Revenues</b>	<b>493,726</b>	<b>325,014</b>	<b>265,869</b>
<b>Operating Costs and Expenses:</b>			
Oil and gas production lifting costs	60,945	56,262	51,559
Production taxes and other costs	43,704	32,772	28,167
Gas gathering, marketing and processing	29,112	25,373	15,100
Oil field services	5,016	3,119	2,474
Depreciation, depletion, amortization and accretion	127,179	99,614	86,468
Gain on sale of assets	(288)	(171)	(61)
General and administrative	22,125	15,347	13,293
<b>Total Operating Costs and Expenses</b>	<b>287,793</b>	<b>232,316</b>	<b>197,000</b>
<b>Operating Profit</b>	<b>205,933</b>	<b>92,698</b>	<b>68,869</b>
Equity in (loss) earnings of affiliate		(162)	792
Other income	2,584	889	452
Provision for impairment of investments			(621)
Costs associated with early retirement of debt	(12,250)	(6,716)	(1,000)
Non-cash hedging adjustments	1,124	1,482	(6,626)
Interest expense	(38,059)	(47,260)	(47,935)
<b>Income Before Income Tax</b>	<b>159,332</b>	<b>40,931</b>	<b>13,931</b>
Provision for income tax (expense) benefit			
<b>Current</b>	<b>(1,977)</b>	<b>250</b>	
<b>Deferred</b>	<b>(53,782)</b>	<b>(15,463)</b>	<b>1,591</b>
<b>Total Provision for Income Tax (Expense) Benefit</b>	<b>(55,759)</b>	<b>(15,213)</b>	<b>1,591</b>
<b>Income Before Cumulative Effect of a Change in Accounting Principle</b>	<b>103,573</b>	<b>25,718</b>	<b>15,522</b>
Cumulative effect of a change in accounting principle, net of income tax expense of \$244		399	
<b>Net Income</b>	<b>\$ 103,573</b>	<b>\$ 26,117</b>	<b>\$ 15,522</b>
<b>Income per Common Share Basic</b>			
<b>Income before cumulative effect of a change in accounting principle</b>	<b>\$ 1.35</b>	<b>\$ 0.38</b>	<b>\$ 0.25</b>

Explanation of Responses:

Edgar Filing: O'Neill Andrew J - Form 4

For the Years Ended December 31,

<b>Cumulative effect of a change in accounting principle</b>				0.01		
Income per Common Share Basic	\$	1.35	\$	0.39	\$	0.25
Income per Common Share Diluted						
<b>Income before cumulative effect of a change in accounting principle</b>	\$	1.31	\$	0.38	\$	0.25
<b>Cumulative effect of a change in accounting principle</b>				0.01		
Income per Common Share Diluted	\$	1.31	\$	0.39	\$	0.25
Common Shares Used in Per Share Calculation						
<b>Basic</b>		76,952,204		66,191,816		61,493,428
<b>Diluted</b>		78,958,618		67,501,811		62,513,548

The accompanying notes are an integral part of these consolidated financial statements.

IV-60

## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)

FOR THE YEAR ENDED DECEMBER 31, 2002

(thousands)

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid in Capital	Accumulated Deficit	Receivable from Stockholder	Unearned Shares in KSOP	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity	Total Comprehensive Income (Loss)
<b>Balance at January 1, 2002</b>	\$ 1	\$ 73	\$ (1,914)	\$ 157,836	\$ (36,636)	\$ (442)	\$ (2,576)	\$ 1,632	\$ 117,974	
Issuance of 34,063 shares of common stock and warrants pursuant to Prize Energy Corp. merger, less fees		68		260,454					260,522	
Issuance of 985 shares of common stock pursuant to employee stock option plan		2		3,627					3,629	
Deferred tax benefit on exercise of employee stock options				859					859	
Employer contribution of 158 shares to KSOP				71			867		938	
Exercise of warrants				5					5	
Purchase of warrants				(128)					(128)	
Repayment of shareholder loan						442			442	
Issuance of 72 shares to KSOP for 2001 employer contribution				601					601	
Purchase of 2,726 shares of treasury stock			(18,494)						(18,494)	
Employee salary deferrals to KSOP representing 86 shares				39			473		512	
Loan of 532 shares to KSOP							(3,652)		(3,652)	
Net income, net of income tax benefit of \$1,591					15,522				15,522	15,522
Reclassification adjustment related to derivative contracts, net of deferred income tax expense of \$1,684								2,762	2,762	2,762
Change in fair value of outstanding hedge positions, net of deferred income tax benefits of \$19,871								(32,593)	(32,593)	(32,593)
Purchased hedge positions, net of deferred income tax benefit of \$1,508								(2,474)	(2,474)	(2,474)
Amortization of purchased hedge positions, net of deferred income tax expense of \$2,299								3,771	3,771	3,771

Edgar Filing: O'Neill Andrew J - Form 4

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid in Capital	Accumulated Deficit	Receivable from Stockholder	Unearned Shares in KSOP	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity	Total Comprehensive Income (Loss)
Unrealized loss on investments, net of deferred income tax benefit of \$197								(323)	(323)	(323)
Reclassification adjustment for loss on investments, net of deferred income tax expense of \$197								323	323	323
<b>Balance at December 31, 2002</b>	\$ 1	\$ 143	\$ (20,408)	\$ 423,364	\$ (21,114)		\$ (4,888)	\$ (26,902)	\$ 350,196	\$ (13,012)

The accompanying notes are an integral part of these consolidated financial statements.

IV-61

## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS) (Continued)

FOR THE YEAR ENDED DECEMBER 31, 2003

(thousands)

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid in Capital	Retained Earnings (Accumulated Deficit)	Deferred Compensation	Unearned Shares in KSOP	Accumulated Comprehensive Income (Loss)	Other	Total Stockholders' Equity	Total Comprehensive Income (Loss)
<b>Balance at January 1, 2003</b>	\$ 1	\$ 143	\$ (20,408)	\$ 423,364	\$ (21,114)		\$ (4,888)	\$ (26,902)		350,196	
Issuance of 270 shares of common stock pursuant to employee stock option plan		1		1,244						1,245	
Issuance of 548 treasury shares upon exercise of warrants			2,728	720						3,448	
Deferred tax benefit on exercise of employee stock options				613						613	
Purchase of 1,340 shares of treasury stock			(7,413)							(7,413)	
Loan to KSOP to purchase 486 shares							(2,711)			(2,711)	
Employee deferrals to KSOP to purchase 59 shares				105			380			485	
Purchase 53 shares for deferred compensation plan						(295)				(295)	
Employer contribution of 172 shares to KSOP				336			1,109			1,445	
Stock compensation				3,017						3,017	
Purchase of 18 treasury shares by deferred compensation plan			53	47		(100)					
Release of 36 shares from deferred compensation plan						203				203	
Net Income, net of income tax expense of \$15,213					26,117					26,117	26,117
Reclassification adjustments related to derivative contracts, net of deferred income tax expense of \$28,330								46,469		46,469	46,469
Change in fair value of outstanding hedge positions, net of deferred income tax benefit of \$19,715								(32,338)		(32,338)	(32,338)
Amortization of purchased hedge positions, net of deferred income tax								(805)		(805)	(805)

Edgar Filing: O'Neill Andrew J - Form 4

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid in Capital	Retained Earnings (Accumulated Deficit)	Deferred Compensation	Unearned Shares in KSOP	Accumulated Comprehensive Income (Loss)	Other Stockholders' Equity	Total Comprehensive Income (Loss)
benefit of \$491										
<b>Balance at December 31, 2003</b>	\$ 1	\$ 144	\$ (25,040)	\$ 429,446	\$ 5,003	\$ (192)	\$ (6,110)	\$ (13,576)	\$ 389,676	\$ 39,443

The accompanying notes are an integral part of these consolidated financial statements.

IV-62

## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS) (Continued)

FOR THE YEAR ENDED DECEMBER 31, 2004

(thousands)

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid in Capital	Retained Earnings	Deferred Compensation	Unearned Shares in KSOP	Accumulated Comprehensive Income (Loss)	Other Stockholders' Equity	Total Comprehensive Income (Loss)
<b>Balance at January 1, 2004</b>	\$ 1	\$ 144	\$ (25,040)	\$ 429,446	\$ 5,003	\$ (192)	\$ (6,110)	\$ (13,576)		\$ 389,676
Issuance of 2,128 shares of common stock pursuant to employee stock option plan		4		10,427						10,431
Issuance of 17,250 shares through secondary offering, net of offering costs		35		169,279						169,314
Stock compensation				768						768
Deferred tax benefit on exercise of employee stock options				2,765						2,765
Loan to KSOP to purchase 225 shares Employer contribution of 223 shares to KSOP				1,515			(2,259)			(2,259)
Employee salary deferrals to KSOP, representing 134 shares				776			807			1,583
Issuance of 11 shares for Directors' compensation			75	70						145
Net Income, net of income tax expense of \$55,759					103,573					103,573
Reclassification adjustments related to derivative contracts, net of deferred income tax expense of \$15,859								27,950		27,950
Change in fair value of outstanding hedge positions, net of deferred income tax benefit of \$15,038								(26,503)		(26,503)
Amortization of purchased hedge positions, net of deferred income tax benefit of \$279								(492)		(492)
<b>Balance at December 31, 2004</b>	\$ 1	\$ 183	\$ (24,965)	\$ 615,046	\$ 108,576	\$ (192)	\$ (6,215)	\$ (12,621)		\$ 679,813

The accompanying notes are an integral part of these consolidated financial statements.



## MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of dollars)

	For the Years Ended December 31,		
	2004	2003	2002
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>			
Net Income	\$ 103,573	\$ 26,117	\$ 15,522
Adjustments to reconcile net income to cash provided by operating activities:			
Cumulative effect of a change in accounting principle		(399)	
Depreciation, depletion, amortization and accretion	127,179	99,614	86,468
Impairment of investments			621
Amortization of financing fees	2,647	2,377	2,037
Imputed interest on debt due to merger			108
Increase in allowance for doubtful accounts	841	231	206
Deferred income taxes (benefits)	53,782	15,463	(1,591)
Equity in (income) loss of unconsolidated affiliate		162	(792)
Costs associated with early extinguishment of debt	12,250	6,716	1,000
Cost of shares released from KSOP suspense	1,347	1,109	867
Minority interest in consolidated subsidiary	(64)	89	
Stock compensation	768	3,017	
Non-cash directors' compensation	145		
Excess of fair value over cost of shares released from KSOP suspense	2,291	441	110
Gain on sale of assets	(288)	(171)	(61)
Other non-cash hedging adjustments	(1,124)	(1,482)	6,626
Changes in certain assets and liabilities, net of the effect of acquisitions			
Accounts and notes receivable	(40,357)	6,565	(17,429)
Derivative assets			3,600
Deposits and other current assets	(2,872)	(4,264)	(9,314)
Accounts payable and accrued liabilities	42,931	(1,081)	(7,449)
(Payment) refund of income taxes	(2,439)	8,134	2,874
Net Cash Provided by Operating Activities	300,610	162,638	83,403
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from sale of assets	22,902	17,123	95,988
Proceeds from sale of unconsolidated affiliate		5,160	
Purchase of land to be held for sale		(7,563)	
Purchase of controlling interest in Metrix Networks, Inc., net of cash acquired		(253)	
Additions to property and equipment	(303,125)	(175,535)	(141,046)
Cash paid for New Mexico property acquisition	(234,180)		
Cash paid in Prize merger net of cash acquired			(41,095)
(Increase) decrease in other assets	(136)	(17)	238
Loan made for promissory note receivable			(2,596)
Payments received on promissory note receivable	600	500	
Distribution from unconsolidated affiliate		1,510	256
Investment in unconsolidated affiliate		(600)	(1,165)
Net Cash Used In Investing Activities	(513,939)	(159,675)	(89,420)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Proceeds from issuance of debt	466,000	517,375	627,850
Fees paid related to financing activities	(1,011)	(4,428)	(11,961)
Payments of principal on long-term debt and production payment liability	(313,012)	(486,348)	(591,451)
Redemption of notes payable	(115,080)	(134,374)	
Proceeds from issuance of convertible notes		125,000	
Loan repaid by stockholder			742
Loan to KSOP	(2,259)	(2,711)	(3,652)
Loan repaid from KSOP	807	380	473
Proceeds from issuance of common stock	10,431	1,245	3,634

Edgar Filing: O'Neill Andrew J - Form 4

For the Years Ended December 31,

Proceeds from issuance of secondary offering of common stock	169,314		
Proceeds from issuance of treasury stock		3,448	
Purchase of warrants			(128)
Purchase of treasury stock		(7,413)	(18,494)
(Increase) decrease in restricted cash for payment of notes payable	(212)	682	(682)
Net decrease in note receivable from affiliate		100	
Purchase common stock for deferred compensation plan		(295)	
Net Cash Provided by Financing Activities	214,978	12,661	6,331
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,649	15,624	314
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	18,693	3,069	2,755
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 20,342	\$ 18,693	\$ 3,069

The accompanying notes are an integral part of these consolidated financial statements.

IV-64

**MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Organization and Nature of Operations**

Magnum Hunter Resources, Inc. ("Magnum Hunter"), is incorporated under the laws of the state of Nevada. The company and our subsidiaries are engaged in the acquisition, operation and development of oil and gas properties, the gathering, processing, transmission, and marketing of natural gas and natural gas liquids and providing management, advisory consulting and measurement services on oil and gas properties for third parties. In conjunction with the above activities, we own and operate oil and gas properties in twelve states, predominantly in the Southwest region of the United States. In addition, we own and operate five gathering systems located in Texas, Oklahoma and New Mexico and own an interest in four natural gas processing plants located in Texas, Oklahoma and Arkansas.

**Consolidation**

The accompanying consolidated financial statements include the accounts of Magnum Hunter and our existing wholly-owned subsidiaries, Gruy Petroleum Management Co., Magnum Hunter Production, Inc., ConMag Energy Corporation, Trapmar Properties, Inc., Hunter Gas Gathering, Inc. ("Hunter"), Canvasback Energy, Inc., Pintail Energy, Inc., Redhead Energy, Inc. ("Redhead"), Prize Operating Co., PEC (Delaware), Inc., Oklahoma Gas Processing, Inc., and Prize Energy Resources, LP. We consolidate on a pro rata basis our approximately 29% ownership of TEL Offshore Trust, our 1% interest in Mallard Hunter, LP, our 5% interest in Teal Hunter, LP and our 40% interest in Appletree Holdings LLC. Prior to December 2003, we accounted for our approximately 32% interest in Metrix Networks, Inc. ("Metrix") under the equity method. We acquired an 80% controlling interest in Metrix during December 2003, and thus fully consolidate them with a minority interest for the outside owners' 20%. Prior to its sale in September 2003, we also accounted for our investment in NGTS, LLC ("NGTS") under the equity method. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the consolidated financial statements of the prior years to conform to the current presentation.

Magnum Hunter is a holding company with no significant assets or operations other than our investments in our subsidiaries. Our wholly-owned subsidiaries, except for Canvasback Energy, Inc., Redhead and Metrix, collectively referred to as Canvasback, are direct guarantors of our 9.6% Senior Notes and our Convertible Notes, and have fully and unconditionally guaranteed these notes on a joint and several basis. The guarantors comprise all of our direct and indirect subsidiaries (other than Canvasback), and we have presented separate condensed consolidating financial statements and other disclosures concerning each guarantor and Canvasback (See Note 16). Except for Canvasback, there is no restriction on the ability of consolidated or unconsolidated subsidiaries to transfer funds to Magnum Hunter in the form of cash dividends, loans, or advances.

**Cash and Cash Equivalents**

We consider all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. We have cash deposits in excess of federally insured limits.

**Investments**

We follow accounting procedures according to Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Under this standard, all of our equity securities that have readily determinable fair values are classified as current

or non-current assets, available-for-sale and are measured at fair value and are recognized as either current or non-current assets. Unrealized gains and losses for these investments are reported as comprehensive income and accumulated as a separate component of stockholders' equity. Realized gains and losses are calculated based on the specific identification method. We recorded an impairment on an investment in the common stock of another entity whose stock was held by us for resale for its full carrying value of \$621 thousand during 2002. At December 31, 2003 and 2004, we carried no value for our available-for-sale securities.

#### **KSOP**

As required under Statement of Position 93-6 "Employers Accounting for Employee Stock Ownership Plans," compensation expense is recorded for shares committed to be released to employees based on the fair market value of those shares when they are committed to be released. The difference between cost and the fair market value of the committed to be released shares is recorded in additional paid-in-capital. Unreleased shares held by the KSOP are excluded from the calculation of earnings per share.

#### **Suspended Revenues**

Suspended revenue interests represent oil and gas sales payable to third parties largely on properties operated by the company. We distribute such amounts to third parties upon receipt of signed division orders or resolution of other legal matters.

#### **Oil and Gas Properties**

We use the full-cost method of accounting for our investments in oil and gas properties. Accordingly, all costs associated with acquisition, exploration and development of oil and gas reserves, including directly related overhead costs, are capitalized into a "full-cost pool" on a country-by-country basis as incurred. Internal costs that directly relate to acquisition, exploration and development activities that were capitalized totaled \$1.3 million for the years ended December 31, 2004 and 2003. The balance of capitalized costs included in oil and gas properties for the years ended December 31, 2004 and 2003 were \$6.5 million and \$5.2 million, respectively. Management believes that the basis we use to determine the amount of internal costs capitalized is appropriate.

All capitalized costs of oil and gas properties, including the estimated future costs to develop proved reserves and estimated dismantlement and abandonment costs, net of salvage values, are amortized on the unit-of-production method using estimates of proved reserves. Costs directly associated with the acquisition and evaluation of unproved properties are excluded from the amortization base until the related properties are evaluated. Such unproved properties are assessed for impairment quarterly and any provision for impairment is transferred to the full-cost amortization base. Sales of oil and gas properties, including consideration received from sales or transfers of properties in connection with partnerships, joint venture operations or drilling arrangements, are credited to the full-cost pool unless the sale would have a significant effect on the amortization rate. Abandonment of properties is accounted for as an adjustment to capitalized costs with no loss recognized.

In accordance with SFAS 143, "Accounting for Asset Retirement Obligations," we carry a liability for any legal retirement obligations on our oil and gas properties. The associated asset retirement costs are capitalized as part of the full cost pool. We adopted SFAS 143 on January 1, 2003 and recorded

proved property additions of \$30.4 million in relation to the transition entry. See Note 3 for additional information on our asset retirement obligations.

Reserve engineering is a subjective process that is dependent on the quality of available data and on engineering and geological interpretation and judgment. Reserve estimates are subject to change over time as additional information becomes available.

A summary of the unproved properties excluded from proved oil and gas properties being amortized at December 31, 2004 and 2003, respectively, and the year in which they were incurred follows:

<b>December 31, 2004</b>					
	<b>Prior</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>Total</b>
(in thousands)					
Property Acquisition Costs	\$ 3,585	\$ 54,648	\$ 9,279	\$ 19,582	\$ 87,094
Exploration Costs			896	6,482	7,378
<b>Total</b>	<b>\$ 3,585</b>	<b>\$ 54,648</b>	<b>\$ 10,175</b>	<b>\$ 26,064</b>	<b>\$ 94,472</b>
<b>December 31, 2003</b>					
	<b>Prior</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>Total</b>
(in thousands)					
Property Acquisition Costs	\$ 304	\$ 4,900	\$ 83,836	\$ 12,207	\$ 101,247
Exploration Costs				9,220	9,220
<b>Total</b>	<b>\$ 304</b>	<b>\$ 4,900</b>	<b>\$ 83,836</b>	<b>\$ 21,427</b>	<b>\$ 110,467</b>

Costs are transferred into the amortization base on an ongoing basis as the projects are evaluated and proved reserves are established or impairment determined. Pending determination of proved reserves attributable to the above costs, we cannot assess the future impact on the amortization rate.

The capitalized costs are subject to a "ceiling test", which generally limits such costs less accumulated amortization and related deferred income taxes to the aggregate of the estimated present value of future net revenues from proved reserves discounted at ten percent based on current economic and operating conditions less income tax effects related to the differences between the book and tax basis of the oil and gas properties. The ceiling test is performed on a quarterly basis. We experienced no impairment in 2004, 2003, or 2002.

For purposes of the ceiling test, we remove the discounted present value included in our future development costs on our reserve report for which we have already booked an obligation under SFAS 143. For purposes of our depletion calculation, we include in future development costs the estimated plugging and abandonment costs, net of estimated salvage values, for proved undeveloped wells. For purposes of both of these calculations, we do not include plugging and abandonment costs in our future development costs on developed proportions for which we have booked an obligation under SFAS 143.

All costs relating to production activities are charged to expense as incurred.

Amortization expense per thousand cubic feet equivalent was \$1.50, \$1.28 and \$1.17 for the years ended December 31, 2004, 2003 and 2002, respectively.

#### **Derivative Instruments**

Our product price and interest hedging activities are described in Note 12 to the consolidated financial statements. Periodically we enter into derivative instruments such as futures, swaps and options contracts to reduce the adverse effects of fluctuations in natural gas and crude oil prices. Under our risk management policy, at inception, commodity hedge positions may not exceed 75% of natural gas and 90% of crude oil current forecasted (18 months) commodity production. For forecasted non-current (greater than 18 months) commodity production, at inception, commodity hedge positions for both natural gas and crude oil may not exceed 75% of forecasted production for each product. We also may utilize, from time to time, financial derivative instruments to hedge the risk associated with interest on our outstanding variable-rate debt. Generally, the cash settlement of all derivative instruments is recognized as income or expense in the period in which the hedged transaction affects earnings.

All freestanding financial derivative instruments, including certain derivative instruments embedded in other contracts if certain criteria are met, are recognized at estimated fair value on our balance sheet. We determine our fair values based on market values obtained from our counterparties. Derivative instruments that are not designated as hedges must be adjusted to fair value through net income. Changes in the fair value of derivative instruments that are fair value hedges are offset against changes in the fair value of the hedged items, and are recognized in net income. Changes in the fair value of derivative instruments that are cash-flow hedges are recognized in other comprehensive income until such time as the hedged items are recognized in net income. Ineffective portions of a derivative instrument's change in fair value are immediately recognized in net income.

#### **Gas Processing Plants and Pipelines**

Gas processing plants and pipelines are carried at cost. Depreciation is provided using the straight-line method over an estimated useful life of 15 years. Gain or loss on retirement or sale or other disposition of assets is included in results of operations in the period of disposition. We review the carrying value of pipelines and processing plants and other long-lived assets (other than oil and gas assets accounted for under the full-cost method) for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where the undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The fair value is determined using the discounted cash flows method.

#### **Other Property**

Other property and equipment are carried at cost. Depreciation is provided using the straight-line method over estimated useful lives ranging from three to 39 years. Gain or loss on retirement or sale or other disposition of assets is included in results of operations in the period of disposition.

### **Other Oil and Gas Related Services**

Other oil and gas related services consist largely of fees earned from our operation and monitoring services of oil and gas properties for third parties. Such fees are recognized in the month the service is provided.

Magnum Hunter does not recognize income in connection with drilling, well service or other services provided in connection with oil and gas properties in which we hold an ownership or other economic interest to the extent of our interest. Any proceeds received for services performed that are not recognized as income are credited to the full cost pool.

### **Stock Compensation**

At December 31, 2004, we had four stock-based employee compensation plans, which are described more fully in Note 13. We currently account for our employee stock option plans under SFAS No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure, an Amendment to FASB Statement No. 123," in December 2002. SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation and amends the disclosure requirements of SFAS No. 123. On June 1, 2003, and effective January 1, 2003, we began expensing the fair market value of stock options newly granted, modified or settled pursuant to SFAS No. 123, "Accounting for Stock-Based Compensation," and as allowed under the prospective method of SFAS No. 148. The fair value of each option granted after December 31, 2002, is estimated on the grant date, using the Black-Scholes option-pricing model. For the years ended December 31, 2003 and 2004, we recorded stock compensation expense of \$3.0 million and \$768 thousand, respectively, which is reflected in our general and administrative expenses. For options granted prior to January 1, 2003, we continue to use the intrinsic method under APB No. 25, "Accounting for Stock Issued to Employees and Related Interpretations," whereby no compensation expense is recognized for stock options granted with an exercise price equal to the market value of our stock on the grant date. Our future accounting for stock-based compensation will be impacted by the issuance of SFAS No. 123(R). Please see our Recently Issued Statements discussion below for additional information.

## Edgar Filing: O'Neill Andrew J - Form 4

If we had recorded stock option expense under the fair value provisions of SFAS No. 123 for all prior and current grants, our net income and earnings per share ("EPS") would have been as shown in the below pro forma tables (in thousands):

	Year Ended December 31,		
	2004	2003	2002
Net income, as reported	\$ 103,573	\$ 26,117	\$ 15,522
Total Stock-based employee compensation expense included in reported net income, net of income taxes of \$278 and \$1,144, respectively	490	1,873	
Deduct: Total stock-based employee compensation determined under fair value-based method for all awards, net of income taxes of \$1,871, \$2,896, and \$1,962 respectively	(3,298)	(4,751)	(3,219)
Pro forma net income	\$ 100,765	\$ 23,239	\$ 12,303
Earnings per share:			
Basic as reported	\$ 1.35	\$ 0.39	\$ 0.25
Basic pro forma	\$ 1.31	\$ 0.35	\$ 0.20
Diluted as reported	\$ 1.31	\$ 0.39	\$ 0.25
Diluted pro forma	\$ 1.28	\$ 0.34	\$ 0.20

The company estimated the fair value of each stock based grant (options and warrants) using the Black-Scholes option pricing method while using the following weighted average assumptions:

	2004(a)	2003(b)	2002
Risk-free interest rate	3.38%	1.58%	3.68%
Expected life	4.1 years	2.1 years	7.4 years
Expected volatility	40.7%	46.3%	49.5%
Dividend yield			
Weighted average fair value of options granted	\$ 3.81	\$ 3.03	\$ 3.17

(a) We granted 1,403,000 options during 2004, which had a reduced term of four years. Prior grants have ten-year terms.

(b) We granted 999,260 options during 2003, which had a reduced term of three years. Prior grants have ten-year terms.

### Insurance Proceeds

As a result of damages incurred during Hurricane Lili, we received proceeds of \$904 thousand and \$1 million, during the years ended 2004 and 2003 respectively. We credited \$608 thousand in each of the years 2004 and 2003 against proved property to represent damages paid for equipment losses. In



2004 and 2003, we included \$296 thousand and \$399 thousand, respectively, of these proceeds in oil and gas sales, which represented business interruption proceeds.

### **Income Taxes**

We file a consolidated federal income tax return. Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due, if any, plus net deferred taxes related primarily to differences between the basis of assets and liabilities for financial and income tax reporting. Deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets include recognition of operating losses that are available to offset future taxable income and tax credits that are available to offset future income taxes. Valuation allowances are recognized to limit recognition of deferred tax assets where appropriate. Such allowances may be reversed when circumstances provide evidence that the deferred tax assets will more likely than not be realized. We recorded a valuation allowance of \$2.0 million on deferred tax assets representing state operating loss carryforwards during 2004 due to management's estimate that these operating loss carryforwards would not be realized before their expiration.

### **Goodwill**

As a result of our merger with Prize, we currently have recorded \$56.5 million of goodwill. Under SFAS No. 142, we will not amortize any of the goodwill acquired in the merger. All goodwill has been allocated to the Exploration and Production reporting unit. We test our goodwill for impairment on an annual basis or whenever indicators of impairment exist. We performed our annual impairment test at December 31, 2004, and determined that no impairment existed. The annual impairment test requires management to make significant estimates and judgments. If impairment is determined to exist, we will measure our impairment based on a comparison of the carrying value of goodwill to the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the Exploration and Production reporting unit to all of the assets and liabilities of that unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. If the carrying amount of goodwill exceeds the implied fair value of that goodwill, impairment will be recognized in the income statement.

### **Asset Retirement Obligations**

SFAS No. 143, "Accounting for Asset Retirement Obligations," became effective beginning January 1, 2003. SFAS No. 143 requires the recognition of a fair value liability for any retirement obligation associated with long-lived assets in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over the asset's useful life. See Note 3 for additional information on our asset retirement obligations. Upon adoption of SFAS No. 143, we recorded an addition to oil and gas properties of \$25.4 million, an asset retirement obligation of \$30.4 million, a reduction of accumulated depletion of \$5.6 million, and a pre-tax gain of \$643 thousand. The retirement obligation requires management to make significant estimates and judgments regarding our expected plugging costs and retirement dates.

## Recently Issued Statements

The Financial Accounting Standards Board ("FASB") has issued FASB Staff Position ("FSP") No. 142-2, "Application of FASB Statement 142, Goodwill and Other Intangible Assets, to Oil-and-Gas Producing Entities" after evaluating an issue involving the classification of mineral rights. In June 2001, FASB issued Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations," which requires the purchase method of accounting for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method. In July 2001, the FASB also issued SFAS No. 142, "Goodwill and Other Intangible Assets," which discontinues the practice of amortizing goodwill and indefinite lived intangible assets and initiates an annual review of impairment. Intangible assets with a determinable useful life will continue to be amortized over that period. The amortization provisions apply to goodwill and intangible assets acquired after June 30, 2001. SFAS No. 141 and 142 clarify that more assets should be distinguished and classified between tangible and intangible. We did not change or reclassify contractual mineral rights included in proved and unproved oil and gas properties on our balance sheet upon adoption of SFAS No. 142. We believe the treatment of such mineral rights as tangible assets under the full cost method of accounting for oil and gas properties is appropriate. An issue was raised regarding whether these mineral rights should be classified as tangible or intangible assets. FSP No. 142-2 addressed this issue and supports our current accounting treatment of mineral rights and will not impact our financial statements. This FSP is effective for reporting periods beginning after September 2, 2004.

FASB issued FSP FAS 129-1, "Disclosure Requirements Under FASB Statement No. 129, *Disclosure of Information About Capital Structure*," in April 2004. This FSP provides additional guidance on the disclosure requirements of contingently convertible securities. We have made the required disclosures related to the terms of our Convertible Notes and have provided explanations in Note 5 about the dilutive effects of these notes on our earnings per share.

FASB's Emerging Issues Task Force ("EITF") has issued an EITF Abstract for EITF Issue No. 04-8, "The Effect of Contingently Convertible Debt on Diluted Earnings per Share," which addresses the issue of when the dilutive effects of contingently convertible debt instruments should be included in diluted earnings per share. This guidance would require companies to include the dilutive effect of convertible debt securities in diluted earnings per share regardless of whether or not the contingent conversion features have been triggered. This EITF is effective for periods ending after December 15, 2004. We have accordingly included approximately 94 thousand potential shares to be issued for our Convertible Notes in our earnings per share computations for the year ending 2004 based on the spread between our average market price during the year and the conversion price on these notes. We did not include any potential dilution for the 2003 period because the conversion price did not exceed our average market price during that period.

The SEC Staff Accounting Bulletin ("SAB") 106 was released in September 2004. SAB 106 expresses the SEC staff's views on the interaction of SFAS No. 143 and the full cost method and provides guidance on computing the full cost ceiling as well as depreciation, depletion, and amortization. The SAB also requires additional disclosures regarding how the application of SFAS No. 143 has affected the ceiling test and depreciation, depletion and amortization. This guidance is effective for the first fiscal quarter beginning after its publication. We implemented this guidance for our ceiling test and depletion calculations during the fourth quarter of 2004 and experienced no significant impact.

FASB issued SFAS No. 123(R), "Share-Based Payment", during December 2004. Under this revised guidance, all share-based equity and liability instruments will be recorded as compensation expense based on their fair values, and all liability instruments will be remeasured each reporting period. This guidance will be effective as of the beginning of the first annual or interim reporting period that begins after June 15, 2005, which would cause us to adopt this statement July 1, 2005. We currently account for our stock-based compensation under the prospective method, under which we only record compensation expense on awards granted after 2003. Upon adoption of this statement, we will apply the modified prospective method to our equity instruments under which compensation expense will also be recorded on the unvested portions of awards granted prior to 2003. At this time, we estimate the pre-tax impact of these prior years' grants on 2005 earnings to be an additional pre-tax expense of \$1.2 million.

FASB also issued SFAS No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29", during December 2004. SFAS No. 153 amends APB Opinion No. 29 by eliminating the exception from fair value measurement prescribed in that statement and replaces it with an exception for exchanges that have no significant impact on future cash flows. This statement is effective for exchanges that take place in fiscal periods beginning after June 15, 2005. We do not expect this statement to have an impact on our future financial results.

### **Income or Loss Per Common Share**

Basic net income or loss per common share is computed by dividing the net income or loss attributable to common stockholders by the weighted average number of shares of common stock outstanding during the period. Diluted net income or loss per common share is calculated in the same manner, but also considers the impact to net income and common shares for the potential dilution from stock options, stock warrants and any other outstanding convertible securities.

Edgar Filing: O'Neill Andrew J - Form 4

The following table reconciles the numerators and denominators used in the computations of both basic and diluted EPS (in thousands, except for per share amounts):

	For the Year Ended								
	December 31, 2004			December 31, 2003			December 31, 2002		
	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Shares (Denominator)	Per Share Amount
Income before Cumulative Effect	\$ 103,573	76,952	\$ 1.35	\$ 25,718	66,192	\$ 0.38	\$ 15,522	61,493	\$ 0.25
Add: Cumulative Effect				399		0.01			
<b>Basic EPS</b>									
Income available to common stockholders	\$ 103,573	76,952	\$ 1.35	\$ 26,117	66,192	\$ 0.39	\$ 15,522	61,493	\$ 0.25
Effect of dilutive securities									
Warrants					57			35	
Convertible Notes		94							
Options		1,913			1,253			986	
<b>Diluted EPS</b>									
Income available to common stockholders and assumed conversions	\$ 103,573	78,959	\$ 1.31	\$ 26,117	67,502	\$ 0.39	\$ 15,522	62,514	\$ 0.25
Less: Cumulative Effect				(399)		(0.01)			
Income before Cumulative Effect	\$ 103,573		\$ 1.31	\$ 25,718		\$ 0.38	\$ 15,522		\$ 0.25

At December 31, 2004, we had 7,228,457 warrants outstanding at a weighted average exercise price of \$15.00 per share, 5,938,102 options outstanding at a weighted average price of \$7.88 per share, and no outstanding convertible preferred stock. Warrants totaling 7,228,457 shares and options totaling 376,125 shares were excluded from the diluted net income per share computation in 2004 because their exercise price exceeded the average market price of our stock. There was a 93,750 share dilutive effect from our Convertible Notes for the year ending December 31, 2004. Please see Note 5 for a discussion of the conversion features of these Notes.

At December 31, 2003, we had 7,228,457 warrants outstanding at a weighted average exercise price of \$15.00 per share, 6,740,764 options outstanding at a weighted average exercise price of \$6.36 per share, and no outstanding convertible preferred stock. Warrants totaling 7,550,832 shares and options totaling 2,299,300 shares were excluded from the diluted net income per share computation in 2003 as the exercise price exceeded the average market price of our common stock. There was no dilutive effect from our Convertible Notes because their conversion price exceeded the average market price during the period, and only the conversion spread is issuable in shares.

At December 31, 2002, we had 7,873,206 warrants outstanding at a weighted average exercise price of \$14.32 per share, 6,044,800 options outstanding at a weighted average exercise price of \$6.37 per share, and no outstanding convertible preferred stock. Warrants totaling 7,838,600 shares and options totaling 5,059,286 shares were excluded from the diluted net income per share computation in 2002 as the exercise price exceeded the average market price of our common stock.

### **Revenue Recognition**

Revenues are recognized when title to the product transfers to purchasers. We follow the "sales method" of accounting for revenue for oil and natural gas production, so that sales revenue is recognized on all production sold to purchasers, regardless of whether the sales are proportionate to our ownership in the property. In these instances when our sales are not proportionate to our interest, a receivable or liability is recognized only to the extent that we have an imbalance on a specific property greater than the expected remaining proved reserves. Current revenues are accrued based on expectations of actual deliveries and actual prices received. Plant revenues are recognized as product is sold, and our gathering fees are recognized as the gathering services are performed. Revenues for our oilfield management services segment are recognized as services are performed and equipment is delivered.

### **Inflation and Changes in Prices**

Our results of operations and cash flow have been, and will continue to be, affected by the volatility in oil and gas prices. Should we experience a significant increase in oil and gas prices that is sustained over a prolonged period, we would expect that there would also be a corresponding increase in oil and gas finding costs, lease acquisition costs, and operating expenses.

We market oil and gas for our own account, which exposes us to the attendant commodities risk. A significant portion of our gas production is currently sold to end-users either (i) on the spot market on a month-to-month basis at prevailing spot market prices or (ii) under long-term contracts based on current spot market prices. We normally sell our oil under month-to-month contracts to a variety of purchasers.

### **Use of Estimates and Certain Significant Estimates**

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires our management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates. Significant assumptions are required in the valuation of proved oil and gas reserves, which, as described above, may affect the amount at which oil and gas properties are recorded. It is at least reasonably possible those estimates could be revised in the near term and those revisions could be material.

### **Treasury Stock**

We may repurchase shares of common stock in stock repurchase programs. Our repurchases of shares of common stock are recorded as treasury stock at cost and result in a reduction of stockholders' equity. When treasury shares are reissued, we use a first-in first-out method and the difference between repurchase cost and reissuance price is treated as an adjustment to paid-in capital.

## NOTE 2 ACQUISITIONS AND DISPOSITIONS

On July 30, 2004, we purchased oil and gas properties located in the state of New Mexico, primarily in Lea and Eddy counties for \$239.1 million, subject to certain purchase price adjustments. The properties include both proved producing oil and gas wells and proved undeveloped leasehold mineral interests. The effective date of the acquisition was May 1, 2004. We purchased additional properties related to this acquisition during September 2004 for a purchase price of \$1.4 million, net of certain purchase price adjustments. We also recorded additional asset retirement obligations of \$1.5 million as a result of the acquisition. Pro forma information related to this acquisition has not been presented, as the effect was not material to our historical results of operations.

On August 30, 2004, we entered into an agreement to purchase approximately 170 producing wells located in the Permian Basin of West Texas for \$40 million, net of certain purchase price adjustments. Closing occurred on October 29, 2004 and had an effective date of September 1, 2004. Pro forma information related to this acquisition has not been presented, as the effect was not material to our historical results of operations.

On July 29, 2003, we exercised our option to sell our 30% interest in NGTS. At that date, we reduced the carrying value and recorded a charge to equity in earnings of affiliate of approximately \$791 thousand to state our investment at its estimated fair value. The sale closed on September 30, 2003, and we received proceeds of \$5.2 million on that date which we used to repay indebtedness. No gain or loss was recorded at the time of sale. Pro forma information related to this acquisition has not been presented, as the effect was not material to our historical results of operations.

On November 19, 2003, we acquired an 80% controlling ownership interest in Metrix, an internet-based field marketing service company, through the settlement of outstanding litigation in our favor as well as the conversion of our \$325 thousand loan to Metrix into equity of that company. As a result of the settlement, we have fully consolidated Metrix, effective December 1, 2003. Prior to this acquisition, we accounted for our approximate 32% ownership interest in Metrix as an equity investment. No goodwill was recorded on this acquisition. Pro forma information related to this acquisition has not been presented, as the effect was not material to our historical results of operations.

On March 15, 2002, we merged with Prize Energy Corp. ("Prize"), a publicly traded independent oil and gas development and production company. The transaction was accounted for by us as a purchase of Prize in accordance with the provisions of SFAS No. 141 "Business Combinations". As a result of our merger with Prize, we acquired oil and gas properties located in three of our core operating areas: the Permian Basin of West Texas and Southeast New Mexico, the onshore Gulf Coast area of Texas and Louisiana and the Mid-Continent area of Oklahoma and the Texas Panhandle. This allowed us to meet our goal of increasing reserves in geographic regions similar to our own which allows us to achieve operating synergies and production enhancements. Under the terms of the merger, we distributed 2.5 shares of common stock plus \$5.20 in cash for each Prize share outstanding. The purchase price, computed from the equity and cash consideration given at the time of the merger, was allocated to the fair value of the net assets acquired. The amount of purchase price in excess of the fair value of Prize's net assets was assigned to goodwill. We assigned the goodwill to our exploration and production segment when the purchase price allocation was finalized in June 2003. The following table

Edgar Filing: O'Neill Andrew J - Form 4

summarizes the total assumed purchase price and related final allocation to the net assets acquired (amounts in thousands) as of June 30, 2003:

Total Purchase Price:	
Fair Value of 34,062,963 shares of Magnum Hunter common stock	\$ 257,175
Cash consideration	70,851
Fair Value of Prize warrants	3,416
Total	\$ 331,442
Net Preliminary Purchase Price Allocation:	
Net purchase price	\$ 331,442
Historical net assets acquired	(148,272)
Excess purchase price	183,170
Adjustment of proved oil and gas properties to fair value	(63,915)
Adjustment of unproved oil and gas properties to fair value	(139,395)
Adjustment of gas plant to fair value	(18,856)
Write-off of historical Prize deferred financing costs	2,363
Other fair value adjustments	1,436
Imputed interest on debt due to merger	(108)
Additional deferred income taxes	91,865
Excess purchase price allocated to goodwill	\$ 56,560

During the third and fourth quarters of 2003, we divested of a number of oil and gas properties. In accordance with SFAS No. 142, we attached \$93 thousand of goodwill to the divested properties. Proceeds (net of goodwill) of approximately \$17 million were applied against the full cost pool. The remaining goodwill balance at December 31, 2004 was \$56.5 million. Also in accordance with SFAS No. 142, we performed a goodwill impairment test at December 31, 2004. Test results showed no impairment of goodwill. The goodwill acquired is not deductible for tax purposes. Historical net assets acquired in the merger were as follows (in thousands):

Current assets	\$ 78,440
Properties, plant and equipment, net	398,409
Other assets	3,093
Current liabilities	(42,626)
Long-term debt	(245,819)
Deferred income taxes	(40,677)
Other non-current liabilities	(2,548)
Historical net assets acquired	\$ 148,272

## Edgar Filing: O'Neill Andrew J - Form 4

Changes to the carrying value of goodwill during the twelve months ended December 31, 2003 and 2004, are as follows (in thousands):

Balance at December 31, 2002	\$ 50,710
Goodwill acquired	
Purchase price adjustments	5,850
Adjustment for divested properties	(93)
	56,467
Balance at December 31, 2003	56,467
Goodwill acquired	
Purchase price adjustments	
Adjustment for divested properties	
	56,467
Balance at December 31, 2004	\$ 56,467

The following summary, prepared on a pro forma basis, presents the results of operations for the year ended December 31, 2002, as if the acquisition of Prize occurred as of the beginning of the respective periods. The pro forma information includes the effects of adjustments for interest expense, depreciation, depletion and amortization, and income taxes. The pro forma results are not necessarily indicative of what actually would have occurred if the acquisition had been completed as of the beginning of each period presented, nor are they necessarily indicative of future consolidated results. Prize was included in our consolidated results of operations beginning March 1, 2002.

### Pro Forma Results of Operations (Unaudited) (in thousands of dollars, except for per share amounts)

	Year Ended December 31, 2002
Revenue	\$ 292,872
Total Operating Costs and Expenses	(219,575)
	73,297
Operating Profit	73,297
Interest Expense and Other	(60,202)
	13,095
Income before Tax	13,095
Benefit for Income Tax	892
	13,987
Net Income	\$ 13,987
Net Income Per Common Share	
Basic	\$ 0.20
Diluted	\$ 0.20

#### NOTE 3 ASSET RETIREMENT OBLIGATIONS

SFAS No. 143, "Accounting for Asset Retirement Obligations," became effective beginning January 1, 2003. SFAS No. 143 requires the recognition of a fair value liability for any legal retirement obligations associated with long-lived assets in the period in which it is incurred if a reasonable

estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over the asset's useful life. Prior to adopting SFAS No. 143 on January 1, 2003, we accounted for asset retirement obligations in accordance with SFAS No. 19.

Our long-lived assets captured under SFAS No. 143 are developed oil and gas properties, production and distribution facilities, and natural gas processing plants. Our asset retirement obligations include plugging, abandonment, decommission, and remediation costs. We have included \$1.2 million of our asset retirement obligations in other current liabilities at December 31, 2004.

The following is a reconciliation of the asset retirement obligation liability at December 31, 2004 (in thousands):

Beginning balance at January 1, 2004	\$ 32,489
Liabilities incurred	7,260
Liabilities settled	(761)
Liabilities sold/disposed	(1,120)
Accretion expense	2,941
Change in retirement cost estimates	468
	<hr/>
Ending balance at December 31, 2004	\$ 41,277
	<hr/>

The following pro forma data summarizes our net income and net income per share as if we had adopted SFAS No. 143 on January 1, 2002. The associated pro forma asset retirement obligation was \$16.9 million on January 1, 2002, and an additional asset retirement obligation of \$12.9 million would have been recorded at March 1, 2002, in conjunction with the Prize merger. The balance at December 31, 2002 would have been \$30.4 million. Values in the pro forma summary are in thousands, except for the per share amounts.

	Year Ended December 31,		
	2004	2003	2002
	<hr/>	<hr/>	<hr/>
Net income, as reported	\$ 103,573	\$ 26,117	\$ 15,522
Pro forma adjustment to reflect retroactive adoption of SFAS No. 143, net of related tax effects		(399)	1
	<hr/>	<hr/>	<hr/>
Pro forma net income	\$ 103,573	\$ 25,718	\$ 15,523
	<hr/>	<hr/>	<hr/>
Earnings per share:			
Basic as reported	\$ 1.35	\$ 0.39	\$ 0.25
	<hr/>	<hr/>	<hr/>
Basic pro forma	\$ 1.35	\$ 0.38	\$ 0.25
	<hr/>	<hr/>	<hr/>
Diluted as reported	\$ 1.31	\$ 0.39	\$ 0.25
	<hr/>	<hr/>	<hr/>
Diluted pro forma	\$ 1.31	\$ 0.38	\$ 0.25
	<hr/>	<hr/>	<hr/>

**NOTE 4 RELATED PARTY TRANSACTIONS**

At December 31, 2004 and 2003, our note receivable from the Magnum Hunter 401(k) Employee Stock Ownership Plan (KSOP) was \$6.2 million and \$6.1 million, respectively. The purpose of the loan is to allow the KSOP to purchase Magnum Hunter common stock on the open market. The loan is interest free, due December 31, 2005, and is secured by shares of the company's common stock which have not been earned by participants in the KSOP. At December 31, 2004 and 2003, the number of unearned shares in the KSOP were 880,083 and 1,012,203, respectively. The unearned shares and their corresponding costs were reflected on our consolidated balance sheets as reductions to stockholders' equity.

There are no loans or extensions of credit to directors and executive officers of Magnum Hunter as of December 31, 2003 or 2004.

**NOTE 5 DEBT**

Notes payable and long-term debt at December 31, 2004 and 2003 consisted of the following (in thousands):

	<u>2004</u>	<u>2003</u>
<b>Long-Term Debt:</b>		
Bank debt under revolving credit agreements due May 2, 2007, 3.92% at December 31, 2004	\$ 320,000	\$ 165,000
Capital lease obligations, 5.58% at December 31, 2004	5,500	7,500
Senior unsecured notes, due March 15, 2012, 9.6%	195,000	300,000
Floating rate convertible senior notes, due December 15, 2023 2.49% at December 31, 2004	125,000	125,000
Production payment liability, non-recourse		12
	<u>645,500</u>	<u>597,512</u>
Less current portion	2,458	2,009
	<u>643,042</u>	<u>595,503</u>
<b>Total Long-Term Debt</b>	<b>\$ 643,042</b>	<b>\$ 595,503</b>

The following table presents the approximate annual maturities of debt:

	<u>(in thousands)</u>
2005	\$ 2,458
2006	807
2007	322,235
Thereafter	320,000
	<u>645,500</u>
<b>Total</b>	<b>\$ 645,500</b>

We have a Senior Bank Credit Facility ("Facility"), which provides for total borrowings of \$750 million, on which our borrowing base was limited to \$525 million at December 31, 2004. The level of the borrowing base is dependent on the valuation by the lenders of the assets pledged, which are primarily oil and gas reserves.

## Edgar Filing: O'Neill Andrew J - Form 4

During 2004, we amended our Facility in April, July, and October to ultimately increase the borrowing base to \$525 million, up \$270 million from our previous \$255 million borrowing base. We also extended the expiration date of the Facility to May 2, 2007. The amended facility allowed us to use proceeds from our secondary common stock offering to redeem and retire \$105 million in principal of our 9.6% Senior Notes outstanding. We used the increased borrowing base to fund the costs of issuing our Convertible Notes and to fund the acquisitions of oil and gas properties in New Mexico and West Texas. The Facility provides for both a LIBOR and "Base rate" (Prime) interest rate option. At December 31, 2004, we had no borrowings under the Base rate option and \$320 million outstanding at LIBOR + 1.50%. We also have a letter of credit posted against our borrowing base of \$2.5 million. While we have no actual borrowings against this letter of credit, it reduces our funds available under the borrowing base. The letter of credit was posted to cover any plugging and abandonment costs, as well as potential environmental remediation costs after the property is plugged, of a property previously owned by Prize. We have entered non-binding arbitration to attempt to eliminate the need for this letter of credit. At December 31, 2004, we had available credit under this Facility of \$202.5 million.

Our Facility includes covenants, the most restrictive of which requires maintenance of a funded debt to EBITDA ratio and an interest coverage ratio, as defined in the loan agreement. We were in compliance with the covenants in 2003 and 2004. We expect to be able to comply with these covenants in the future. The lenders to the Facility must approve all dividends paid on common stock, other than those paid in common stock, and have approved both the redemption of our 10% Senior Notes, the partial redemption of our 9.6% Senior Notes and the issuance of our Convertible Notes.

On a semi-annual basis, our borrowing base under our Facility is redetermined by the financial institutions who have committed to the company based on their review of our pledged proved oil and gas reserves and other assets. If the outstanding balance on the Facility exceeds the redetermined borrowing base, we must repay the excess over the next six months. The last redetermination date had an effective date of June 30, 2004, and was completed on October 15, 2004. This redetermination increased our borrowing base by \$45 million. Our next redetermination date will have an effective date of December 31, 2004, and has an estimated completion date of no later than May 9, 2005.

On March 15, 2002, Canvasback entered into a \$10 million revolving credit agreement with a financial institution. The credit agreement provided for both LIBOR and prime based interest rate options. On June 30, 2002, we converted the \$5.8 million balance under this agreement to a term loan due March 7, 2004. Proceeds from the loan were used to purchase \$5.8 million of our 10% Senior Notes from Magnum Hunter, which had been purchased by Magnum Hunter during 2001 and held for investment. These 10% Senior Notes, along with \$4.7 million in 10% Senior Notes contributed to Canvasback from Bluebird, served as the only collateral for this loan. We borrowed additional funds of \$1.2 million during the fourth quarter of 2002, increasing the balance to \$7 million. This loan was non-recourse to Magnum Hunter. In conjunction with the redemption of our 10% Senior Notes during 2003, this loan was paid in full and the agreement was terminated.

On January 15, 2002, we entered into a sale-leaseback transaction on three newly-constructed production platforms and associated pipelines located in the Gulf of Mexico that had already been placed into service. We received total proceeds of \$11.2 million in new funding, which we used for general corporate purposes. The production platforms are being leased from a syndicate group of lenders over terms from three to five years at a cost of funds based on LIBOR, yielding a weighted average rate of 5.58% at December 31, 2004.

## Edgar Filing: O'Neill Andrew J - Form 4

On May 29, 1997, we completed a private placement of \$140 million in unsecured 10% Senior Notes, due June 1, 2007. During 2003, we paid \$145.2 million to redeem the \$140 million in principal of our 10% Senior Notes. This redemption was funded by borrowings under our Facility as well as the issuance of \$125 million in Convertible Notes during December 2003. We paid approximately \$5.2 million in premiums to redeem these notes. Of the notes redeemed, Canvasback received approximately \$10.9 million in principal and received premiums of approximately \$273 thousand.

We completed a private placement of \$300 million in unsecured 9.6% Senior Notes on March 15, 2002. The 9.6% Senior Notes are due March 15, 2012, with interest payable semi-annually on March 15 and September 15. We used the funds received to: i) retire outstanding indebtedness under the Prize commercial bank credit facility, ii) pay fees related to the issuance of the new Senior Notes, and iii) for general corporate purposes. On August 27, 2004, we redeemed \$105 million in principal of our 9.6% Senior Notes at a redemption price of 109.6% of par. We paid the holders of these redeemed notes \$115.1 million plus accrued and unpaid interest of \$4.5 million. We used a portion of the proceeds from our secondary offering to fund this redemption. We recorded \$12.3 million in costs associated with this redemption comprised of \$10.1 million in premiums and \$2.2 million in unamortized deferred financing fees which were written off.

During December 2003, we issued \$125 million in face value of Convertible Notes. These Convertible Notes bear interest equal to the three-month LIBOR, to be adjusted quarterly. The rate on the Convertible Notes was 2.49% at December 31, 2004. They are convertible into a combination of cash and Magnum Hunter common stock upon certain events. The initial conversion price is \$12.19, subject to adjustment under certain conditions. The Convertible Notes are due December 2023, but holders of these notes have the right to require us to repurchase all or a portion of the notes on December 15, 2008, 2013, and 2018. If repurchase is elected, we will repurchase these notes for an amount of cash equal to 100% of the principal plus accrued but unpaid interest up to but not including the date of repurchase. The repurchase notice given by each holder electing repurchase may be withdrawn by the holder by written notice of withdrawal delivered prior to the close of business on the date of repurchase. The proceeds from these Convertible Notes were used to reduce borrowings under the Facility by approximately \$25 million.

Holders may surrender Convertible Notes for conversion into cash and shares of our common stock prior to the Convertible Notes' maturity date in the following circumstances: i) during any calendar quarter commencing after the issuance of the Convertible Notes, if our common stock price for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the calendar quarter preceding the quarter in which the conversion occurs is more than 110% of the conversion price per share of our common stock in effect on that 30<sup>th</sup> trading day; ii) if we have called the particular Convertible Notes for redemption and the redemption has not yet occurred; iii) during the five trading day period after any five consecutive trading day period in which the trading price of \$1,000 principal amount of the Convertible Notes for each day of such five-day period was less than 95% of the product of the closing sale price of our common stock on that day multiplied by 82.0345 (the "Conversion Rate"); or iv) upon the occurrence of specified corporate transactions.

Upon the occurrence of the circumstances described above, holders may convert any outstanding notes into cash and shares of our common stock at an initial conversion price per share of \$12.19. Subject to certain exceptions, at the time notes are tendered for conversion, the value (the "Conversion Value") of the cash and shares of our common stock, if any, to be received by a holder converting

\$1,000 principal amount of the notes will be determined by multiplying the Conversion Rate by the ten-day average closing stock price of our common stock. We will deliver the Conversion Value to holders as follows: i) an amount in cash (the "Principal Return") equal to the lesser of (a) the Conversion Value and (b) the principal amount of the notes to be converted and, if the Conversion Value is greater than the Principal Return, ii) an amount in shares equal to the Conversion Value less the Principal Return ("the Net Share Amount"). The number of Net Shares to be paid will be determined by dividing the Net Share Amount by the ten day average closing stock price of our common stock.

Metrix has a \$500 thousand revolving credit facility with a lender. This facility matures on December 16, 2005 and is governed by a borrowing base. Magnum Hunter is a guarantor to this facility. As of December 31, 2004, there were no borrowings outstanding under this facility.

In November 1996, we entered into a production payment conveyance. We received a production payment amount of \$750 thousand and agreed to make payments of up to 50% of the monthly net revenue proceeds received from certain oil and gas properties. The balance owed under the conveyance was \$12 thousand at December 31, 2003 and was paid in full in 2004.

#### NOTE 6 INCOME TAXES

We account for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes", which requires the recognition of a liability or asset, net of a valuation allowance, for the deferred tax consequences of all temporary differences between the tax bases and the reported amounts of assets and liabilities, and for the future benefit of operating loss carryforwards. The following is a reconciliation of income tax expense reported in the statement of operations (in thousands):

	2004	2003	2002
	<u>          </u>	<u>          </u>	<u>          </u>
Income tax expense at statutory rates			
Federal tax expense	\$ 55,766	\$ 14,550	\$ 4,847
State tax expense	1,912	229	403
Adjustment of deferred state tax rate	(4,811)		
Change in valuation allowance	2,042		(7,100)
Other	850	434	259
	<u>          </u>	<u>          </u>	<u>          </u>
Tax expense (benefit)	\$ 55,759	\$ 15,213	\$ (1,591)
	<u>          </u>	<u>          </u>	<u>          </u>

IV-83

## Edgar Filing: O'Neill Andrew J - Form 4

The tax effects of significant temporary differences and carryforwards are as follows (in thousands):

	December 31,	
	2004	2003
Property and equipment, including intangible drilling costs	\$ (236,580)	\$ (184,713)
Plugging costs and other	(1,730)	
	\$ (238,310)	\$ (184,713)
Allowance for doubtful accounts	\$ 1,294	\$ 1,105
Depletion carryforwards	1,147	1,200
Derivative instruments	7,175	9,570
Alternative minimum tax credit	278	
Employee stock options	877	
Operating loss and other carryforwards	45,849	40,073
Other	376	28
	\$ 56,996	\$ 51,976
Valuation allowance on state NOL carryforwards	(2,042)	
	\$ (183,356)	\$ (132,737)

During 2004, an adjustment was made to lower deferred state income taxes payable by \$4.8 million to reflect a change in our deferred state income tax rate from 2.875% to 1.2%, due to an increase in income not subject to state income taxes. In addition, during 2004, a valuation allowance of \$2 million was established for state NOL carryforwards, due primarily to a five-year state carryforward limitation, and the likelihood that these NOL's would not be realized before expiration.

Magnum Hunter and our subsidiaries have net operating loss carryforwards of approximately \$113.8 million that expire, if unused, in years 2012 through 2023. Current tax laws and regulations relating to specified changes in ownership limit the utilization of our net operating loss and tax credit carryforwards. A change in ownership of greater than 50% of a corporation within a three-year period causes the annual limitations to be placed in effect. Such a change is deemed to have occurred February 3, 1999 in connection with the purchase of preferred stock by ONEOK Resources Company, which has subsequently been either redeemed or converted to common stock. Approximately \$51.4 million of the net operating losses are subject to a limitation of \$7.8 million per year. We also have \$9.5 million of net operating losses subject to a limitation of \$3.7 million per year as a result of the merger with Prize Energy Corp. on March 15, 2002. In addition, we have depletion carryforwards of \$3.2 million with no expiration period.

### NOTE 7 STOCKHOLDERS' EQUITY

#### *Preferred Stock*

Shares of preferred stock may be issued in such series, with such designations, preferences, stated values, rights, qualifications or limitations as determined solely by the Board of Directors. Of the 10,000,000 shares of \$.001 par value preferred stock we are authorized to issue, 216,000 shares have been designated as Series A Preferred Stock, 1,000,000 shares have been designated as 1996 Series A

convertible preferred stock and 50,000 shares have been designated as 1999 Series A 8% convertible preferred stock. Thus, 8,734,000 preferred shares have been authorized for issuance but have not been issued nor have the rights of these preferred shares been designated. No dividends can be paid on the common stock until the dividend requirements of the preferred shares have been satisfied. The preferred shareholders are not entitled to vote except on those matters in which the consent of the holders of preferred stock is specifically required by Nevada law. If we were to liquidate prior to payment of the full dividend requirements on the preferred stock, the preferred stock would receive a liquidation preference from the liquidation proceeds. On liquidation, holders of all series of the preferred stock would be entitled to receive the par value, \$.001 per share, in preference to the common stock shareholders.

Dividend payments and preferential rights to Series A preferred shareholders are tied to wells that have been plugged and abandoned. The liquidation value of the Series A Preferred Stock is \$216.

On December 23, 1996, we issued 1,000,000 shares of new Series A Preferred Stock, known as the 1996 Series A convertible preferred stock, in a private placement, resulting in net proceeds after offering costs of \$9.3 million. Dividends of \$438 thousand and \$875 thousand were declared in 2000 and 1999, respectively. On June 30, 2000 the holders of the 1996 Series A convertible preferred stock agreed to exchange the convertible preferred securities for 900 thousand warrants to purchase restricted common shares of our stock at an exercise price of \$5.25 per share with an expiration date of June 3, 2003 and payment of \$10 million. The convertible preferred shares are currently listed as issued but held by Canvasback as of December 31, 2004.

### Warrants

The following is a summary of warrant activity for the periods ended December 31, 2004, 2003 and 2002:

		2004		2003		2002	
		Number of Warrants	Weighted Average Exercise Price	Number of Warrants	Weighted Average Exercise Price	Number of Warrants	Weighted Average Exercise Price
Outstanding	Beginning of Year	7,228,457	\$ 15.00	7,873,206	\$ 14.32	644,749	\$ 6.75
	Issued					11,500,270	12.80
	Exercised			(644,749)	6.75	(578)	9.12
	Redeemed						
	Expired					(4,271,235)	9.09
Outstanding	End of Year	7,228,457	\$ 15.00	7,228,457	\$ 15.00	7,873,206	\$ 14.32

On November 27, 2000, the Board of Directors allowed a total of 644,749 warrants held by certain key officers and directors with an exercise price of \$6.50 per share and an expiration date of June 30, 2000, to be exchanged for an equal number of new warrants with an exercise price of \$6.75 per share expiring on December 31, 2003. The exercise price of the new warrants was fair market value on the date of the new grant. All of these warrants were exercised during 2003.

On December 5, 2001, we announced that a distribution of one warrant for every five shares of common stock owned on January 10, 2002. 7,228,457 warrants were distributed on March 21, 2002.

Each new warrant entitles the holder to purchase one share of common stock at \$15. The warrants will expire three years from the date of distribution, unless extended by the Board of Directors.

We also converted outstanding Prize warrants into Magnum Hunter stock warrants pursuant to the merger (see Note 2). We distributed 4,271,813 of these warrants on March 15, 2002, at a weighted average exercise price of \$9.09. These warrants expired in June and November 2002.

### ***Common Stock***

We have a Shareholder Rights Plan, under which the Rights initially represent the right to purchase one one-hundredth of a share of 1998 Series A Junior Participating Preferred Stock for \$35.00 per one one-hundredth of a share. The Rights become exercisable only if a person or a group acquires or commences a tender offer for 15% or more of our common stock. Until they become exercisable, the Rights attach to and trade with our common stock. The Rights expire January 20, 2008.

We have not previously paid any cash dividends on our common stock and we do not anticipate paying cash dividends on our common stock in the foreseeable future. We intend to reinvest all available funds for the development and growth of our business. In addition, our Facility and the indenture governing our 9.6% Senior Notes restrict the payment of cash dividends on our common stock.

On May 1, 2002, our Board of Directors announced an expansion of our existing stock repurchase program established in June 2001. Under this program, we and our affiliates are authorized to repurchase up to two million shares of our common stock. On October 17, 2002, our Board of Directors approved a new three million share repurchase program in addition to our June 2001 program. At December 31, 2004, approximately 4.2 million shares had been repurchased under these two programs, and approximately 818 thousand shares remained available for repurchase.

On March 15, 2002, we issued 34.1 million shares at a value of \$257.2 million pursuant to our merger with Prize. See Note 2 for further discussion on the Prize merger.

On June 30, 2004, we sold 15 million shares of Magnum Hunter common stock at \$10.25 per share under a previously filed universal shelf registration statement. The proceeds from this issuance were \$147.2 million, net of offering costs. We also granted the underwriters an option to purchase an additional 2.25 million shares to cover over-allotments, which they exercised on July 2, 2004. The net proceeds from this sale were approximately \$22.1 million. We used proceeds from these issuances to finance a portion of our acquisition of oil and gas properties in the state of New Mexico (see Note 2) and to redeem a portion of our 9.6% Senior Notes (see Note 5).

We issued 2.1 million, 270 thousand and 985 thousand shares pursuant to employee stock option exercises for proceeds of \$10.4 million, \$1.2 million and \$3.6 million during 2004, 2003 and 2002, respectively. Upon the exercise of warrants, we issued 548 thousand treasury shares for proceeds of \$3.4 million during 2003. Of the treasury shares issued for warrants in 2003, 37 thousand shares were issued in a cashless exercise of 134 thousand warrants. No warrants were exercised in 2004.

Our KSOP purchased 225 thousand, 486 thousand and 532 thousand shares at costs of \$2.3 million, \$2.7 million and \$3.7 million during 2004, 2003 and 2002, respectively. During the same periods, the KSOP released shares totaling 357 thousand, 231 thousand and 244 thousand to participants. During 2004, 2003 and 2002, we made new loans to the KSOP of \$2.3 million, \$2.7 million

and \$3.7 million and the KSOP repaid loan amounts of \$2.2 million, \$1.5 million, and \$1.3 million, respectively. Of the 2004 repayments, \$1.3 million represented our contribution of 223 thousand shares to the plan. Of the 2003 repayments, \$1.1 million represented our contribution of 172 thousand shares to the KSOP plan. Additionally, in 2002, we contributed 158 thousand shares to our 401(K) plan.

**NOTE 8 SUPPLEMENTAL CASH FLOW INFORMATION**

During 2004, we contributed 223 thousand shares of our common stock valued at a cost of \$1.3 million to our KSOP plan. Interest paid on our outstanding indebtedness was \$49.7 million. Tax payments in 2004 were \$2.6 million.

During 2003, we contributed 172 thousand shares of our common stock valued at a cost of \$1.1 million to our KSOP plan. Interest paid on our outstanding indebtedness was \$55.2 million. Tax refunds received in 2003 were \$8.1 million, net of payments.

During 2002, we contributed 158 thousand shares at a cost of \$867 thousand to our KSOP plan. Interest paid on our outstanding indebtedness was \$48.4 million. Taxes paid in 2002 were \$666 thousand. We also completed the Prize merger by issuing 34.1 million shares of common stock valued at \$257.2 million and 4.3 million warrants valued at \$3.4 million.

**NOTE 9 ENVIRONMENTAL ISSUES**

We may become subject to certain liabilities as they relate to environmental clean up of well sites or other environmental restoration procedures as they relate to the drilling of oil and gas wells and the operation thereof. In our acquisition of existing or previously drilled well bores, we may not be aware of what environmental safeguards were taken at the time such wells were drilled or during the time that such wells were operated. Should it be determined that a liability exists with respect to any environmental clean up or restoration, the liability to cure such a violation would most likely fall upon the company. In certain acquisitions, we have received contractual warranties that no such violations exist, while in other acquisitions, we have waived our rights to pursue a claim for such violations from the selling party. No claim has been made nor has a claim been asserted. We are not aware of the existence of any material liability relating to any environmental clean-up, restoration or the violation of any rules or regulations relating thereto.

**NOTE 10 COMMITMENTS AND CONTINGENCIES**

We have certain lease agreements for the use of office space, office equipment, and vehicles. The Irving, Texas office space lease extends through November 2005, with an option to renew the lease for a three-year term, and the Grapevine, Texas office lease extends through December 2005. The various office equipment leases extend until 2007. The various vehicle leases extend until 2012. The leases have

been classified as operating leases. The following is a schedule by years of future minimum lease payments required under the operating lease agreements (in thousands):

Year Ended December 31:	
2005	\$ 2,381
2006	1,129
2007	950
2008	751
2009	559
Thereafter	762
	Total Minimum Payments Required
	\$ 6,532

Rental expense was \$2.3 million, \$2.3 million, and \$2.2 million for 2004, 2003 and 2002, respectively.

In the past we have provided trade guarantees on behalf of an unconsolidated affiliate which has since been sold. The last of these guarantees expired in July 2003. On February 18, 2005 our 40% owned subsidiary, Apple Tree Holdings, LLC entered into a \$20.6 million construction loan agreement ("Construction Loan"). The Construction Loan provides financing for the construction of a processing plant, natural gas lateral, carbon dioxide line and related infrastructure in Huerfano County, Colorado. The Construction loan bears interest at either LIBOR plus 2.25% or a base rate plus 1.25% and will mature no later than July 31, 2006. We have provided a guaranty to the lender for this Construction Loan. In return for our guaranty, we received an up-front cash payment as well as 55% distribution of cash flows from the entity until certain financial tests are met. In the event that the Construction Loan goes into default and Magnum Hunter has to pay on the guaranty, we will have recourse against the project and related subsidiaries.

#### **NOTE 11 FINANCIAL INSTRUMENTS AND CONCENTRATION OF CREDIT RISK**

Financial instruments that subject Magnum Hunter to credit risk consist principally of accounts and notes receivable. The receivables are primarily from companies in the oil and gas business or from individual oil and gas investors. These parties are primarily located in the Southwestern region of the United States. No single receivable is considered to be sufficiently material as to constitute a concentration. During the year ended December 31, 2004, we recorded \$841 thousand in additional allowances for doubtful accounts. During the year ended December 31, 2003 we recorded \$231 thousand in additional allowances for doubtful accounts. We do not ordinarily require collateral, but in the case of receivables for joint operations, we often have the ability to offset amounts due against the participant's share of production from the related property. We believe the allowance for doubtful accounts at December 31, 2004 is adequate.

Under our hedging programs, to the extent we receive the spread between the contract floor and the index price applied to related contract volumes, we have a credit risk in the event of nonperformance of the counterparty to the agreement. We do not anticipate any material impact to our results of operations as a result of nonperformance by such parties.

Management estimates the market values of notes receivable and payable based on expected cash flows. At December 31, 2004 and 2003, we provided a reserve for the carrying value of a note

receivable of \$1.2 million. After establishing this reserve, management believes those market values approximate carrying values at December 31, 2004 and 2003. The market values of equity investments are based upon quoted market prices (see Note 1). At December 31, 2004, the fair value of our debt was equal to its carrying value, except for the 9.6% Senior Notes and Convertible Notes. The fair value of the 9.6% Senior Notes was \$221.3 million and the fair value of the Convertible Notes was \$151.7 million.

## NOTE 12 COMMODITY DERIVATIVES AND HEDGING ACTIVITIES

### *Crude Oil and Natural Gas Hedges*

Periodically, we enter into futures, options, and swap contracts to mitigate the effects of significant fluctuations in crude oil and natural gas prices. At December 31, 2004, we had open contracts with the following terms:

<b>Commodity</b>	<b>Type</b>	<b>Volume/Day</b>	<b>Duration</b>	<b>Wtd. Avg. Price</b>
Natural Gas	Collar	60,000 MMBTU	Jan 05 - Dec 05	\$4.21 - \$6.85
Natural Gas	Swap	20,000 MMBTU	Jan 05 - Dec 05	\$6.25
Natural Gas	Collar	20,000 MMBTU	Jan 06 - Dec 06	\$5.25 - \$6.30
Crude Oil	Swap	1,000 BBL	Jan 05 - Dec 05	\$34.90
Crude Oil	Collar	1,000 BBL	Jan 05 - Dec 05	\$35.00 - \$55.00
Crude Oil	Collar	1,000 BBL	Jan 06 - Dec 06	\$30.00 - \$35.85

At December 31, 2004, based on future market prices, the fair value of our open commodity derivative contracts were as follows (in thousands):

<i>Derivative Assets</i>	
Natural gas collars	\$ 207
<hr/>	
Total derivative assets	\$ 207
<i>Derivative Liabilities</i>	
Natural gas collars	\$ (13,847)
Natural gas swaps	(528)
Crude oil collars	(2,343)
Crude oil swaps	(3,310)
<hr/>	
Total derivative liabilities	\$ (20,028)
<hr/>	
Net derivative liabilities	\$ (19,821)
<hr/>	

In conjunction with the Prize merger in March 2002, we acquired ten natural gas derivative contracts for the periods April 2002 through December 2004. We also acquired seven crude oil derivative contracts for the periods March 2002 through December 2003. We recorded a derivative asset of \$7.6 million to reflect the fair value of these contracts at the merger date. In June 2002, we closed one of the derivative contracts procured in the Prize merger, realizing proceeds of \$3.6 million, which were charged against derivative assets. The net derivative balance of \$4.0 million was amortized as a charge to other non-cash hedging adjustments over the remaining life of the derivative contracts.

## Edgar Filing: O'Neill Andrew J - Form 4

At December 31, 2004, we had five crude oil derivatives and seven natural gas derivatives, which are categorized in the tables above. The net fair value of these derivatives was \$19.8 million, recognized as a \$207 thousand derivative asset and a \$20.0 million derivative liability. For the year ended December 31, 2004, the consolidated statement of operations includes a loss of \$21.8 million related to crude oil derivatives and a loss of \$23.2 million related to natural gas derivatives, including amounts reclassified out of other comprehensive income. The consolidated statement of operations also included a non-cash hedging ineffectiveness gain of \$332 thousand related to crude oil and natural gas derivatives and a non-cash gain of \$792 million related to the amortization of hedge contracts acquired in the Prize merger. It is estimated at this time that \$8.8 million of other comprehensive loss will be reclassified to the consolidated statement of operations during the next 12 months.

Net losses related to crude oil and natural gas derivative transactions for the years ended December 31, 2004, 2003 and 2002 were \$43.9 million, \$72.4 million and \$9.9 million, respectively.

### NOTE 13 STOCK COMPENSATION PLANS

We have four stock compensation plans for our employees and directors, (i) the Magnum Hunter Resources 401(k) Employee Stock Ownership Plan, (the "KSOP"), (ii) the Magnum Hunter Resources, Inc. 1996 Incentive Stock Option Plan (the "1996 Option Plan"), and (iii) the Magnum Hunter Resources, Inc. 2002 Incentive Stock Option Plan (the "2002 Option Plan"). In addition, we made non-incentive stock option grants in 2004, 2003 and 2002.

#### KSOP

We established an ESOP and a related trust in 1996 as a long-term benefit for our employees. On January 1, 2001, the ESOP was merged with the 401(k) plan to form the KSOP. Under terms of the KSOP, eligible participants may choose to make elective deferred contributions of not less than 1% or more than 15% of their annual compensation, limited in combination with the 401(k) plan to the maximum allowable per year by the Internal Revenue Code. Company contributions to the KSOP are made on a discretionary basis. It is also our intent to invest all employer contributions in our common stock. All employees who have reached the age of 21 and have one year of service, are eligible to participate in the plan. Shares purchased by the KSOP with loans from the company are released to participants as company contributions and participant salary deferrals are made and the related loans are repaid. We have no repurchase obligations with respect to released shares.

During 2004, we loaned the KSOP \$2.3 million to purchase 224,600 shares of our common stock on the open market at an average price of \$10.06 per share. During 2004, employees purchased 133,638 shares of the KSOP's unreleased shares at an average price of \$6.04 per share through salary deferrals. Employee purchases totaled \$807 thousand, which the KSOP used to repay that portion of its outstanding loan, and 133,638 shares were allocated among the Plan participants. We contributed \$1.3 million to the KSOP in December 2004 as a discretionary contribution under the Plan. The KSOP then repaid that portion of its outstanding loan and 223,081 shares were allocated among participants.

During 2003, we loaned the KSOP \$2.7 million to purchase 485,622 shares of our common stock on the open market at an average price of \$5.58 per share. During 2003, employees purchased 58,797 shares of the KSOP's unreleased shares at an average price of \$6.46 per share through salary deferrals. Employee purchases totaled \$380 thousand, which the KSOP used to repay that portion of its outstanding loan, and 58,797 shares were allocated among the Plan participants. We contributed

\$1.1 million to the KSOP in December 2003 as a discretionary contribution under the Plan. The KSOP then repaid that portion of its outstanding loan and 171,868 shares were allocated among participants.

During 2002, we loaned the KSOP \$3.7 million to purchase 532,400 shares of our common stock on the open market at an average price of \$6.86 per share. During 2002, employees purchased 86,147 shares of the KSOP's unreleased shares at an average price of \$5.50 per share through salary deferrals. Employee purchases totaled \$473 thousand, which the KSOP used to repay that portion of its outstanding loan, and 86,147 shares were allocated among the Plan participants. We contributed \$867 thousand to the KSOP in December 2002, as a discretionary contribution under the Plan. The KSOP then repaid that portion of its outstanding loan and 157,659 shares were allocated among participants.

The KSOP loan is interest-free and due December 31, 2005. The loan was secured by 880,083 shares and 1,012,203 shares of our common stock at December 31, 2004 and 2003, respectively.

As required under Statement of Position 93-6 "Employers Accounting for Employee Stock Ownership Plans", compensation expense is recorded for shares committed to be released to employees based on the fair market value of those shares when they are committed to be released. The difference between cost and the fair market value of the committed to be released shares is recorded in additional paid-in-capital. Unreleased shares held by the KSOP are excluded from the calculation of earnings per share.

The KSOP shares are summarized as follows:

	December 31,	
	2004	2003
Allocated shares	1,289,981	1,072,128
Unreleased shares	880,083	1,012,203
<b>Total KSOP shares</b>	<b>2,170,064</b>	<b>2,084,331</b>
Fair value of unreleased shares at December 31, 2004 and 2003, respectively	\$ 11,353,071	\$ 9,626,051

The KSOP expense for the years ending December 31, 2004, 2003 and 2002, was \$3.6 million, \$1.6 million, and \$997 thousand, respectively.

## Stock Option Plans

### *Incentive Stock Option Plan*

We established this plan beginning April 1, 1996. It is governed by Section 422 of the Internal Revenue Code, and Section 16(b) of the Securities Exchange Act of 1934. This stock option plan covers 1,200,000 shares of our common stock. Eligibility is limited to employees and directors of Magnum Hunter and our subsidiaries. The actual selection of grantees is made by the Board of Directors. The term of the individual option grants, while at the discretion of the Board, was five years. All options granted in 1996 were fully vested and exercisable when granted. The exercise price was fair market value at the date of each grant.

*Non-Incentive Stock Option Grants*

During 2002, the Board granted 2,059,750 new stock options to employees at a weighted average price of \$5.61 per share, of which 20% vested at the date of grant, with the balance vesting an additional 20% per year on the anniversary date, with a weighted average term of 9.9 years. The exercise price was the fair market value on the date of grant.

On June 20, 2003, the Board granted 999,260 new stock options to employees as part of the 2003 compensation package. These options carry an exercise price of \$5.92 and were fully vested on December 31, 2003. They will expire June 20, 2006. During 2003, we also issued 113,000 options to certain employees and board members. These options carry a weighted average exercise price of \$5.675 and have a weighted average remaining life of 8.2 years.

On July 1, 2004, the Board granted 1,336,500 new stock options to employees as part of the 2004 compensation package. These options carry an exercise price of \$10.48 and were unvested on December 31, 2004. They will expire July 1, 2009. During 2004, we also issued 116,500 options to certain employees and board members. These options carry a weighted average exercise price of \$9.70 and have a weighted average remaining life of 6.39 years.

The following is a summary of stock option activity under the Option Plans:

	2004		2003		2002	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding Beginning of Year	6,740,764	\$ 6.36	6,044,800	\$ 6.37	5,217,584	\$ 6.22
Granted	1,453,000	10.41	1,112,260	5.90	2,059,750	5.61
Exercised	(2,128,412)	4.90	(269,862)	4.46	(983,834)	3.71
Cancelled	(127,250)	6.28	(146,434)	6.58	(248,700)	7.47
Outstanding End of Year	5,938,102	\$ 7.88	6,740,764	\$ 6.36	6,044,800	\$ 6.37
Exercisable End of Year	3,483,419	\$ 7.29	4,624,614	\$ 6.21	2,775,770	\$ 6.04

IV-92

## Edgar Filing: O'Neill Andrew J - Form 4

The following is a summary of stock options outstanding at December 31, 2004:

Exercise Price	Number of Options Outstanding	Weighted Average Remaining Contractual Life (Years)	Number of Exercisable Options
5.01	46,000	7.74	26,000
5.20	9,000	7.58	3,000
5.23	2,600	7.75	
5.38	1,190,084	7.69	555,851
5.45	100,000	7.72	80,000
5.46	3,000	8.15	
5.61	1,800	8.22	
5.82	3,000	7.66	1,800
5.92	547,128	1.47	547,128
6.625	8,000	0.56	8,000
7.20	3,000	8.42	
7.51	12,000	7.30	4,000
7.55	88,700	7.21	46,500
7.57	15,000	7.42	9,000
7.75	5,000	7.22	3,000
7.90	6,000	8.48	
7.9375	1,169,540	5.94	1,169,540
7.95	10,000	8.74	4,000
8.44	1,254,500	6.95	979,600
8.50	8,000	6.67	4,000
9.19	30,000	9.17	6,000
9.3125	20,000	0.97	20,000
10.48	1,378,250	4.50	
11.08	20,000	6.25	16,000
12.00	1,000	1.05	
12.89	6,500	4.88	
	5,938,102	5.84	3,483,419

Effective January 1, 2003, we adopted the prospective method for expensing stock option grants under SFAS No. 148 and SFAS No. 123. For the year ended December 31, 2004, we recorded expense of \$768 thousand for our current year's grants. For grants made prior to January 1, 2003, we continue to follow the disclosures only portion of SFAS No. 123 and continue to apply the provisions of APB No. 25, which applies the intrinsic value method of accounting for stock-based compensation. See Note 1 for disclosure of pro forma earnings assuming adoption of SFAS No. 123.

### *Deferred Compensation Plan*

In March 2003, the company implemented and adopted the 2003 Bonus Deferral Plan. This plan allows eligible participants to defer all or a portion of their annual bonuses until a later date. The Compensation Committee of the Board of Directors determines the participants who are eligible to make deferral elections under the plan. The bonuses that are subject to the plan are those bonuses

determined by or under the authority of the Board of Directors and are based upon the performance of the company during a fiscal year. The amount to be deferred, as specified by any participant, shall be invested solely in common stock of the company. Participants may designate the date on which shares of common stock covered by a deferral election shall be distributed, provided that such distribution date is at least twelve months after the date such deferral election was made. During 2003, we purchased approximately 53 thousand shares at a cost of \$295 thousand, contributed approximately 18 thousand treasury shares with a market value of \$100 thousand, and released approximately 36 thousand shares of participants who elected not to defer under the plan. We were holding approximately 34 thousand shares in the plan at December 31, 2003. During 2004, no activity occurred in the plan; therefore, we were holding approximately 34 thousand shares in the plan at December 31, 2004.

**NOTE 14 EMPLOYMENT CONTRACTS AND TERMINATION OF EMPLOYMENT AND CHANGE-IN-CONTROL ARRANGEMENTS**

Mr. Gary C. Evans, Mr. Richard R. Frazier, Mr. M. Bradley Davis, Mr. R. Douglas Cronk, Mr. Charles R. Erwin and Mr. Morgan F. Johnston each have employment agreements with the company. Mr. Evans' agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$300,000 per annum, unless increased by the Board. Mr. Evans' salary for the year 2005 is \$475,000. Mr. Frazier's agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$175,000 per annum unless increased by the Board. Mr. Frazier's salary for the year 2005 is \$300,000. Mr. Davis' agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$190,000 per annum, unless increased by the Board. Mr. Davis' salary for the year 2005 is \$200,000. Mr. Cronk's agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$167,500 per annum, unless increased by the Board. Mr. Cronk's salary for the year 2005 is \$200,000. Mr. Erwin's agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$185,000 per annum unless increased by the Board. Mr. Erwin's salary for the year 2005 is \$225,000. Mr. Johnston's agreement terminates January 1, 2006 and continues thereafter on a year-to-year basis and provides for a salary of \$180,000 per annum unless increased by the Board. Mr. Johnston's salary for the year 2005 is \$195,000. All of the agreements provide that the same benefits supplied to other company employees shall be available to the employee. The employment agreements also contain, among other things, covenants by the employee that in the event of termination, he will not compete with the company in certain geographical areas or hire any of our employees for a period of two years after cessation of employment.

In addition, all of the agreements contain a provision that upon a change in control, the employee's position is terminated, or the employee leaves for "good cause", the employee is entitled to receive immediately, in one lump sum, certain compensation. In the case of Mr. Evans and Mr. Frazier, the employee shall receive three times the employee's current base salary and bonus, plus any other compensation received by him in the last fiscal year. In the case of Mr. Davis, Mr. Cronk, Mr. Erwin and Mr. Johnston, the employee shall receive two times the employee's base salary and bonus, plus any other compensation received by him in the last fiscal year. Also, any medical, dental and group life insurance covering the employee and his dependents shall continue until the earlier of (i) 12 months after the change in control or (ii) the date the employee becomes a participant in the group insurance

benefit program of a new employer. We also have key man life insurance on Mr. Evans in the amount of \$12,000,000.

**NOTE 15 SEGMENT DATA**

We have three reportable segments. The Exploration and Production segment is engaged in exploratory drilling and acquisition, production, and sale of crude oil, condensate, and natural gas. The Gas Gathering, Marketing and Processing segment is engaged in the gathering and compression of natural gas from the wellhead, the purchase and resale of natural gas, which it gathers, and the processing of natural gas liquids. The Oil Field Services segment is engaged in the managing, operation, and monitoring of producing oil and gas properties for interest owners.

Our reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different technology and marketing strategies. The Exploration and Production segment has six geographic areas that are aggregated. The Gas Gathering, Marketing and Processing segment includes the activities of the five gathering systems and four natural gas liquids processing plants in two geographic areas that are aggregated. The Oil Field Services segment has six geographic areas that are aggregated. The reason for aggregating the segments, in each case, was due to the similarity in nature of the products, the production processes, the type of customers, the method of distribution, and the regulatory environments.

The accounting policies of the segments are the same as those described in Note 1 Summary of Significant Accounting Policies. We evaluate performance based on profit or loss from operations before income taxes. The accounting for intersegment sales and transfers is done as if the sales or transfers were to third parties, that is, at current market prices.

IV-95

---

Edgar Filing: O'Neill Andrew J - Form 4

Segment data for the three years ended December 31, 2004, 2003 and 2002 are as follows (in thousands):

	Exploration & Production	Gas Gathering, Marketing & Processing	Oil Field Services	All Other	Elimination	Consolidated
<b>2004:</b>						
Revenue from external customers	\$ 443,412	\$ 41,900	\$ 8,414	\$	\$	\$ 493,726
Intersegment revenues	1,972	26,275	14,700		(42,947)	
Depreciation, depletion, amortization and accretion	123,567	2,363	1,136	113		127,179
Segment profit (loss)	215,196	10,425	2,262	(21,950)		205,933
Equity losses of affiliates						
Interest expense				(38,059)		(38,059)
Costs associated with early retirement of debt				(12,250)		(12,250)
Other income				3,708		3,708
Income before income taxes						159,332
Current income tax expense				(1,977)		(1,977)
Deferred income tax expense				(53,782)		(53,782)
Net income						103,573
Capital expenditures (net of asset sales)	\$ 513,844	\$ 2,458	\$ 810			\$ 517,112
<b>2003:</b>						
Revenue from external customers	\$ 284,929	\$ 35,317	\$ 4,768	\$	\$	\$ 325,014
Intersegment revenues	1,738	23,111	13,649		(38,498)	
Depreciation, depletion, amortization and accretion	96,086	2,320	604	604		99,614
Segment profit (loss)	99,809	7,624	1,045	(15,780)		92,698
Equity losses of affiliates				(162)		(162)
Interest expense				(47,260)		(47,260)
Costs associated with early retirement of debt				(6,716)		(6,716)
Other income				2,371		2,371
Income before income taxes						\$ 40,931
Current income tax benefit				250		250
Deferred income tax expense				(15,463)		(15,463)
Cumulative effect of a change in accounting principle				399		399
Net income						\$ 26,117
Capital expenditures (net of asset sales)	\$ 157,481	\$ 199	\$ 566	\$ 166		\$ 158,412

IV-96

Edgar Filing: O'Neill Andrew J - Form 4

2002:	Exploration & Production	Gas Gathering, Marketing & Processing	Oil Field Services	All Other	Elimination	Consolidated
Revenue from external customers	\$ 240,964	\$ 20,809	\$ 4,096	\$	\$	\$ 265,869
Intersegment revenues	1,647	14,052	14,128		(29,827)	
Depreciation, depletion, amortization and accretion	82,950	2,066	507	945		86,468
Segment profit (loss)	78,288	3,643	1,115	(14,177)		68,869
Equity earnings of affiliates				792		792
Interest expense				(47,935)		(47,935)
Costs associated with early retirement of debt				(1,000)		(1,000)
Provision for non-cash impairment of investments				(621)		(621)
Other income (loss)				(6,174)		(6,174)
Income before income taxes						13,931
Deferred income tax benefit				1,591		1,591
Net income						\$ 15,522
Capital expenditures (net of asset sales)	\$ 643,683	\$ 21,309	\$ 843	\$ 2,153		\$ 667,988
<b>As of December 31, 2004</b>	<b>Exploration &amp; Production</b>	<b>Gas Gathering, Marketing &amp; Processing</b>	<b>Oil Field Services</b>	<b>All Other</b>	<b>Elimination</b>	<b>Consolidated</b>
Segment assets	\$ 1,616,712	\$ 32,346	\$ 18,855	\$ 34,588		\$ 1,702,501
<b>As of December 31, 2003</b>						
Segment assets	\$ 1,142,621	\$ 30,710	\$ 14,917	\$ 77,644	\$	1,265,892

IV-97

**NOTE 16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS**

The company and its subsidiaries, except Canvasback and certain inconsequential subsidiaries, are direct guarantors of our 9.6% Senior Notes and our Convertible Notes, and have fully and unconditionally guaranteed these notes on a joint and several basis. In addition to not being a guarantor of these notes, Canvasback cannot be included in determining compliance with certain financial covenants under our credit agreements. Management has determined that separate financial statements relating to the Guarantors are not material to investors. Condensed consolidating balance sheets for Magnum Hunter Resources, Inc. and subsidiaries as of December 31, 2004 and 2003 and condensed consolidating statements of operations and cash flows for the years ended December 31, 2004, 2003 and 2002 are as follows:

December 31, 2004				
Magnum Hunter Resources, Inc. And Guarantor Subs	Canvasback Energy, Inc. (Non Guarantor)	Eliminations	Magnum Hunter Resources, Inc. Consolidated	
(Amounts in Thousands)				
<b>ASSETS</b>				
Current assets	\$ 146,219	\$ 5,310	\$ (12,015)	\$ 139,514
Property and equipment (using full-cost accounting)	1,490,881	6,031		1,496,912
Investment in subsidiaries (equity method)	19,065		(19,065)	
Investment in Parent		34,127	(34,127)	
Other assets	65,924	151		66,075
<b>Total Assets</b>	<b>\$ 1,722,089</b>	<b>\$ 45,619</b>	<b>\$ (65,207)</b>	<b>\$ 1,702,501</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>				
Current liabilities	\$ 144,451	12,318	(12,015)	144,754
Long-term liabilities	863,698	14,236		877,934
Shareholders' equity	713,940	19,065	(53,192)	679,813
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 1,722,089</b>	<b>\$ 45,619</b>	<b>\$ (65,207)</b>	<b>\$ 1,702,501</b>

## Edgar Filing: O'Neill Andrew J - Form 4

December 31, 2003

	<b>Magnum Hunter Resources, Inc. And Guarantor Subs</b>	<b>Canvasback Energy, Inc. (Non Guarantor)</b>	<b>Eliminations</b>	<b>Magnum Hunter Resources, Inc. Consolidated</b>
(Amounts in Thousands)				
<b>ASSETS</b>				
Current assets	\$ 108,801	\$ 18,163	\$ (26,627)	\$ 100,337
Property and equipment (using full-cost accounting)	1,089,366	6,517		1,095,883
Investment in subsidiaries (equity method)	17,875		(17,875)	
Investment in Parent		34,127	(34,127)	
Other assets	69,672			69,672
<b>Total Assets</b>	<b>\$ 1,285,714</b>	<b>\$ 58,807</b>	<b>\$ (78,629)</b>	<b>\$ 1,265,892</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>				
Current liabilities	\$ 104,806	\$ 27,324	\$ (26,627)	\$ 105,503
Long-term liabilities	757,105	13,608		770,713
Shareholders' equity	423,803	17,875	(52,002)	389,676
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 1,285,714</b>	<b>\$ 58,807</b>	<b>\$ (78,629)</b>	<b>\$ 1,265,892</b>

Year Ended December 31, 2004

	<b>Magnum Hunter Resources, Inc. And Guarantor Subs</b>	<b>Canvasback Energy, Inc. (Non Guarantor)</b>	<b>Eliminations</b>	<b>Magnum Hunter Resources, Inc. Consolidated</b>
(Amounts in Thousands)				
Revenues	\$ 486,737	\$ 8,002	\$ (1,013)	\$ 493,726
Expenses	329,060	6,187	(853)	334,394
Income before Equity in net earnings of subsidiaries	157,677	1,815	(160)	159,332
Equity in net earnings of subsidiaries	1,058		(1,058)	
Income (loss) before income taxes	158,735	1,815	(1,218)	159,332
Income tax provision	(55,162)	(657)	60	(55,759)
<b>Net Income</b>	<b>\$ 103,573</b>	<b>\$ 1,158</b>	<b>\$ (1,158)</b>	<b>\$ 103,573</b>

IV-99

Edgar Filing: O'Neill Andrew J - Form 4

Year Ended December 31, 2003

	Magnum Hunter Resources, Inc. And Guarantor Subs	Canvasback Energy, Inc. (Non Guarantor)	Eliminations	Magnum Hunter Resources, Inc. Consolidated
(Amounts in Thousands)				
Revenues	\$ 320,335	\$ 4,846	\$ (167)	\$ 325,014
Expenses	282,945	1,264	(126)	284,083
Income before Equity in net earnings of subsidiaries	37,390 2,184	3,582	(41) (2,184)	40,931
Income before income taxes	39,574	3,582	(2,225)	40,931
Income tax provision	(13,856)	(1,357)		(15,213)
Income before extraordinary loss	25,718	2,225	(2,225)	25,718
Cumulative effect of a change in accounting principle	399			399
Net Income	\$ 26,117	\$ 2,225	\$ (2,225)	\$ 26,117

Year Ended December 31, 2002

	Magnum Hunter Resources, Inc. And Guarantor Subs	Canvasback Energy, Inc. (Non Guarantor)	Eliminations	Magnum Hunter Resources, Inc. Consolidated
(Amounts in Thousands)				
Revenues	\$ 264,152	\$ 1,717	\$	\$ 265,869
Expenses	250,974	964		251,938
Income before Equity in net earnings of subsidiaries	13,178 468	753	(468)	13,931
Income before income taxes	13,646	753	(468)	13,931
Income tax (provision) benefit	1,876	(285)		1,591
Net Income	\$ 15,522	\$ 468	\$ (468)	\$ 15,522

Year Ended December 31, 2004

	Magnum Hunter Resources, Inc. And Guarantor Subs	Canvasback Energy, Inc. (Non Guarantor)	Eliminations	Magnum Hunter Resources, Inc. Consolidated
(Amounts in Thousands)				
Cash flow from operating activities	\$ 312,881	\$ (12,271)	\$	\$ 300,610
Cash flow used by investing activities	(513,692)	(247)		(513,939)
Cash flow (used) provided by financing activities	214,978			214,978

Edgar Filing: O'Neill Andrew J - Form 4

Year Ended December 31, 2004

Net increase (decrease) in cash	14,167	(12,518)	1,649
Cash at beginning of period	3,482	15,211	18,693
Cash at end of period	\$ 17,649	\$ 2,693	\$ 20,342

IV-100

Edgar Filing: O'Neill Andrew J - Form 4

Year Ended December 31, 2003

	<b>Magnum Hunter Resources, Inc. And Guarantor Subs</b>	<b>Canvasback Energy, Inc. (Non Guarantor)</b>	<b>Eliminations</b>	<b>Magnum Hunter Resources, Inc. Consolidated</b>
(Amounts in Thousands)				
Cash flow from operating activities	\$ 148,019	\$ 14,892	\$ (273)	\$ 162,638
Cash flow (used) provided by investing activities	(160,261)	6,008	(5,422)	(159,675)
Cash flow (used) provided by financing activities	13,184	(6,218)	5,695	12,661
Net increase in cash	942	14,682		15,624
Cash at beginning of period	2,540	529		3,069
Cash at end of period	\$ 3,482	\$ 15,211	\$	\$ 18,693

Year Ended December 31, 2002

	<b>Magnum Hunter Resources, Inc. And Guarantor Subs</b>	<b>Canvasback Energy, Inc. (Non Guarantor)</b>	<b>Eliminations</b>	<b>Magnum Hunter Resources, Inc. Consolidated</b>
(Amounts in Thousands)				
Cash flow from operating activities	\$ 63,522	\$ 19,881	\$	\$ 83,403
Cash flow used by investing activities	(85,398)	(4,022)		(89,420)
Cash flow (used) provided by financing activities	23,686	(17,355)		6,331
Net increase (decrease) in cash	1,810	(1,496)		314
Cash at beginning of period	730	2,025		2,755
Cash at end of period	\$ 2,540	\$ 529	\$	\$ 3,069

IV-101

**NOTE 17 SUMMARY OF QUARTERLY DATA (Unaudited)**

The following tables set forth unaudited summary financial results on a quarterly basis for the two most recent years.

	<b>2004</b>			
	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Revenues	\$ 100,378	\$ 110,036	\$ 128,460	\$ 154,852
Depreciation, depletion, amortization and accretion	25,480	27,645	35,226	38,828
Operating Profit	40,608	44,963	52,255	68,107
Cost of early debt retirement			(12,250)	
Net Income	19,262	23,230	18,964	42,117
Income per common share, basic	0.28	0.34	0.22	0.49
Income per common share, diluted	\$ 0.28	\$ 0.33	\$ 0.22	\$ 0.47
	<b>2003</b>			
	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Revenues	\$ 80,054	\$ 78,438	\$ 82,575	\$ 83,947
Depreciation, depletion, amortization and accretion	21,524	24,978	26,682	26,430
Operating Profit	25,914	21,444	21,153	24,187
Cost of early debt retirement	(1,855)	(2,211)	(19)	(2,631)
Cumulative effect of change in accounting principle	399			
Net Income	7,990	4,170	6,669	7,288
Income per common share, basic	0.12	0.06	0.10	0.11
Income per common share, diluted	\$ 0.12	\$ 0.06	\$ 0.10	\$ 0.11

**NOTE 18 RECENT ANNOUNCEMENT TO BE ACQUIRED BY CIMAREX ENERGY**

On January 26, 2005, Magnum Hunter and Cimarex Energy, Inc. announced that their respective boards of directors had approved an agreement and plan of merger that provides for the acquisition of Magnum Hunter by Cimarex. Closing is anticipated before the end of the second quarter in 2005, subject to customary regulatory approvals.

Under the terms of the proposed agreement, Magnum Hunter shareholders will receive 0.415 shares of Cimarex common stock for each share of Magnum Hunter common stock that they own. The merger is expected to be non-taxable to the shareholders of both companies. In addition to the merger consideration and prior to closing, Magnum Hunter intends to distribute its ownership interest in TEL Offshore Trust to its common stockholders as a special dividend.

Cimarex Energy Co., headquartered in Denver, CO, is an independent oil and gas exploration and production company with operations focused in the Mid-Continent and Gulf Coast areas of the U.S. Its principal operations offices are located in Tulsa, New Orleans and Houston.

**MAGNUM HUNTER RESOURCES, INC. AND SUBSIDIARIES**

**SUPPLEMENTAL INFORMATION ON OIL AND GAS PRODUCING ACTIVITIES**

**(Unaudited)**

Proved oil and gas reserves consist of those estimated quantities of crude oil, natural gas and natural gas liquids that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions. Proved developed oil and gas reserves are reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

Estimates of petroleum reserves have been made by independent engineers and company employees. These estimates include reserves in which we hold an economic interest under production-sharing and other types of operating agreements. These estimates do not include probable or possible reserves. The estimated net interests in Proved Reserves are based upon subjective engineering judgments and may be affected by the limitations inherent in such estimation. The process of estimating reserves is subject to continual revision as additional information becomes available as a result of drilling, testing, reservoir studies and production history. There can be no assurance that such estimates will not be materially revised in subsequent periods. The revisions of previous estimates of our proved oil and gas reserves were primarily due to changes in commodity prices at December 31, 2002, 2003 and 2004 that impacted whether such reserves were economically recoverable. The impact of price changes disproportionately affects our long life reserves because of the more gradual decline curve of the applicable production.

We adopted FASB Statement 143, "Accounting for Asset Retirement Obligations" ("FAS 143") January 1, 2003. Among other things, FAS 143 requires the recognition of a liability for legal obligations associated with the retirement of long-lived assets. The initial recognition of a liability for an asset retirement obligation increases the carrying amount of the related long-lived asset by the same amount as the liability. In periods subsequent to the initial measurement, period-to-period changes in the liability are recognized for passage of time in the form of accretion expense as well as revisions to the original estimate. In accordance with FAS 143, we recorded a liability of \$30.4 million, increased costs carried for our oil and gas properties by \$25.4 million, and reduced our accumulated depletion by \$5.6 million. During 2003, we incurred additional liabilities of \$2.7 million, settled or sold liabilities of \$1.2 million, and recorded accretion expense of \$2.5 million. During 2004, we incurred additional liabilities of \$7.3 million, settled or sold liabilities of \$1.9 million, and recorded accretion expense of \$2.9 million. We have included the initial costs recorded upon adoption of FAS 143 as well as the costs associated with the liabilities incurred during 2003 and 2004 in the carrying value of our oil and gas properties. Our accumulated depletion also reflects initial reduction as well as the depletion of these retirement costs during 2003 and 2004. We have included the cost associated with the liabilities incurred during 2003 and 2004 in our costs incurred analysis. Our results of operations include depletion on these retirement costs as well as the accretion expense related to the liability, and our discounted cash flows presented include our estimated futures costs of retiring our oil and gas properties.

IV-103

---

Estimated quantities of proved oil and gas reserves were as follows:

	<u>Oil</u> <u>(Mbbbl)</u>	<u>Gas</u> <u>(MMcf)</u>
<b>December 31, 2002</b>		
Proved Reserves	63,082	458,644
Proved Developed Reserves	48,512	362,325
<b>December 31, 2003</b>		
Proved Reserves	57,397	494,052
Proved Developed Reserves	42,989	368,530
<b>December 31, 2004</b>		
Proved Reserves	66,081	610,118
Proved Developed Reserves	48,009	442,631

We included estimated quantities in the above table which we claim exclusively through our gas plant ownership. The amounts attributable to our ownership in gas plants are as follows:

	<u>Oil</u> <u>(Mbbbl)</u>	<u>Gas</u> <u>(MMcf)</u>	<u>NGL</u> <u>(Mbbbl)</u>
<b>December 31, 2002</b>			
Proved Reserves	127	8,359	4,529
Proved Developed Reserves	122	8,031	4,180
<b>December 31, 2003</b>			
Proved Reserves	197	9,513	4,090
Proved Developed Reserves	167	9,162	3,637
<b>December 31, 2004</b>			
Proved Reserves	136	9,769	4,948
Proved Developed Reserves	127	9,419	4,398

IV-104

Edgar Filing: O'Neill Andrew J - Form 4

The changes in proved reserves for the years ended December 31, 2002, 2003 and 2004 were as follows:

	Oil (Mbbbl)	Gas (MMcf)
<b>Reserves at December 31, 2001</b>	21,601	248,480
Purchase of minerals-in-place	45,650	275,873
Sale of minerals-in-place	(4,621)	(75,034)
Extensions and discoveries	2,986	53,939
Production	(4,050)	(46,487)
Revisions of estimates	1,516	1,873
<b>Reserves at December 31, 2002</b>	63,082	458,644
Purchase of minerals-in-place	26	67
Sale of minerals-in-place	(1,243)	(13,303)
Extensions and discoveries	1,776	86,001
Production	(3,893)	(49,695)
Revisions of estimates	(2,351)	12,338
<b>Reserves at December 31, 2003</b>	57,397	494,052
Purchase of minerals-in-place	8,324	135,017
Sale of minerals-in-place	(196)	(2,263)
Extensions and discoveries	3,085	70,554
Production	(4,080)	(55,961)
Revisions of estimates	1,551	(31,281)
<b>Reserves at December 31, 2004</b>	66,081	610,118

The aggregate amounts of capitalized costs relating to oil and gas producing activities and the related accumulated depreciation, depletion, amortization and impairment as of December 31, 2004, 2003 and 2002 were as follows (in thousands):

	2004	2003	2002
Unproved oil and gas properties	\$ 94,472	\$ 110,467	\$ 165,676
Proved properties	1,828,839	1,292,388	1,053,426
Gross Capitalized Costs	1,923,311	1,402,855	1,219,102
Accumulated depreciation, depletion, amortization and impairment	(458,731)	(338,109)	(250,515)
<b>Net Capitalized Costs</b>	<b>\$ 1,464,580</b>	<b>\$ 1,064,746</b>	<b>\$ 968,587</b>

IV-105

## Edgar Filing: O'Neill Andrew J - Form 4

Capitalized costs incurred in oil and gas producing activities during the years ended December 31, 2004, 2003 and 2002 were as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Property acquisition costs			
Proved properties	\$ 297,957	\$ 3,021	\$ 460,908
Unproved properties	19,515	12,213	147,024
Exploration costs	52,743	36,788	34,310
Development costs	166,484	125,308	91,521
	<u>          </u>	<u>          </u>	<u>          </u>
<b>Total Costs Incurred</b>	<b>\$ 536,699</b>	<b>\$ 177,330</b>	<b>\$ 733,763</b>

Results of operations from oil and gas producing activities for the years ended December 31, 2004, 2003 and 2002 were as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Oil and gas production revenue	\$ 443,412	\$ 284,929	\$ 240,964
Production costs	(104,649)	(89,034)	(79,726)
Depreciation, depletion, amortization, impairment and accretion	(123,567)	(96,087)	(83,028)
Income taxes	(75,319)	(34,933)	(27,374)
	<u>          </u>	<u>          </u>	<u>          </u>
<b>Results of Operations for Producing Activities</b>	<b>\$ 139,877</b>	<b>\$ 64,875</b>	<b>\$ 50,836</b>

The standardized measure of discounted estimated future net cash flows related to proved oil and gas reserves at December 31, 2004, 2003 and 2002 were as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Future cash flows	\$ 6,133,855	\$ 4,341,980	\$ 3,728,575
Future development costs	(401,540)	(295,273)	(178,961)
Future production costs	(1,805,299)	(1,318,811)	(1,159,303)
	<u>          </u>	<u>          </u>	<u>          </u>
Future net cash flows, before income tax	3,927,016	2,727,896	2,390,311
Future income taxes	(1,050,979)	(712,167)	(619,850)
	<u>          </u>	<u>          </u>	<u>          </u>
<b>Future Net Cash Flows</b>	<b>2,876,037</b>	<b>2,015,729</b>	<b>1,770,461</b>
	<u>          </u>	<u>          </u>	<u>          </u>
10% annual discount	(1,312,440)	(948,041)	(800,652)
	<u>          </u>	<u>          </u>	<u>          </u>
<b>Standardized Measure of Discounted Future Net Cash Flows</b>	<b>\$ 1,563,597</b>	<b>\$ 1,067,688</b>	<b>\$ 969,809</b>

IV-106

Edgar Filing: O'Neill Andrew J - Form 4

The primary changes in the standardized measure of discounted estimated future net cash flows for the years ended December 31, 2004, 2003 and 2002 were as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Purchases of minerals-in-place	\$ 356,883	\$ 676	\$ 737,736
Sales of minerals-in-place	(6,227)	(44,759)	(85,460)
Extensions, discoveries and improved recovery, less related costs	82,750	262,022	167,334
Sales of oil and gas produced, net of production costs	(338,763)	(195,895)	(161,238)
Development costs incurred during the period	166,484	125,308	91,521
Revision of prior estimates:			
Net change in prices and costs	353,969	(79,252)	154,738
Change in quantity estimates	(60,379)	(22,086)	18,007
Accretion of discount	106,769	96,981	30,569
Net change in income taxes	(165,577)	(45,115)	(289,091)
	<u>                    </u>	<u>                    </u>	<u>                    </u>
Net Change	\$ 495,909	\$ 97,880	\$ 664,116
	<u>                    </u>	<u>                    </u>	<u>                    </u>

Estimated future cash inflows are computed by applying year-end prices of oil and gas to year-end quantities of Proved Reserves. Estimated future development and production costs are determined by estimating the expenditures to be incurred in developing and producing the proved oil and gas reserves at the end of the year, based on year-end costs and assuming continuation of existing economic conditions. Estimated future income tax expense is calculated by applying year-end statutory tax rates to estimated future pre-tax net cash flows related to proved oil and gas reserves, less the tax basis of the properties involved.

The assumptions used to compute the standardized measure are those prescribed by the Financial Accounting Standards Board and as such, do not necessarily reflect our expectations of actual revenues to be derived from those reserves nor their present worth. The limitations inherent in the reserve quantity estimation process are equally applicable to the standardized measure computations since these estimates are the basis for the valuation process.

**MAGNUM HUNTER RESOURCES, INC.**  
**SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS**  
**FOR EACH OF THE THREE YEARS IN THE PERIOD ENDED DECEMBER 31, 2004**  
(in thousands)

Classification	Balance at Beginning of Year	Additions		Deductions(2)	Balance at End of Year
		Charged to Costs and Expenses	Charged to Other Accounts(1)		
<b>Year Ended December 31, 2004</b>					
Allowance for Doubtful Accounts on Trade Accounts Receivable	\$ 4,331	\$ 772	\$	\$ (327)	\$ 4,776
Reserve on Current Portion of Long-term Notes Receivable	1,170			\$	\$ 1,170
<b>Year Ended December 31, 2003</b>					
Allowance for Doubtful Accounts on Trade Accounts Receivable	\$ 4,573	\$ 231	\$ 19	\$ (492)	\$ 4,331
Reserve on Current Portion of Long-term Notes Receivable	1,620			(450)	1,170
Reserve on Investment in Unconsolidated Affiliate	\$ 4,527	\$	\$	\$ (4,527)	\$
<b>Year Ended December 31, 2002</b>					
Allowance for Doubtful Accounts on Trade Accounts Receivable	\$ 3,264	\$ 206	\$ 1,103	\$	\$ 4,573
Reserve on Current Portion of Long-term Notes Receivable	1,620				1,620
Reserve on Investment in Unconsolidated Affiliate	\$ 4,527	\$	\$	\$	\$ 4,527

(1) Allowances acquired in Prize merger during 2002 and Metrix acquisition during 2003.

(2) Write-offs

**Annex A**

---

**AGREEMENT AND PLAN OF MERGER  
AMONG  
CIMAREX ENERGY CO. ("PARENT"),  
CIMAREX NEVADA ACQUISITION CO. ("MERGER SUB")  
AND  
MAGNUM HUNTER RESOURCES, INC. ("COMPANY")  
JANUARY 25, 2005**

---

TABLE OF CONTENTS

ARTICLE I DEFINITIONS

- Section 1.1 Defined Terms
- Section 1.2 References and Titles

ARTICLE II THE MERGER

- Section 2.1 The Merger
- Section 2.2 Effect of the Merger
- Section 2.3 Governing Instruments, Directors and Officers of the Surviving Corporation
- Section 2.4 Effect on Securities
- Section 2.5 Exchange of Certificates
- Section 2.6 Associated Rights
- Section 2.7 Withholding
- Section 2.8 Closing
- Section 2.9 Effective Time of the Merger
- Section 2.10 Taking of Necessary Action: Further Action

ARTICLE III REPRESENTATIONS AND WARRANTIES OF THE COMPANY

- Section 3.1 Organization
- Section 3.2 Other Equity Interests
- Section 3.3 Authority and Enforceability
- Section 3.4 No Violations
- Section 3.5 Consents and Approvals
- Section 3.6 SEC Documents
- Section 3.7 Financial Statements
- Section 3.8 Capital Structure
- Section 3.9 No Undisclosed Liabilities
- Section 3.10 Absence of Certain Changes or Events
- Section 3.11 Compliance with Laws, Material Agreements and Permits
- Section 3.12 Governmental Regulation
- Section 3.13 Litigation
- Section 3.14 No Restrictions
- Section 3.15 Taxes
- Section 3.16 Employee Benefit Plans
- Section 3.17 Employment Contracts and Benefits
- Section 3.18 Labor Matters
- Section 3.19 Insurance
- Section 3.20 Intellectual Property
- Section 3.21 Title to Assets
- Section 3.22 Oil and Gas Operations
- Section 3.23 Oil and Gas Reserves
- Section 3.24 Derivative Transactions and Hedging
- Section 3.25 Natural Gas Act
- Section 3.26 Environmental Matters
- Section 3.27 Books and Records
- Section 3.28 Brokers
- Section 3.29 Vote Required
- Section 3.30 State Takeover Laws
- Section 3.31 Affiliate Transactions
- Section 3.32 Disclosure Controls and Procedures



Section 3.33	<u>Rights Agreement</u>
Section 3.34	<u>Opinion of Financial Advisor</u>

ARTICLE IV REPRESENTATIONS AND WARRANTIES OF PARENT AND MERGER SUB

Section 4.1	<u>Organization</u>
Section 4.2	<u>Other Equity Interests</u>
Section 4.3	<u>Authority and Enforceability</u>
Section 4.4	<u>No Violations</u>
Section 4.5	<u>Consents and Approvals</u>
Section 4.6	<u>SEC Documents</u>
Section 4.7	<u>Financial Statements</u>
Section 4.8	<u>Capital Structure</u>
Section 4.9	<u>No Undisclosed Liabilities</u>
Section 4.10	<u>Absence of Certain Changes or Events</u>
Section 4.11	<u>Compliance with Laws, Material Agreements and Permits</u>
Section 4.12	<u>Governmental Regulation</u>
Section 4.13	<u>Litigation</u>
Section 4.14	<u>Interim Operations of Merger Sub</u>
Section 4.15	<u>No Restrictions</u>
Section 4.16	<u>Taxes</u>
Section 4.17	<u>Employee Benefit Plans</u>
Section 4.18	<u>Employment Contracts and Benefits</u>
Section 4.19	<u>Labor Matters</u>
Section 4.20	<u>Insurance</u>
Section 4.21	<u>Intellectual Property</u>
Section 4.22	<u>Title to Assets</u>
Section 4.23	<u>Oil and Gas Operations</u>
Section 4.24	<u>Oil and Gas Reserves</u>
Section 4.25	<u>Derivative Transactions and Hedging</u>
Section 4.26	<u>Natural Gas Act</u>
Section 4.27	<u>Environmental Matters</u>
Section 4.28	<u>Books and Records</u>
Section 4.29	<u>Funding</u>
Section 4.30	<u>Brokers</u>
Section 4.31	<u>Vote Required</u>
Section 4.32	<u>Rights Agreement</u>
Section 4.33	<u>State Takeover Laws</u>
Section 4.34	<u>Affiliate Transactions</u>
Section 4.35	<u>Disclosure Controls and Procedures</u>
Section 4.36	<u>Opinion of Financial Advisor</u>

ARTICLE V COVENANTS

Section 5.1	<u>Conduct of Business by Parent Pending Closing</u>
Section 5.2	<u>Conduct of Business by the Company Pending Closing</u>
Section 5.3	<u>Access to Assets, Personnel and Information</u>
Section 5.4	<u>No Solicitation</u>
Section 5.5	<u>Company Stockholders Meeting</u>
Section 5.6	<u>Parent Stockholders Meeting</u>
Section 5.7	<u>Registration Statement and Proxy Statement/Prospectus</u>
Section 5.8	<u>Stock Exchange Listing</u>
Section 5.9	<u>Additional Arrangements</u>

Section 5.10	<u>Agreements of Affiliates</u>
Section 5.11	<u>Section 16</u>
Section 5.12	<u>Public Announcements</u>
Section 5.13	<u>Notification of Certain Matters</u>
Section 5.14	<u>Payment of Expenses</u>
Section 5.15	<u>Indemnification and Insurance</u>
Section 5.16	<u>Employees; Employee Benefits</u>
Section 5.17	<u>Parent Board of Directors</u>
Section 5.18	<u>Registration Statements Relating to Company Warrants and Company Convertible Notes</u>
Section 5.19	<u>Bank Credit Agreements</u>
Section 5.20	<u>Tax Matters</u>
Section 5.21	<u>Termination of the Company Stock Ownership Plan</u>
Section 5.22	<u>SOX 404 Certification</u>
Section 5.23	<u>Reserve Data</u>
Section 5.24	<u>Dividend of TEL Offshore Trust Units</u>
Section 5.25	<u>Company Debt Instruments</u>
Section 5.26	<u>Conversion of 1996 Preferred</u>

#### ARTICLE VI CONDITIONS

Section 6.1	<u>Conditions to Each Party's Obligation to Effect the Merger</u>
Section 6.2	<u>Conditions to Obligations of Parent and Merger Sub</u>
Section 6.3	<u>Conditions to Obligation of the Company</u>

#### ARTICLE VII TERMINATION

Section 7.1	<u>Termination Rights</u>
Section 7.2	<u>Effect of Termination</u>
Section 7.3	<u>Fees and Expenses</u>

#### ARTICLE VIII MISCELLANEOUS

Section 8.1	<u>Nonsurvival of Representations and Warranties</u>
Section 8.2	<u>Amendment</u>
Section 8.3	<u>Notices</u>
Section 8.4	<u>Counterparts</u>
Section 8.5	<u>Severability</u>
Section 8.6	<u>Entire Agreement; No Third Party Beneficiaries</u>
Section 8.7	<u>Applicable Law</u>
Section 8.8	<u>No Remedy in Certain Circumstances</u>
Section 8.9	<u>Assignment</u>
Section 8.10	<u>Waivers</u>
Section 8.11	<u>Confidentiality Agreement</u>
Section 8.12	<u>Incorporation</u>

#### SCHEDULES

Company Disclosure Schedule

Parent Disclosure Schedule

#### EXHIBIT

5.10 Form of Affiliate Letter

## TABLE OF DEFINED TERMS

1996 Preferred	A-23
1998 Preferred	A-23
1999 Preferred	A-23
Affiliate	A-1
Agreement	A-1
Approved Budgets	A-61, A-64
Articles of Merger	A-1
Capital Expenditures	A-1
Capital Project	A-2
CERCLA	A-2
CERCLIS	A-2
Claim	A-74
Closing	A-2
Closing Date	A-2
Code	A-1
Company	A-1
Company Bank Credit Agreement	A-2
Company Benefit Program or Agreement	A-31
Company Certificate	A-2
Company Common Stock	A-2
Company Convertible Notes	A-2
Company Disclosure Schedule	A-2
Company Employee Benefit Plans	A-31
Company ERISA Affiliate	A-31
Company Financial Statements	A-3
Company Material Agreement(s)	A-3
Company Meeting	A-3
Company Permits	A-28
Company Plan	A-31
Company Preferred Stock	A-3
Company Proposal	A-3
Company Representative	A-4
Company Reserve Report	A-4
Company Rights	A-20
Company Rights Agreement	A-20
Company SEC Documents	A-23
Company Senior Secured Notes	A-4
Company Stock Option	A-3
Company Subsidiary(ies)	A-4
Company Warrant	A-4
Company's Oil And Gas Interests	A-7
Confidentiality Agreement	A-4
Continuing Employees	A-75
Control	A-1
Controlled By	A-1
Conversion Number	A-4
Defensible Title	A-4
Derivative Transaction	A-4
Disclosure Schedule	A-4
Dissenting Stockholder	A-4
Drilling or Completion Expenditures	A-5
Effective Time	A-20
Environmental Law	A-5
ERISA	A-5
Exchange Act	A-5
Exchange Agent	A-5
Exchange Fund	A-15
FERC	A-36
GAAP	A-5
Governmental Action	A-5

Edgar Filing: O'Neill Andrew J - Form 4

Governmental Authority	A-5
Hazardous Material	A-5
HSR Act	A-5
Hydrocarbons	A-6
Indemnified Parties	A-74
Indentures	A-80
IRS	A-32
KSOP	A-79
Laws	A-5
Lien	A-6
Market Price	A-6
Material Adverse Effect	A-6
Merger	A-12
Merger Consideration	A-13
Merger Sub	A-1
Merger Sub Common Stock	A-6
National Stock Exchange	A-6
NGA	A-36
Non-U.S. Holder	A-6
Notes	A-80
NRS	A-7
Oil and Gas Interest(s)	A-7
Oil and Gas Interests of Parent	A-7
Oil and Gas Interests of the Company	A-7
Option Consents	A-13
Ownership Interests	A-7
Parent	A-1
Parent Alternative Transaction	A-69
Parent Bank Credit Agreement	A-7
Parent Benefit Program or Agreement	A-49
Parent Certificate	A-7
Parent Common Stock	A-7
Parent Companies	A-7
Parent Disclosure Schedule	A-7
Parent Employee Benefit Plans	A-49
Parent ERISA Affiliate	A-49
Parent Financial Statements	A-8

Edgar Filing: O'Neill Andrew J - Form 4

Parent Material Agreement(s)	A-8
Parent Meeting	A-8
Parent Permits	A-46
Parent Plan	A-49
Parent Preferred Stock	A-8
Parent Representative	A-8
Parent Reserve Report	A-8
Parent Rights	A-8
Parent Rights Agreement	A-9
Parent SEC Documents	A-42
Parent Subsidiary(ies)	A-9
Parent's Oil and Gas Interests	A-7
Parties	A-1
Party	A-9
PBGC	A-32
Permitted Encumbrances	A-9
Person	A-10
Proxy Statement/Prospectus	A-10
RCRA	A-10
Registration Statement	A-10
Required Company Stockholder Vote	A-81
Required Parent Stockholder Vote	A-81
Responsible Officers	A-10
SEC	A-10
Securities Act	A-10
Series A Certificate	A-10
Series A Certificate of Designations, Preferences and Rights	A-10
Series A Merger Consideration	A-14
Series A Preferred Stock	A-10
Series B Preferred	A-23
Series C Preferred	A-23
SOX	A-10
Stock Consideration	A-13
Superior Proposal	A-69
Surviving Corporation	A-12
Takeover Proposal	A-69
Target Companies	A-10
Tax Return	A-11
Taxes	A-11
TEL Distribution	A-80
TEL Distribution Record Date	A-80
TEL Units	A-80
Third-Party Consent	A-11
Under Common Control With	A-1
West Dilley Prospect	A-11

A-v

# Edgar Filing: O'Neill Andrew J - Form 4

## AGREEMENT AND PLAN OF MERGER

This Agreement and Plan of Merger (this "*Agreement*") is made and entered into as of January 25, 2005, by and among Cimarex Energy Co., a Delaware corporation ("*Parent*"); Cimarex Nevada Acquisition Co., a Nevada corporation and a wholly-owned subsidiary of Parent ("*Merger Sub*"); and Magnum Hunter Resources, Inc., a Nevada corporation (the "*Company*").

### RECITALS

The Board of Directors of each of Parent and the Company has determined that it is in the best interests of its respective stockholders to approve the merger of Merger Sub with and into the Company upon the terms and subject to the conditions set forth in this Agreement.

For United States federal income tax purposes, it is intended that such merger qualify as a "reorganization" within the meaning of Section 368(a) of the Internal Revenue Code of 1986, as amended (the "*Code*").

Parent, Merger Sub and the Company (the "*Parties*") desire to make certain representations, warranties, covenants and agreements in connection with such merger and also to prescribe various conditions to such merger.

NOW, THEREFORE, for and in consideration of the recitals and the mutual covenants and agreements set forth in this Agreement, the Parties agree as follows:

### ARTICLE I

#### DEFINITIONS

Section 1.1 *Defined Terms.* As used in this Agreement, each of the following terms has the meaning set forth below:

"*Affiliate*" means, with respect to any Person, each other Person that directly or indirectly (through one or more intermediaries or otherwise) controls, is controlled by, or is under common control with such Person. The term "*Control*" (including the terms "*Controlled By*" and "*Under Common Control With*") means the possession, directly or indirectly, of the actual power to direct or cause the direction of the management policies of a Person, whether through the ownership of stock, by contract, credit arrangement or otherwise.

"*Agreement*" means this Agreement and Plan of Merger, as amended, supplemented or modified from time to time.

"*Articles of Merger*" means the articles of merger, prepared and executed in accordance with the applicable provisions of the NRS, filed with the Secretary of State of Nevada to effect the Merger in Nevada.

"*Capital Expenditures*" means costs and expenses associated with the acquisition, development or redevelopment of Oil and Gas Interests or any other fixed or capital assets of the Target Companies or Parent Companies, as applicable, which pursuant to GAAP are required to be capitalized and subject to depletion, depreciation or amortization, including Drilling or Completion Expenditures.

"*Capital Project*" means any project, transaction, agreement, arrangement or series of transactions, agreements or arrangements to which one or more of the Target Companies or the Parent Companies, as the case may be, is a party involving a Capital Expenditure, including (a) any purchase, lease, acquisition, developmental drilling, completion and/or recompletion of proved developed producing, proved developed non-producing, or proved undeveloped Oil and Gas Interests; (b) any purchase, lease or acquisition and/or exploratory drilling of Oil and Gas Interests; and (c) any purchase, lease,

## Edgar Filing: O'Neill Andrew J - Form 4

acquisition, construction, development or completion of transportation, compression, gathering or related facilities for oil, gas or related products or the provision of services, equipment or other property for use in developing, completing or transporting oil, gas or related products or otherwise directly related and ancillary to the oil and gas business, including the transportation, production, storage and handling of water utilized or disposed of in oil and gas production.

"*CERCLA*" means the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, and any regulations promulgated thereunder.

"*CERCLIS*" means the Comprehensive Environmental Response, Compensation and Liability Information System List.

"*Closing*" means the closing of the Merger and the consummation of the other transactions contemplated by this Agreement.

"*Closing Date*" means the date on which the Closing occurs, which date shall be the first business day following the day by which both the Company Meeting and the Parent Meeting have been held (or such later date as is agreed upon by the Parties).

"*Company Bank Credit Agreement*" means the Fourth Amended and Restated Credit Agreement dated March 15, 2002, between the Company, as borrower, and Bankers Trust Company and others, as agents and lenders (as amended and supplemented).

"*Company Certificate*" means a certificate representing shares of Company Common Stock.

"*Company Common Stock*" means the common stock, par value \$.002 per share, of the Company.

"*Company Convertible Notes*" means the Floating Rate Convertible Senior Notes due 2023 of the Company.

"*Company Disclosure Schedule*" means the Company Disclosure Schedule delivered in connection with this Agreement and any documents listed on such Company Disclosure Schedule or expressly incorporated therein by reference.

"*Company Financial Statements*" means the audited and unaudited consolidated financial statements of the Company and its subsidiaries (including the related notes) included (or incorporated by reference) in the Company's Annual Report on Form 10-K for the year ended December 31, 2003 and Quarterly Reports on Form 10-Q for the quarters ended March 31, June 30, and September 30, 2004, in each case as filed with the SEC.

"*Company Material Agreement(s)*" means (a) the Company Bank Credit Agreement, (b) any hedging agreement to which any of the Target Companies is a party or by which any of its assets is bound, (c) any agreement, contract, commitment or understanding, written or oral, (i) granting any Person registration, purchase or sale rights with respect to any security of any of the Target Companies, (ii) which materially restrains, limits or impedes any of the Target Companies, or will materially restrain, limit or impede the Surviving Corporation's, ability to compete with or conduct any business or any line of business, including geographic limitations on any of the Target Companies' or the Surviving Corporation's activities, (iii) which is a material production sharing agreement, joint venture or operating agreement, balancing agreement, farm-out or farm-in agreement, enhanced oil recovery agreement, unitization and pooling agreement or other similar contract or agreement relating to the exploration, development and production of oil and natural gas, (iv) which is a material take-or-pay agreement or other similar agreement that entitles purchasers of production to receive delivery of Hydrocarbons without paying therefor, (v) which is a material seismic license or software license relating to primary geological or financial processes to which any of the Target Companies is subject, or (vi) which is a fixed price commodity sales agreement with a remaining term of more than 60 days, (d) any agreement, contract, commitment or understanding, written or oral, granting any Person a right

## Edgar Filing: O'Neill Andrew J - Form 4

of indemnification and/or contribution by any of the Target Companies, (e) any voting agreement relating to any security of any of the Target Companies, and/or (f) any other written or oral agreement, contract, commitment or understanding (or amendment or modification thereof) to which any of the Target Companies is a party, by which any of the Target Companies is directly or indirectly bound, or to which any asset of any of the Target Companies may be subject, that is (i) included in Section 3.11 of the Company Disclosure Schedule, (ii) listed (in the Company's Form 10-K for the year ended December 31, 2003 or in subsequent filings) as an exhibit to the Company SEC Documents or (iii) material to the Target Companies, taken as a whole, in each case as amended and supplemented.

"*Company Meeting*" means the meeting of the stockholders of the Company called for the purpose of voting on the Company Proposal or any adjournment thereof.

"*Company Stock Option*" means an option (issued and outstanding immediately prior to the Effective Time) to acquire shares of Company Common Stock granted pursuant to the Company Employee Benefit Plans.

"*Company Preferred Stock*" means the preferred stock, par value \$.001 per share, of the Company.

"*Company Proposal*" means the proposal to approve this Agreement and the Merger, which proposal is to be presented to the stockholders of the Company and Parent in the Proxy Statement/Prospectus.

"*Company Representative*" means any director, officer, employee, agent, advisor (including legal, accounting and financial advisors) or other representative of any of the Target Companies.

"*Company Reserve Report*" means the reserve report dated October 1, 2004, referenced on page 2 of the Management Presentation prepared by the Company and provided to Parent.

"*Company Senior Secured Notes*" means the 9.60% Senior Secured Notes due 2012 of the Company.

"*Company Subsidiary(ies)*" means any corporation more than 50% of whose outstanding voting securities, or any general partnership, joint venture, or similar entity more than 50% of whose total equity interests, is owned, directly or indirectly, by the Company, or any limited partnership of which the Company or any Company Subsidiary is a general partner.

"*Company Warrant*" means a common stock purchase warrant (issued and outstanding on the date hereof and at the Effective Time) representing the right to purchase shares or a fraction of a share of Company Common Stock.

"*Confidentiality Agreement*" means the letter agreement dated November 3, 2003, as amended on November 23, 2004, between the Company and Parent relating to the Company's furnishing of information to Parent and Parent's furnishing of information to the Company in connection with Parent's and the Company's evaluation of the possibility of the Merger.

"*Conversion Number*" means 0.415.

"*Defensible Title*" means such right, title and interest that is (a) evidenced by an instrument or instruments filed of record in accordance with the conveyance and recording laws of the applicable jurisdiction to the extent necessary to prevail against competing claims of bona fide purchasers for value without notice, and (b) subject to Permitted Encumbrances, free and clear of all Liens, claims, infringements, burdens and other defects.

"*Derivative Transaction*" means any swap transaction, option, warrant, forward purchase or sale transaction, futures transaction, cap transaction, floor transaction or collar transaction relating to one or more currencies, commodities, bonds, equity securities, loans, interest rates, catastrophe events, weather-related events, credit-related events or conditions or any indexes, or any other similar

## Edgar Filing: O'Neill Andrew J - Form 4

transaction (including any option with respect to any of these transactions) or combination of any of these transactions, including collateralized mortgage obligations or other similar instruments or any debt or equity instruments evidencing or embedding any such types of transactions, and any related credit support, collateral or other similar arrangements related to such transactions.

"*Disclosure Schedule*" means, as applicable, the Company Disclosure Schedule or the Parent Disclosure Schedule.

"*Dissenting Stockholder*" means a holder of Series A Preferred Stock who has validly perfected dissenters' rights under the NRS.

"*Drilling or Completion Expenditures*" means any expenditure incurred, or required to be incurred by the Target Companies or Parent Companies, as applicable, with respect to exploratory drilling of Oil and Gas Interests or any developmental drilling, completion and/or recompletion of proved developed producing, proved developed non-producing, or proved undeveloped Oil and Gas Interests.

"*ERISA*" means the Employee Retirement Income Security Act of 1974, as amended.

"*Environmental Law*" means any federal, state, local or foreign statute, code, ordinance, rule, regulation, policy, guideline, permit, consent, approval, license, judgment, order, writ, decree, common law (including but not limited to common law under which claims for personal injury and property damage can be pursued), injunction or other authorization (collectively, "*Laws*") in effect on the date hereof or at a previous time: (a) relating to emissions, discharges, releases or threatened releases of Hazardous Materials into the environment, including into air, soil, sediments, land surface or subsurface, buildings or facilities, surface water, groundwater, publicly-owned treatment works, septic systems or land; (b) relating to the generation, treatment, storage, disposal, use, handling, manufacturing, recycling, transportation or shipment of Hazardous Materials; (c) relating to occupational health and safety; (d) relating to environmental regulation of oil and gas operations; or (e) otherwise relating to the pollution of the environment, Hazardous Materials handling, treatment or disposal, reclamation or remediation activities, or protection of environmentally sensitive areas.

"*Exchange Act*" means the Securities Exchange Act of 1934, as amended.

"*Exchange Agent*" means Continental Stock Transfer & Trust Company, the transfer agent for shares of Parent Common Stock.

"*GAAP*" means generally accepted accounting principles, as recognized by the U.S. Financial Accounting Standards Board (or any generally recognized successor).

"*Governmental Action*" means any authorization, application, approval, consent, exemption, filing, license, notice, registration, permit or other requirement of, to or with any Governmental Authority.

"*Governmental Authority*" means any national, state, provincial, county, parish, tribal or municipal government, domestic or foreign, any agency, board, bureau, commission, court, department or other instrumentality of any such government, or any arbitrator in any case that has jurisdiction over any of the Target Companies or the Parent Companies or any of their respective properties or assets.

"*HSR Act*" means the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

"*Hazardous Material*" means (a) any "hazardous substance," as defined by CERCLA; (b) any "hazardous waste" or "solid waste," in either case as defined by RCRA; (c) any solid, gas, liquid, chemical, material, waste or substance regulated by any Environmental Law; (d) any radioactive material, and any source, special or byproduct material as defined in 42 U.S.C. 2011 et seq.; (e) any asbestos-containing materials in any form or condition; (f) any polychlorinated biphenyls in any form or condition; or (g) petroleum, petroleum hydrocarbons, petroleum products or any fraction or byproducts thereof.

## Edgar Filing: O'Neill Andrew J - Form 4

"*Hydrocarbons*" means oil, condensate, gas, casinghead gas and other liquid or gaseous hydrocarbons.

"*Lien*" means any lien, mortgage, deed of trust, security interest, pledge, deposit, production payment, restriction, burden, encumbrance, title defect, easement, covenant, rights of a vendor under any title retention or conditional sale agreement, or lease or other arrangement substantially equivalent thereto.

"*Market Price*" means the average (rounded to the second decimal place) of the per share closing sales prices of Parent Common Stock on Parent's primary National Stock Exchange (as reported by The Wall Street Journal, or if not so reported, by another authoritative source) over the 20 trading days ending on the fourth trading day preceding the Closing Date.

"*Material Adverse Effect*" means, when used with respect to a Party, a violation, inaccuracy, event, result or consequence that (i) has had or would reasonably be expected to have a material adverse effect on the financial condition, capitalization, results of operations or business of such Party and its wholly owned subsidiaries (as identified on its Disclosure Schedule) (taken as a whole) or the aggregate value of their assets and liabilities, except for results or consequences attributable to the effects of, or changes in, general economic or capital markets conditions, regulatory or political conditions, other effects and changes that generally affect the energy industry, such as commodity prices, or effects and changes attributable to the announcement or pendency of this Agreement (to the extent in any case that such effects and changes do not disproportionately affect such Party and its wholly owned subsidiaries (as identified on its Disclosure Schedule) taken as a whole, *provided*, that a decline in such Party's stock price shall not, in and of itself, constitute a Material Adverse Effect on such Party), (ii) has impaired materially or would reasonably be expected to impair materially the ability of such Party and its wholly owned subsidiaries (as identified on its Disclosure Schedule) (taken as a whole) to own, hold, develop and operate their assets or (iii) has impaired materially or would reasonably be expected to impair materially (x) the ability of such Party to consummate the Merger and the other transactions contemplated hereby or to perform any of its obligations hereunder or (y) Parent's ability to vote, receive dividends, or otherwise exercise ownership rights with respect to the stock of the Surviving Corporation and, indirectly, control over the assets of the Surviving Corporation.

"*Merger Sub Common Stock*" means the capital stock, par value \$.001 per share, of Merger Sub.

"*National Stock Exchange*" means the New York Stock Exchange, the American Stock Exchange or the Nasdaq Stock Market.

"*Non-U.S. Holder*" means a stockholder who is not (i) an individual who is a citizen or resident of the United States, (ii) a corporation, or other Person taxable as a corporation, created or organized in or under the laws of the United States, any state thereof or the District of Columbia, (iii) an estate, the income of which is subject to U.S. federal income taxation regardless of its source, (iv) a trust if (x) a court within the United States is able to exercise primary supervision over the administration of the trust and (y) one or more U.S. Persons have the authority to control all substantial decisions of the trust or if the trust has made a valid election to be treated as a U.S. Person, or (v) a partnership, or other Person treated as a partnership for United States federal income Tax purposes, to the extent that the beneficial ownership of Company Common Stock is attributed to its partners who fall into the categories described in clauses (i)-(iv) above.

"*NRS*" means the Nevada Revised Statutes.

"*Oil and Gas Interest(s)*" means: (a) direct and indirect interests in and rights with respect to oil, gas, mineral and related properties and assets of any kind and nature, direct or indirect, including working, royalty and overriding royalty interests, production payments, operating rights, net profits interests, other non-working interests and non-operating interests; (b) interests in and rights with respect to Hydrocarbons and other minerals or revenues therefrom and contracts in connection

therewith and claims and rights thereto (including oil and gas leases, operating agreements, unitization and pooling agreements and orders, division orders, transfer orders, mineral deeds, royalty deeds, oil and gas sales, exchange and processing contracts and agreements and, in each case, interests thereunder), surface interests, fee interests, reversionary interests, reservations and concessions; (c) easements, rights of way, licenses, permits, leases, and other interests associated with, appurtenant to, or necessary for the operation of any of the foregoing; and (d) interests in equipment and machinery (including well equipment and machinery), oil and gas production, gathering, transmission, compression, treating, processing and storage facilities (including tanks, tank batteries, pipelines and gathering systems), pumps, water plants, electric plants, gasoline and gas processing plants, refineries and other tangible personal property and fixtures associated with, appurtenant to, or necessary for the operation of any of the foregoing. References in this Agreement to the "*Oil and Gas Interests of the Company*" or "*Company's Oil and Gas Interests*" mean the collective Oil and Gas Interests of the Target Companies. References in this Agreement to the "*Oil and Gas Interests of Parent*" or "*Parent's Oil and Gas Interests*" mean the collective Oil and Gas Interests of the Parent Companies.

"*Ownership Interests*" means, as applicable: (a) the ownership interests of the Company in its proved properties, as set forth in the Company Reserve Report and (b) the ownership interests of Parent in its proved properties, as set forth in the Parent Reserve Report.

"*Parent Bank Credit Agreement*" means the Credit Agreement dated October 2, 2002, as amended, between Parent and J.P. Morgan Securities, as agent.

"*Parent Certificate*" means a certificate representing shares of Parent Common Stock.

"*Parent Common Stock*" means the common stock, par value \$.01 per share, of Parent.

"*Parent Companies*" means Parent and each of the Parent Subsidiaries.

"*Parent Disclosure Schedule*" means the Parent Disclosure Schedule delivered in connection with this Agreement and any documents listed on such Parent Disclosure Schedule or expressly incorporated therein by reference.

"*Parent Financial Statements*" means the audited and unaudited consolidated financial statements of Parent and its subsidiaries (including the related notes) included (or incorporated by reference) in Parent's Annual Report on Form 10-K for the year ended December 31, 2003 and Quarterly Reports on Form 10-Q for the quarters ended March 31, June 30, and September 30, 2004, in each case as filed with the SEC.

"*Parent Material Agreement(s)*" means (a) the Parent Bank Credit Agreement, (b) any hedging agreement to which any of the Parent Companies is a party or by which any of its assets is bound, (c) any agreement, contract, commitment or understanding, written or oral, granting any Person registration, purchase or sale rights with respect to any security of any Parent Company, (d) any agreement, contract, commitment or understanding, written or oral, (i) granting any Person a right of indemnification and/or contribution by any Parent Company, (ii) which materially restrains, limits or impedes any of the Parent Companies' ability to compete with or conduct any business or any line of business, including geographic limitations on any of the Parent Companies' activities, (iii) which is a material production sharing agreement, joint venture or operating agreement, balancing agreement, farm-out or farm-in agreement, enhanced oil recovery agreement, unitization and pooling agreement or other similar contract or agreement relating to the exploration, development and production of oil and natural gas, (iv) which is a material take-or-pay agreement or other similar agreement that entitles purchasers of production to receive delivery of Hydrocarbons without paying therefor, (v) which is a material seismic license or software license relating to primary geological or financial processes to which any of the Parent Companies is subject or (vi) which is a fixed price commodity sales agreement with a remaining term of more than 60 days, (e) any voting agreement relating to any security of any Parent Company, and/or (f) any other written or oral agreement, contract, commitment or

understanding (or amendment or modification thereof) to which any of the Parent Companies is a party, by which any of the Parent Companies is directly or indirectly bound, or to which any asset of any of the Parent Companies may be subject, that is (i) included in Section 4.11 of the Parent Disclosure Schedule, (ii) listed (in Parent's Form 10-K for the year ended December 31, 2003 or in subsequent filings) as an exhibit to the Parent SEC Documents, (iii) material to the Parent Companies, taken as a whole, or (iv) outside the ordinary course of business of the Parent Companies, in each case as amended or supplemented.

"*Parent Meeting*" means the meeting of the stockholders of Parent called for the purpose of voting on the Company Proposal, or any adjournment thereof.

"*Parent Preferred Stock*" means the preferred stock, par value \$.01 per share, of Parent.

"*Parent Representative*" means any director, officer, employee, agent, advisor (including legal, accounting and financial advisors) or other representative of Parent or its subsidiaries.

"*Parent Reserve Report*" means the Aries report on reserves and economics dated December 1, 2004, prepared by Parent and provided to the Company.

"*Parent Rights*" means the preferred share purchase rights issued pursuant to the Parent Rights Agreement.

"*Parent Rights Agreement*" means that certain Rights Agreement dated February 23, 2002 between Parent and UMB Bank, as Rights Agent.

"*Parent Subsidiary(ies)*" means any corporation more than 50% of whose outstanding voting securities, or any general partnership, joint venture, or similar entity more than 50% of whose total equity interests, is owned, directly or indirectly, by Parent, or any limited partnership of which Parent or any Parent Subsidiary is a general partner.

"*Party*" means each of the Company, Parent and Merger Sub.

"*Permitted Encumbrances*" means: (a) Liens for Taxes, assessments or other governmental charges or levies (i) if the same shall not at the particular time in question be due and payable or (if foreclosure, distraint, sale or other similar proceedings shall not have been commenced or, if commenced, shall have been stayed) are being contested in good faith by appropriate proceedings and (ii) provided that any of the Target Companies or the Parent Companies, as applicable, shall have set aside on its books such reserves (segregated to the extent required by sound accounting practices) as may be required by or consistent with GAAP; (b) Liens of carriers, warehousemen, mechanics, laborers, materialmen, landlords, vendors, workmen and operators arising by operation of law in the ordinary course of business or by a written agreement existing as of the date hereof and necessary or incident to the exploration, development, operation and maintenance of Hydrocarbon properties and related facilities and assets for sums not yet due and payable or are being contested in good faith by appropriate proceedings, provided that any of the Target Companies or the Parent Companies, as applicable, shall have set aside on its books such reserves (segregated to the extent required by sound accounting practices) as may be required by or consistent with GAAP; (c) Liens incurred in the ordinary course of business in connection with workers' compensation, unemployment insurance and other social security legislation (other than ERISA) which would not and will not, individually or in the aggregate, result in a Material Adverse Effect on the Target Companies or the Parent Companies, as applicable; (d) Liens incurred in the ordinary course of business to secure the performance of bids, tenders, trade contracts, leases, statutory obligations, surety and appeal bonds, performance and repayment bonds and other obligations of a like nature which would not and will not, individually or in the aggregate, result in a Material Adverse Effect on the Target Companies or the Parent Companies, as applicable; (e) Liens, easements, rights-of-way, restrictions, servitudes, permits, conditions, covenants, exceptions, reservations and other similar encumbrances incurred in the ordinary course of business or

## Edgar Filing: O'Neill Andrew J - Form 4

existing on property and not materially impairing the value of the assets of any of the Target Companies or any of the Parent Companies, as applicable, or interfering with the ordinary conduct of the business of any of the Target Companies or any of the Parent Companies, as applicable, or rights to any of their assets; (f) Liens created or arising by operation of law to secure a party's obligations as a purchaser of oil and gas; (g) all rights to consent by, required notices to, filings with, or other actions by Governmental Authorities to the extent customarily obtained subsequent to closing; (h) farm-out, carried working interest, joint operating, unitization, royalty, overriding royalty, sales and similar agreements relating to the exploration or development of, or production from, Hydrocarbon properties entered into in the ordinary course of business and not in violation of Section 5.1(a), Section 5.1(b), Section 5.2(a) or Section 5.2(b), as applicable, provided the effect thereof of any of such in existence as of the date hereof on the working and net revenue interest of the Target Companies or the Parent Companies, as applicable, has been properly reflected in its respective Ownership Interests; (i) any defects, irregularities or deficiencies in title to easements, rights of way or other surface use agreements that do not materially adversely affect the value of any asset of any of the Target Companies or any of the Parent Companies, as applicable; (j) Liens arising under or created pursuant to the Parent Bank Credit Agreement or the Company Bank Credit Agreement, as applicable; (k) Liens described on the applicable Disclosure Schedule; and, (l) defects in title which have not had, and would not reasonably be likely to result in, individually or in the aggregate, a Material Adverse Effect on the Target Companies or the Parent Companies, as applicable.

"*Person*" means any natural person, corporation, company, limited or general partnership, joint stock company, joint venture, association, limited liability company, trust, bank, trust company, land trust, business trust or other entity or organization, whether or not a Governmental Authority.

"*Proxy Statement/Prospectus*" means a joint proxy statement in definitive form relating to the Company Meeting and the Parent Meeting, which proxy statement shall be included in the prospectus contained in the Registration Statement.

"*RCRA*" means the Resource Conservation and Recovery Act, as amended, and any regulations promulgated thereunder.

"*Registration Statement*" means the Registration Statement on Form S-4 to be filed by Parent in connection with the issuance of Parent Common Stock pursuant to the Merger.

"*Responsible Officers*" means (a) for the Company, Gary C. Evans, Richard R. Frazier and Brad Davis, and (b) for Parent, F. H. Merelli and Paul Korus.

"*SEC*" means the Securities and Exchange Commission.

"*Securities Act*" means the Securities Act of 1933, as amended.

"*Series A Certificate*" means a certificate representing shares of Series A Preferred Stock.

"*Series A Certificate of Designations, Preferences and Rights*" means the Certificate of Designations, Preferences and Rights of Preferred Shares by Resolution of the Board of Directors Providing for Issue of Preferred Shares Designated as Series A Preferred Stock.

"*Series A Preferred Stock*" means the Company's Series A Preferred Stock, \$.001 par value per share, for which the Series A Certificate of Designations, Preferences and Rights was filed in the Office of the Secretary of State of the State of Nevada on May 21, 1993.

"*SOX*" means the Sarbanes-Oxley Act of 2002, and the rules and regulations promulgated thereunder.

"*Target Companies*" means the Company and each of the Company Subsidiaries.

"*Tax Return*" means any return, estimated Tax return, report, declaration, form, claim for refund or information statement relating to Taxes, including any schedule or attachment thereto, and including any amendment thereof.

"*Taxes*" means taxes of any kind, levies or other like assessments, customs, duties, imposts, charges or fees, including income, gross receipts, ad valorem, conservation, value added, excise, real or personal property, asset, sales, use, federal royalty, license, payroll, transaction, capital, net worth and franchise taxes, estimated taxes, withholding, employment, social security, workers' compensation, utility, severance, production, unemployment compensation, occupation, premium, windfall profits, transfer and gains taxes and other governmental taxes imposed or payable to the United States or any state, local or foreign governmental subdivision or agency thereof, and in each instance such term shall include any interest, penalties or additions to tax attributable to any such tax, including penalties for the failure to file any Tax Return or report.

"*Third-Party Consent*" means the consent or approval of any Person other than the Target Companies, any of the Parent Companies or any Governmental Authority.

"*West Dilley Prospect*" means, jointly, the West Dilley Prospect and Hope Prospect referenced in the Series A Certificate of Designations, Preferences and Rights.

Section 1.2 *References and Titles.* All references in this Agreement to Exhibits, Schedules, Articles, Sections, subsections and other subdivisions refer to the corresponding Exhibits, Schedules, Articles, Sections, subsections and other subdivisions of or to this Agreement unless expressly provided otherwise. Titles appearing at the beginning of any Articles, Sections, subsections or other subdivisions of this Agreement are for convenience only, do not constitute any part of this Agreement, and shall be disregarded in construing the language hereof. The words "this Agreement," "herein," "hereby," "hereunder" and "hereof," and words of similar import, refer to this Agreement as a whole and not to any particular subdivision unless expressly so limited. The words "this Article," "this Section" and "this subsection," and words of similar import, refer only to the Article, Section or subsection hereof in which such words occur. The word "or" is not exclusive, and the word "including" (in its various forms) means including without limitation. Pronouns in masculine, feminine or neuter genders shall be construed to state and include any other gender, and words, terms and titles (including terms defined herein) in the singular form shall be construed to include the plural and vice versa, unless the context otherwise requires. As used in the representations and warranties contained in this Agreement, the phrase "to the knowledge" of the representing Party shall mean that Responsible Officers of such Party, individually or collectively, either (a) know that the matter being represented and warranted is true and accurate or (b) have no reason, after reasonable inquiry (including, without limitation, review of their files and inquiry of pertinent management personnel), to believe that the matter being represented and warranted is not true and accurate.

## ARTICLE II

### THE MERGER

Section 2.1 *The Merger.* Subject to the terms and conditions set forth in this Agreement, at the Effective Time, Merger Sub shall be merged with and into the Company in accordance with the provisions of this Agreement. Such merger is referred to herein as the "*Merger*."

Section 2.2 *Effect of the Merger.* Upon the effectiveness of the Merger, the separate existence of Merger Sub shall cease and the Company, as the surviving corporation in the Merger (the "*Surviving Corporation*"), shall continue its corporate existence under the laws of the State of Nevada. The Merger shall have the effects specified in this Agreement and the NRS.

## Edgar Filing: O'Neill Andrew J - Form 4

### Section 2.3 *Governing Instruments, Directors and Officers of the Surviving Corporation.*

- (a) The articles of incorporation of Merger Sub, as in effect immediately prior to the Effective Time, shall be the articles of incorporation of the Surviving Corporation until duly amended in accordance with their terms and applicable law.
- (b) The bylaws of Merger Sub, as in effect immediately prior to the Effective Time, shall be the bylaws of the Surviving Corporation until duly amended in accordance with their terms and applicable law.
- (c) The directors and officers of Merger Sub at the Effective Time shall be the directors and officers, respectively, of the Surviving Corporation from the Effective Time until their respective successors have been duly elected or appointed in accordance with the articles of incorporation and bylaws of the Surviving Corporation and applicable law.

### Section 2.4 *Effect on Securities.*

- (a) *Merger Sub Stock.* At the Effective Time, by virtue of the Merger and without any action on the part of any holder thereof, each share of Merger Sub Common Stock outstanding immediately prior to the Effective Time shall be converted into one share of capital stock of the Surviving Corporation and each certificate evidencing ownership of any such shares shall continue to evidence ownership of the same number of shares of the capital stock of the Surviving Corporation.
- (b) *Parent Capital Stock.* At the Effective Time, each share of Parent capital stock then issued and outstanding shall remain issued, outstanding and unchanged.
- (c) *Company Securities.*
  - (i) *Company Common Stock.* At the Effective Time, by virtue of the Merger and without any action on the part of any holder thereof, each share of Company Common Stock that is issued and outstanding immediately prior to the Effective Time shall be converted into the right to receive shares of validly issued, fully paid and nonassessable Parent Common Stock, with each such share of Company Common Stock being converted into that number of shares of Parent Common Stock equal to the Conversion Number (the "*Merger Consideration*"). Each share of Company Common Stock, when so converted, shall automatically be cancelled and retired, shall cease to exist and shall no longer be outstanding; and the holder of any certificate representing any such shares shall cease to have any rights with respect thereto, except the right to receive the Merger Consideration (along with any cash in lieu of fractional shares of Parent Common Stock as provided in Section 2.5(e) and any unpaid dividends and distributions with respect to such shares of Parent Common Stock as provided in Section 2.5(c)), without interest, upon the surrender of such certificate in accordance with Section 2.5.
  - (ii) *Company Treasury Stock.* At the Effective Time, by virtue of the Merger, all shares of Company Common Stock that are issued and held directly by the Company as treasury stock shall be cancelled and retired and shall cease to exist, and no shares of Parent Common Stock or other consideration shall be paid or payable in exchange therefor.
  - (iii) *Company Stock Options.* Promptly after the date hereof, the Company shall use its commercially reasonable efforts to solicit the consent of the holders ("*Option Consents*") of the outstanding Company Stock Options which require holder consent to cancel such Company Stock Options (whether or not then exercisable) and the Company shall take such action as may be necessary with respect to outstanding Company Stock Options which do not require holder consent to cancel such Company Stock Options

(whether or not then exercisable), to cancel the Company Stock Options effective as of the Effective Time in exchange for a single lump sum cash payment from the Company or, at Parent's option, Parent equal to the product of (i) the number of shares of Company Common Stock subject to each such Company Stock Option (whether or not then exercisable) immediately prior to the Effective Time and (ii) the excess, if any, of the closing price of Company Common Stock on the day prior to the Closing Date over the exercise price per share under each such Company Stock Option (less the amount of any withholding taxes that may be required with respect thereto). The Company shall use its commercially reasonable efforts to obtain any required Option Consents prior to the Closing Date, but notwithstanding any provision of this Agreement to the contrary, the failure to obtain any or all of such Option Consents shall not result in a failure of a condition to Closing. In the event that any required Option Consent with respect to a Company Stock Option is not obtained prior to the Closing Date, then each such outstanding Company Stock Option, whether vested or unvested, shall be assumed by Parent and shall continue to be subject to the same terms and conditions of the Company Stock Option agreement and the 2001 Stock Option Plan (as described in Section 3.16 of the Company Disclosure Schedule), together with amendments thereto, by which it is evidenced as of the Effective Time, except that from and after the Effective Time, each such Company Stock Option shall be converted into an option to purchase Parent Common Stock in a manner that meets the requirements of Treasury Regulation Section 1.424-1.

(iv) *Company Warrants.* All Company Warrants shall remain outstanding (if outstanding in accordance with their currently existing terms) following the Effective Time. At the Effective Time, by virtue of the Merger and without any action on the part of the Company or any holder thereof, each Company Warrant shall be assumed by Parent and shall be exercisable for Parent Common Stock based on the Conversion Number but otherwise on substantially the same terms and conditions as apply immediately prior to the Effective Time.

(v) *1996 Preferred.* Prior to the Effective Time and pursuant to Section 5.26, the Company shall cause each of the Company Subsidiaries that is Controlled By the Company and who owns shares of the 1996 Preferred to convert all of the issued and outstanding shares of the 1996 Preferred into shares of Company Common Stock, pursuant to the terms set forth in the certificate of designations for the 1996 Preferred.

(vi) *Series A Preferred Stock.* At the Effective Time, by virtue of the Merger and without any action on the part of any holder thereof, each share of Series A Preferred Stock that is issued and outstanding immediately prior to the Effective Time shall be converted into the right to receive shares of validly issued, fully paid and nonassessable Parent Common Stock, with each such share of Series A Preferred Stock being converted into that number of shares of Parent Common Stock equal to the quotient obtained by dividing 20 by the number of shares of Series A Preferred Stock outstanding immediately prior to the Effective Time (the "*Series A Merger Consideration*"). Each share of Series A Preferred Stock, when so converted, shall automatically be cancelled and retired, shall cease to exist and shall no longer be outstanding; and the holder of any Series A Certificate shall cease to have any rights with respect thereto, except the right to receive the Series A Merger Consideration, which shall be issued in the form of whole shares of Parent Common Stock to the extent possible and otherwise in fractional shares of Parent Common Stock (along with any unpaid dividends and distributions with respect to such whole or fractional shares of Parent Common Stock as provided in Section 2.5(c)), without interest, upon the surrender of such certificate in accordance with Section 2.5.

Any fractional shares of Parent Common Stock issued pursuant to this Section 2.4(c)(vi) shall entitle the owner thereof to vote in the same manner as the holder of a whole share of Parent Common Stock but proportionately to the fractional interest. Parent shall (until the date referenced in the last sentence of Section 2.5(g)), if it so elects in its sole discretion, offer holders of such fractional shares of Parent Common Stock one or both of the following options: (1) the right to purchase an additional fraction of a share of Parent Common Stock (at the closing sales price of the Parent Common Stock on Parent's primary National Stock Exchange on the day immediately prior to holder's acceptance of such option) sufficient to provide the holder with a whole share and/or (2) the establishment of an agency arrangement which, on or prior to the date referenced in the last sentence of Section 2.5(g), combines fractional shares of participating holders of Parent Common Stock into whole shares, sells such shares for the account of the participating holders (to a party other than Parent, a Parent Subsidiary or an Affiliate of Parent) and then distributes the resulting sales proceeds to the participating holders in proportion to their contributed fractional share interests (with related transaction costs to be borne by Parent); provided, that the provisions of this sentence shall not preclude Parent from offering other alternatives to holders of fractional shares of Parent Common Stock and that, in no event, shall Parent effectively force holders of fractional shares of Parent Common Stock to receive cash in respect of such fractional shares.

(vii) *Other Interests.* Except as provided in Section 2.4(c) or as otherwise agreed to by the Parties, the provisions of any other plan, program or arrangement providing for the issuance or grant of any other interest in respect of the capital stock of the Target Companies shall become null and void without any payment of cash, or agreement therefor.

(viii) *Shares of Dissenting Stockholders.* Any issued and outstanding shares of Series A Preferred Stock held by a Dissenting Stockholder shall be converted into the right to receive such consideration as may be determined to be due to such Dissenting Stockholder pursuant to the provisions of the NRS, which consideration, in any case, shall be paid by the Company or the Surviving Corporation (as opposed to the Parent); provided, however, shares of Series A Preferred Stock outstanding at the Effective Time and held by a Dissenting Stockholder who shall, after the Effective Time, withdraw his demand for appraisal or lose his right of appraisal as provided in the NRS, shall be deemed to be converted, as of the Effective Time, into the right to receive the Series A Merger Consideration (without interest) in accordance with Section 2.4(c)(vi) and Section 2.5. The Company shall give Parent (A) prompt notice of any written assertions of dissenters' rights, withdrawals of such assertions and any other instruments served pursuant to the NRS received by the Company, and (B) the opportunity to direct all negotiations and proceedings with respect to assertions of dissenters' rights under the NRS. The Company shall not voluntarily make any payment with respect to any assertions of dissenters' rights and shall not, except with the prior written consent of Parent, settle or offer to settle any such demands.

Section 2.5 *Exchange of Certificates.*

(a) *Exchange Fund.* Immediately after the Effective Time, Parent shall deposit with the Exchange Agent, for the benefit of (i) the holders of shares of Company Common Stock and for exchange in accordance with this Agreement, certificates representing the shares of Parent Common Stock to be issued as Merger Consideration, and funds necessary to pay the cash amount for any fractional shares as specified in Section 2.5(e), in exchange for shares of Company Common Stock pursuant to Section 2.4(c)(i), and (ii) the holders of shares of

## Edgar Filing: O'Neill Andrew J - Form 4

Series A Preferred Stock and for exchange in accordance with this Agreement, certificates representing the shares of Parent Common Stock to be issued as Series A Merger Consideration, in exchange for shares of Series A Preferred Stock pursuant to Section 2.4(c)(vi). Such shares of Parent Common Stock, together with any dividends or distributions with respect thereto (as provided in Section 2.5(c)) and such funds, are referred to herein as the "*Exchange Fund*." The Exchange Agent, pursuant to irrevocable instructions consistent with the terms of this Agreement, shall deliver the Parent Common Stock to be issued or paid pursuant to Section 2.4(c)(i) (and the cash amount for any fractional shares as specified in Section 2.5(e) and any unpaid dividends and distributions pursuant to Section 2.5(c)) and Section 2.4(c)(vi) out of the Exchange Fund, and the Exchange Fund shall not be used for any other purpose whatsoever. The Exchange Agent shall not be entitled to vote or exercise any rights of ownership with respect to the Parent Common Stock held by it from time to time hereunder, except that it shall receive and hold all dividends or other distributions paid or distributed with respect thereto for the account of Persons entitled thereto.

(b) *Exchange Procedures.*

(i) *Common Stock.*

(1) As soon as reasonably practicable after the Effective Time, Parent shall cause the Exchange Agent to mail to each holder of record of a Company Certificate that, immediately prior to the Effective Time, represented shares of Company Common Stock, which was converted into the right to receive the Merger Consideration pursuant to Section 2.4(c)(i), a letter of transmittal to be used to effect the exchange of such Company Certificate for a Parent Certificate (and cash in lieu of fractional shares), along with instructions for using such letter of transmittal to effect such exchange. The letter of transmittal (or the instructions thereto) shall specify that delivery of any Company Certificate shall be effected, and risk of loss and title thereto shall pass, only upon delivery of such Company Certificate to the Exchange Agent and shall be in such form and have such other provisions as Parent may reasonably specify.

(2) Upon surrender to the Exchange Agent of a Company Certificate for cancellation, together with a duly completed and executed letter of transmittal and any other required documents (including, in the case of any Person constituting an "affiliate" of the Company for purposes of Rule 145(c) and (d) under the Securities Act, a written agreement from such Person as described in Section 5.10, if not theretofore delivered to Parent): (A) the holder of such Company Certificate shall be entitled to receive in exchange therefor a Parent Certificate representing the number of whole shares of Parent Common Stock that such holder has the right to receive pursuant to Section 2.4(c)(i), any cash in lieu of fractional shares of Parent Common Stock as provided in Section 2.5(e), and any unpaid dividends and distributions that such holder has the right to receive pursuant to Section 2.5(c) (after giving effect to any required withholding of taxes); and (B) the Company Certificate so surrendered shall forthwith be cancelled. No interest shall be paid or accrued on the Merger Consideration, cash in lieu of fractional shares, or unpaid dividends and distributions, if any, payable to holders of Company Certificates.

(3) In the event of a transfer of ownership of Company Common Stock that is not registered in the transfer records of the Company, a Parent Certificate representing the appropriate number of shares of Parent Common Stock (along with any cash in lieu of fractional shares and any unpaid dividends and distributions that such holder has the right to receive) may be issued or paid to a transferee if the Company Certificate representing such shares of Company Common Stock is presented to the Exchange Agent

accompanied by all documents required to evidence and effect such transfer, including such signature guarantees as Parent or the Exchange Agent may request, and to evidence that any applicable stock transfer taxes have been paid.

(4) Until surrendered as contemplated by this Section 2.5(b)(i), each Company Certificate shall be deemed at any time after the Effective Time to represent only the right to receive upon such surrender a Parent Certificate representing shares of Parent Common Stock as provided in Section 2.4(c)(i) (along with any cash in lieu of fractional shares and any unpaid dividends and distributions).

(ii) *Series A Preferred Stock.*

(1) As soon as reasonably practicable after the Effective Time, Parent shall cause the Exchange Agent to mail, to the extent such holder's mailing address is known, to each holder of record of a Series A Certificate that, immediately prior to the Effective Time, represented shares of Series A Preferred Stock, which was converted into the right to receive the Series A Merger Consideration pursuant to Section 2.4(c)(vi), a letter of transmittal to be used to effect the exchange of such Series A Certificate for a Parent Certificate, along with instructions for using such letter of transmittal to effect such exchange. The letter of transmittal (or the instructions thereto) shall specify that delivery of any Series A Certificate shall be effected, and risk of loss and title thereto shall pass, only upon delivery of such Series A Certificate to the Exchange Agent and shall be in such form and have such other provisions as Parent may reasonably specify.

(2) Upon surrender to the Exchange Agent of a Series A Certificate for cancellation, together with a duly completed and executed letter of transmittal and any other required documents (including, in the case of any Person constituting an "affiliate" of the Company for purposes of Rule 145(c) and (d) under the Securities Act, a written agreement from such Person as described in Section 5.10, if not theretofore delivered to Parent): (A) the holder of such Series A Certificate shall be entitled to receive in exchange therefor a Parent Certificate representing the number of shares of Parent Common Stock that such holder has the right to receive pursuant to Section 2.4(c)(vi) and any unpaid dividends and distributions that such holder has the right to receive pursuant to Section 2.5(c) (after giving effect to any required withholding of taxes); and (B) the Series A Certificate so surrendered shall forthwith be cancelled. No interest shall be paid or accrued on the Series A Merger Consideration or unpaid dividends and distributions, if any, payable to holders of Series A Certificates.

(3) In the event of a transfer of ownership of Series A Preferred Stock that is not registered in the transfer records of the Company, a Parent Certificate representing the appropriate number of shares of Parent Common Stock (along with any unpaid dividends and distributions that such holder has the right to receive) may be issued or paid to a transferee if the Series A Certificate representing such shares of Series A Preferred Stock is presented to the Exchange Agent accompanied by all documents required to evidence and effect such transfer, including such signature guarantees as Parent or the Exchange Agent may request, and to evidence that any applicable stock transfer taxes have been paid.

(4) Until surrendered as contemplated by this Section 2.5(b)(ii), each Series A Certificate shall be deemed at any time after the Effective Time to represent only the right to receive upon such surrender a Parent Certificate representing shares of Parent Common Stock as provided in Section 2.4(c)(vi) (along with any unpaid dividends and distributions).

(c) *Distributions with Respect to Unexchanged Shares.*

(i) *Common Stock.* No dividends or other distributions with respect to Parent Common Stock declared or made after the Effective Time with a record date after the Effective Time shall be paid to the holder of any unsurrendered Company Certificate. Subject to the effect of applicable laws: (A) at the time of the surrender of a Company Certificate for exchange in accordance with the provisions of this Section 2.5, there shall be paid to the surrendering holder, without interest, the amount of dividends or other distributions (having a record date after the Effective Time but on or prior to surrender and a payment date on or prior to surrender) theretofore paid with respect to the number of whole shares of Parent Common Stock that such holder is entitled to receive (less the amount of any withholding taxes that may be required with respect thereto); and (B) at the appropriate payment date, and, without duplicating any payment made under clause (A) above, there shall be paid to the surrendering holder, without interest, the amount of dividends or other distributions (having a record date after the Effective Time but on or prior to surrender and a payment date subsequent to surrender) payable with respect to the number of whole shares of Parent Common Stock that such holder receives (less the amount of any withholding taxes that may be required with respect thereto).

(ii) *Series A Preferred Stock.* No dividends or other distributions with respect to Parent Common Stock declared or made after the Effective Time with a record date after the Effective Time shall be paid to the holder of any unsurrendered Series A Certificate. Subject to the effect of applicable laws: (A) at the time of the surrender of a Series A Certificate for exchange in accordance with the provisions of this Section 2.5, there shall be paid to the surrendering holder, without interest, the amount of dividends or other distributions (having a record date after the Effective Time but on or prior to surrender and a payment date on or prior to surrender) theretofore paid with respect to the number of shares of Parent Common Stock that such holder is entitled to receive (less the amount of any withholding taxes that may be required with respect thereto); and (B) at the appropriate payment date, and, without duplicating any payment made under clause (A) above, there shall be paid to the surrendering holder, without interest, the amount of dividends or other distributions (having a record date after the Effective Time but on or prior to surrender and a payment date subsequent to surrender) payable with respect to the number of shares of Parent Common Stock that such holder receives (less the amount of any withholding taxes that may be required with respect thereto).

(d) *No Further Ownership Rights in Company Common Stock or Series A Preferred Stock.* All shares of Parent Common Stock issued as the Merger Consideration upon the surrender for exchange of shares of Company Common Stock in accordance with the terms hereof (together with any cash paid pursuant to Section 2.5(e)) shall be deemed to have been issued in full satisfaction of all rights pertaining to such shares of Company Common Stock. All shares of Parent Common Stock issued as the Series A Merger Consideration upon the surrender for exchange of shares of Series A Preferred Stock in accordance with the terms hereof shall be deemed to have been issued in full satisfaction of all rights pertaining to such shares of Series A Preferred Stock. After the Effective Time, there shall be no further registration of transfers on the Surviving Corporation's stock transfer books of the shares of Company Common Stock or Series A Preferred Stock that were outstanding immediately prior to the Effective Time. If, after the Effective Time, a Company Certificate or Series A Certificate is presented to the Surviving Corporation for any reason, it shall be cancelled and exchanged as provided in this Section 2.5.

(e) *Treatment of Fractional Shares.* Fractional shares, if any, of Parent Common Stock shall be issued in the Merger to a holder of Series A Preferred Stock in accordance with

Section 2.4(c)(vi), no Parent Certificates or scrip representing fractional shares of Parent Common Stock shall be issued in the Merger to a holder of Company Common Stock and, except as provided in this Section 2.5(e), Section 2.4(c)(vi) or Section 2.5(c)(ii) no dividend or other distribution, stock split or interest shall relate to any such fractional share, and except as provided in Section 2.4(c)(vi) such fractional share shall not entitle the owner thereof to vote or to any other rights of a stockholder of Parent. In lieu of any fractional share of Parent Common Stock to which a holder of Company Common Stock would otherwise be entitled, such holder, upon surrender of a Company Certificate as described in this Section 2.5, shall be paid an amount in cash (without interest) determined by multiplying (i) the Market Price by (ii) the fraction of a share of Parent Common Stock to which such holder would otherwise be entitled, in which case Parent shall make available to the Exchange Agent, as part of the Exchange Fund, the amount of cash necessary to make such payments. The Parties acknowledge that such payment of cash consideration in lieu of issuing fractional shares of Parent Common Stock to a holder of Company Common Stock was not separately bargained for consideration, but merely represents a mechanical rounding off for purposes of simplifying the corporate and accounting problems that would otherwise be caused by the issuance of such fractional shares of Parent Common Stock.

(f) *Termination of Exchange Fund.* Any portion of the Exchange Fund held by the Exchange Agent in accordance with the terms of this Section 2.5 that remains unclaimed by the former stockholders of the Company for a period of six months following the Effective Time shall be delivered to Parent, upon demand. Thereafter, any former stockholders of the Company who have not theretofore complied with the provisions of this Section 2.5 shall look only to Parent for payment of their claim for Parent Common Stock, any cash in lieu of fractional shares of Parent Common Stock (with respect to former holders of Company Common Stock) and any dividends or distributions with respect to Parent Common Stock (all without interest).

(g) *No Liability.* Neither Parent, the Company, the Surviving Corporation, the Exchange Agent nor any other Person shall be liable to any former holder of shares of Company Common Stock or Series A Preferred Stock for any amount properly delivered to any public official pursuant to any applicable abandoned property, escheat or similar law. Any amounts remaining unclaimed by former holders of Company Common Stock or Series A Preferred Stock for a period of three years following the Effective Time (or such earlier date immediately prior to the time at which such amounts would otherwise escheat to or become property of any governmental entity) shall, to the extent permitted by applicable law, become the property of Parent, free and clear of any claims or interest of any such holders or their successors, assigns or personal representatives previously entitled thereto.

(h) *Lost, Stolen, or Destroyed Certificates.* If any Company Certificate or Series A Certificate shall have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the Person claiming such Company Certificate or Series A Certificate to be lost, stolen or destroyed, and, if required by Parent or the Exchange Agent, the posting by such Person of a bond, in such reasonable amount as Parent or the Exchange Agent may direct, as indemnity against any claims that may be made against it with respect to such Company Certificate or Series A Certificate, the Exchange Agent shall (i) issue in exchange for such lost, stolen or destroyed Company Certificate the shares of Parent Common Stock (along with any cash in lieu of fractional shares pursuant to Section 2.5(e) and any unpaid dividends and distributions pursuant to Section 2.5(c)) deliverable with respect thereto pursuant to this Agreement and (ii) issue in exchange for such lost, stolen or destroyed Series A Certificate the shares of Parent Common Stock (along with any unpaid dividends and distributions pursuant to Section 2.5(c)) deliverable with respect thereto pursuant to this Agreement.

Section 2.6 *Associated Rights.* References in this Agreement to Company Common Stock shall include, unless the context requires otherwise, the associated rights (the "*Company Rights*") issued pursuant to the Rights Agreement dated as of January 6, 1998 between the Company and Securities Transfer Corporation (the "*Company Rights Agreement*").

Section 2.7 *Withholding.* Each of Parent, the Surviving Corporation, and the Exchange Agent shall be entitled to deduct and withhold from the consideration otherwise payable pursuant to this Agreement to any holder of Company Common Stock (including Company Common Stock held as a result of the conversion of the 1996 Preferred prior to the Effective Time pursuant to Section 5.26) and any holder of Series A Preferred Stock such amounts as Parent, the Surviving Corporation, or the Exchange Agent are required to deduct and withhold under the Code or any provision of state, local, or foreign Tax law, with respect to the making of such payment. To the extent that amounts are so withheld by Parent, the Surviving Corporation, or the Exchange Agent, such withheld amounts shall be treated for all purposes of this Agreement as having been paid to the holder of Company Common Stock or Series A Preferred Stock, as the case may be, in respect of whom such deduction and withholding was made by Parent, the Surviving Corporation, or the Exchange Agent, as the case may be.

Section 2.8 *Closing.* The Closing shall take place on the Closing Date at such time and place as is agreed upon by Parent and the Company.

Section 2.9 *Effective Time of the Merger.* The Merger shall become effective immediately when the Articles of Merger and any other filings or recordings required under the NRS are accepted for filing by the Secretary of State of Nevada, or at such time thereafter as is provided in the Articles of Merger (the "*Effective Time*"). As soon as practicable after the Closing, the Articles of Merger shall be filed, and the Effective Time shall occur, on the Closing Date; provided, however, that the Articles of Merger may be filed prior to the Closing Date or prior to the Closing so long as they provide for an effective time that occurs on the Closing Date immediately after the Closing.

Section 2.10 *Taking of Necessary Action; Further Action.* Subject to the other terms and conditions of this Agreement, each of Parent, Merger Sub and the Company shall use all reasonable efforts to take all such actions as may be necessary or appropriate in order to effectuate the Merger under the NRS as promptly as commercially practicable. If, at any time after the Effective Time, any further action is necessary or desirable to carry out the purposes of this Agreement and to vest the Surviving Corporation with full right, title and possession to all assets, real estate and other property, rights, privileges, powers and franchises of either of Merger Sub or the Company, the officers and directors of the Surviving Corporation are fully authorized, in the name of the Surviving Corporation or otherwise to take, and shall take, all such lawful and necessary action.

### ARTICLE III

#### REPRESENTATIONS AND WARRANTIES OF THE COMPANY

The Company hereby represents and warrants to Parent and Merger Sub as follows, except as set forth, specifically with reference to a particular section below, on the Company Disclosure Schedule:

Section 3.1 *Organization.* Each of the Target Companies: (a) is a corporation or other entity duly organized, validly existing and in good standing under the laws of its state of incorporation or formation; (b) has the requisite power and authority to own, lease and operate its properties and to conduct its business as it is presently being conducted; and (c) is duly qualified to do business as a foreign corporation or limited partnership, as applicable, and is in good standing, in each jurisdiction where the character of the properties owned or leased by it or the nature of its activities makes such qualification necessary (except where any failure to be so qualified or to be in good standing would not, individually or in the aggregate, have a Material Adverse Effect on the Company). Accurate and

## Edgar Filing: O'Neill Andrew J - Form 4

complete copies of the certificate of incorporation, bylaws, minute books and/or other organizational documents of each of the Target Companies have heretofore been delivered to Parent. The Company has no corporate or other subsidiaries other than the Company Subsidiaries.

Section 3.2 *Other Equity Interests.* None of the Target Companies owns any equity interest in any general or limited partnership, corporation, limited liability company or joint venture other than the Company Subsidiaries or as listed on the Company Disclosure Schedule (other than joint operating and other ownership arrangements and tax partnerships entered into in the ordinary course of business that, individually or in the aggregate, are not material to the operations or business of the Target Companies, taken as a whole, and that do not entail any material liabilities).

Section 3.3 *Authority and Enforceability.* The Company has the requisite corporate power and authority to enter into and deliver this Agreement and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of the Company) to consummate the transactions contemplated hereby. The execution and delivery of this Agreement and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of the Company) the consummation of the transactions contemplated hereby have been duly and validly authorized by all necessary corporate action on the part of the Company, including approval by the Board of Directors of the Company, and no other corporate proceedings on the part of the Company are necessary to authorize the execution or delivery of this Agreement or (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of the Company) to consummate the transactions contemplated hereby. This Agreement has been duly and validly executed and delivered by the Company and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of the Company and assuming that this Agreement constitutes a valid and binding obligation of Parent and Merger Sub) constitutes a valid and binding obligation of the Company, enforceable against the Company in accordance with its terms.

Section 3.4 *No Violations.* The execution and delivery of this Agreement do not, and the consummation of the transactions contemplated hereby and compliance by the Company with the provisions hereof will not, conflict with, result in any violation of or default (with or without notice or lapse of time or both) under, give rise to a right of termination, cancellation or acceleration of any obligation or to the loss of a material benefit under, or result in the creation of any Lien on any of the properties or assets of any of the Target Companies under, any provision of (a) the certificate or articles of incorporation, bylaws or any other organizational documents of any of the Target Companies, (b) any loan or credit agreement, note, bond, mortgage, indenture, lease, permit, concession, franchise, license or other agreement or instrument applicable to the Target Companies, or (c) assuming the consents, approvals, authorizations, permits, filings and notifications referred to in Section 3.5 are duly and timely obtained or made, any judgment, order, decree, statute, law, ordinance, rule or regulation applicable to the Target Companies or any of their respective properties or assets, other than (y) in the case of clause (b) above, any such conflict, violation, default, right, loss or Lien that may arise under the Company Bank Credit Agreement, and (z) in the case of clause (b) or (c) above, any such conflict, violation, default, right, loss or Lien that, individually or in the aggregate, would not have a Material Adverse Effect on the Company.

Section 3.5 *Consents and Approvals.* No consent, approval, order or authorization of, registration, declaration or filing with, or permit from, any Governmental Authority is required by or with respect to any of the Target Companies in connection with the execution and delivery of this Agreement by the Company or the consummation by the Company of the transactions contemplated hereby, except for the following: (a) any such consent, approval, order, authorization, registration, declaration, filing or permit which the failure to obtain or make would not, individually or in the aggregate, have a Material Adverse Effect on the Company; (b) the filing of the Articles of Merger with the Secretary of State of Nevada pursuant to applicable provisions of the NRS; (c) the filing of a

## Edgar Filing: O'Neill Andrew J - Form 4

pre-merger notification report by the Company as may be required under the HSR Act and the expiration or termination of the applicable waiting period; (d) the filing with the SEC of the Proxy Statement/Prospectus and such reports under Section 13(a) of the Exchange Act and such other compliance with the Exchange Act and the Securities Act and the rules and regulations of the SEC thereunder as may be required in connection with this Agreement and the transactions contemplated hereby and the obtaining from the SEC of such orders as may be so required; (e) such filings and approvals as may be required by any applicable state securities, "blue sky" or takeover laws or Environmental Laws; and (f) such filings and approvals as may be required by any foreign pre-merger notification, securities, corporate or other law, rule or regulation. No Third-Party Consent is required by or with respect to any of the Target Companies in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby, except for (x) any such Third-Party Consent which the failure to obtain would not, individually or in the aggregate, have a Material Adverse Effect on the Company, (y) the valid approval of the Company Proposal by the stockholders of the Company, and (z) any consent, approval or waiver required by the terms of the Company Bank Credit Agreement.

**Section 3.6 SEC Documents.** The Company (i) has made available to Parent a true and complete copy of each report, schedule, registration statement and definitive proxy statement filed by the Company with the SEC since January 1, 2001, and prior to the date of this Agreement (and any amendments thereto), including exhibits and other information incorporated therein (the "*Company SEC Documents*"), which are all the documents (other than preliminary material) that the Company was required to file with the SEC since such date, and (ii) has delivered to Parent a true and complete copy of all correspondence between the SEC and any of the Target Companies since January 1, 2003. Each of the Company SEC Documents was timely filed with the SEC. As of their respective dates, each of the Company SEC Documents, as amended (including the financial statements and schedules provided therein or incorporated by reference therein) (i) complied in all material respects with the requirements of the Securities Act, the Exchange Act and SOX, as the case may be, and the rules and regulations of the SEC thereunder applicable to such Company SEC Documents, and (ii) did not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading.

**Section 3.7 Financial Statements.** The Company Financial Statements were prepared in accordance with GAAP applied on a consistent basis during the periods involved (except as may be indicated in the notes thereto or, in the case of unaudited statements, as permitted by Rule 10-01 of Regulation S-X of the SEC) and fairly present (in the case of the unaudited statements, subject to normal, recurring adjustments) the consolidated financial position of the Company and its subsidiaries as of their respective dates and the consolidated results of operations and the consolidated cash flows of the Company and its subsidiaries for the periods presented therein. The books and records of the Target Companies have been, and are being, maintained in accordance with GAAP and any other applicable legal and accounting requirements and reflect only actual transactions. Deloitte & Touche LLC is an independent public accounting firm with respect to the Target Companies and has not resigned or been dismissed by the Target Companies from such capacity.

### Section 3.8 Capital Structure.

(a) The authorized capital stock of the Company consists of 200,000,000 shares of Company Common Stock and 10,000,000 shares of Company Preferred Stock, 216,000 shares of which have been designated as Series A Preferred Stock, 925,000 shares of which have been designated as Series B Preferred Stock (the "*Series B Preferred*"), 625,000 shares of which have been designated as Series C Preferred Stock (the "*Series C Preferred*"), 1,000,000 shares of which have been designated as 1996 Series A Convertible Preferred Stock (the "*1996 Preferred*"), 500,000 shares of which have been designated as 1998 Series A Junior Participating Preferred Stock (the "*1998 Preferred*") and 50,000 shares of which have been designated as 1999 Series A 8% Convertible Preferred Stock (the "*1999 Preferred*").

## Edgar Filing: O'Neill Andrew J - Form 4

(b) As of the close of business on January 24, 2005, there were (i) 91,469,696 issued and outstanding shares of Company Common Stock (including 2,163,992 shares of Company Common Stock held by the KSOP (as herein defined) and including 3,926,034 shares of Company Common Stock held directly or indirectly by the Company as treasury stock), (ii) 80,000 issued and outstanding shares of Series A Preferred Stock, (iii) no shares of the Series B Preferred issued or outstanding, (iv) no shares of the Series C Preferred issued or outstanding, (v) 1,000,000 shares of the 1996 Preferred issued and outstanding, (vi) no shares of the 1998 Preferred issued or outstanding, (vii) no shares of the 1999 Preferred issued or outstanding, (viii) Company Stock Options that were issued and outstanding relating to 5,673,002 shares of Company Common Stock, (ix) reserved for issuance up to 10,255,000 shares of Company Common Stock upon conversion of the Company Convertible Notes (assuming the Company Convertible Notes were to be converted as of January 24, 2005 and the Ten Day Average Closing Stock Price (as defined in the indenture relating to the Company Convertible Notes) were calculated for the period ended January 24, 2005, the number of shares of Company Common Stock issuable upon the conversion of the Company Convertible Notes would be 353,366), and (x) Company Warrants relating to 7,228,457 shares of Company Common Stock that were issued and outstanding. As of the close of business on January 24, 2005 and as of the date hereof, 3,926,034 shares of Company Common Stock were issued and held directly or indirectly by the Company as treasury stock and no shares of Company Preferred Stock were issued and held directly by the Company as treasury stock. As of the close of business on January 24, 2005 and as of the date hereof, shares of Company Common Stock were issued and held by a Company Subsidiary or Affiliate of the Company and 1,000,000 shares of the 1996 Preferred were issued and held by Company Subsidiaries that are Controlled By the Company, which represents all the issued and outstanding shares of the 1996 Preferred.

(c) Except as set forth in Section 3.8(b), there are outstanding (i) no shares of capital stock or other voting securities of the Company, (ii) no securities of the Company or any other Person convertible into or exchangeable or exercisable for shares of capital stock or other voting securities of the Company, (iii) no stock appreciation rights or phantom stock rights to which any of the Target Companies are obligated and (iv) no subscriptions, options, warrants, calls, rights (including preemptive rights), commitments, understandings or agreements to which the Company is a party or by which it is bound obligating the Company to issue, deliver, sell, purchase, redeem or acquire shares of capital stock or other voting securities of the Company (or securities convertible into or exchangeable or exercisable for shares of capital stock or other voting securities of the Company) or obligating the Company to grant, extend or enter into any such subscription, option, warrant, call, right, commitment, understanding or agreement.

(d) All outstanding shares of Company capital stock are validly issued, fully paid and nonassessable and not subject to any preemptive right. There are no shares of Company capital stock reserved for issuance.

(e) All outstanding shares of capital stock and other voting securities of each of the corporate Company Subsidiaries are (i) validly issued, fully paid and nonassessable and not subject to any preemptive right, and (ii) owned by the Target Companies, free and clear of all Liens, claims and options of any nature (except for Permitted Encumbrances). There are outstanding (y) no securities of any Company Subsidiary or any other Person convertible into or exchangeable or exercisable for shares of capital stock, other voting securities or other equity interests of such Company Subsidiary, and (z) no subscriptions, options, warrants, calls, rights (including preemptive rights), commitments, understandings or agreements to which any Company Subsidiary is a party or by which it is bound obligating such Company Subsidiary to issue, deliver, sell, purchase, redeem or acquire shares of capital stock, other voting securities or other equity interests of such Company Subsidiary (or securities convertible into or exchangeable or exercisable for shares of capital stock, other voting securities or other equity interests of such Company Subsidiary) or

obligating any Company Subsidiary to grant, extend or enter into any such subscription, option, warrant, call, right, commitment, understanding or agreement.

(f) There is no stockholder agreement, voting trust or other agreement or understanding to which the Company is a party or by which it is bound relating to the voting of any shares of the capital stock of any of the Target Companies. There are no bonds, debentures, notes or other indebtedness of the Target Companies having the right to vote (or convertible into, or exchangeable for, securities having the right to vote) on any matters on which the stockholders of any of the Target Companies may vote.

(g) None of the Target Companies is obligated to redeem or otherwise repurchase any of its capital stock.

(h) The Company is in compliance with the applicable listing rules of the New York Stock Exchange and has not, since January 1, 2003, received any notice from the New York Stock Exchange asserting any non-compliance with such rules.

(i) Following the Effective Time, there shall be no securities of any of the Surviving Corporation, the Target Companies or any other Person convertible into or exchangeable or exercisable for shares of capital stock or other voting securities of the Surviving Corporation or any of the Target Companies.

(j) The Board of Directors has made an irrevocable determination that an event similar to the commencement of a tender or exchange offer which would, if successful, result in a Change of Control (as defined in the Company's stock option agreements) has occurred and would, if consummated, materially alter the structure or business of the Company.

(k) The exercise price for the Company Warrants is \$15.00 per share of Company Common Stock. The conversion price of the Company Convertible Notes is, as of the date of this Agreement, \$12.19 per share of Company Common Stock which price will be adjusted immediately following the TEL Distribution pursuant to the terms of the indenture relating to the Company Convertible Notes. For example, based on an average closing price for Company Common Stock for the 20-trading day period ended January 18, 2005 of \$12.427, and the closing price of the TEL Units on January 18, 2005 of \$10.395, the revised conversion price would be \$12.032.

(l) There have never been any liquidation proceeds of any kind regarding the West Dille Prospect. There are no accrued or unpaid dividends on the Series A Preferred Stock.

Section 3.9 *No Undisclosed Liabilities.* There are no material liabilities of any of the Target Companies of any kind whatsoever, whether accrued, contingent, absolute, determined, determinable or otherwise, other than (a) liabilities adequately provided for in the Company Financial Statements, (b) liabilities incurred in the ordinary course of business subsequent to September 30, 2004, (c) liabilities under this Agreement, and (d) liabilities set forth on Section 3.9 of the Company Disclosure Schedule.

Section 3.10 *Absence of Certain Changes or Events.* Except as specifically contemplated by this Agreement, since September 30, 2004, none of the Target Companies has done any of the following:

(a) Discharged or satisfied any Lien or paid any obligation or liability, absolute or contingent, other than current liabilities incurred and paid in the ordinary course of business and consistent with past practices;

(b) Paid or declared any dividends or distributions (other than in relation to the TEL Distribution), purchased, redeemed, acquired or retired any indebtedness, stock or other securities from its stockholders or other securityholders (except as relates to the conversion of the 1996 Preferred in accordance with Section 5.26), made any loans or advances or guaranteed any loans

## Edgar Filing: O'Neill Andrew J - Form 4

or advances to any Person (other than loans, advances or guaranties made in the ordinary course of business and consistent with past practices), or otherwise incurred or suffered to exist any liabilities (other than current liabilities incurred in the ordinary course of business and consistent with past practices);

(c) Except for Permitted Encumbrances, suffered or permitted any Lien to arise or be granted or created against or upon any of its assets;

(d) Canceled, waived or released any rights or claims against, or indebtedness owed by, third parties (including, without limitation, any standstill agreements);

(e) Amended its articles of incorporation, bylaws or other organizational documents;

(f) Made or permitted any amendment, supplement, modification or termination of, or any acceleration under, any Company Material Agreement;

(g) Sold, leased, transferred, assigned or otherwise disposed of (i) any Oil and Gas Interests of the Company that, individually or in the aggregate, had a value of \$1,000,000 or more, or (ii) any other assets that, individually or in the aggregate, had a value at the time of such lease, transfer, assignment or disposition of \$1,000,000 or more (and, in each case where a sale, lease, transfer, assignment or other disposition was made, it was made for fair consideration in the ordinary course of business); provided, however, that this Section 3.10(g) shall not apply to the sale of Hydrocarbons in the ordinary course of business;

(h) Made any investment in or contribution, payment, advance or loan to any Person (other than investments, contributions, payments or advances, or commitments with respect thereto, less than \$1,000,000 in the aggregate, made in the ordinary course of business and consistent with past practices);

(i) Paid, loaned or advanced (other than the payment, advance or reimbursement of expenses in the ordinary course of business and consistent with past practices) any amounts to, or sold, transferred or leased any of its assets to, or entered into any other transaction with, any of its Affiliates other than the Target Companies;

(j) Made any material change in any of the accounting principles followed by it or the method of applying such principles;

(k) Entered into any material transaction (other than this Agreement) except in the ordinary course of business and consistent with past practices;

(l) Increased benefits or benefit plan costs or changed bonus, insurance, pension, compensation or other benefit plan or arrangement or granted any bonus or increase in wages, salary or other compensation or made any other change in employment terms to (or entered into severance or retention arrangements of any type with) any officer, director or employee of any of the Target Companies (except in the ordinary course of business and consistent with past practices);

(m) Issued any note, bond or other debt security or created, incurred, assumed, or guaranteed any indebtedness for borrowed money or capitalized lease obligation involving more than \$1,000,000 in the aggregate (other than pursuant to the Company Bank Credit Agreement);

(n) Delayed, postponed or accelerated the payment of accounts payable or other liabilities (except in the ordinary course of business and consistent with past practices);

(o) Canceled, compromised, waived or released any right or claim (or series of related rights and claims) involving more than \$1,000,000 in the aggregate (except in the ordinary course of business and consistent with past practices);

## Edgar Filing: O'Neill Andrew J - Form 4

(p) Except as relates to the conversion of the 1996 Preferred in accordance with Section 5.26, issued, sold, or otherwise disposed of any of its capital stock or other equity interest or granted any option, warrant, or other right to purchase or obtain (including upon conversion, exchange, or exercise) any of its capital stock or other equity interest (or reduced the exercise or conversion price or extended the time for exercise or conversion, other than in accordance with mandatory contractual provisions, of any rights, options or warrants to acquire its capital stock or securities);

(q) Made any loan to, or entered into any other transaction with, any of its directors, officers or employees (except in the ordinary course of business and consistent with past practices and not involving more than \$100,000 in the aggregate);

(r) Made or pledged to make any charitable or other capital contribution outside the ordinary course of business and consistent with past practices;

(s) Made or committed to make capital expenditures in excess of \$195,000,000 in the aggregate;

(t) Made or changed any material Tax election or settled or compromised any material income Tax liability;

(u) Entered into, modified or amended any Derivative Transaction;

(v) Otherwise been involved in any other material occurrence, event, incident, action, failure to act, or transaction involving any of the Target Companies (except in the ordinary course of business and consistent with past practices);

(w) Entered into any transaction with an Affiliate (except in the ordinary course of business and consistent with past practices);

(x) Agreed, whether in writing or otherwise, to do any of the foregoing; or

(y) Suffered any Material Adverse Effect.

Section 3.11 *Compliance with Laws, Material Agreements and Permits.* None of the Target Companies is in violation of, or in default under, and no event has occurred that (with notice or the lapse of time or both) would constitute a violation of or default under: (a) its certificate of incorporation, bylaws or other organizational documents, (b) any applicable law, rule, regulation, ordinance, order, writ, decree or judgment of any Governmental Authority, or (c) any Company Material Agreement, except (in the case of clause (b) or (c) above) for any violation or default that would not, individually or in the aggregate, have a Material Adverse Effect on the Company. Each of the Target Companies has obtained and holds all permits, licenses, variances, exemptions, orders, franchises, approvals and authorizations of all Governmental Authorities necessary for the lawful conduct of its business and the lawful ownership, use and operation of its assets ("*Company Permits*"), except for Company Permits which the failure to obtain or hold would not, individually or in the aggregate, have a Material Adverse Effect on the Company. None of the Company Permits shall be adversely affected by the consummation of the transactions contemplated under this Agreement or requires any filing or consent in connection therewith. Each of the Target Companies is in compliance with the terms of its Company Permits, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on the Company. No investigation or review by any Governmental Authority with respect to any of the Target Companies is pending or, to the knowledge of the Company, threatened, other than those the outcome of which would not, individually or in the aggregate, have a Material Adverse Effect on the Company. To the knowledge of the Company, no other party to any Company Material Agreement is in material breach of the terms, provisions or conditions of such Company Material Agreement. Each Company Material Agreement (other than those listed in the Company's Form 10-K for the year ended December 31, 2003, or in subsequent

## Edgar Filing: O'Neill Andrew J - Form 4

filings, as an exhibit to the Company SEC Documents) is listed on Section 3.11 of the Company Disclosure Schedule.

**Section 3.12 *Governmental Regulation.*** None of the Target Companies is subject to regulation under the Public Utility Holding Company Act of 1935, the Federal Power Act, the Interstate Commerce Act, the Investment Company Act of 1940 or any state public utilities laws.

**Section 3.13 *Litigation.*** (a) No litigation, arbitration, investigation or other proceeding is pending or, to the knowledge of the Company, threatened against any of the Target Companies or their respective assets which could reasonably be expected to have a Material Adverse Effect on the Company; and (b) none of the Target Companies is subject to any outstanding injunction, judgment, order, decree or ruling (other than routine oil and gas field regulatory orders). There is no litigation, proceeding or investigation pending or, to the knowledge of the Company, threatened against or affecting any of the Target Companies that questions the validity or enforceability of this Agreement or any other document, instrument or agreement to be executed and delivered by the Company in connection with the transactions contemplated hereby.

**Section 3.14 *No Restrictions.*** None of the Target Companies is a party to: (a) any agreement, indenture or other instrument that contains restrictions with respect to the payment of dividends or other distributions with respect to its capital, other than the Company Bank Credit Agreement; (b) any financial arrangement with respect to or creating any indebtedness to any Person (other than indebtedness (i) reflected in the Company Financial Statements and, with respect to any indebtedness that is material (individually or, together with related items, in the aggregate) listed in Section 3.14 of the Company Disclosure Schedule, (ii) under the Company Bank Credit Agreement, or (iii) incurred in the ordinary course of business consistent with past practices since September 30, 2004), unless such indebtedness is not material (individually or, together with related items, in the aggregate) to the Target Companies taken as a whole; (c) any agreement, contract or commitment relating to the making of any advance to, or investment in, any Person (other than restrictions under the Company Bank Credit Agreement and advances in the ordinary course of business and consistent with past practices); (d) any guaranty or other contingent liability with respect to any indebtedness or obligation of any Person (other than (i) guaranties pursuant to the Company Bank Credit Agreement, (ii) guaranties undertaken in the ordinary course of business, and (iii) the endorsement of negotiable instruments for collection in the ordinary course of business); or (e) any agreement, contract or commitment limiting in any respect its ability to compete with any Person or otherwise conduct business of any line or nature. The amount of the guaranty by Company under the Continuing Guaranty by the Company to Compass Bank, dated December 20, 2004, with respect to indebtedness of Metrix Networks, Inc., does not exceed \$500,000, in terms of its total commitment or its current guaranty.

### Section 3.15 *Taxes.*

(a) Each of the Target Companies and any affiliated, consolidated, combined, aggregated, or unitary group of which any such entity is or was a member has (i) timely filed in accordance with applicable law all Tax Returns required to be filed by it (all such Tax Returns being accurate and complete in all material respects), (ii) timely paid all Taxes required to be paid by it (whether shown on a Tax Return or not) other than Taxes that are not yet due, (iii) complied with all applicable laws, rules and regulations relating to the payment and withholding of Taxes, and (iv) timely withheld from employee wages and paid over to the proper Governmental Authorities all amounts required to be so withheld and paid over, except where the failure to file, pay, comply with or withhold would not, individually or in the aggregate, have a Material Adverse Effect on the Company.

(b) (i) No audits or other administrative or court proceedings are presently pending with regard to any material Taxes for which any of the Target Companies would be liable; and (ii) there are no pending requests for Tax rulings from any Governmental Authority, no outstanding

subpoenas or requests for information by any Governmental Authority with respect to any Taxes, no proposed reassessments by any Governmental Authority of any property owned or leased, and no agreements in effect to extend the time to file any Tax Return or the period of limitations for the assessment or collection of any Taxes for which any of the Target Companies would be liable.

(c) (i) There are no Liens on any of the assets of the Target Companies for unpaid Taxes, other than Liens for Taxes not yet due and payable; (ii) none of the Target Companies has any liability for the Taxes of any other Person (other than one or more of the Target Companies) under Treasury Regulation Section 1.1502-6 (or any analogous state, local or foreign law), as a successor or transferee, or by contract; and (iii) none of the Target Companies is a party to or bound by any Tax sharing, allocation, indemnification, or similar agreement or arrangement (other than such an agreement or arrangement exclusively between or among two or more of the Target Companies).

(d) The amount of liability for unpaid Taxes of the Target Companies does not, in the aggregate, materially exceed the amount of the liability accruals and reserves for Taxes reflected on the Company Financial Statements. None of the Target Companies shall be required to include any material item of income in, or exclude any material item of deduction from, taxable income for any taxable period (or portion thereof) ending after the Closing Date as a result of any (i) change in method of accounting for a taxable period ending on or prior to the Closing Date under Section 481(c) of the Code (or any corresponding or similar provision of state, local or foreign Tax Law), (ii) "closing agreement" as described in Section 7121 of the Code (or any corresponding or similar provision of state, local or foreign Tax Law) executed on or prior to the Closing Date, or (iii) deferred intercompany gain or excess loss account described in Treasury Regulations under Section 1502 of the Code (or any corresponding or similar provision of state, local or foreign Tax Law).

(e) (i) None of the Target Companies is required to treat any of its assets as owned by another person for United States federal income tax purposes or as tax-exempt bond financed property or tax-exempt use property within the meaning of Section 168 of the Code; (ii) none of the Target Companies has participated in any international boycott as defined in Section 999 of the Code; and (iii) none of the Target Companies has or has ever conducted branch operations in any foreign country within the meaning of Treasury Regulation Section 1.367(a)-6T.

(f) No shareholder of the Company that is a Non-U.S. Holder has owned more than five percent of any class of the outstanding stock of the Company at any time during the immediately preceding five-year period.

(g) None of the Target Companies has been a "distributing corporation" or a "controlled corporation" in a distribution intended to qualify for tax-free treatment under Section 355 of the Code (i) in the two-year period ending on the date of this Agreement or (ii) in a distribution that could, in conjunction with the Merger, otherwise constitute part of a "plan" or "series of related transactions" (within the meaning of Section 355(e) of the Code).

(h) None of the Target Companies has entered into, has any liability in respect of, or has any filing obligations with respect to, any "reportable transactions" as defined in Treasury Regulation Section 1.6011-4(b)(1) or similar provision of state law.

(i) Within the last three years, neither the Company nor any of its Affiliates has owned any material assets located outside the United States or conducted a material trade or business outside the United States.

(j) All of the transactions which the Company has accounted for as hedges under SFAS 133 have also been treated as hedging transactions for United States federal income Tax purposes pursuant to Treasury Regulation Section 1.1221-2.

Section 3.16 *Employee Benefit Plans.*

(a) Section 3.16(a) of the Company Disclosure Schedule sets forth a complete and accurate list of each of the following which is or has been sponsored, maintained or contributed to by the Company or any trade or business, whether or not incorporated (a "*Company ERISA Affiliate*"), or in which any employee or co-employee of any of the Target Companies participates or is covered, that together with the Company would be considered affiliated with the Company or any Company ERISA Affiliate under Section 414(b), (c), (m) or (o) of the Code or Section 4001(b)(1) of ERISA for the benefit of any person who, as of the Closing, is a current or former employee or subcontractor of the Company or any Company ERISA Affiliate: (i) each "employee benefit plan," as such term is defined in Section 3(3) of ERISA (each, a "*Company Plan*"); and (ii) each personnel policy, stock option plan, bonus plan or arrangement, incentive award plan or arrangement, vacation policy, severance or retention pay plan, policy, program or agreement, deferred compensation agreement or arrangement, executive compensation or supplemental income arrangement, retiree benefit plan or arrangement, fringe benefit program or practice (whether or not taxable), employee loan, consulting agreement, employment agreement and each other employee benefit plan, agreement, arrangement, program, practice or understanding which is not described in clause (i) above (each, a "*Company Benefit Program or Agreement*") (the Company Plans and Company Benefit Programs or Agreements are sometimes collectively referred to in this Agreement as the "*Company Employee Benefit Plans*").

(b) True, correct and complete copies of each of the Company Plans and related trusts, if applicable, including all amendments thereto, have been delivered to Parent. There has also been delivered to Parent, with respect to each Company Plan required to file such report and description, the report on Form 5500 for the past three years, to the extent applicable, and the most recent summary plan description and summaries of material modifications thereto. True, correct and complete copies or descriptions of all Company Benefit Programs or Agreements have also been delivered to Parent.

(c) (i) None of the Company, any Company ERISA Affiliate or any entity that, at any time during the past six years, was required to be treated as a single employer together with the Company or a Company ERISA Affiliate pursuant to Section 414 of the Code contributes to or has an obligation to contribute to, nor has at any time contributed to or had an obligation to contribute to, a multiemployer plan within the meaning of Section 3(37) of ERISA or any other plan subject to Title IV of ERISA; (ii) each of the Company and the Company ERISA Affiliates has performed all obligations, whether arising by operation of law or by contract, including ERISA and the Code, required to be performed by it in connection with the Company Employee Benefit Plans, and, to the knowledge of the Company, there have been no defaults or violations by any other party to the Company Employee Benefit Plans; (iii) all reports, returns, notices, disclosures and other documents relating to the Company Plans required to be filed with or furnished to governmental entities, plan participants or plan beneficiaries have been timely filed or furnished in accordance with applicable law, and each Company Employee Benefit Plan has been administered in compliance with its governing written documents; (iv) each of the Company Plans intended to be qualified under Section 401 of the Code satisfies the requirements of such Section and has received a current favorable determination letter from the Internal Revenue Service (the "*IRS*") regarding such qualified status and has not been amended, operated or administered in a way which would adversely affect such qualified status; (v) there are no actions, suits or claims pending (other than routine claims for benefits) or, to the knowledge of the Company, contemplated or threatened against, or with respect to, any of the Company Employee Benefit Plans or their assets; (vi) each trust maintained in connection with each Company Plan, which is qualified under Section 401 of the Code, is tax exempt under Section 501 of the Code; (vii) all contributions required to be made to the Company Employee Benefit Plans have been made timely; (viii) no

accumulated funding deficiency, whether or not waived, within the meaning of Section 302 of ERISA or Section 412 of the Code has been incurred, and there has been no termination or partial termination of any Company Plan within the meaning of Section 411(d)(3) of the Code; (ix) no act, omission or transaction has occurred which could result in imposition on the Company or any Company ERISA Affiliate of (A) breach of fiduciary duty liability damages under Section 409 of ERISA, (B) a civil penalty assessed pursuant to subsections (c), (i) or (1) of Section 502 of ERISA or (C) a tax imposed pursuant to Chapter 43 of Subtitle D of the Code; (x) to the knowledge of the Company, there is no matter pending with respect to any of the Company Plans before the IRS, the Department of Labor or the Pension Benefit Guaranty Corporation (the "PBGC"); (xi) each of the Company Employee Benefit Plans complies, in form and operation, with the applicable provisions of the Code and ERISA; (xii) each Company Employee Benefit Plan may be unilaterally amended or terminated in its entirety (otherwise than with respect to outstanding shares) without any liability or other obligation; (xiii) the Company and the Company ERISA Affiliates have no liabilities or other obligations, whether actual or contingent, under any Company Employee Benefit Plan for post-employment benefits of any nature (other than COBRA continuation coverage); and (xiv) neither the Company nor any of the Company ERISA Affiliates or any present or former director, officer, employee or other agent of the Company or any of the Company ERISA Affiliates has made any written or oral representations or promises to any present or former director, officer, employee or other agent concerning his or her terms, conditions or benefits of employment, including the tenure of any such employment or the conditions under which such employment may be terminated by the Company, any of the Company ERISA Affiliates or Parent which will be binding upon or enforceable against Parent or the Company after the Effective Time.

(d) No employee is currently on a leave of absence due to sickness or disability and no claim is pending or expected to be made by an employee, former employee or independent contractor for workers' compensation benefits.

(e) With respect to the Company Employee Benefit Plans, there exists no condition or set of circumstances in connection with any of the Target Companies that could be expected to result in liability reasonably likely to have a Material Adverse Effect on the Company under ERISA, the Code or any other applicable law. With respect to the Company Employee Benefit Plans, individually and in the aggregate, there are no unfunded benefit obligations which have not been accounted for by reserves, or otherwise properly footnoted in accordance with GAAP, on the financial statements of the Target Companies, which obligations are reasonably likely to have a Material Adverse Effect on the Company.

(f) Neither the execution or delivery of this Agreement nor the consummation of the transactions contemplated hereby shall result in any payment becoming due to any employee or group of employees of any of the Target Companies.

(g) No amounts payable or that could become payable under any Company Employee Benefit Plan as a result of the consummation of the transactions contemplated by this Agreement or otherwise shall fail to be deductible for Federal income tax purposes by virtue of either Section 280G or 162(m) of the Code.

## Edgar Filing: O'Neill Andrew J - Form 4

Section 3.17 *Employment Contracts and Benefits.* Except as otherwise provided for in any Company Employee Benefit Plan: (a) none of the Target Companies is subject to or obligated under any consulting, employment, severance, retention, termination or similar arrangement, any employee benefit, incentive or deferred compensation plan with respect to any Person, or any bonus, profit sharing, pension, stock option, stock purchase or similar plan or other arrangement or other fringe benefit plan entered into or maintained for the benefit of employees of any of the Target Companies or any other Person; and (b) no employee of any of the Target Companies or any other Person owns, or has any right granted by any of the Target Companies to acquire, any interest in any of the assets or business of any of the Target Companies.

### Section 3.18 *Labor Matters.*

(a) No employees of any of the Target Companies are represented by any labor organization. No labor organization or group of employees of any of the Target Companies has made a demand for recognition or certification as a union or other labor organization, and there are no representation or certification proceedings or petitions seeking a representation or certification proceeding presently pending or threatened in writing to be brought or filed with the National Labor Relations Board or any other labor relations tribunal or authority. There are no organizing activities involving any of the Target Companies pending with any labor organization or group of employees of any of the Target Companies.

(b) Each of the Target Companies is in compliance with all laws, rules, regulations and orders relating to the employment of labor, including all such laws, rules, regulations and orders relating to wages, hours, collective bargaining, discrimination, civil rights, safety and health, workers' compensation and the collection and payment of income Tax withholding, Social Security Taxes, Medicare Taxes and similar Taxes, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on the Company.

Section 3.19 *Insurance.* Each of the Target Companies maintains, and through the Closing Date will maintain, insurance with reputable insurers (or pursuant to prudent self-insurance programs described in Section 3.19 of the Company Disclosure Schedule) in such amounts and covering such risks as are in accordance with prudent industry practice for companies engaged in businesses of a size and scope similar to those of the Target Companies and owning properties in the same general area in which the Target Companies conduct their businesses. None of such insurance coverage was obtained through the use of false or misleading information or the failure to provide the insurer with all information requested in order to evaluate the liabilities and risks insured. There is no material default with respect to any provision contained in any such policy or binder, and none of the Target Companies has failed to give any notice or present any claim under any such policy or binder in due and timely fashion. There are no billed but unpaid premiums past due under any such policy or binder. (a) There are no outstanding claims under any such policies or binders and, to the knowledge of the Company, there has not occurred any event that might reasonably form the basis of any claim against or relating to any of the Target Companies that is not covered by any of such policies or binders; (b) no notice of cancellation or non-renewal of any such policies or binders has been received or threatened; and (c) there are no performance bonds outstanding with respect to any of the Target Companies.

Section 3.20 *Intellectual Property.* There is no intellectual or intangible property (including, without limitation, legally enforceable licenses or other rights to use, any and all United States and foreign patents, patent applications, patent disclosures, mask works, computer software, geophysical data, trademarks, trade dress, trade names, logos, Internet domain names, copyrights and service marks, including applications to register and registrations for any of the foregoing, as well as trade secrets, know-how, data and other proprietary rights and information) that is necessary for the operation, or continued operation, of the business of any of the Target Companies or for the ownership and operation, or continued ownership and operation, of any of their assets, for which the Target

## Edgar Filing: O'Neill Andrew J - Form 4

Companies do not hold valid and continuing authority in connection with the use thereof. The businesses of the Target Companies, as presently conducted, do not conflict with, infringe or violate any intellectual property rights of any other Person, and none of the Target Companies has received any claim regarding such conflict, infringement or violation, except where (in either case) any such conflict, infringement or violation could not reasonably be expected to have a Material Adverse Effect on the Company.

Section 3.21 *Title to Assets.* The Target Companies (individually or collectively) have Defensible Title to (i) the Oil and Gas Interests of the Company included or reflected in the Target Companies' Ownership Interests, (ii) the Target Companies' gas plants and gas gathering systems referenced in the Company SEC Documents and (iii) all other assets of the Target Companies (other than in the case of this item (iii) those assets for which the failure to have Defensible Title would not, individually or in the aggregate, result in Material Adverse Effect on the Target Companies, taken as a whole). Each Oil and Gas Interest included or reflected in the Company's Ownership Interests entitles the Target Companies (individually or collectively) to receive not less than the undivided interest set forth in (or derived from) the Ownership Interests of the Target Companies of all Hydrocarbons produced, saved and sold from or attributable to such Oil and Gas Interest, and the portion of the costs and expenses of operation and development of such Oil and Gas Interest that is borne or to be borne by the Target Companies (individually or collectively) is not greater than the undivided interest set forth in (or derived from) the Target Companies' Ownership Interests. The oil and gas leases and other agreements that provide the Target Companies with operating rights in the Oil and Gas Interests included or reflected in the Target Companies' Ownership Interests are legal, valid and binding and in full force and effect, and the rentals, royalties and other payments due thereunder have been properly and timely paid and there is no existing default (or event that, with notice or lapse of time or both, would become a default) under any of such oil and gas leases or other agreements, except in each case as have not had, and would not reasonably be expected to have or result in a Material Adverse Effect on the Company.

### Section 3.22 *Oil and Gas Operations.*

(a) All wells included in the Oil and Gas Interests of the Company have been drilled and (if completed) completed, operated and produced in accordance with generally accepted oil and gas field practices and in compliance in all material respects with applicable oil and gas leases and applicable laws, rules and regulations, except where any failure or violation could not reasonably be expected to have a Material Adverse Effect on the Company.

(b) Proceeds from the sale of Hydrocarbons produced from the Company's Oil and Gas Interests are being received by the Target Companies in a timely manner and are not being held in suspense for any reason (except in the ordinary course of business).

(c) None of the Target Companies has received any material advance, take-or-pay or other similar payments that entitle purchasers of production to receive deliveries of Hydrocarbons without paying therefor, and, on a net, company-wide basis, the Target Companies are neither underproduced nor overproduced, in either case, to any material extent, under gas balancing or similar arrangements.

(d) No claim, notice or order from any Governmental Authority or other Person has been received by any of the Target Companies due to Hydrocarbon production in excess of allowables or similar violations that could result in curtailment of production after the Closing Date from any Oil and Gas Interests of the Company, except any such violations which individually or in the aggregate have not had, and would not be reasonably likely to have or result in, a Material Adverse Effect on the Target Companies.

(e) All material operating equipment owned or leased by the Target Companies is, in the aggregate, in a state of repair so as to be adequate in all material respects for reasonably prudent operations in the areas in which they are operated.

Section 3.23 *Oil and Gas Reserves.* The factual, non-interpretive data related to oil and gas reserves reflected in the Company Reserve Report was, as of the date of the Company Reserve Report, accurate in all material respects.

Section 3.24 *Derivative Transactions and Hedging.* Section 3.24 of the Company Disclosure Schedule contains a complete and correct list of all Derivative Transactions (including each outstanding Hydrocarbon or financial hedging position attributable to the Hydrocarbon production of the Target Companies) entered into by the Target Companies or for the account of any of its customers as of the date of this Agreement. All such Derivative Transactions were, and any Derivative Transactions entered into after the date of this Agreement will be, entered into in accordance with applicable laws, and in accordance with the investment, securities, commodities, risk management and other policies, practices and procedures employed by the Target Companies. The Target Companies have duly performed in all material respects all of their respective obligations under the Derivative Transactions to the extent that such obligations to perform have accrued, and, to the knowledge of the Company, there are no material breaches, violations, collateral deficiencies, requests for collateral or demands for payment (except for ordinary course margin deposit requests), or defaults or allegations or assertions of such by any party thereunder.

Section 3.25 *Natural Gas Act.* Any gas gathering system constituting a part of the properties of the Target Companies has as its primary function the provision of natural gas gathering services, as the term "gathering" is interpreted under Section 1(b) of the Natural Gas Act (the "NGA"); none of the properties has been or is certificated by the Federal Energy Regulatory Commission (the "FERC") under Section 7(c) of the NGA or to the knowledge of the Company is now subject to FERC jurisdiction under the NGA; and none of the properties has been or is providing service pursuant to Section 311 of the NGA.

Section 3.26 *Environmental Matters.*

(a) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies is subject to any liability or obligation (accrued, contingent, or otherwise) to investigate, cleanup, correct, abate, or take any response, remedial or corrective action under Environmental Laws relating to (i) environmental conditions on, under, or about any of the properties or assets owned, leased, operated, or used by the Target Companies or any predecessor at the present time or in the past, or (ii) the past or present use, management, handling, transport, treatment, generation, storage, disposal, or release of any Hazardous Materials, whether on-site or off-site.

(b) Except as would not result in a Material Adverse Effect on the Company, all permits, notices, approvals and authorizations required to be obtained or filed in connection with the operation of the Target Companies' business or the operation or use of any property owned, leased, or operated by the Target Companies have been obtained or filed and are currently in effect, and the Target Companies are in compliance with the terms and conditions of such permits, notices, approvals and authorizations.

(c) Except as would not result in a Material Adverse Effect on the Company, each of the Target Companies has conducted its business and operated its assets, and is conducting its business and operating its assets, in compliance with all Environmental Laws;

(d) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies has been notified by any Governmental Authority or other Person or is otherwise aware that any of the current or prior operations or assets of any of the Target

Companies is the subject of any investigation or inquiry by any Governmental Authority or other Person under Environmental Laws;

(e) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies and, to the knowledge of the Company, no other Person has filed any notice under any federal, state or local law indicating that (i) any of the Target Companies is responsible for a release or threatened release into the environment, or the improper handling, generation, treatment, storage, disposal or recycling, of any Hazardous Material, on any property now or previously owned, leased or operated by any of the Target Companies or (ii) any Hazardous Material is improperly handled, generated, treated, stored, disposed of, or recycled upon any property now or previously owned, leased or operated by any of the Target Companies;

(f) None of the Target Companies has any liability in excess of \$1,000,000 in the aggregate in connection with (i) the release or threatened release into the environment at, beneath or on any property now or previously owned, leased or operated by any of the Target Companies, (ii) any obligations under or violations of Environmental Laws, or (iii) the use, release, treatment, storage, disposal, or recycling of any Hazardous Material;

(g) Except as would not result in a Material Adverse Effect on the Company, there are no pending, or to the knowledge of Company threatened, claims, complaints, notices, inquiries or requests for information involving any matter which remains unresolved (i) under Environmental Laws against any person whose liability for environmental matters any Target Company has retained or assumed either contractually or by operation of law, or (ii) with respect to any alleged violation of any Environmental Law or regarding potential liability under any Environmental Law against any Target Company relating to operations or conditions of any facilities or property (including off-site treatment, storage, disposal, or recycling of any Hazardous Material from such facilities or property) currently or formerly owned, leased or operated by any of the Target Companies;

(h) No property now or previously owned, leased or operated by any of the Target Companies is listed on the National Priorities List pursuant to CERCLA or on the CERCLIS or on any other similar federal or state list as sites requiring investigation or cleanup;

(i) To the knowledge of the Company, none of the Target Companies is transporting, has transported, or is arranging or has arranged for the transportation of any Hazardous Material to any location which is listed on the National Priorities List pursuant to CERCLA, on the CERCLIS, or on any similar federal or state list or which is the subject of federal, state or local enforcement actions or other investigations that may lead to claims in excess of \$1,000,000 in the aggregate against any of the Target Companies for investigation, removal or remedial work, contribution for removal or remedial work, damage to natural resources or personal injury, including claims under CERCLA;

(j) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies owns or operates any underground storage tanks or solid waste storage, treatment and/or disposal facilities;

(k) Except as would not result in a Material Adverse Effect on the Company, to the knowledge of the Company, no asbestos, asbestos containing materials or polychlorinated biphenyls are present on or at any property or facility owned, leased or operated by any of the Target Companies;

(l) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies is operating, or required to be operating, any of its properties or facilities under any order, compliance or consent order, injunction, decree or agreement issued or entered into under, or pertaining to matters regulated by, any Environmental Law;

(m) Except as would not result in a Material Adverse Effect on the Company, none of the Target Companies has assumed contractually, or to the knowledge of the Company, by operation of law, any liabilities or obligations of third parties under Environmental Laws;

(n) Except as would not result in a Material Adverse Effect on the Company, the Company is not aware of any environmental conditions or circumstances that form, or are reasonably likely to give rise to, a claim against any Target Company or any Person whose liability for such claim any Target Company has retained or assumed contractually or by operation of law.

(o) Except as would not result in a Material Adverse Effect on the Company, no Target Company is subject to any environmental indemnification obligation regarding businesses currently or formerly owned or operated by a Target Company or regarding properties currently or formerly owned, leased or operated by a Target Company.

(p) No Target Company is required by virtue of the transactions contemplated by this Agreement to perform an environmental site assessment or to remove or remediate any Hazardous Materials.

(q) The Company has provided or made available to Parent copies of all contracts in which a Target Company has retained, assumed, or provided indemnification for liabilities for environmental matters and all material environmental permits, notices, approvals, authorizations, claims, complaints, inquiries, requests for information, orders, compliance or consent orders, injunctions, decrees, agreements, reports, data, studies, results of investigations, audits, assessments, evaluations and correspondence in the possession, custody or control of any of the Target Companies.

Section 3.27 *Books and Records.* All books, records and files of the Target Companies (including those pertaining to the Company's Oil and Gas Interests, wells and other assets, those pertaining to the production, gathering, transportation and sale of Hydrocarbons, and corporate, accounting, financial and employee records): (a) have been prepared, assembled and maintained in accordance with usual and customary policies and procedures, and (b) fairly and accurately reflect the ownership, use, enjoyment and operation by the Target Companies of their respective assets.

Section 3.28 *Brokers.* No broker, finder, investment banker or other Person is or will be, in connection with the transactions contemplated by this Agreement, entitled to any brokerage, finder's or other fee or compensation based on any arrangement or agreement made by or on behalf of any of the Target Companies and for which Parent, Merger Sub or any of the Target Companies shall have any obligation or liability.

Section 3.29 *Vote Required.* The affirmative vote of the holders of a majority of the outstanding shares of Company Common Stock is the only vote of the holders of any class or series of Company capital stock or other voting securities necessary to approve this Agreement, the Merger and the transactions contemplated hereby.

Section 3.30 *State Takeover Laws.* The Company has taken all necessary action to exempt the Merger from any applicable moratorium, fair price, business combination, control share and other anti-takeover laws under the NRS.

Section 3.31 *Affiliate Transactions.* Section 3.31 of the Company Disclosure Schedule contains a complete and correct list, as of the date of this Agreement, of all agreements, contracts, transfers of assets or liabilities or other commitments or transactions, whether or not entered into in the ordinary course of business, to or by which the Company or any of its subsidiaries, on the one hand, and any of their respective Affiliates (other than the Company or any of its direct or indirect wholly owned subsidiaries) on the other hand, are or have been a party or otherwise bound or affected, and that (a) are currently pending, in effect or have been in effect during the past 12 months, (b) involve

## Edgar Filing: O'Neill Andrew J - Form 4

continuing liabilities and obligations that, individually or in the aggregate, have been, are or will be material to the Target Companies, taken as a whole and (c) are not Company Plans.

**Section 3.32 *Disclosure Controls and Procedures.*** Since January 1, 2003, the Company and each of its subsidiaries has had in place "disclosure controls and procedures" (as defined in Rules 13a-14(c) and 15d-14(c) of the Exchange Act) designed and maintained to ensure in all material respects that (a) transactions are executed in accordance with management's general or specific authorizations, (b) transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain accountability for assets, (c) access to assets is permitted only in accordance with management's general or specific authorization, (d) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences, (e) all information (both financial and non-financial) required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and (f) all such information is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure and to make the certifications of the Chief Executive Officer and Chief Financial Officer of the Company required under the Exchange Act with respect to such reports. The Company's disclosure controls and procedures ensure that information required to be disclosed by the Company in the reports filed with the SEC under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Neither the Company nor its independent auditors have identified any "significant deficiencies" or "material weaknesses" in the Company's or any of its subsidiaries' internal controls as contemplated under Section 404 of SOX. The Company has diligently completed in all material respects its work plan relating to documentation, testing and evaluation of the Company's internal control over financial reporting for purposes of providing the report required by Section 404 of SOX and related SEC rules. As of the date of this Agreement, to the knowledge of the Company, (i) there is no reason that it will not be able, on a timely basis, to complete and include in the Company's Annual Report on Form 10-K for the year ending December 31, 2004, management's assessment of the Company's internal controls and procedures for financial reporting in accordance with Section 404 of SOX and (ii) there is no material weakness or significant deficiency, in each case as such term is defined in PCAOB Auditing Std. No. 2.

**Section 3.33 *Rights Agreement.*** The Company has taken all necessary action (including, if required, amending the Company Rights Agreement) so that the entering into of this Agreement, the acquisition of shares of Parent Common Stock pursuant to the consummation of the Merger and the other transactions contemplated hereby do not and will not enable or require the Company Rights to be exercised or distributed.

**Section 3.34 *Opinion of Financial Advisor.*** The Company has received opinions of Deutsche Bank and Merrill Lynch to the effect that, as of the date of this Agreement, the Conversion Number is fair, from a financial point of view, to the holders of shares of Company Common Stock, a signed copy of which has been delivered to Parent. The Company has received the approval of such financial advisor to permit the inclusion of a copy of its written opinion in its entirety in the Proxy Statement, subject to such advisor's review thereof as presented in the Proxy Statement.

ARTICLE IV

REPRESENTATIONS AND WARRANTIES OF PARENT AND MERGER SUB

Parent and Merger Sub hereby jointly and severally represent and warrant to the Company as follows, except as set forth, specifically with reference to a particular section below, on the Parent Disclosure Schedule:

Section 4.1 *Organization.* Each of the Parent Companies: (a) is a corporation or other entity, duly organized, validly existing and in good standing under the laws of its state of incorporation or formation, (b) has the requisite power and authority to own, lease and operate its properties and to conduct its business as it is presently being conducted, and (c) is duly qualified to do business as a foreign corporation, limited liability company or limited partnership, as applicable, and is in good standing, in each jurisdiction where the character of the properties owned or leased by it or the nature of its activities makes such qualification necessary (except where any failure to be so qualified or to be in good standing would not, individually or in the aggregate, have a Material Adverse Effect on Parent). Accurate and complete copies of the articles of incorporation, minute books, other organizational documents and/or bylaws of each of the Parent Companies have heretofore been delivered to the Company. Parent has no corporate or other subsidiaries other than the Parent Subsidiaries.

Section 4.2 *Other Equity Interests.* None of the Parent Companies owns any equity interest in any general or limited partnership, corporation, limited liability company or joint venture other than the Parent Subsidiaries or as listed on the Parent Disclosure Schedule (other than joint operating and other ownership arrangements and tax partnerships entered into in the ordinary course of business that, individually or in the aggregate, are not material to the operations or business of the Parent Companies, taken as a whole, and that do not entail any material liabilities).

Section 4.3 *Authority and Enforceability.* Each of Parent and Merger Sub has the requisite corporate power and authority to enter into and deliver this Agreement and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of Parent) to consummate the transactions contemplated hereby. The execution and delivery of this Agreement and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of Parent) the consummation of the transactions contemplated hereby have been duly and validly authorized by all necessary corporate action on the part of Parent and Merger Sub, including approval by the Board of Directors of Parent and the Board of Directors and stockholders of Merger Sub, and no other corporate proceedings on the part of Parent or Merger Sub are necessary to authorize the execution or delivery of this Agreement or (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of Parent) to consummate the transactions contemplated hereby. This Agreement has been duly and validly executed and delivered by Parent and Merger Sub and (with respect to consummation of the Merger, subject to the valid approval of the Company Proposal by the stockholders of Parent, and assuming that this Agreement constitutes a valid and binding obligation of the Company) constitutes a valid and binding obligation of each of Parent and Merger Sub enforceable against each of them in accordance with its terms.

Section 4.4 *No Violations.* The execution and delivery of this Agreement do not, and the consummation of the transactions contemplated hereby and compliance by Parent and Merger Sub with the provisions hereof will not, conflict with, result in any violation of or default (with or without notice or lapse of time or both) under, give rise to a right of termination, cancellation or acceleration of any obligation or to the loss of a material benefit under, or result in the creation of any Lien on any of the properties or assets of any of the Parent Companies under, any provision of (a) the certificate or articles of incorporation, bylaws or any other organizational documents of any of the Parent Companies, (b) any loan or credit agreement, note, bond, mortgage, indenture, lease, permit,

## Edgar Filing: O'Neill Andrew J - Form 4

concession, franchise, license or other agreement or instrument applicable to any of the Parent Companies (other than any such conflict, violation, default, right, loss or Lien that may arise under the Parent Bank Credit Agreement), or (c) assuming the consents, approvals, authorizations, permits, filings and notifications referred to in Section 4.5 are duly and timely obtained or made, any judgment, order, decree, statute, law, ordinance, rule or regulation applicable to any of the Parent Companies or any of their respective properties or assets, other than, in the case of clause (b) or (c) above, any such conflict, violation, default, right, loss or Lien that, individually or in the aggregate, would not have a Material Adverse Effect on Parent.

Section 4.5 *Consents and Approvals.* No consent, approval, order or authorization of, registration, declaration or filing with, or permit from, any Governmental Authority is required by or with respect to any of the Parent Companies in connection with the execution and delivery of this Agreement by Parent and Merger Sub or the consummation by Parent and Merger Sub of the transactions contemplated hereby, except for the following: (a) any such consent, approval, order, authorization, registration, declaration, filing or permit which the failure to obtain or make would not, individually or in the aggregate, have a Material Adverse Effect on Parent; (b) the filing of the Articles of Merger with the Secretary of State of Nevada pursuant to applicable provisions of the NRS; (c) the filing of a pre-merger notification report by Parent as may be required under the HSR Act and the expiration or termination of the applicable waiting period; (d) the filing with the SEC of the Registration Statement and such reports under Section 13(a) of the Exchange Act and such other compliance with the Exchange Act and the Securities Act and the rules and regulations of the SEC thereunder as may be required in connection with this Agreement and the transactions contemplated hereby and the obtaining from the SEC of such orders as may be so required; (e) the filing with a National Stock Exchange of a listing application relating to the shares of Parent Common Stock to be issued pursuant to the Merger and the obtaining from such exchange of its approvals thereof; (f) such filings and approvals as may be required by any applicable state securities, "blue sky" or takeover laws or Environmental Laws; and (g) such filings and approvals as may be required by any foreign pre-merger notification, securities, corporate or other law, rule or regulation. No Third-Party Consent is required by or with respect to Parent, Merger Sub or any Parent Subsidiary in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby, except for (x) any such Third-Party Consent which the failure to obtain would not, individually or in the aggregate, have a Material Adverse Effect on Parent, (y) the valid approval of the Company Proposal (including the issuance of the Parent Common Stock in the Merger) by the stockholders of Parent, and (z) any consent, approval or waiver required by the terms of the Parent Bank Credit Agreement.

Section 4.6 *SEC Documents.* Parent (i) has made available to Company a true and complete copy of each report, schedule, registration statement and definitive proxy statement filed by Parent with the SEC since September 30, 2002, (and by Key Production Company, Inc. from January 1, 2001 to September 30, 2002) and prior to the date of this Agreement and any amendments thereto, including exhibits and other information incorporated therein (the "*Parent SEC Documents*"), which are all the documents (other than preliminary material) that Parent was required to file with the SEC since such date, and (ii) has delivered to the Company a true and complete copy of all correspondence between the SEC and any of the Parent Companies since January 1, 2003. Each of the Parent SEC Documents was timely filed with the SEC. As of their respective dates, each of the Parent SEC Documents, as amended (including the financial statements and schedules provided therein or incorporated by reference therein) (i) complied in all material respects with the requirements of the Securities Act, the Exchange Act and SOX, as the case may be, and the rules and regulations of the SEC thereunder applicable to such Parent SEC Documents, and (ii) did not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading.

## Edgar Filing: O'Neill Andrew J - Form 4

Section 4.7 *Financial Statements.* The Parent Financial Statements were prepared in accordance with GAAP applied on a consistent basis during the periods involved (except as may be indicated in the notes thereto or, in the case of unaudited statements, as permitted by Rule 10-01 of Regulation S-X of the SEC) and fairly present (in the case of the unaudited statements, subject to normal, recurring adjustments) the consolidated financial position of Parent and its subsidiaries as of their respective dates and the consolidated results of operations and the consolidated cash flows of Parent and its subsidiaries for the periods presented therein. The books and records of the Parent Companies have been, and are being, maintained in accordance with GAAP and any other applicable legal and accounting requirements and reflect only actual transactions. KPMG LLP is an independent public accounting firm with respect to the Parent Companies and has not resigned or been dismissed by the Parent Companies from such capacity.

### Section 4.8 *Capital Structure.*

(a) The authorized capital stock of Parent consists of 100,000,000 shares of Parent Common Stock and 15,000,000 shares of Parent Preferred Stock. The authorized capital stock of Merger Sub consists of 1,000 shares of Merger Sub Common Stock.

(b) As of the close of business on January 24, 2005, there are issued and outstanding 41,736,475 shares of Parent Common Stock and no shares of Parent Preferred Stock. 2,648,204 shares of Parent Common Stock are issuable upon exercise of outstanding stock options. As of the date hereof, no shares of Parent Common Stock and no shares of Parent Preferred Stock were held by Parent as treasury stock.

(c) Except as set forth in Section 4.8(b), there are outstanding (i) no shares of capital stock or other voting securities of Parent, (ii) no securities of Parent or any other Person convertible into or exchangeable or exercisable for shares of capital stock or other voting securities of Parent, (iii) no stock appreciation rights or phantom stock rights to which any of the Parent Companies are obligated and (iv) no subscriptions, options, warrants, calls, rights (including preemptive rights), commitments, understandings or agreements to which Parent is a party or by which it is bound obligating Parent to issue, deliver, sell, purchase, redeem or acquire shares of capital stock or other voting securities of Parent (or securities convertible into or exchangeable or exercisable for shares of capital stock or other voting securities of Parent) or obligating Parent to grant, extend or enter into any such subscription, option, warrant, call, right, commitment, understanding or agreement.

(d) All outstanding shares of Parent capital stock are, and (when issued) the shares of Parent Common Stock to be issued pursuant to the Merger and upon exercise of the Company Stock Options and Company Warrants will be, validly issued, fully paid and nonassessable and not subject to any preemptive right. There are no shares of Parent capital stock reserved for issuance.

(e) 1,000 shares of Merger Sub Common Stock are issued and outstanding, all of which are owned by Parent. All outstanding shares of capital stock and other voting securities of Merger Sub and of each of the other corporate Parent Subsidiaries are (i) validly issued, fully paid and nonassessable and not subject to any preemptive right, and (ii) owned by the Parent Companies, free and clear of all Liens, claims and options of any nature (except Permitted Encumbrances). There are outstanding (y) no securities of any Parent Subsidiary or any other Person convertible into or exchangeable or exercisable for shares of capital stock, other voting securities or other equity interests of such Parent Subsidiary, and (z) no subscriptions, options, warrants, calls, rights (including preemptive rights), commitments, understandings or agreements to which any Parent Subsidiary is a party or by which it is bound obligating such Parent Subsidiary to issue, deliver, sell, purchase, redeem or acquire shares of capital stock, other voting securities or other equity interests of such Parent Subsidiary (or securities convertible into or exchangeable or exercisable for shares of capital stock, other voting securities or other equity interests of such Parent Subsidiary) or

obligating any Parent Subsidiary to grant, extend or enter into any such subscription, option, warrant, call, right, commitment, understanding or agreement.

(f) There is no stockholder agreement, voting trust or other agreement or understanding to which Parent is a party or by which it is bound relating to the voting of any shares of the capital stock of any of the Parent Companies. There are no bonds, debentures, notes or other indebtedness of the Parent Companies having the right to vote (or convertible into, or exchangeable for, securities having the right to vote) on any matters on which the stockholders of any of the Parent Companies may vote.

(g) None of the Parent Companies is obligated to redeem or otherwise repurchase any of its capital stock.

(h) Parent is in compliance with the applicable listing rules of the New York Stock Exchange and has not, since January 1, 2003, received any notice from the New York Stock Exchange asserting any non-compliance with such rules.

Section 4.9 *No Undisclosed Liabilities.* There are no material liabilities of any of the Parent Companies of any kind whatsoever, whether accrued, contingent, absolute, determined, determinable or otherwise, other than (a) liabilities adequately provided for in the Parent Financial Statements, (b) liabilities incurred in the ordinary course of business subsequent to September 30, 2004, (c) liabilities under this Agreement, and (d) liabilities set forth on Section 4.9 of the Parent Disclosure Schedule.

Section 4.10 *Absence of Certain Changes or Events.* Except as specifically contemplated by this Agreement, since September 30, 2004, none of the Parent Companies has done any of the following:

(a) Discharged or satisfied any Lien or paid any obligation or liability, absolute or contingent, other than current liabilities incurred and paid in the ordinary course of business and consistent with past practices;

(b) Paid or declared any dividends or distributions, purchased, redeemed, acquired or retired any indebtedness, stock or other securities from its stockholders or other securityholders, made any loans or advances or guaranteed any loans or advances to any Person (other than loans, advances or guaranties made in the ordinary course of business and consistent with past practices), or otherwise incurred or suffered to exist any liabilities (other than current liabilities incurred in the ordinary course of business and consistent with past practices);

(c) Except for Permitted Encumbrances, suffered or permitted any Lien to arise or be granted or created against or upon any of its assets;

(d) Canceled, waived or released any rights or claims against, or indebtedness owed by, third parties (including, without limitation, any standstill agreements);

(e) Amended its certificate or articles of incorporation, bylaws or other organizational documents;

(f) Made or permitted any amendment, supplement, modification or termination of, or any acceleration under, any Parent Material Agreement;

(g) Sold, leased, transferred, assigned or otherwise disposed of (i) any Oil and Gas Interests of Parent that, individually or in the aggregate, had a value of \$1,000,000 or more, or (ii) any other assets that, individually or in the aggregate, had a value at the time of such lease, transfer, assignment or disposition of \$1,000,000 or more (and, in each case where a sale, lease, transfer, assignment or other disposition was made, it was made for fair consideration in the ordinary course of business); provided, however, that this Section 4.10(g) shall not apply to the sale of Hydrocarbons in the ordinary course of business;

## Edgar Filing: O'Neill Andrew J - Form 4

- (h) Made any investment in or contribution, payment, advance or loan to any Person (other than investments, contributions, payments or advances, or commitments with respect thereto, less than \$1,000,000 in the aggregate, made in the ordinary course of business and consistent with past practices);
- (i) Paid, loaned or advanced (other than the payment, advance or reimbursement of expenses in the ordinary course of business and consistent with past practices) any amounts to, or sold, transferred or leased any of its assets to, or entered into any other transaction with, any of its Affiliates other than the Parent Companies;
- (j) Made any material change in any of the accounting principles followed by it or the method of applying such principles;
- (k) Entered into any material transaction (other than this Agreement) except in the ordinary course of business and consistent with past practices;
- (l) Increased benefits or benefit plan costs or changed bonus, insurance, pension, compensation or other benefit plan or arrangement or granted any bonus or increase in wages, salary or other compensation or made any other change in employment terms to (or entered into severance or retention arrangements of any type with) any officer, director or employee of any of the Parent Companies (except in the ordinary course of business and consistent with past practices);
- (m) Issued any note, bond or other debt security or created, incurred, assumed or guaranteed any indebtedness for borrowed money or capitalized lease obligation involving more than \$1,000,000 in the aggregate (other than pursuant to the Parent Bank Credit Agreement);
- (n) Delayed, postponed or accelerated the payment of accounts payable or other liabilities (except in the ordinary course of business and consistent with past practices);
- (o) Canceled, compromised, waived or released any right or claim (or series of related rights and claims) involving more than \$1,000,000 in the aggregate (except in the ordinary course of business and consistent with past practices);
- (p) Issued, sold, or otherwise disposed of any of its capital stock or other equity interest or granted any option, warrant, or other right to purchase or obtain (including upon conversion, exchange, or exercise) any of its capital stock or other equity interest (or reduced the exercise or conversion price or extended the time for exercise or conversion, other than in accordance with mandatory contractual provisions, of any rights, options or warrants to acquire its capital stock or securities);
- (q) Made any loan to, or entered into any other transaction with, any of its directors, officers or employees (except in the ordinary course of business and consistent with past practices and not involving more than \$100,000 in the aggregate);
- (r) Made or pledged to make any charitable or other capital contribution outside the ordinary course of business and consistent with past practices;
- (s) Made or committed to make capital expenditures in excess of \$150,000,000 in the aggregate;
- (t) Made or changed any material Tax election or settled or compromised any material income Tax liability;
- (u) Entered into, modified or amended any Derivative Transaction;

- (v) Otherwise been involved in any other material occurrence, event, incident, action, failure to act, or transaction involving any of the Parent Companies (except in the ordinary course of business and consistent with past practices);
- (w) Entered into any transaction with an Affiliate (except in the ordinary course of business and consistent with past practices);
- (x) Agreed, whether in writing or otherwise, to do any of the foregoing; or
- (y) Suffered any Material Adverse Effect.

Section 4.11 *Compliance with Laws, Material Agreements and Permits.* None of the Parent Companies is in violation of, or in default under, and no event has occurred that (with notice or the lapse of time or both) would constitute a violation of or default under: (a) its certificate or articles of incorporation, bylaws or other organizational documents, (b) any applicable law, rule, regulation, ordinance, order, writ, decree or judgment of any Governmental Authority, or (c) any Parent Material Agreement, except (in the case of clause (b) or (c) above) for any violation or default that would not, individually or in the aggregate, have a Material Adverse Effect on Parent. Each of the Parent Companies has obtained and holds all permits, licenses, variances, exemptions, orders, franchises, approvals and authorizations of all Governmental Authorities necessary for the lawful conduct of its business and the lawful ownership, use and operation of its assets ("*Parent Permits*"), except for Parent Permits which the failure to obtain or hold would not, individually or in the aggregate, have a Material Adverse Effect on Parent. None of the Parent Permits shall be adversely affected by the consummation of the transactions contemplated under this Agreement or requires any filing or consent in connection therewith. Each of the Parent Companies is in compliance with the terms of its Parent Permits, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on Parent. No investigation or review by any Governmental Authority with respect to any of the Parent Companies is pending or, to the knowledge of Parent, threatened, other than those the outcome of which would not, individually or in the aggregate, have a Material Adverse Effect on Parent. To the knowledge of Parent, no other party to any Parent Material Agreement is in material breach of the terms, provisions or conditions of such Parent Material Agreement. Each Parent Material Agreement (other than those listed in Parent's Form 10-K for the year ended December 31, 2003, or in subsequent filings, as an exhibit to the Parent SEC Documents) is listed on Section 4.11 of the Parent Disclosure Schedule.

Section 4.12 *Governmental Regulation.* No Parent Company is subject to regulation under the Public Utility Holding Company Act of 1935, the Federal Power Act, the Interstate Commerce Act, the Investment Company Act of 1940 or any state public utilities laws.

Section 4.13 *Litigation.* (a) No litigation, arbitration, investigation or other proceeding is pending or, to the knowledge of Parent, threatened against any of the Parent Companies or their respective assets which could reasonably be expected to have a Material Adverse Effect on Parent; and (b) no Parent Company is subject to any outstanding injunction, judgment, order, decree or ruling (other than routine oil and gas field regulatory orders). There is no litigation, proceeding or investigation pending or, to the knowledge of Parent, threatened against or affecting any of the Parent Companies that questions the validity or enforceability of this Agreement or any other document, instrument or agreement to be executed and delivered by Parent in connection with the transactions contemplated hereby.

Section 4.14 *Interim Operations of Merger Sub.* Merger Sub was formed solely for the purpose of engaging in the transactions contemplated by this Agreement and has not engaged in any business or activity (or conducted any operations) of any kind, entered into any agreement or arrangement with any person or entity, or incurred, directly or indirectly, any liabilities or obligations, except in

## Edgar Filing: O'Neill Andrew J - Form 4

connection with its incorporation, the negotiation of this Agreement, the Merger and the transactions contemplated hereby.

**Section 4.15 *No Restrictions.*** None of the Parent Companies is a party to: (a) any agreement, indenture or other instrument that contains restrictions with respect to the payment of dividends or other distributions with respect to its capital, other than the Parent Bank Credit Agreement; (b) any financial arrangement with respect to or creating any indebtedness to any Person (other than indebtedness (i) reflected in the Parent Financial Statements and, with respect to any indebtedness that is material (individually or, together with related items, in the aggregate) listed in Section 4.15 of the Parent Disclosure Schedule, (ii) under the Parent Bank Credit Agreement, or (iii) incurred in the ordinary course of business consistent with past practices since September 30, 2004) unless such indebtedness is not material (individually or, together with related items, in the aggregate) to the Parent Companies taken as a whole; (c) any agreement, contract or commitment relating to the making of any advance to, or investment in, any Person (other than restrictions under the Parent Bank Credit Agreement and advances in the ordinary course of business and consistent with past practices); (d) any guaranty or other contingent liability with respect to any indebtedness or obligation of any Person (other than (i) guaranties pursuant to the Parent Bank Credit Agreement, (ii) guaranties undertaken in the ordinary course of business, and (iii) the endorsement of negotiable instruments for collection in the ordinary course of business); or (e) any agreement, contract or commitment limiting in any respect its ability to compete with any Person or otherwise conduct business of any line or nature.

### **Section 4.16 *Taxes.***

(a) Each of the Parent Companies and any affiliated, consolidated, combined, aggregated, or unitary group of which any such entity is or was a member has: (i) timely filed in accordance with the applicable law all Tax Returns required to be filed by it (all such Tax Returns being accurate and complete in all material respects), (ii) timely paid all Taxes required to be paid by it (whether shown on a Tax Return or not) other than Taxes that are not yet due, (iii) complied with all applicable laws, rules and regulations relating to the payment and withholding of Taxes, and (iv) timely withheld from employee wages and paid over to the proper Governmental Authorities all amounts required to be so withheld and paid over, except where the failure to file, pay, comply with or withhold would not, individually or in the aggregate, have a Material Adverse Effect on Parent.

(b) (i) No audits or other administrative or court proceedings are presently pending with regard to any material Taxes for which any of the Parent Companies would be liable; and (ii) there are no pending requests for Tax rulings from any Governmental Authority, no outstanding subpoenas or requests for information by any Governmental Authority with respect to any Taxes, no proposed reassessments by any Governmental Authority of any property owned or leased, and no agreements in effect to extend the time to file any Tax Return or the period of limitations for the assessment or collection of any Taxes for which any of the Parent Companies would be liable.

(c) (i) There are no Liens on any of the assets of the Parent Companies for unpaid Taxes, other than Liens for Taxes not yet due and payable; (ii) no Parent Company has any liability for the Taxes of any other Person (other than one or more of the Parent Companies) under Treasury Regulation Section 1.1502-6 (or any analogous state, local or foreign law), as a successor or transferee, or by contract; and (iii) no Parent Company is a party to or bound by any Tax sharing, allocation, indemnification, or similar agreement or arrangement (other than such an agreement or arrangement exclusively between or among two or more of the Parent Companies).

## Edgar Filing: O'Neill Andrew J - Form 4

(d) The amount of liability for unpaid Taxes of the Parent Companies does not, in the aggregate, materially exceed the amount of the liability accruals and reserves for Taxes reflected on the Parent Financial Statements. None of the Parent Companies shall be required to include any material item of income in, or exclude any material item of deduction from, taxable income for any taxable period (or portion thereof) ending after the Closing Date as a result of any (i) change in method of accounting for a taxable period ending on or prior to the Closing Date under Section 481(c) of the Code (or any corresponding or similar provision of state, local or foreign Tax Law), (ii) "closing agreement" as described in Section 7121 of the Code (or any corresponding or similar provision of state, local or foreign Tax Law) executed on or prior to the Closing Date, or (iii) deferred intercompany gain or excess loss account described in Treasury Regulations under Section 1502 of the Code (or any corresponding or similar provision of state, local or foreign Tax Law).

(e) (i) no Parent Company is required to treat any of its assets as owned by another person for United States federal income tax purposes or as tax-exempt bond financed property or tax-exempt use property within the meaning of Section 168 of the Code; (ii) no Parent Company has participated in any international boycott as defined in Section 999 of the Code; and (iii) no Parent Company has or has ever conducted branch operations in any foreign country within the meaning of Treasury Regulation Section 1.367(a)-6T.

(f) No shareholder of Parent that is a Non-U.S. Holder has owned more than five percent of any class of the outstanding stock of Parent at any time during the immediately preceding five-year period.

(g) None of the Parent Companies has been a "distributing corporation" or a "controlled corporation" in a distribution intended to qualify for tax-free treatment under Section 355 of the Code (i) in the two-year period ending on the date of this Agreement or (ii) in a distribution that could, in conjunction with the Merger, otherwise constitute part of a "plan" or "series of related transactions" (within the meaning of Section 355(e) of the Code).

(h) None of the Parent Companies has entered into, has any liability in respect of, or has any filing obligations with respect to, any "reportable transactions" as defined in Treasury Regulation Section 1.6011-4(b)(1) or similar provision of state law.

(i) Within the last three years, neither Parent nor any of its Affiliates has owned any material assets located outside the United States or conducted a material trade or business outside the United States.

(j) All of the transactions which Parent has accounted for as hedges under SFAS 133 have also been treated as hedging transactions for United States federal income Tax purposes pursuant to Treasury Regulation Section 1.1221-2.

### Section 4.17 *Employee Benefit Plans.*

(a) Section 4.17 of the Parent Disclosure Schedule sets forth a complete and accurate list of each of the following which is or has been sponsored, maintained or contributed to by Parent or any trade or business, whether or not incorporated (a "*Parent ERISA Affiliate*"), or in which any employee or co-employee of any of the Parent Companies participates or is covered, that together with Parent would be considered affiliated with Parent or any Parent ERISA Affiliate under Section 414(b), (c), (m) or (o) of the Code or Section 4001(b)(1) of ERISA for the benefit of any person who, as of the Closing, is a current or former employee or subcontractor of Parent or any Parent ERISA Affiliate: (i) each "employee benefit plan," as such term is defined in Section 3(3) of ERISA (each, a "*Parent Plan*"); and (ii) each personnel policy, stock option plan, bonus plan or arrangement, incentive award plan or arrangement, vacation policy, severance or retention pay plan, policy, program or agreement, deferred compensation agreement or arrangement, executive

## Edgar Filing: O'Neill Andrew J - Form 4

compensation or supplemental income arrangement, retiree benefit plan or arrangement, fringe benefit program or practice (whether or not taxable), employee loan, consulting agreement, employment agreement and each other employee benefit plan, agreement, arrangement, program, practice or understanding which is not described in clause (i) above (each, a "*Parent Benefit Program or Agreement*") (the Parent Plans and Parent Benefit Programs or Agreements are sometimes collectively referred to in this Agreement as the "*Parent Employee Benefit Plans*").

(b) True, correct and complete copies of each of the Parent Plans and related trusts, if applicable, including all amendments thereto, have been delivered to the Company. There has also been delivered to the Company, with respect to each Parent Plan required to file such report and description, the report on Form 5500 for the past three years, to the extent applicable, and the most recent summary plan description and summaries of material modifications thereto. True, correct and complete copies or descriptions of all Parent Benefit Programs or Agreements have also been delivered to the Company.

(c) (i) None of Parent, any Parent ERISA Affiliate or any entity that, at any time during the past six years, was required to be treated as a single employer together with Parent or a Parent ERISA Affiliate pursuant to Section 414 of the Code contributes to or has an obligation to contribute to, nor has at any time contributed to or had an obligation to contribute to, a multiemployer plan within the meaning of Section 3(37) of ERISA or any other plan subject to Title IV of ERISA; (ii) each of Parent and the Parent ERISA Affiliates has performed all obligations, whether arising by operation of law or by contract, including ERISA and the Code, required to be performed by it in connection with the Parent Employee Benefit Plans, and, to the knowledge of Parent, there have been no defaults or violations by any other party to the Parent Employee Benefit Plans; (iii) all reports, returns, notices, disclosures and other documents relating to the Parent Plans required to be filed with or furnished to governmental entities, plan participants or plan beneficiaries have been timely filed or furnished in accordance with applicable law, and each Parent Employee Benefit Plan has been administered in compliance with its governing written documents; (iv) each of the Parent Plans intended to be qualified under Section 401 of the Code satisfies the requirements of such Section and has received a current favorable determination letter from the IRS regarding such qualified status and has not been amended, operated or administered in a way which would adversely affect such qualified status; (v) there are no actions, suits or claims pending (other than routine claims for benefits) or, to the knowledge of Parent, contemplated or threatened against, or with respect to, any of the Parent Employee Benefit Plans or their assets; (vi) each trust maintained in connection with each Parent Plan, which is qualified under Section 401 of the Code, is tax exempt under Section 501 of the Code; (vii) all contributions required to be made to the Parent Employee Benefit Plans have been made timely; (viii) no accumulated funding deficiency, whether or not waived, within the meaning of Section 302 of ERISA or Section 412 of the Code has been incurred, and there has been no termination or partial termination of any Parent Plan within the meaning of Section 411(d)(3) of the Code; (ix) no act, omission or transaction has occurred which could result in imposition on Parent or any Parent ERISA Affiliate of (A) breach of fiduciary duty liability damages under Section 409 of ERISA, (B) a civil penalty assessed pursuant to subsections (c), (i) or (1) of Section 502 of ERISA or (C) a tax imposed pursuant to Chapter 43 of Subtitle D of the Code; (x) to the knowledge of Parent, there is no matter pending with respect to any of the Parent Plans before the IRS, the Department of Labor or the PBGC; (xi) each of the Parent Employee Benefit Plans complies, in form and operation, with the applicable provisions of the Code and ERISA; (xii) each Parent Employee Benefit Plan may be unilaterally amended or terminated in its entirety (otherwise than with respect to outstanding shares) without any liability or other obligation; (xiii) Parent and the Parent ERISA Affiliates have no liabilities or other obligations, whether actual or contingent, under any Parent Employee Benefit Plan for post-employment benefits of any nature (other than COBRA continuation coverage); and (xiv) neither Parent nor any of the Parent

ERISA Affiliates or any present or former director, officer, employee or other agent of Parent or any of the Parent ERISA Affiliates has made any written or oral representations or promises to any present or former director, officer, employee or other agent concerning his or her terms, conditions or benefits of employment, including the tenure of any such employment or the conditions under which such employment may be terminated by Parent, any of the Parent ERISA Affiliates or the Company which will be binding upon or enforceable against Parent or the Company after the Effective Time.

(d) No employee is currently on a leave of absence due to sickness or disability and no claim is pending or expected to be made by an employee, former employee or independent contractor for workers' compensation benefits.

(e) (i) With respect to the Parent Employee Benefit Plans, there exists no condition or set of circumstances in connection with any of the Parent Companies that could be expected to result in liability reasonably likely to have a Material Adverse Effect on Parent under ERISA, the Code or any other applicable law; and (ii) with respect to the Parent Employee Benefit Plans, individually and in the aggregate, there are no unfunded benefit obligations which have not been accounted for by reserves, or otherwise properly footnoted in accordance with GAAP, on the financial statements of the Parent Companies, which obligations are reasonably likely to have a Material Adverse Effect on Parent.

(f) Neither the execution or delivery of this Agreement nor the consummation of the transactions contemplated hereby shall result in any payment becoming due to any employee or group of employees of any of the Parent Companies.

(g) No amounts payable or that could become payable under any Parent Employee Benefit Plan as a result of the consummation of the transactions contemplated by this Agreement or otherwise shall fail to be deductible for Federal income tax purposes by virtue of either Section 280G or 162(m) of the Code.

Section 4.18 *Employment Contracts and Benefits.* Except as otherwise provided for in any Parent Employee Benefit Plan: (a) none of the Parent Companies is subject to or obligated under any consulting, employment, severance, retention, termination or similar arrangement, any employee benefit, incentive or deferred compensation plan with respect to any Person, or any bonus, profit sharing, pension, stock option, stock purchase or similar plan or other arrangement or other fringe benefit plan entered into or maintained for the benefit of employees of any of the Parent Companies or any other Person; and (b) no employee of any of the Parent Companies or any other Person owns, or has any right granted by any of the Parent Companies to acquire, any interest in any of the assets or business of any of the Parent Companies.

Section 4.19 *Labor Matters.*

(a) No employees of any of the Parent Companies are represented by any labor organization. No labor organization or group of employees of any of the Parent Companies has made a demand for recognition or certification as a union or other labor organization, and there are no representation or certification proceedings or petitions seeking a representation or certification proceeding presently pending or threatened in writing to be brought or filed with the National Labor Relations Board or any other labor relations tribunal or authority. There are no organizing activities involving any of the Parent Companies pending with any labor organization or group of employees of any of the Parent Companies.

(b) Each of the Parent Companies is in compliance with all laws, rules, regulations and orders relating to the employment of labor, including all such laws, rules, regulations and orders relating to wages, hours, collective bargaining, discrimination, civil rights, safety and health, workers' compensation and the collection and payment of income Tax withholding, Social Security

Taxes, Medicare Taxes and similar Taxes, except where the failure to comply would not, individually or in the aggregate, have a Material Adverse Effect on Parent.

Section 4.20 *Insurance*. Each of the Parent Companies maintains, and through the Closing Date will maintain, insurance with reputable insurers (or pursuant to prudent self-insurance programs described in Section 4.20 of the Parent Disclosure Schedule) in such amounts and covering such risks as are in accordance with prudent industry practice for companies engaged in businesses of a size and scope similar to those of the Parent Companies and owning properties in the same general area in which the Parent Companies conduct their businesses. None of such insurance coverage was obtained through the use of false or misleading information or the failure to provide the insurer with all information requested in order to evaluate the liabilities and risks insured. There is no material default with respect to any provision contained in any such policy or binder, and none of the Parent Companies has failed to give any notice or present any claim under any such policy or binder in due and timely fashion. There are no billed but unpaid premiums past due under any such policy or binder. (a) There are no outstanding claims under any such policies or binders and, to the knowledge of Parent, there has not occurred any event that might reasonably form the basis of any claim against or relating to any of the Parent Companies that is not covered by any of such policies or binders; (b) no notice of cancellation or non-renewal of any such policies or binders has been received or threatened; and (c) there are no performance bonds outstanding with respect to any of the Parent Companies.

Section 4.21 *Intellectual Property*. There is no intellectual or intangible property (including, without limitation, legally enforceable licenses or other rights to use, any and all United States and foreign patents, patent applications, patent disclosures, mask works, computer software, geophysical data, trademarks, trade dress, trade names, logos, Internet domain names, copyrights and service marks, including applications to register and registrations for any of the foregoing, as well as trade secrets, know-how, data and other proprietary rights and information) that is necessary for the operation, or continued operation, of the business of any of the Parent Companies, or for the ownership and operation, or continued ownership and operation, of any of their assets, for which the Parent Companies do not hold valid and continuing authority in connection with the use thereof. The businesses of the Parent Companies, as presently conducted, do not conflict with, infringe or violate any intellectual property rights of any other Person, and none of the Parent Companies has received any claim regarding such conflict, infringement or violation, except where (in either case) any such conflict, infringement or violation could not reasonably be expected to have a Material Adverse Effect on Parent.

Section 4.22 *Title to Assets*. The Parent Companies (individually or collectively) have Defensible Title to (i) the Oil and Gas Interests of the Parent Companies included or reflected in the Parent Companies' Ownership Interests and (ii) all other assets of the Parent Companies (other than in the case of this item (ii) those assets for which the failure to have Defensible Title would not, individually or in the aggregate, result in Material Adverse Effect on the Parent Companies, taken as a whole). Each Oil and Gas Interest included or reflected in the Parent Companies' Ownership Interests entitles the Parent Companies (individually or collectively) to receive not less than the undivided interest set forth in (or derived from) Parent Companies' Ownership Interests of all Hydrocarbons produced, saved and sold from or attributable to such Oil and Gas Interest, and the portion of the costs and expenses of operation and development of such Oil and Gas Interest that is borne or to be borne by the Parent Companies (individually or collectively) is not greater than the undivided interest set forth in (or derived from) Parent Companies' Ownership Interests. The oil and gas leases and other agreements that provide the Parent Companies with operating rights in the Oil and Gas Interests included or reflected in the Parent Companies' Ownership Interests are legal, valid and binding and in full force and effect, and the rentals, royalties and other payments due thereunder have been properly and timely paid and there is no existing default (or event that, with notice or lapse of time or both, would become

## Edgar Filing: O'Neill Andrew J - Form 4

a default) under any of such oil and gas leases or other agreements, except in each case as have not had, and would not reasonably be expected to have or result in a Material Adverse Effect on Parent.

### Section 4.23 *Oil and Gas Operations.*

(a) All wells included in the Oil and Gas Interests of Parent have been drilled and (if completed) completed, operated and produced in accordance with generally accepted oil and gas field practices and in compliance in all material respects with applicable oil and gas leases and applicable laws, rules and regulations, except where any failure or violation could not reasonably be expected to have a Material Adverse Effect on Parent.

(b) Proceeds from the sale of Hydrocarbons produced from Parent's Oil and Gas Interests are being received by the Parent Companies in a timely manner and are not being held in suspense for any reason (except in the ordinary course of business).

(c) None of the Parent Companies has received any material advance, take-or-pay or other similar payments that entitle purchasers of production to receive deliveries of Hydrocarbons without paying therefor, and, on a net, company-wide basis, the Parent Companies are neither underproduced nor overproduced, in either case, to any material extent, under gas balancing or similar arrangements.

(d) No claim, notice or order from any Governmental Authority or other Person has been received by any of the Parent Companies due to Hydrocarbon production in excess of allowables or similar violations that could result in curtailment of production after the Closing Date from any Oil and Gas Interests of the Parent Companies, except any such violations which individually or in the aggregate have not had, and would not be reasonably likely to have or result in, a Material Adverse Effect on the Parent Companies.

(e) All material operating equipment owned or leased by the Parent Companies is, in the aggregate, in a state of repair so as to be adequate in all material respects for reasonably prudent operations in the areas in which they are operated.

Section 4.24 *Oil and Gas Reserves.* The factual, non-interpretive data related to oil and gas reserves reflected in the Parent Reserve Report was, as of the date of the Parent Reserve Report, accurate in all material respects.

Section 4.25 *Derivative Transactions and Hedging.* Section 4.25 of the Parent Disclosure Schedule contains a complete and correct list of all Derivative Transactions (including each outstanding Hydrocarbon or financial hedging position attributable to the Hydrocarbon production of the Parent Companies) entered into by the Parent Companies or for the account of any of its customers as of the date of this Agreement. All such Derivative Transactions were, and any Derivative Transactions entered into after the date of this Agreement will be, entered into in accordance with applicable laws, and in accordance with the investment, securities, commodities, risk management and other policies, practices and procedures employed by the Parent Companies. The Parent Companies have duly performed in all material respects all of their respective obligations under the Derivative Transactions to the extent that such obligations to perform have accrued, and, to the knowledge of the Parent, there are no material breaches, violations, collateral deficiencies, requests for collateral or demands for payment (except for ordinary course margin deposit requests), or defaults or allegations or assertions of such by any party thereunder.

Section 4.26 *Natural Gas Act.* Any gas gathering system constituting a part of the properties of the Parent Companies has as its primary function the provision of natural gas gathering services, as the term "gathering" is interpreted under Section 1(b) of the NGA; none of the properties has been or is certificated by the FERC under Section 7(c) of the NGA or to the knowledge of Parent are now

## Edgar Filing: O'Neill Andrew J - Form 4

subject to FERC jurisdiction under the NGA; and none of the properties has been or is providing service pursuant to Section 311 of the NGA.

### Section 4.27 *Environmental Matters.*

(a) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies is subject to any liability or obligation (accrued, contingent, or otherwise) to investigate, cleanup, correct, abate, or take any response, remedial or corrective action under Environmental Laws relating to (i) environmental conditions on, under, or about any of the properties or assets owned, leased, operated, or used by the Parent Companies or any predecessor at the present time or in the past, or (ii) the past or present use, management, handling, transport, treatment, generation, storage, disposal, or release of any Hazardous Materials, whether on-site or off-site.

(b) Except as would not result in a Material Adverse Effect on Parent, all permits, notices, approvals and authorizations required to be obtained or filed in connection with the operation of the Parent Companies' business or the operation or use of any property owned, leased, or operated by the Parent Companies have been obtained or filed and are currently in effect, and the Parent Companies are in compliance with the terms and conditions of such permits, notices, approvals and authorizations.

(c) Except as would not result in a Material Adverse Effect on Parent, each of the Parent Companies has conducted its business and operated its assets, and is conducting its business and operating its assets, in compliance with all Environmental Laws;

(d) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies has been notified by any Governmental Authority or other Person or is otherwise aware that any of the current or prior operations or assets of any of the Parent Companies is the subject of any investigation or inquiry by any Governmental Authority or other Person under Environmental Laws;

(e) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies and, to the knowledge of Parent, no other Person has filed any notice under any federal, state or local law indicating that (i) any of the Parent Companies is responsible for release or threatened release into the environment, or the improper handling, generation, treatment, storage, disposal or recycling, of any Hazardous Material, on any property now or previously owned, leased or operated by any of the Parent Companies; or (ii) any Hazardous Material is improperly handled, generated, treated, stored, disposed of, or recycled upon any property now or previously owned, leased or operated by any of the Parent Companies;

(f) None of the Parent Companies has any liability in excess of \$1,000,000 in the aggregate in connection with (i) the release or threatened release into the environment at, beneath or on any property now or previously owned, leased or operated by any of the Parent Companies, (ii) any obligations under or violations of Environmental Laws, or (iii) the use, release, treatment, storage, disposal, or recycling of any Hazardous Material;

(g) Except as would not result in a Material Adverse Effect on the Parent, there are no pending, or to the knowledge of Parent threatened claims, complaints, notices, inquiries or requests for information involving any matter which remains unresolved (i) under Environmental Laws against any person whose liability for environmental matters any Parent Company has retained or assumed either contractually or by operation of law, or (ii) with respect to any alleged violation of any Environmental Law or regarding potential liability under any Environmental Law against any Parent Company relating to operations or conditions of any facilities or property (including off-site treatment, storage, disposal, or recycling of any Hazardous Material from such

## Edgar Filing: O'Neill Andrew J - Form 4

facilities or property) currently or formerly owned, leased or operated by any of the Parent Companies;

(h) No property now or previously owned, leased or operated by any of the Parent Companies is listed on the National Priorities List pursuant to CERCLA or on the CERCLIS or on any other similar federal or state list as sites requiring investigation or cleanup;

(i) To the knowledge of Parent, none of the Parent Companies is transporting, has transported, or is arranging or has arranged for the transportation of any Hazardous Material to any location which is listed on the National Priorities List pursuant to CERCLA, on the CERCLIS, or on any similar federal or state list or which is the subject of federal, state or local enforcement actions or other investigations that may lead to claims in excess of \$1,000,000 in the aggregate against any of the Parent Companies for investigation, removal or remedial work, contribution for removal or remedial work, damage to natural resources or personal injury, including claims under CERCLA;

(j) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies owns or operates any underground storage tanks or solid waste storage, treatment and/or disposal facilities;

(k) Except as would not result in a Material Adverse Effect on Parent, to the knowledge of Parent, no asbestos, asbestos containing materials or polychlorinated biphenyls are present on or at any property or facility owned, leased or operated by any of the Parent Companies;

(l) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies is operating, or required to be operating, any of its properties or facilities under any order, compliance or consent order, injunction, decree or agreement issued or entered into under, or pertaining to matters regulated by, any Environmental Law;

(m) Except as would not result in a Material Adverse Effect on Parent, none of the Parent Companies has assumed contractually, or to the knowledge of Parent, by operation of law, any liabilities or obligations of third parties under Environmental Laws;

(n) Except as would not result in a Material Adverse Effect on Parent, Parent is not aware of any environmental conditions or circumstances that form, or are reasonably likely to give rise to, a claim against any Parent Company or any Person whose liability for such claim any Parent Company has retained or assumed contractually or by operation of law.

(o) Except as would not result in a Material Adverse Effect on Parent, no Parent Company is subject to any environmental indemnification obligation regarding businesses currently or formerly owned or operated by a Parent Company or regarding properties currently or formerly owned, leased or operated by a Parent Company.

(p) No Parent Company is required by virtue of the transactions contemplated by this Agreement to perform an environmental site assessment or to remove or remediate any Hazardous Materials.

(q) Parent has provided or made available to the Company copies of all contracts in which a Parent Company has retained, assumed, or provided indemnification for liabilities for environmental matters and all material environmental permits, notices, approvals, authorizations, claims, complaints, inquiries, requests for information, orders, compliance or consent orders, injunctions, decrees, agreements, reports, data, studies, results of investigations, audits, assessments, evaluations and correspondence in the possession, custody or control of any of the Parent Companies.

## Edgar Filing: O'Neill Andrew J - Form 4

Section 4.28 *Books and Records.* All books, records and files of the Parent Companies (including those pertaining to Parent's Oil and Gas Interests, wells and other assets, those pertaining to the production, gathering, transportation and sale of Hydrocarbons, and corporate, accounting, financial and employee records): (a) have been prepared, assembled and maintained in accordance with usual and customary policies and procedures, and (b) fairly and accurately reflect the ownership, use, enjoyment and operation by the Parent Companies of their respective assets.

Section 4.29 *Funding.* Parent has available adequate funds in an aggregate amount sufficient to pay (a) all amounts required to be paid to the stockholders of the Company upon consummation of the Merger, (b) all amounts required to be paid by Parent in respect of all Company Stock Options and Company Warrants upon exercise thereof, and (c) all expenses incurred by Parent and Merger Sub in connection with this Agreement and the transactions contemplated hereby.

Section 4.30 *Brokers.* No broker, finder, investment banker or other Person is or will be, in connection with the transactions contemplated by this Agreement, entitled to any brokerage, finder's or other fee or compensation based on any arrangement or agreement made by or on behalf of any of the Parent Companies or Merger Sub and for which Parent, Merger Sub or any of the Target Companies shall have any obligation or liability.

Section 4.31 *Vote Required.* The affirmative vote of the holders of a majority of votes cast at a meeting at which a majority of the outstanding shares of Parent Common Stock are present and voting is the only vote of the holders of any class or series of Parent capital stock or other voting securities necessary to approve this Agreement, the Merger (including the issuance of the Parent Common Stock) and the transactions contemplated hereby.

Section 4.32 *Rights Agreement.* Parent has taken all necessary action (including, if required, amending the Parent Rights Agreement) so that the entering into of this Agreement, the acquisition of shares of Parent Common Stock pursuant to the consummation of the Merger and the other transactions contemplated hereby do not and will not enable or require the Parent Rights to be exercised or distributed.

Section 4.33 *State Takeover Laws.* Parent has taken all necessary action to exempt the Merger from any applicable moratorium, fair price, business combination, control share and other anti-takeover laws under the NRS.

Section 4.34 *Affiliate Transactions.* Section 4.34 of the Parent Disclosure Schedule contains a complete and correct list, as of the date of this Agreement, of all agreements, contracts, transfers of assets or liabilities or other commitments or transactions, whether or not entered into in the ordinary course of business, to or by which Parent or any of its subsidiaries, on the one hand, and any of their respective Affiliates (other than Parent or any of its direct or indirect wholly owned subsidiaries) on the other hand, are or have been a party or otherwise bound or affected, and that (a) are currently pending, in effect or have been in effect during the past 12 months, (b) involve continuing liabilities and obligations that, individually or in the aggregate, have been, are or will be material to the Parent Companies, taken as a whole and (c) are not Parent Plans.

Section 4.35 *Disclosure Controls and Procedures.* Since January 1, 2003, Parent and each of its subsidiaries has had in place "disclosure controls and procedures" (as defined in Rules 13a-14(c) and 15d-14(c) of the Exchange Act) designed and maintained to ensure in all material respects that (a) transactions are executed in accordance with management's general or specific authorizations, (b) transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain accountability for assets, (c) access to assets is permitted only in accordance with management's general or specific authorization, (d) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences, (e) all information (both financial and non-financial) required to be

## Edgar Filing: O'Neill Andrew J - Form 4

disclosed by Parent in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and (f) all such information is accumulated and communicated to Parent's management as appropriate to allow timely decisions regarding required disclosure and to make the certifications of the Chief Executive Officer and Chief Financial Officer of Parent required under the Exchange Act with respect to such reports. Parent's disclosure controls and procedures ensure that information required to be disclosed by Parent in the reports filed with the SEC under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Neither Parent nor its independent auditors have identified any "significant deficiencies" or "material weaknesses" in Parent's or any of its subsidiaries' internal controls as contemplated under Section 404 of SOX. Parent has diligently completed in all material respects its work plan relating to documentation, testing and evaluation of Parent's internal control over financial reporting for purposes of providing the report required by Section 404 of SOX and related SEC rules. As of the date of this Agreement, to the knowledge of Parent, (i) there is no reason that it will not be able, on a timely basis, to complete and include in the Parent's Annual Report on Form 10-K for the year ending December 31, 2004, management's assessment of Parent's internal controls and procedures for financial reporting in accordance with Section 404 of SOX and (ii) there is no material weakness or significant deficiency, in each case as such term is defined in PCAOB Auditing Std. No. 2.

Section 4.36 *Opinion of Financial Advisor.* Parent has received an opinion of Lehman Brothers to the effect that, as of the date of this Agreement, the Conversion Number is fair, from a financial point of view, to Parent, a signed copy of which has been delivered to the Company. Parent has received the approval of such financial advisor to permit the inclusion of a copy of its written opinion in its entirety in the Proxy Statement, subject to such advisor's review thereof as presented in the Proxy Statement.

### ARTICLE V

#### COVENANTS

Section 5.1 *Conduct of Business by Parent Pending Closing.* Parent covenants and agrees with the Company that, from the date of this Agreement until the Effective Time or the date, if any, on which this Agreement is earlier terminated pursuant to Section 7.1, each of the Parent Companies shall conduct its business only in the ordinary and usual course consistent with past practices, except as specifically contemplated in this Agreement or required by applicable law, from the date of this Agreement until the Effective Time or the date, if any, on which this Agreement is earlier terminated pursuant to Section 7.1. Without the prior written consent of the Company:

(a) None of the Parent Companies shall: (i) amend its certificate or articles of incorporation, bylaws or other organizational documents; (ii) adjust, split, combine or reclassify any of its outstanding capital stock; (iii) declare, set aside or pay any dividends or other distributions (whether payable in cash, property or securities) with respect to its capital stock; (iv) issue, sell or agree to issue or sell or amend any phantom stock or stock appreciation rights or any securities or other equity interests, including its capital stock, any rights, options or warrants to acquire its capital stock, or securities convertible into or exchangeable or exercisable for its capital stock (other than shares of Parent Common Stock issued pursuant to the exercise of any Parent Stock Option outstanding on the date of this Agreement); (v) reduce the exercise or conversion price or extend the time for exercise or conversion, other than in accordance with mandatory contractual provisions, of any rights, options or warrants to acquire its capital stock or securities; (vi) purchase, cancel, retire, redeem or otherwise acquire any of its outstanding capital stock or other securities or other equity interests, except pursuant to the terms of the Parent Employee Benefit Plans in effect as of the date of this Agreement; (vii) merge or consolidate with, or transfer all or

## Edgar Filing: O'Neill Andrew J - Form 4

substantially all of its assets to, any other Person (other than the Merger); (viii) liquidate, wind-up or dissolve (or suffer any liquidation or dissolution); or (ix) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing.

(b) None of the Parent Companies shall (i) acquire any corporation, partnership or other business entity or any interest therein (other than interests in joint ventures, joint operation or ownership arrangements or tax partnerships acquired in the ordinary course of business) having an acquisition price in excess of \$10,000,000; (ii) sell, lease or sublease, transfer or otherwise dispose of or mortgage, pledge or otherwise encumber any Oil and Gas Interests of Parent that have a value in excess of \$5,000,000, individually, or any other assets that have a value at the time of such sale, lease, sublease, transfer or disposition in excess of \$5,000,000, individually (except that this clause shall not apply to the sale of Hydrocarbons in the ordinary course of business or encumbrances under the Parent Bank Credit Agreement); (iii) farm-out any Oil and Gas Interest of Parent having a value in excess of \$2,000,000 or interest therein; (iv) sell, transfer or otherwise dispose of or mortgage, pledge or otherwise encumber any securities of any other Person (including any capital stock or other securities or equity interest in any Parent Subsidiary); (v) make any loans, advances or capital contributions to, or investments in, any Person (other than loans or advances in the ordinary course of business) in an aggregate amount in excess of \$500,000; (vi) enter into any Parent Material Agreement or any other agreement not terminable by any of the Parent Companies upon notice of 30 days or less and without penalty or other obligation; or (vii) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing.

(c) None of the Parent Companies shall (i) permit to be outstanding at any time under the Parent Bank Credit Agreement indebtedness for borrowed money in excess of \$50,000,000; (ii) incur any indebtedness for borrowed money other than under trade credit vendor lines not exceeding \$1,000,000 in the aggregate or under the Parent Bank Credit Agreement; (iii) incur any other obligation or liability (other than liabilities incurred in the ordinary course of business); (iv) assume, endorse (other than endorsements of negotiable instruments in the ordinary course of business), guarantee or otherwise become liable or responsible (whether directly, contingently or otherwise) for the liabilities or obligations of any other Person (other than Parent guarantees of Cimarex Energy Services, Inc. regarding obligations under transportation agreements) in an amount in excess of \$500,000; (v) enter into, amend or modify any Derivative Transactions; or (vi) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing.

(d) The Parent Companies shall operate, maintain and otherwise deal with the Oil and Gas Interests of Parent in accordance with good and prudent oil and gas field practices and in accordance with all applicable oil and gas leases and other contracts and agreements and all applicable laws, rules and regulations, including but not limited to Environmental Laws.

(e) None of the Parent Companies shall voluntarily resign, transfer or otherwise relinquish any right it has as of the date of this Agreement, (i) as operator of any Oil and Gas Interest of Parent, except as required by law, regulation or contract, except to the extent such action would not be reasonably likely to have a Material Adverse Effect on Parent, or (ii) with respect to any standstill agreement.

(f) None of the Parent Companies shall (i) enter into, or otherwise become liable or obligated under or pursuant to: (1) any employee benefit, pension or other plan (whether or not subject to ERISA), (2) any other stock option, stock purchase, incentive or deferred compensation plan or arrangement or other fringe benefit plan, or (3) any consulting, employment, severance, retention, termination or similar agreement with any Person, or amend or extend any such plan, arrangement or agreement; (ii) except for payments made pursuant to any Parent Employee

Benefit Plan or any other plan, agreement or arrangement described in Section 4.17 of the Parent Disclosure Schedule, grant, or otherwise become liable for or obligated to pay, any severance, retention or termination payment, bonus or increase in compensation or benefits (other than payments, bonuses or increases that are mandated by the terms of agreements existing as of the date hereof or that are paid in the ordinary course of business, consistent with past practices, and not individually or in the aggregate material in amount) to, or forgive any indebtedness of, any employee or consultant of any of the Parent Companies; or (iii) enter into any contract, agreement, commitment or arrangement to do any of the foregoing.

(g) None of the Parent Companies shall create, incur, assume or permit to exist any Lien on any of its assets, except for Permitted Encumbrances

(h) The Parent Companies shall (i) keep and maintain accurate books, records and accounts; (ii) maintain in full force and effect the policies or binders of insurance described in Section 4.20; (iii) pay all Taxes, assessments and other governmental charges imposed upon any of their assets or with respect to their franchises, business, income or assets before any penalty or interest accrues thereon; (iv) pay all material claims (including claims for labor, services, materials and supplies) that have become due and payable and which by law have or may become a Lien upon any of their assets prior to the time when any penalty or fine shall be incurred with respect thereto or any such Lien shall be imposed thereon; and (v) comply in all material respects with the requirements of all applicable laws, rules, regulations and orders of any Governmental Authority, obtain or take all Governmental Actions necessary in the operation of their businesses, and comply with and enforce the provisions of all Parent Material Agreements, including paying when due all rentals, royalties, expenses and other liabilities relating to their businesses or assets; provided, however, that Parent shall not be in violation of this Section 5.1(h) if any of the Parent Companies incurs obligations for penalties and interest in connection with gross production tax reporting or other Taxes in the ordinary course of business; and provided further, that the Parent Companies may contest the imposition of any such Taxes, assessments and other governmental charges, any such claim, or the requirements of any applicable law, rule, regulation or order or any Parent Material Agreement if done so in good faith by appropriate proceedings and if adequate reserves are established in accordance with GAAP.

(i) The Parent Companies shall at all times preserve and keep in full force and effect their corporate existence and rights and franchises material to their performance under this Agreement.

(j) None of the Parent Companies shall:

(i) take any action that would reasonably be expected to result in the breach of any of the representations and warranties contained in ARTICLE IV, except as specifically permitted under other provisions of this Section 5.1(j);

(ii) approve or implement budgets for general and administrative expenses of the Parent Companies (including salary, bonuses, general operating and overhead expenses) or budgets for Capital Expenditures of the Parent Companies, or incur expenses or disburse funds for any of such purposes except pursuant to the budgets which have been approved by the Company or revisions to such budgets which are approved by the Company, such approval not to be unreasonably withheld (any budgets which have been or are approved as required herein are referred to as "*Approved Budgets*");

(iii) except to the extent already included in an Approved Budget, enter into any agreements or other arrangements with respect to, or make any payments, incur any expenses or disburse any funds for (1) any Capital Project, the completion or full capitalization of which can reasonably be expected to require the Parent Companies to expend, in the aggregate, in excess of \$5,000,000, or (2) any Capital Project for the exploration of Oil and Gas Interests

with undeveloped reserves (including the acquisition of leasehold interests and seismic data, the drilling of wells and all related costs and expenses) which can reasonably be expected to require the Parent Companies to expend, in the aggregate, in excess of \$5,000,000;

(iv) make any Capital Expenditure or general and administrative expense payment which exceeds, for any project, by more than 10 percent the amount set forth in the appropriate line item for such expenditure in an Approved Budget; or

(v) knowingly take, or agree to commit to take any action that would reasonably be expected to result in the failure of a condition set forth in Section 6.1 and Section 6.3(a) and (b) at, or as of any time prior to, the Effective Time, or that would impair materially the ability of the Company, Parent, Merger Sub or the holders of shares of Company Common Stock to consummate the Merger in accordance with the terms hereof or delay materially such consummation.

Section 5.2 *Conduct of Business by the Company Pending Closing.* The Company covenants and agrees with Parent and Merger Sub that, from the date of this Agreement until the Effective Time or the date, if any, on which this Agreement is earlier terminated pursuant to Section 7.1, each of the Target Companies shall conduct its business only in the ordinary and usual course and consistent with past practices, except as specifically contemplated in this Agreement or required by applicable law, from the date of this Agreement until the Effective Time or the date, if any, on which this Agreement is earlier terminated pursuant to Section 7.1. Without the prior written consent of Parent:

(a) None of the Target Companies shall: (i) amend its certificate or articles of incorporation, bylaws or other organizational documents; (ii) adjust, split, combine or reclassify any of its outstanding capital stock; (iii) declare, set aside or pay any dividends or other distributions (whether payable in cash, property or securities) with respect to its capital stock (except as contemplated by Section 5.24 for the TEL Distribution); (iv) issue, sell or agree to issue or sell or amend any phantom stock or stock appreciation rights or any securities or other equity interests, including its capital stock, any rights, options or warrants to acquire its capital stock, or securities convertible into or exchangeable or exercisable for its capital stock (other than shares of Company Common Stock issued pursuant to the exercise of any Company Warrant outstanding on the date of this Agreement, pursuant to the exercise of any Company Stock Options outstanding on the date of this Agreement, or relating to the conversion of the 1996 Preferred in accordance with Section 5.26); (v) reduce the exercise or conversion price or extend the time for exercise or conversion, other than in accordance with mandatory contractual provisions, of any rights, options or warrants to acquire its capital stock or securities; (vi) purchase, cancel, retire, redeem or otherwise acquire any of its outstanding capital stock or other securities or other equity interests, except pursuant to the terms of the Company Employee Benefit Plans in effect as of the date of this Agreement or as relates to the cancellation of the Company Stock Options in accordance with Section 2.4(c)(iii); (vii) merge or consolidate with, or transfer all or substantially all of its assets to, any other Person (other than the Merger); (viii) liquidate, wind-up or dissolve (or suffer any liquidation or dissolution); or (ix) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing.

(b) None of the Target Companies shall (i) acquire any corporation, partnership or other business entity or any interest therein (other than interests in joint ventures, joint operation or ownership arrangements or tax partnerships acquired in the ordinary course of business) having an acquisition price in excess of \$2,000,000; (ii) sell, lease or sublease, transfer or otherwise dispose of or mortgage, pledge or otherwise encumber any Oil and Gas Interests of the Company that have a value in excess of \$1,000,000, individually, or any other assets that have a value at the time of such sale, lease, sublease, transfer or disposition in excess of \$1,000,000, individually (except that this clause shall not apply to the sale of Hydrocarbons in the ordinary course of business or

encumbrances under the Company Bank Credit Agreement); (iii) farm-out any Oil and Gas Interest of the Company having a value in excess of \$2,000,000 or interest therein; (iv) sell, transfer or otherwise dispose of or mortgage, pledge or otherwise encumber any securities of any other Person (including any capital stock or other securities or equity interest in any Company Subsidiary); (v) make any loans, advances or capital contributions to, or investments in, any Person (other than loans or advances in the ordinary course of business) in an aggregate amount in excess of \$500,000; (vi) enter into any Company Material Agreement or any other agreement not terminable by any of the Target Companies upon notice of 30 days or less and without penalty or other obligation; or (vii) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing.

(c) None of the Target Companies shall (i) permit to be outstanding at any time under the Company Bank Credit Agreement indebtedness for borrowed money in excess of \$400,000,000, exclusive of any indebtedness incurred to fund costs relating to the transactions contemplated under this Agreement; (ii) incur any indebtedness for borrowed money other than under trade credit vendor lines not exceeding \$1,000,000 in the aggregate or under the Company Bank Credit Agreement or as relates to the cash payment for the cancellation of the Company Stock Options in accordance with Section 2.4(c)(iii); (iii) incur any other obligation or liability (other than liabilities incurred in the ordinary course of business); (iv) assume, endorse (other than endorsements of negotiable instruments in the ordinary course of business), guarantee or otherwise become liable or responsible (whether directly, contingently or otherwise) for the liabilities or obligations of any other Person in an amount in excess of \$500,000; (v) enter into, amend or modify any Derivative Transactions; or (vi) enter into any contract, agreement, commitment or arrangement with respect to any of the foregoing. None of the Target Companies shall incur any obligation or liability (through notes or any other instrument or form of obligation) under the Continuing Guaranty by the Company to Compass Bank, dated December 20, 2004, with respect to indebtedness of Metrix Networks, Inc., that exceeds \$500,000.

(d) The Target Companies shall operate, maintain and otherwise deal with the Oil and Gas Interests of the Company in accordance with good and prudent oil and gas field practices and in accordance with all applicable oil and gas leases and other contracts and agreements and all applicable laws, rules and regulations, including but not limited to Environmental Laws.

(e) None of the Target Companies shall voluntarily resign, transfer or otherwise relinquish any right it has as of the date of this Agreement, (i) as operator of any Oil and Gas Interest of the Company, except as required by law, regulation or contract, except to the extent such action would not be reasonably likely to have a Material Adverse Effect on the Company, or (ii) with respect to any standstill agreement.

(f) None of the Target Companies shall (i) enter into, or otherwise become liable or obligated under or pursuant to: (1) any employee benefit, pension or other plan (whether or not subject to ERISA), (2) any other stock option, stock purchase, incentive or deferred compensation plan or arrangement or other fringe benefit plan, or (3) any consulting, employment, severance, retention, termination or similar agreement with any Person, or amend or extend any such plan, arrangement or agreement; (ii) except for payments made pursuant to any Company Employee Benefit Plan or any other plan, agreement or arrangement described in Section 3.16 of the Company Disclosure Schedule, grant, or otherwise become liable for or obligated to pay, any severance, retention or termination payment, bonus or increase in compensation or benefits (other than payments, bonuses or increases that are mandated by the terms of agreements existing as of the date hereof or that are paid in the ordinary course of business, consistent with past practices, and not individually or in the aggregate material in amount) to, or forgive any indebtedness of, any employee or consultant of any of the Target Companies; or (iii) enter into any contract, agreement, commitment or arrangement to do any of the foregoing.

## Edgar Filing: O'Neill Andrew J - Form 4

(g) None of the Target Companies shall create, incur, assume or permit to exist any Lien on any of its assets, except for Permitted Encumbrances.

(h) The Target Companies shall (i) keep and maintain accurate books, records and accounts; (ii) maintain in full force and effect the policies or binders of insurance described in Section 3.19; (iii) pay all Taxes, assessments and other governmental charges imposed upon any of their assets or with respect to their franchises, business, income or assets before any penalty or interest accrues thereon; (iv) pay all material claims (including claims for labor, services, materials and supplies) that have become due and payable and which by law have or may become a Lien upon any of their assets prior to the time when any penalty or fine shall be incurred with respect thereto or any such Lien shall be imposed thereon; and (v) comply in all material respects with the requirements of all applicable laws, rules, regulations and orders of any Governmental Authority, obtain or take all Governmental Actions necessary in the operation of their businesses, and comply with and enforce the provisions of all Company Material Agreements, including paying when due all rentals, royalties, expenses and other liabilities relating to their businesses or assets; provided, however, that the Company shall not be in violation of this Section 5.2(h) if any of the Target Companies incurs obligations for penalties and interest in connection with gross production tax reporting or other Taxes in the ordinary course of business; and provided further, that the Target Companies may contest the imposition of any such Taxes, assessments and other governmental charges, any such claim, or the requirements of any applicable law, rule, regulation or order or any Company Material Agreement if done so in good faith by appropriate proceedings and if adequate reserves are established in accordance with GAAP.

(i) The Target Companies shall at all times preserve and keep in full force and effect their corporate existence and rights and franchises material to their performance under this Agreement.

(j) None of the Target Companies shall:

(i) take any action that would reasonably be expected to result in the breach of any of the representations and warranties contained in ARTICLE III, except as specifically permitted under other provisions of this Section 5.2(j);

(ii) approve or implement budgets for general and administrative expenses of the Target Companies (including salary, bonuses, general operating and overhead expenses) or budgets for Capital Expenditures of the Target Companies, or incur expenses or disburse funds for any of such purposes except pursuant to the budgets which have been approved by Parent or revisions to such budgets which are approved by Parent, such approval not to be unreasonably withheld (any budgets which have been or are approved as required herein are referred to as "*Approved Budgets*");

(iii) except to the extent already included in an Approved Budget, enter into any agreements or other arrangements with respect to, or make any payments, incur any expenses or disburse any funds for (1) any onshore Capital Project, the completion or full capitalization of which can reasonably be expected to require the Target Companies to expend, in the aggregate, in excess of \$2,000,000, or (2) any Capital Project for the onshore exploration of Oil and Gas Interests with undeveloped reserves (including the acquisition of onshore leasehold interests and seismic data, the drilling of onshore wells and all related costs and expenses) which can reasonably be expected to require the Target Companies to expend, in the aggregate, in excess of \$2,000,000;

## Edgar Filing: O'Neill Andrew J - Form 4

(iv) except to the extent already included in an Approved Budget, enter into any agreements or other arrangements requiring payment in any single case or series of related cases exceeding \$1,000,000 with respect to, or make any payments, incur any expenses or disburse any funds (in any single case or series of related cases exceeding \$1,000,000) for (1) any offshore Capital Project or (2) any Capital Project for the offshore exploration of Oil and Gas Interests with undeveloped reserves (including the acquisition of offshore leasehold interests and seismic data, the drilling of offshore wells and all related costs and expenses);

(v) make any Capital Expenditure or general and administrative expense payment which, for any project, exceeds by more than 10 percent the amount set forth in the appropriate line item for such expenditure in an Approved Budget; or

(vi) knowingly take, or agree to commit to take, any action that would reasonably be expected to result in the failure of a conditions set forth in Section 6.1 and Section 6.2(a) and (b) at, or as of any time prior to, the Effective Time, or that would impair materially the ability of the Company, Parent, Merger Sub or the holders of shares of Company Common Stock to consummate the Merger in accordance with the terms hereof or delay materially such consummation.

### Section 5.3 *Access to Assets, Personnel and Information.*

(a) Upon reasonable notice and subject to applicable Laws relating to the exchange of information, from the date hereof until the Effective Time, Parent shall: (i) afford to the Company and the Company Representatives, at the Company's sole expense, reasonable access to any of the assets, books and records, contracts, employees, representatives, agents and facilities of the Parent Companies; and (ii) upon request, furnish promptly to the Company (at the Company's expense) access to, or a copy of, any file, book, record, contract, permit, correspondence, or other written information, document or data concerning any of the Parent Companies (or any of their respective assets) that is within the possession or control of any of the Parent Companies.

(b) Upon reasonable notice and subject to applicable Laws relating to the exchange of information, from the date hereof until the Effective Time, the Company shall: (i) afford to Parent and the Parent Representatives, at Parent's sole expense, reasonable access to any of the assets, books and records, contracts, employees, representatives, agents and facilities of the Target Companies; and (ii) upon request, furnish promptly to Parent (at Parent's expense) access to, or a copy of, any file, book, record, contract, permit, correspondence, or other written information, document or data concerning any of the Target Companies (or any of their respective assets) that is within the possession or control of any of the Target Companies.

(c) The Company and the Company Representatives shall, at the Company's sole expense, have the right to make an environmental and physical assessment of the assets of the Parent Companies and, in connection therewith, shall have the right (during normal business hours, or as otherwise permitted by Parent) to enter and inspect such assets and all buildings and improvements thereon, and generally conduct such non-invasive tests, examinations, investigations and studies as the Company reasonably deems necessary, desirable or appropriate for the preparation of engineering or other reports relating to such assets, their condition and the presence of Hazardous Materials and compliance with Environmental Laws. Parent shall be provided not less than 24 hours prior notice of such activities, and Parent Representatives shall have the right to witness all such tests and investigations. The Company shall (and shall cause the Company Representatives to) keep any data or information acquired by any such examinations and the results of any analyses of such data and information strictly confidential and shall not (and shall cause the Company Representatives not to) disclose any of such data, information or results to any Person unless otherwise required by law or regulation and then only after written notice to Parent of the determination of the need for disclosure. The Company shall provide Parent a copy

of any environmental report or assessment prepared on behalf of the Company with respect to any of the Parent Companies or any of their properties or assets. The Company shall indemnify, defend and hold the Parent Companies and the Parent Representatives harmless from and against any and all claims to the extent arising out of or as a result of the activities of the Company and the Company Representatives on the assets of the Parent Companies in connection with conducting such environmental and physical assessment, except to the extent of and limited by the negligence or willful misconduct of any of the Parent Companies or any Parent Representative.

(d) Parent and the Parent Representatives shall, at Parent's sole expense, have the right to make an environmental and physical assessment of the assets of the Target Companies and, in connection therewith, shall have the right (during normal business hours, or as otherwise permitted by the Company) to enter and inspect such assets and all buildings and improvements thereon, and generally conduct such non-invasive tests, examinations, investigations and studies as Parent reasonably deems necessary, desirable or appropriate for the preparation of engineering or other reports relating to such assets, their condition and the presence of Hazardous Materials and compliance with Environmental Laws. The Company shall be provided not less than 24 hours prior notice of such activities, and Company Representatives shall have the right to witness all such tests and investigations. Parent shall (and shall cause the Parent Representatives to) keep any data or information acquired by any such examinations and the results of any analyses of such data and information strictly confidential and shall not (and shall cause the Parent Representatives not to) disclose any of such data, information or results to any Person unless otherwise required by law or regulation and then only after written notice to the Company of the determination of the need for disclosure. Parent shall provide the Company a copy of any environmental report or assessment prepared on behalf of Parent with respect to any of the Target Companies or any of their properties or assets. Parent shall indemnify, defend and hold the Target Companies and the Company Representatives harmless from and against any and all claims to the extent arising out of or as a result of the activities of Parent and the Parent Representatives on the assets of the Target Companies in connection with conducting such environmental and physical assessment, except to the extent of and limited by the negligence or willful misconduct of any of the Target Companies or any Company Representative.

(e) From the date hereof until the Effective Time, each of Parent and the Company shall: (i) furnish to the other, promptly upon receipt, filing or other submission (as the case may be), a copy of each communication between such Party and the SEC after the date hereof relating to the Merger, the Registration Statement or otherwise and each report, schedule, registration statement or other document filed by such Party with the SEC after the date hereof relating to the Merger, the Registration Statement or otherwise; and (ii) promptly advise the other of the substance of any oral communications between such Party and the SEC relating to the Merger, the Registration Statement or otherwise.

(f) The Company shall not (and shall cause the Company Subsidiaries and the Company Representatives not to), and Parent shall not (and shall cause the Parent Subsidiaries and the Parent Representatives not to), use any information obtained pursuant to this Section 5.3 for any purpose unrelated to the consummation of the transactions contemplated by this Agreement.

(g) Notwithstanding anything in this Section 5.3 to the contrary: (i) the Company shall not be obligated under the terms of this Section 5.3 to disclose to Parent or the Parent Representatives, or grant Parent or the Parent Representatives access to, information that is within the possession or control of any of the Target Companies but subject to a valid and binding confidentiality agreement with a third party without first obtaining the consent of such third party, provided, that the Company shall use its reasonable efforts to obtain any such consent, and, provided further, that the Company shall make appropriate substitute disclosure arrangements in circumstances in which such consent is not obtained promptly; and (ii) Parent shall not be obligated under the

terms of this Section 5.3 to disclose to the Company or the Company Representatives, or grant the Company or the Company Representatives access to, information that is within the possession or control of any of the Parent Companies but subject to a valid and binding confidentiality agreement with a third party without first obtaining the consent of such third party, provided, that Parent shall use its reasonable efforts to obtain any such consent and, provided further, that the Parent shall make appropriate substitute disclosure arrangements in circumstances in which such consent is not obtained promptly.

(h) To facilitate approvals of activities of the Parties that are restricted under Section 5.1 and Section 5.2, Parent Representatives and Company Representatives agree to meet on a regular basis to review matters relating to their respective Capital Projects (including the status of expenditures under Approved Budgets (such as outstanding authorizations for expenditures), the success of their Capital Projects to date, proposals to initiate new Capital Projects or substantially increase commitments to existing Capital Projects), commodity hedging issues and any other matters restricted under Section 5.1 and Section 5.2.

Section 5.4 *No Solicitation.*

(a) From the date of this Agreement until the Effective Time or, if earlier, the termination of this Agreement in accordance with its terms, the Company shall not, shall cause each of the Target Companies to not, shall cause each officer, director or employee of the Company or any of the Target Companies to not, and shall cause each investment banker, attorney or other advisor or representative of the Company or any of the Target Companies to not (with respect to any of the Target Companies),

(i) solicit, initiate, or knowingly encourage the submission of, any Takeover Proposal (as herein defined),

(ii) approve or recommend any Takeover Proposal, enter into any agreement, agreement-in-principle or letter of intent with respect to or accept any Takeover Proposal (or resolve to or publicly propose to do any of the foregoing), or

(iii) participate or engage in any discussions or negotiations regarding, or furnish to any Person any information with respect to, or knowingly take any action to facilitate any inquiries or the making of any proposal that constitutes, or would reasonably be expected to lead to, any Takeover Proposal;

provided, however, that (x) if (under circumstances in which the Company has complied with all of its obligations under this Section 5.4(a)), prior to this Agreement having been approved by the Required Company Stockholder Vote (as herein defined), the Company receives an unsolicited written Takeover Proposal from a third party that the Board of Directors of the Company determines in good faith (after consulting with its financial advisors) is, or is reasonably likely to result in, a Superior Proposal (as herein defined), the Company and its representatives may conduct such additional discussions and provide such information as the Board of Directors of the Company shall determine, but only if, prior to such provision of such information or conduct of such additional discussions (A) such third party shall have entered into a confidentiality agreement in customary form that is no less favorable to the Company than the Confidentiality Agreement (and containing additional provisions that expressly permit the Company to comply with the provisions of this Section 5.4) and (B) the Board of Directors of the Company determines in its good faith judgment, after receiving the advice of outside legal counsel, that such action is required in order for the Board of Directors of the Company to comply with its fiduciary duties under applicable law; (y) at any time prior to this Agreement having been approved by the Required Company Stockholder Vote, and subject to the Company's compliance with its obligations under this Section 5.4(a), the Company's Board of Directors may (1) withdraw (or

amend or modify in a manner adverse to Parent or Merger Sub), or publicly propose to withdraw (or amend or modify in a manner adverse to Parent or Merger Sub), the recommendation or declaration of advisability by the Company's Board of Directors of this Agreement, the Merger or the other transactions contemplated by this Agreement and recommend, or publicly propose to recommend, any Takeover Proposal, or (2) recommend, adopt or approve or publicly propose to recommend, adopt or approve any Takeover Proposal, and/or (3) in compliance with Section 7.3, allow the Company to enter into a binding written agreement concerning a transaction that constitutes a Superior Proposal, in the case of subclauses (1), (2) and (3) of this clause (y) only after (A) the Board of Directors of the Company determines in good faith (after providing Parent and Merger Sub with three business days to propose a Parent Alternative Transaction (as defined herein) and after consulting with its financial advisors) that such Takeover Proposal is a Superior Proposal and (B) the Board of Directors of the Company determines in its good faith judgment, after receiving the advice of outside legal counsel, that such action is required in order for the Board of Directors of the Company to comply with its fiduciary duties under applicable law; and (z) nothing contained in subclauses (i) or (ii) above shall prohibit the Company or its Board of Directors from disclosing to the Company's stockholders a position with respect to any tender or exchange offer by a third party pursuant to Rules 14d-9 and 14e-2 promulgated under the Exchange Act, in either case to the extent required by applicable law, provided that the Board of Directors of the Company shall not recommend that the stockholders of the Company tender their Company Common Stock in connection with any such tender or exchange offer unless the Board of Directors of the Company determines in good faith (after receiving the advice of its financial adviser and after providing Parent and Merger Sub with three business days to propose an alternative transaction, which alternative transaction may be conditioned upon receipt of further evidence of the ability and intent of the other prospective purchaser to close (a "*Parent Alternative Transaction*")) that such Takeover Proposal is a Superior Proposal. The Company shall immediately cease and cause to be terminated and shall cause its affiliates and the Target Companies and its or their respective officers, directors, employees, representatives or agents, to terminate all existing discussions or negotiations, if any, with any Persons conducted heretofore with respect to, or that could reasonably be expected to lead to, a Takeover Proposal and shall communicate with any such parties (and their agents or advisors) in possession of confidential information regarding any of the Target Companies directing them to return or destroy such information. The Company shall ensure that its officers, directors and key employees and its investment bankers, attorneys and other representatives are aware of and comply with the provisions of this Section.

(b) For purposes of this Agreement, (i) "*Takeover Proposal*" shall mean any inquiry, proposal or offer from any Person (other than Parent, Merger Sub or any of their affiliates) relating to any acquisition, merger, consolidation, reorganization, share exchange, recapitalization, liquidation, direct or indirect business combination, asset acquisition or other similar transaction involving any of the Target Companies of (A) assets or businesses that constitute or represent 10% or more of the total revenue, operating income, EBITDA or assets of the Target Companies, taken as a whole, or (B) 10% or more of the outstanding shares of Company Common Stock or any other Company capital stock (or other equity or voting interests in the Company) or capital stock of, or other equity or voting interests in, any of the Target Companies directly or indirectly holding, individually or taken together, the assets or business referred to in clause (A) above, in each case other than the transactions contemplated by this Agreement and (ii) the term "*Superior Proposal*" means any bona fide, fully financed written Takeover Proposal to effect a merger, consolidation, reorganization, share exchange, recapitalization, liquidation, direct or indirect business combination, or other similar transaction made by a third party to acquire, directly or indirectly, (x) 50% or more of the assets of the Target Companies, taken as a whole or (y) 50% or more of the outstanding voting securities of the Company, in any such case on terms that the Board of Directors of the Company determines in its good faith judgment (after consulting with its financial

advisors and outside counsel), taking into account all financial, legal and regulatory terms and conditions of the Takeover Proposal and this Agreement, including any changes to the terms of this Agreement offered by Parent through a Parent Alternative Transaction in response to such Takeover Proposal, including any conditions to such Takeover Proposal, the timing of the closing thereof, the risk of nonconsummation, the ability of the Person making the Takeover Proposal to finance the transaction contemplated thereby, any required governmental or other consents, filings and approvals, (A) would, if consummated, result in a transaction that is more favorable to the Company's stockholders from a financial point of view as compared to the transactions contemplated by this Agreement (as modified by a Parent Alternative Transaction) and (B) is reasonably likely to be completed without undue delay.

(c) In addition to the other obligations of the Company set forth in this Section 5.4, the Company shall promptly advise Parent orally and in writing of any request for information with respect to any Takeover Proposal, or any inquiry with respect to or which could result in a Takeover Proposal, the material terms and conditions of such request, Takeover Proposal or inquiry, and the identity of the Person making the same.

(d) Nothing in this Section 5.4 shall permit the Company to terminate this Agreement except as specifically provided in ARTICLE VII.

**Section 5.5 *Company Stockholders Meeting.*** The Company shall take all action necessary in accordance with applicable law and its articles of incorporation and bylaws to convene a meeting of its stockholders as promptly as practicable after the date hereof for the purpose of voting on the Company Proposal. Subject to Section 5.4(a), the Board of Directors of the Company shall recommend approval of the Company Proposal and shall take all lawful action to solicit such approval, including timely mailing the Proxy Statement/Prospectus to the stockholders of the Company.

**Section 5.6 *Parent Stockholders Meeting.*** Parent shall take all action necessary in accordance with applicable law and its articles of incorporation and bylaws to convene a meeting of its stockholders as promptly as practicable after the date hereof for the purpose of voting on the Company Proposal. The Board of Directors of Parent shall recommend approval of the Company Proposal and shall take all lawful action to solicit such approval, including timely mailing the Proxy Statement/Prospectus to the stockholders of Parent.

**Section 5.7 *Registration Statement and Proxy Statement/Prospectus.***

(a) Parent and the Company shall cooperate and promptly prepare the Registration Statement, and, subject to Parent's receiving promptly the required information from the Company, Parent shall file the Registration Statement with the SEC as soon as practicable after the date hereof. Parent shall use all reasonable efforts, and the Company shall cooperate with Parent (including furnishing promptly all information concerning the Company and the holders of Company Common Stock as may be reasonably requested by Parent), to have the Registration Statement (as it may be amended or supplemented) declared effective under the Securities Act as promptly as practicable after such filing. Parent shall use all reasonable efforts, and the Company shall cooperate with Parent, to obtain all necessary state securities laws or "blue sky" permits, approvals and registrations in connection with the issuance of Parent Common Stock pursuant to the Merger.

(b) Parent shall cause the Registration Statement (including the Proxy Statement/Prospectus), at the time it becomes effective under the Securities Act, to comply as to form in all material respects with the applicable provisions of the Securities Act, the Exchange Act and the rules and regulations of the SEC thereunder. The Company shall cause the information it provides for such purpose to comply as to form in all material respects with such provisions.

(c) The Company hereby covenants and agrees with Parent that: (i) the Registration Statement (at the time it becomes effective under the Securities Act and at the Effective Time) shall not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein not misleading (provided, however, that this clause (i) shall apply only to information contained in the Registration Statement that was supplied by the Company for inclusion therein); and (ii) the Proxy Statement/Prospectus (at the time it is first mailed to stockholders of the Company and Parent, at the time of the Company Meeting and the Parent Meeting, and at the Effective Time) shall not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they are made, not misleading (provided, however, that this clause (ii) shall apply only to information contained in the Proxy Statement/Prospectus that was supplied by the Company for inclusion therein). If, at any time prior to the Effective Time, any event with respect to the Company, or with respect to other information supplied by the Company for inclusion in the Registration Statement, occurs and such event is required to be described in an amendment to the Registration Statement, the Company shall promptly notify Parent of such occurrence and shall cooperate with Parent in the preparation and filing of such amendment. If, at any time prior to the Effective Time, any event with respect to the Company, or with respect to other information supplied by the Company for inclusion in the Proxy Statement/Prospectus, occurs and such event is required to be described in a supplement to the Proxy Statement/Prospectus, the Company shall promptly notify Parent of such occurrence and shall cooperate with Parent in the preparation, filing and dissemination of such supplement.

(d) Parent hereby covenants and agrees with the Company that: (i) the Registration Statement (at the time it becomes effective under the Securities Act and at the Effective Time) shall not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein not misleading (provided, however, that this clause (i) shall not apply to any information contained in the Registration Statement that was supplied by the Company for inclusion therein); and (ii) the Proxy Statement/Prospectus (at the time it is first mailed to stockholders of the Company and Parent, at the time of the Company Meeting and the Parent Meeting, and at the Effective Time) shall not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they are made, not misleading (provided, however, that this clause (ii) shall not apply to any information contained in the Proxy Statement/Prospectus that was supplied by the Company for inclusion therein). If, at any time prior to the Effective Time, any event with respect to Parent, or with respect to other information (not supplied by the Company) included in the Registration Statement, occurs and such event is required to be described in an amendment to the Registration Statement, such event shall be so described and such amendment shall be promptly prepared and filed. If, at any time prior to the Effective Time, any event with respect to Parent, or with respect to other information (not supplied by the Company) included in the Proxy Statement/Prospectus, occurs and such event is required to be described in a supplement to the Proxy Statement/Prospectus, Parent shall promptly notify the Company of such occurrence and shall cooperate with the Company in the preparation, filing and dissemination of such supplement.

(e) Neither the Registration Statement nor the Proxy Statement/Prospectus nor any amendment or supplement thereto shall be filed or disseminated to the stockholders of the Company or Parent without the approval of both Parent and the Company (not to be unreasonably withheld). Parent shall advise the Company, promptly after it receives notice thereof, of the time when the Registration Statement has become effective under the Securities Act, the issuance of any stop order with respect to the Registration Statement, the suspension of the qualification of the Parent Common Stock issuable in connection with the Merger for offering or sale in any

jurisdiction, or any comments or requests for additional information by the SEC with respect to the Registration Statement.

Section 5.8 *Stock Exchange Listing.* Parent shall cause the shares of Parent Common Stock to be issued in the Merger and upon exercise of the Company Stock Options and the Company Warrants (if still outstanding and as assumed by Parent) to be approved for listing on Parent's primary National Stock Exchange, subject to official notice of issuance, prior to the Closing Date. Parent shall also cause the Company Warrants (if still outstanding and as assumed by Parent) to be approved for listing on a National Stock Exchange prior to the Closing Date.

Section 5.9 *Additional Arrangements.* Subject to the terms and conditions herein provided, each of the Company and Parent shall take, or cause to be taken, all action and shall do, or cause to be done, all things necessary, appropriate or reasonably desirable under any applicable laws and regulations (including the HSR Act) or under applicable governing agreements to consummate and make effective the transactions contemplated by this Agreement, including using its reasonable best efforts to obtain all necessary waivers, consents and approvals and effecting all necessary registrations and filings. Each of the Company and Parent shall take, or cause to be taken, all action or shall do, or cause to be done, all things necessary, appropriate or reasonably desirable to cause the covenants and conditions applicable to the transactions contemplated hereby to be performed or satisfied as soon as practicable. In addition, if any Governmental Authority shall have issued any order, decree, ruling or injunction, or taken any other action that would have the effect of restraining, enjoining or otherwise prohibiting or preventing the consummation of the transactions contemplated hereby, each of the Company and Parent shall use its reasonable efforts to have such order, decree, ruling or injunction or other action declared ineffective as soon as practicable.

Section 5.10 *Agreements of Affiliates.* At least 10 days prior to the Effective Time, the Company shall cause to be prepared and delivered to Parent a list identifying all Persons who, at the time of the Company Meeting, may be deemed to be "affiliates" of the Company as that term is used in paragraphs (c) and (d) of Rule 145 under the Securities Act. The Company shall use its best efforts (without payment or compensation) to cause each Person who is identified as an affiliate of the Company in such list to execute and deliver to Parent, on or prior to the Closing Date, a written agreement, in the form attached hereto as Exhibit 5.10. Parent shall be entitled to place legends as specified in such agreements on the Parent Certificates representing any Parent Common Stock to be issued to such Persons in the Merger, irrespective of whether or not they sign such agreements.

Section 5.11 *Section 16.* Prior to the Closing Date, Parent and the Company, and their respective boards of directors, shall adopt resolutions consistent with the interpretive guidance of the SEC and take any other actions as may be required to cause any dispositions of Company Common Stock (including derivative securities with respect to Company Common Stock) or acquisitions of Parent Common Stock (including derivative securities with respect to Parent Common Stock) resulting from the transactions contemplated hereby by each individual who is subject to the reporting requirements of Section 16(a) of the Exchange Act to be exempt from Section 16(b) of the Exchange Act under Rule 16b-3 promulgated under the Exchange Act.

Section 5.12 *Public Announcements.* Prior to the Closing, the Company and Parent shall consult with each other before issuing any press release or otherwise making any public statement with respect to the transactions contemplated by this Agreement and shall not issue any press release or make any such public statement prior to obtaining the approval of the other party; provided, however, that such approval shall not be required where such release or announcement is required by applicable law or stock exchange rule; and provided further, that either the Company or Parent may respond to inquiries by the press or others regarding the transactions contemplated by this Agreement, so long as such responses are consistent with such Party's previously issued press releases.

Section 5.13 *Notification of Certain Matters.* The Company shall give prompt notice to Parent of any of the following: (a) any representation or warranty contained in ARTICLE III being untrue or inaccurate when made, (b) the occurrence of any event or development that would cause (or could reasonably be expected to cause) any representation or warranty contained in ARTICLE III to be untrue or inaccurate on the Closing Date, or (c) any failure of the Company to comply with or satisfy any covenant, condition, or agreement to be complied with or satisfied by it hereunder. Parent shall give prompt notice to the Company of any of the following: (x) any representation or warranty contained in ARTICLE IV being untrue or inaccurate when made, (y) the occurrence of any event or development that would cause (or could reasonably be expected to cause) any representation or warranty contained in ARTICLE IV to be untrue or inaccurate on the Closing Date, or (z) any failure of Parent to comply with or satisfy any covenant, condition, or agreement to be complied with or satisfied by it hereunder.

Section 5.14 *Payment of Expenses.* Subject to the provisions of Section 7.2 and Section 7.3, each Party shall pay its own expenses incident to preparing for, entering into and carrying out this Agreement and the consummation of the transactions contemplated hereby, whether or not the Merger shall be consummated, except that: (a) the fee for filing the Registration Statement with the SEC and the costs and expenses associated with printing the Proxy Statement/Prospectus and complying with any applicable state securities or "blue sky" laws shall be borne by Parent; and (b) the costs and expenses associated with mailing the Proxy Statement/Prospectus to the stockholders of (i) the Company, and soliciting the votes of the stockholders of the Company, shall be borne by the Company, and (ii) Parent, and soliciting the votes of the stockholders of Parent, shall be borne by Parent.

Section 5.15 *Indemnification and Insurance.*

(a) Parent agrees that all rights to indemnification now existing in favor of any officers, directors, employees, controlling stockholders or agents of any of the Target Companies, as provided in their respective charters or bylaws (or similar organizational documents), and any existing indemnification agreements or arrangements of any of the Target Companies, shall survive the Merger and shall continue in full force and effect for a period of not less than six years from the Effective Time (or such longer period as may be provided in any existing indemnification agreement between any of the Target Companies, and any current or former officer or director thereof); provided, that, in the event any claim or claims are asserted or made within such six-year period, all rights to indemnification in respect of any such claim or claims shall continue until final disposition of any and all such claims.

(b) From and after the Effective Time, Parent shall, for a period of six years after the Effective Time, indemnify, defend and hold harmless each person who is now, or has been at any time prior to the date of this Agreement or who becomes prior to the Effective Time, an officer, director, employee, controlling stockholder or agent of any of the Target Companies (collectively, the "*Indemnified Parties*") against all losses, expenses (including attorneys' fees), claims, damages, liabilities and amounts that are paid in settlement with the approval of the indemnifying party (which approval shall not be unreasonably withheld) of, or otherwise in connection with, any threatened or actual claim, action, suit, proceeding or investigation (a "*Claim*"), based in whole or in part on or arising in whole or in part out of the fact that the Indemnified Party (or the person controlled by the Indemnified Party) is or was a director, officer, employee, controlling stockholder or agent (including a trustee or fiduciary of any Company Employee Benefit Plan but subject to any conditions or limitations on the indemnity set forth in the applicable Company Employee Benefit Plan) and pertaining to any matter existing or arising out of actions or omissions occurring at or prior to the Effective Time (including any Claim arising out of this Agreement or any of the transactions contemplated hereby), whether asserted or claimed prior to, at or after the Effective Time, in each case to the fullest extent permitted under applicable Nevada law, and shall pay any expenses, as incurred, in advance of the final disposition of any such action or proceeding to each

Indemnified Party to the fullest extent permitted under applicable Nevada law. In determining whether an Indemnified Party is entitled to indemnification under this Section 5.15, if requested by such Indemnified Party, such determination shall be made by special, independent counsel selected by Parent and approved by the Indemnified Party (which approval shall not be unreasonably withheld), and who has not otherwise performed services for Parent or any of its Affiliates within the last three years (other than in connection with such matters). Without limiting the foregoing, in the event any such claim, action, suit, proceeding or investigation is brought against any Indemnified Party(ies) (whether arising before or after the Effective Time): (i) Parent shall have the right to control the defense of such matter with Parent's regularly engaged independent legal counsel or other counsel selected by Parent and reasonably satisfactory to the Indemnified Party(ies), and Parent shall pay all reasonable fees and expenses of such counsel; and (ii) the Indemnified Party(ies) shall cooperate with Parent, at Parent's expense, in the defense of any such matter. Parent shall not be liable for any settlement effected without its prior written consent, which consent shall not unreasonably be withheld. In the event of any Claim, any Indemnified Party wishing to claim indemnification shall promptly notify Parent thereof (provided, that failure to so notify Parent shall not affect the obligations of Parent except to the extent that Parent shall have been prejudiced as a result of such failure) and shall deliver to Parent the undertaking contemplated by the applicable provisions of the NRS, but without any requirement for the posting of a bond. Without limiting the foregoing, in the event any such Claim is brought against any of the Indemnified Parties, such Indemnified Party(ies) may retain only one law firm (plus one local counsel, if necessary) to represent them with respect to each such matter unless the use of counsel chosen to represent the Indemnified Parties would present such counsel with a conflict of interest, or the representation of all of the Indemnified Parties by the same counsel would be inappropriate due to actual or reasonably probable differing interests between them, in which case such additional counsel as may be required (as shall be reasonably determined by the Indemnified Parties and Parent) may be retained by the Indemnified Parties at the cost and expense of Parent and Parent shall pay all reasonable fees and expenses of such counsel for such Indemnified Parties. Notwithstanding the foregoing, nothing contained in this Section 5.15 shall be deemed to grant any right to any Indemnified Party which is not permitted to be granted to an officer, director, employee, controlling stockholder or agent of Parent under applicable Nevada law.

(c) From and after the Effective Time, Parent shall cause to be maintained in effect for not less than six years from the Effective Time the current policies of directors' and officers' liability insurance maintained by the Company, but only to the extent related to actions or omissions prior to the Effective Time; provided, that (i) Parent may substitute therefor policies of at least the same coverage containing terms and conditions which are no less advantageous; (ii) such substitution shall not result in gaps or lapses in coverage with respect to matters occurring prior to the Effective Time; and (iii) Parent shall not be required to pay an annual premium in excess of 200% of the last annual premium paid by the Company prior to the date hereof and if Parent is unable to obtain the insurance required by this Section 5.15(c) it shall obtain as much comparable insurance as possible for an annual premium equal to such maximum amount.

(d) Following the Merger, if Parent or any of its successors or assigns (i) consolidates with or merges into any other Person and shall not be the continuing or surviving corporation or entity of such consolidation or merger, or (ii) transfers or conveys all or substantially all of its properties and assets to any Person or Persons, then, and in each such case, proper provision shall be made so that the successors and assigns of Parent and any of their successors and assigns, assume the obligations of the Parties and Parent set forth in this Section 5.15.

(e) This Section 5.15 shall survive the consummation of the Merger at the Effective Time, is intended to benefit the Company and the Indemnified Parties (each of whom may enforce the provisions of this Section 5.15) and shall be binding on the successors and assigns of Parent.

Section 5.16 *Employees; Employee Benefits.*

(a) For a period of six months following the Closing Date, the Company or its Subsidiaries shall, subject to earlier termination of employment for cause (as determined in accordance with the definition of "cause" set forth in the Company's Extraordinary Transaction Compensation Policy) or by voluntary termination, continue to provide those Persons (other than Persons currently covered by written employment agreements) who are employed by the Company or any of its Subsidiaries immediately prior to the Effective Time (the "*Continuing Employees*"), with employment at respective levels of base salary and incentive and bonus opportunities (but not equity compensation) and benefits (including vacation, paid time off, medical, dental, vision, life, accidental death and dismemberment and disability benefits) that are substantially comparable, in the aggregate to each Continuing Employee, to those provided by the Target Companies immediately prior to the Effective Time; provided, that on and after October 1, 2005, each such Continuing Employee may, at the option of Parent, be enrolled in one or more of the Parent Employee Benefit Plans (with benefits of similarly situated employees of Parent and its Subsidiaries) rather than in any remaining Company Employee Benefit Plans. The Continuing Employees shall be eligible to participate in Parent's 401(k) plan immediately after the Effective Time, according to the terms of Parent's 401(k) plan and applicable law, and with the prior service credit provided for in Section 5.16(b).

(b) The service of each Continuing Employee with the Company or its Subsidiaries (or any predecessor employer) prior to the Effective Time shall be treated as service with Parent and its Subsidiaries for purposes of each Parent Employee Benefit Plan (including retirement, vacation, paid time off and severance plans) in which such Continuing Employee is eligible to participate after the Effective Time, including for purposes of eligibility, vesting and benefit levels and accruals (other than defined benefit pension plan accruals).

(c) Following the Effective Time, Parent shall, or shall cause its Subsidiaries to, (i) waive any pre-existing condition, exclusion, actively-at-work requirements or waiting periods and (ii) provide full credit for any co-payments, deductibles or similar payments made or incurred prior to the Effective Time (or, if later, any applicable plan transition date) for the plan year in which the Effective Time (or such transition date) occurs, in each case for purposes of each Parent Plan in which any Continuing Employee or his or her eligible dependents is eligible to participate after the Effective Time.

(d) Parent shall, and shall cause its Subsidiaries to, honor, in accordance with its terms (but without duplication or multiple effect), each severance policy or plan listed on Section 5.16(d) of the Company Disclosure Schedule and all obligations thereunder, including any rights or benefits arising as a result of the transactions contemplated hereby (either alone or in combination with any other event); provided that the period of time during which severance may be triggered under any severance policy or plan listed on Section 5.16(d) of the Company Disclosure Schedule (without duplication or multiple effect) shall be extended, with respect to each Continuing Employee to which such policy or plan applies, for the period of such Continuing Employee's actual employment with the Company or its Subsidiaries after Closing (up to a maximum extension of six months for all covered participants under the Magnum Hunter Resources, Inc. Employee Severance Policy and all covered participants under the Magnum Hunter Resources, Inc. Extraordinary Transaction Compensation Policy who are entitled to receive, as a Termination Payment thereunder, three months or less of Base Salary (as defined therein)). Parent hereby acknowledges that the consummation of the Merger constitutes a change of control, change in control or extraordinary transaction, as the case may be, for all purposes under such Company Employee Benefit Plans.

(e) Notwithstanding anything herein to the contrary, the Company shall be entitled to (i) amend, modify or terminate any nonqualified deferred compensation plan (as defined in Section 409A of the Code) maintained by any of the Target Companies prior to the Effective Time, as determined by the Company (with the approval of Parent), in order to comply with any rules, regulations or other guidance promulgated by any Governmental Entity under Section 409A of the Code or otherwise to avoid the imposition of any Tax or interest penalty on any participant therein under Section 409A of the Code and (ii) adopt and operate a nonqualified deferred compensation plan that will provide for the deferral of compensation in taxable years beginning on and after January 1, 2005, in lieu of deferral of such compensation under any nonqualified deferred compensation plan in existence as of the date hereof, and having such other terms and conditions as are substantially similar to the terms of any such existing nonqualified deferred compensation plan and are in compliance with Section 409A of the Code. Following the Effective Time, Parent shall not, and shall not permit any of its Subsidiaries or any of its or their respective employees to, take any action or omit to take any action that results, or would be reasonably likely to result, in the imposition of any Tax or interest penalty under Section 409A of the Code on any current or former participant in any such existing or new nonqualified deferred compensation plan, including any "material modification" (within the meaning of Section 885(d)(2)(B) of the American Jobs Creation Act of 2004) of any such nonqualified deferred compensation plan with respect to amounts deferred in taxable years beginning before January 1, 2005. Parent shall indemnify and hold harmless each such participant on an after-tax basis from any Tax or interest penalty imposed under Section 409A of the Code to the extent imposed as a result of any such act or omission.

(f) The parties agree that the consummation of the transactions contemplated by this Agreement shall constitute a "Change in Control" as defined in those employment agreements entered into among the Company, Gruy Petroleum Management Co. and certain executives as identified on Section 5.16(f) of the Company Disclosure Schedule and that on and after the Effective Time such executives shall have "Good Reason" to voluntarily terminate employment in accordance with such agreements, which termination shall entitle such executives to lump sum termination payments, benefits continuation and other benefits pursuant to Sections 8(c)-(e) of such agreements. The lump sum termination payments payable to the executives upon voluntary termination of employment pursuant to Section 8(c) of the employment agreements are set forth on Section 5.16(f) of the Company Disclosure Schedule.

(g) The parties agree that the consummation of the transactions contemplated by this Agreement shall constitute a "Change of Control" as defined in the Company's Outside Director Policy and that the removal of the Company's directors as of the Effective Time as provided in Section 2.3(c) of this Agreement entitles the outside directors of the Company to additional compensation pursuant to Section 3.1 of such policy. The additional compensation payable to each outside director pursuant to Section 3.1 of the Company's Outside Director Policy is set forth on Section 5.16(g) of the Company Disclosure Schedule. Company Stock Options held by outside directors of the Company shall be cashed out in accordance with the provisions of Section 2.4(c)(iii) of this Agreement.

(h) Payments required to be made under the executive employment agreements described in Section 5.16(f) and the Company's Outside Director Policy and the other severance policies or plans described in Section 5.16(d) shall be made at the time provided in such agreements, policies or plans, or, if time of payment is not provided for, within 5 days of an employee or director satisfying the requirements for entitlement to such payments; provided, however, that any payments subject to Section 409A of the Code and related rules, regulations or other guidance made to a key employee (as defined in Code Section 416(i) without regard to subsection (5) thereof) shall be made at a time that will not result in the imposition of any Tax or interest

penalty under Section 409A of the Code, even if compliance with Section 409A of the Code will result in a delay in payment.

(i) To the extent that any employment agreement or written Company policy does not already so specifically provide, if any of the persons set forth on Section 5.16(i) of the Company Disclosure Schedule pays or becomes obligated to pay any excise tax under Section 4999 of the Code on any payment he receives (whether under any such employment agreement, policy or otherwise, and including but not limited to the value of accelerated vesting of Company Stock Options) in connection with the transactions contemplated by this Agreement, the parties agree that the Company shall pay to such person an amount equal to the total excise tax paid or payable.

**Section 5.17 *Parent Board of Directors.*** At the Effective Time, Parent shall cause one then existing member of the Company's Board of Directors selected by Parent to be elected to the Board of Directors of Parent.

**Section 5.18 *Registration Statements Relating to Company Warrants and Company Convertible Notes.*** Prior to the Effective Time, Parent shall file with the SEC a registration statement on Form S-3 with respect to the shares of Parent Common Stock to be issued upon exercise of the Company Warrants (if reasonably expected to be outstanding at the Effective Time in accordance with their currently existing terms) and conversion of the Company Convertible Notes. Parent shall use all reasonable efforts to have such registration statement become effective at the Effective Time and to maintain the effectiveness of such registration statement (and maintain the current status of the related prospectus) for so long as any Company Warrants and Company Convertible Notes remain outstanding in accordance with their currently existing terms. The provisions of this Section 5.18 are intended to be for the benefit of, and shall be enforceable by, the Parties and each holder of a Company Warrant and their respective heirs and representatives. To the extent required by applicable securities law and regulations, Parent shall also file with the SEC a registration statement with respect to the Company Warrants and Company Convertible Notes.

**Section 5.19 *Bank Credit Agreements.*** Each of Parent and the Company shall use its reasonable best efforts to obtain, on or before the Closing Date: (a) any required consents of the lenders under the Parent Bank Credit Agreement and the Company Bank Credit Agreement, respectively, to the Merger and the other transactions contemplated by this Agreement (which in the case of the Company Bank Credit Agreement shall include the lenders' consent to the TEL Distribution and the lenders' agreement to waive any default that could arise if any of the holders of the Company Convertible Notes exercises its right to convert or to have the Company repurchase its Notes); or (b) a new credit facility for Parent in an amount sufficient to pay off all then outstanding indebtedness under both the Parent Bank Credit Agreement and the Company Bank Credit Agreement and provide a similar amount of borrowing capacity as the Parent Bank Credit Agreement and the Company Bank Credit Agreement.

**Section 5.20 *Tax Matters.***

(a) Parent, Merger Sub and the Company shall each, and shall cause its respective subsidiaries to, use its reasonable efforts to cause the Merger to qualify as a "reorganization" within the meaning of Section 368(a) of the Code and to obtain the Tax opinions set forth in Section 6.2(d) and Section 6.3(c). Parent, Merger Sub and the Company agree to file all Tax Returns consistent with the treatment of the Merger as a "reorganization" within the meaning of Section 368(a) of the Code. This Agreement is intended to constitute a "plan of reorganization" within the meaning of Treasury Regulation Section 1.368-2(g).

(b) Officers of Parent, Merger Sub and the Company shall execute and deliver to Thompson & Knight LLP, Tax counsel for the Company, and Holme Roberts & Owen LLP, Tax counsel for Parent, certificates substantially in the form agreed to by the Parties and such law firms

at such time or times as may reasonably be requested by such law firms, including prior to the time the Registration Statement is declared effective by the SEC and the Effective Time, in connection with such Tax counsel's respective delivery of opinions pursuant to Section 6.2(d) and Section 6.3(c). Each of Parent, Merger Sub and the Company shall use its reasonable best efforts not to take or cause to be taken any action that would cause to be untrue (or fail to take or cause not to be taken any action which would cause to be untrue) any of the certifications and representations included in the certificates described in this Section 5.20.

**Section 5.21 Termination of the Company Stock Ownership Plan.** The Company sponsors and maintains the Company 401(k) Employee Stock Ownership Plan (the "*KSOP*"). Prior to the Closing Date, the Board of Directors of the Company shall take all such action as may be necessary to terminate the *KSOP* effective as of a date prior to the Closing Date. As soon as practicable after the date hereof, the current trustee of the *KSOP* shall be replaced by a qualified institutional trustee selected by the Company and acceptable to Parent. On or prior to the termination date, the new trustee of the *KSOP* shall cause the *KSOP* to repay any existing loan(s) of the *KSOP* (in accordance with the terms of the loan, the terms of the *KSOP*, applicable law and in a manner mutually acceptable to the Company and Parent) and the plan administrator shall allocate any unallocated assets remaining after the loan is repaid in accordance with the terms of the *KSOP* document and applicable law. Upon the termination date, the accounts of all participants affected by the termination shall become fully vested and the plan administrator of the *KSOP* shall direct the trustee of the trust related to the *KSOP* to distribute the assets remaining in the trust, after payment of any expenses properly allocable thereto and after receipt of a determination letter from the Internal Revenue Service to the effect that the termination of the *KSOP* will not adversely affect its qualified status, to participants and beneficiaries in proportion to their respective account balances; provided, however, that distributions will not be delayed until after receipt of a favorable determination letter with respect to those participants who are otherwise entitled to a distribution under the *KSOP* by reason of death, disability, retirement, termination of employment or any other reason permitted under the terms of the *KSOP* (other than plan termination). Except as otherwise provided in the *KSOP*, any distributions made after termination of the *KSOP* may be made, in whole or in part, in cash or in kind; provided, however, that participants shall have the right, as provided in the *KSOP* document, to demand payment from their vested *KSOP* Accounts under the *KSOP* in the form of Company Common Stock or if the distribution occurs after the Closing Date, Parent Common Stock (except to the extent of the value of any fractional shares, which shall be distributed in cash). The termination of the *KSOP* and the exercise of all rights, including but not limited to voting, appurtenant to Company stock in the *KSOP* shall be effected in a manner mutually acceptable to Company and Parent. Parent agrees to take all such action as may be necessary to permit rollovers of participant distributions from the *KSOP* to a defined contribution plan maintained by Parent or one of its Subsidiaries, provided that such defined contribution plan shall be required to accept a direct rollover in kind only to the extent permitted under the terms of such plan.

**Section 5.22 SOX 404 Certification.** Each of the Company and Parent shall complete and include in its Annual Report on Form 10-K for the year ending December 31, 2004, management's assessment of the Company's internal controls and procedures for financial reporting in accordance with Section 404 of SOX.

**Section 5.23 Reserve Data.** Each of the Company and Parent shall deliver to the other Party, promptly after filing with the SEC its respective Annual Report on Form 10-K for the year ending December 31, 2004, a true and complete copy of all oil and gas reserve data supporting the oil and gas reserve disclosures by such Party in its respective Annual Report.

**Section 5.24 Dividend of TEL Offshore Trust Units.**

(a) Prior to the tenth day before the date of the Company Meeting, the Board of Directors of the Company may declare a distribution (the "*TEL Distribution*") of trust units of TEL Offshore

## Edgar Filing: O'Neill Andrew J - Form 4

Trust (the "*TEL Units*") to the holders of Company Common Stock, with each share of Company Common Stock entitled to receive that number of TEL Units equal to the quotient obtained by dividing the number of TEL Units owned by the Company on the TEL Distribution Record Date by the number of then outstanding shares of Company Common Stock; provided, however, that the Company may pay cash in lieu of fractional TEL Units or, in any jurisdiction in which the Company reasonably determines on the advice of counsel that distribution of the TEL Units is inadvisable under applicable state "blue sky" laws (provided, that the Company shall use its reasonable best efforts beginning as soon as practicable following the date hereof to pursue diligently appropriate registrations or exemptions in such jurisdictions) or will likely delay the distribution of the TEL Units beyond the Effective Time. In the event of any stock split, combination, reclassification, share dividend or other event similarly altering or affecting the value of TEL Units, the foregoing shall be adjusted to the extent deemed appropriate by the Board of Directors of the Company, and subject to the reasonable approval of Parent, to accomplish the purposes hereof. The resolutions of the Board of Directors declaring the TEL Distribution and setting forth the terms and conditions described above shall in form and substance be reasonably satisfactory to Parent.

(b) The TEL Distribution shall occur on a date, if at all, prior to the Effective Time and be payable to the holders of record of Company Common Stock at the close of business on the record date fixed by the Company's Board of Directors for the TEL Distribution (the "*TEL Distribution Record Date*").

### Section 5.25 *Company Debt Instruments.*

(a) The Company shall provide, or shall cause to be provided, in accordance with the applicable provisions of each of the indentures relating to the Company Convertible Notes and the Company Senior Secured Notes (such Company Convertible Notes and Company Senior Secured Notes, collectively, the "*Notes*" and such indentures, collectively, the "*Indentures*"), to the trustee under each such Indenture and to each Holder (as defined in each respective Indenture), any notices required by the Indentures by virtue of a Change of Control (as defined in each Indenture).

(b) The Surviving Corporation shall, on the Closing Date, execute such supplemental indentures to the Indentures as are required under the Indentures.

(c) The Surviving Corporation shall take all such further actions, including the delivery of any officers' certificates and opinions of counsel required by the Indentures, as may be necessary to comply with all of the terms and conditions of the Indentures.

(d) Parent and the Surviving Corporation shall deliver to all Holders the notices required by the Indentures with respect to the right of the Holders to require repurchase of the Notes and or the conversion thereof upon the occurrence of a Change of Control, and thereafter Parent and the Surviving Corporation shall comply with all other provisions of the Indentures relating to the right of Holders to require repurchase of the Notes and/or the conversion thereof.

Section 5.26 *Conversion of 1996 Preferred.* Prior to the Effective Time, the Company shall cause each of the Company Subsidiaries that is Controlled By the Company and who owns shares of 1996 Preferred to convert all of the issued and outstanding shares of the 1996 Preferred into shares of Company Common Stock, pursuant to the terms set forth in the certificate of designations for the 1996 Preferred.

ARTICLE VI

CONDITIONS

Section 6.1 *Conditions to Each Party's Obligation to Effect the Merger.* The respective obligations of each Party to effect the Merger shall be subject to the satisfaction, at or prior to the Closing Date, of the following conditions, any or all of which may be waived in whole or in part by both Parent and the Company:

(a) *Stockholder Approval.* The Company Proposal shall have been duly and validly approved and adopted by a vote of a majority of the shares of Company Common Stock, all as required by the NRS and the articles of incorporation and bylaws of the Company (the "*Required Company Stockholder Vote*"). The Company Proposal shall have been duly and validly approved and adopted by the stockholders of Parent, all as required by the NRS and the articles of incorporation and bylaws of Parent (the "*Required Parent Stockholder Vote*").

(b) *Approvals of Governmental Authorities.* Any applicable waiting period under the HSR Act shall have expired or been terminated and all filings required to be made prior to the Effective Time with, and all consents, approvals, permits and authorizations required to be obtained prior to the Effective Time from, any Governmental Authority in connection with the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby by the Company, Parent and Merger Sub shall have been made or obtained (as the case may be), except where the failure to obtain any such consents, approvals, permits and authorizations (other than those from the SEC or with respect to the HSR Act) would not be reasonably likely to result in a Material Adverse Effect on Parent (assuming the Merger has taken place) or to materially adversely affect the consummation of the Merger.

(c) *Securities Law Matters.* The Registration Statement shall have been declared effective by the SEC under the Securities Act and shall be effective at the Effective Time, and no stop order suspending such effectiveness shall have been issued, no action, suit, proceeding or investigation by the SEC to suspend such effectiveness shall have been initiated and be continuing, and all necessary approvals under state securities laws relating to the issuance or trading of the Parent Common Stock to be issued in the Merger shall have been received.

(d) *No Injunctions or Restraints.* No temporary restraining order, preliminary or permanent injunction or other order issued by any court of competent jurisdiction or other legal restraint or prohibition preventing the consummation of the Merger shall be in effect; provided, however, that, prior to invoking this condition, each Party shall have complied fully with its obligations under Section 5.9 and, in addition, shall have used all reasonable efforts to have any such decree, ruling, injunction or order vacated, except as otherwise contemplated by this Agreement.

(e) *Stock Exchange Listing.* The shares of Parent Common Stock to be issued in the Merger and upon exercise of the Company Stock Options and the Company Warrants shall have been authorized for listing on Parent's primary National Stock Exchange, subject to official notice of issuance. The Company Warrants shall have been authorized for listing on Parent's primary National Stock Exchange.

Section 6.2 *Conditions to Obligations of Parent and Merger Sub.* The obligations of Parent and Merger Sub to effect the Merger are subject to the satisfaction of the following conditions, any or all of which may be waived in whole or in part by Parent and Merger Sub:

(a) *Representations and Warranties.* The representations and warranties of the Company set forth in ARTICLE III shall, taken individually and together, be true and correct in all

## Edgar Filing: O'Neill Andrew J - Form 4

respects (provided that any representation or warranty contained therein that is qualified by a materiality standard or a Material Adverse Effect qualification or a knowledge qualification, or qualification of like effect, shall not be deemed to be so qualified for purposes of compliance with this condition) as of the date of this Agreement and (except to the extent such representation or warranty speaks only as of an earlier date) as of the Closing Date as though made on and as of that time, and Parent shall have received a certificate signed by a Responsible Officer of the Company to such effect; provided, however, that the condition set forth in this Section 6.2(a) shall be deemed to be satisfied even if one or more of such representations and warranties are not true and correct, so long as the failure of such representations and warranties (without, as set forth above, giving effect to the individual materiality thresholds or qualifications (such as, without limitation, a Material Adverse Effect qualification) or knowledge qualifications otherwise included as a part of such representations and warranties) to be true and correct (individually or in the aggregate) has not had and would not be reasonably likely to have or result in a Material Adverse Effect on the Company or materially adversely affect the ability of the Company to consummate the transactions contemplated hereby.

(b) *Performance of Covenants and Agreements by the Company.* The Company shall have performed in all material respects all covenants and agreements required to be performed by it under this Agreement at or prior to the Closing Date, and Parent shall have received a certificate signed by a Responsible Officer of the Company to such effect.

(c) *No Material Adverse Change.* From the date of this Agreement through the Closing, there shall not have occurred any Material Adverse Effect on the Target Companies, taken as a whole.

(d) *Tax Opinion.* Parent shall have received an opinion (reasonably acceptable in form and substance to Parent) from counsel selected by Parent, on the date on which the Registration Statement is declared effective by the SEC and on the Closing Date, in each case dated as of such respective date, to the effect that (i) the Merger will be treated for United States federal income tax purposes as a reorganization within the meaning of Section 368(a) of the Code, (ii) each of Parent, the Company and Merger Sub will be a party to the reorganization within the meaning of Section 368(b) of the Code, (iii) no gain or loss will be recognized by Parent, the Company or Merger Sub as a result of the Merger, and such opinion shall not have been withdrawn, revoked or modified. Such opinion may be based upon customary assumptions and on representations of the Parties and stockholders of the Parties. If Parent does not receive such opinion from such counsel, the Company has the right to provide such opinion from its counsel, and if so provided, then the condition contained in this Section 6.2(d) shall be deemed to have been satisfied.

(e) *Rights Agreement.* Neither this Agreement nor consummation of the Merger shall have caused or shall cause any of the Company Rights to become exercisable or to be distributed.

(f) *Consents.* All consents and approvals required to be obtained by any of the Target Companies prior to the Effective Time from any Persons (other than any Governmental Authority) in connection with the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby shall have been made or obtained, except to the extent that the failure to obtain such consents and approvals, individually or in the aggregate, has not had and would not be reasonably likely to have or result in a Material Adverse Effect on the Target Companies, taken as a whole, or materially adversely affect the consummation of the transactions contemplated hereby.

Section 6.3 *Conditions to Obligation of the Company.* The obligation of the Company to effect the Merger is subject to the satisfaction of the following conditions, any or all of which may be waived in whole or in part by the Company:

(a) *Representations and Warranties.* The representations and warranties of Parent and Merger Sub set forth in ARTICLE IV shall, taken individually and together, be true and correct in all respects (provided that any representation or warranty contained therein that is qualified by a materiality standard or a Material Adverse Effect qualification or a knowledge qualification, or qualification of like effect, shall not be deemed to be so qualified for purposes of compliance with this condition) as of the date of this Agreement and (except to the extent such representation or warranty speaks only as of an earlier date) as of the Closing Date as though made on and as of that time, and the Company shall have received a certificate signed by a Responsible Officer of Parent to such effect; provided, however, that the condition set forth in this Section 6.3(a) shall be deemed to be satisfied even if one or more of such representations and warranties are not true and correct, so long as the failure of such representations and warranties (without, as set forth above, giving effect to the individual materiality thresholds or qualifications (such as, without limitation, a Material Adverse Effect qualification) or knowledge qualifications otherwise included as a part of such representations and warranties) to be true and correct (individually or in the aggregate) has not had and would not be reasonably likely to have or result in a Material Adverse Effect on Parent or materially adversely affect the ability of the Parent and Merger Sub to consummate the transactions contemplated hereby.

(b) *Performance of Covenants and Agreements by Parent and Merger Sub.* Parent and Merger Sub shall have performed in all material respects all covenants and agreements required to be performed by them under this Agreement at or prior to the Closing Date, and the Company shall have received a certificate signed by a Responsible Officer of Parent to such effect.

(c) *Tax Opinion.* The Company shall have received an opinion (reasonably acceptable in form and substance to the Company) from counsel selected by the Company, on the date on which the Registration Statement is declared effective by the SEC and on the Closing Date, in each case dated as of such respective date, to the effect that (i) the Merger will be treated for United States federal income tax purposes as a reorganization within the meaning of Section 368(a) of the Code, (ii) each of Parent, the Company and Merger Sub will be a party to the reorganization within the meaning of Section 368(b) of the Code, (iii) no gain or loss will be recognized by Parent, the Company and Merger Sub as a result of the Merger, and (iv) no gain or loss, except with respect to the amount of cash received in lieu of fractional shares by former holders of Company Common Stock and except with respect to any cash received by any Dissenting Stockholder, will be recognized by a stockholder of the Company as a result of the Merger, and such opinion shall not have been withdrawn, revoked or modified. Such opinion may be based upon customary assumptions and on representations of the Parties and stockholders of the Parties. If the Company does not receive such opinion from such counsel, Parent has the right to provide such opinion from its counsel, and if so provided, then the condition contained in this Section 6.3(c) shall be deemed to have been satisfied.

(d) *No Material Adverse Change.* From the date of this Agreement through the Closing, there shall not have occurred any Material Adverse Effect on the Parent Companies, taken as a whole.

(e) *Rights Agreement.* Neither this Agreement nor consummation of the Merger shall have caused or shall cause any of the Parent Rights to become exercisable or to be distributed.

(f) *Delivery of Transfer Instructions.* Parent shall have delivered to its authorized transfer agent an irrevocable letter of instruction in a form reasonably satisfactory to the Company authorizing and directing the transfer to holders of shares of Company Common Stock one or more Parent Certificates representing those shares of Parent Common Stock to be issued to such holders upon surrender of such holders' certificates representing such shares of Company Common Stock.

(g) *Consents.* All consents and approvals required to be obtained by any of the Parent Companies prior to the Effective Time from any Persons (other than any Governmental Authority) in connection with the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby shall have been made or obtained, except to the extent that the failure to obtain such consents and approvals, individually or in the aggregate, has not had and would not be reasonably likely to have or result in a Material Adverse Effect on the Parent Companies, taken as a whole, or materially adversely affect the consummation of the transactions contemplated hereby.

## ARTICLE VII

### TERMINATION

Section 7.1 *Termination Rights.* This Agreement may be terminated and the Merger may be abandoned at any time prior to the Effective Time, whether before or after the Required Company Stockholder Vote or the Required Parent Company Vote, respectively:

(a) By mutual written consent of Parent and the Company;

(b) By either the Company or Parent if (i) the Merger has not been consummated by July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005) (provided, however, that the right to terminate this Agreement pursuant to this clause (i) shall not be available to any Party whose breach of any representation or warranty or failure to perform any covenant or agreement under this Agreement has been the cause of or resulted in the failure of the Merger to occur on or before such date); (ii) any Governmental Authority shall have issued an order, decree or ruling or taken any other action permanently restraining, enjoining or otherwise prohibiting the Merger and such order, decree, ruling or other action shall have become final and nonappealable (provided, however, that the right to terminate this Agreement pursuant to this clause (ii) shall not be available to any Party until such Party has used all reasonable efforts to remove such injunction, order or decree); or (iii) the Company Proposal shall not have been approved by (A) the Required Company Stockholder Vote at the Company Meeting or at any adjournment thereof or (B) the Required Parent Stockholder Vote at the Parent Meeting or at any adjournment thereof;

(c) By Parent if (i) there has been a breach of the representations and warranties made by the Company in ARTICLE III of this Agreement such that the condition described in Section 6.2(a) is not met (provided, however, that Parent shall not be entitled to terminate this Agreement pursuant to this clause (i) unless Parent has given the Company notice of such breach and the Company has failed to cure such breach within 10 days following such notice (but in any event not later than July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005)), and the condition described in Section 6.2(a), other than the provision thereof relating to the certificate signed by a Responsible Officer of the Company, would not be satisfied if the Closing

were to occur on the day on which Parent gives the Company notice of such termination); or (ii) the Company has failed to comply in any material respect with any of its covenants or agreements contained in this Agreement and such failure has not been, or cannot be, cured within 10 days after notice and demand for cure thereof (but in any event not later than July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005));

(d) By the Company if (i) there has been a breach of the representations and warranties made by Parent and Merger Sub in ARTICLE IV of this Agreement such that the condition described in Section 6.3(a) is not met (provided, however, that the Company shall not be entitled to terminate this Agreement pursuant to this clause (i) unless the Company has given Parent notice of such breach and Parent has failed to cure such breach within 10 days following such notice (but in any event not later than July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005))), and the condition described in Section 6.3(a), other than the provision thereof relating to the certificate signed by a Responsible Officer of Parent, would not be satisfied if the Closing were to occur on the day on which the Company gives Parent notice of such termination); or (ii) Parent or Merger Sub has failed to comply in any material respect with any of its respective covenants or agreements contained in this Agreement, and, in either such case, such breach or failure has not been, or cannot be, cured within 10 days after notice and a demand for cure thereof (but in any event not later than July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005));

(e) by Parent, if

(i) the Board of Directors of the Company shall have withdrawn or modified or amended in any respect adverse to Parent its adoption of or recommendation in favor of this Agreement or the Merger or shall have failed to make such favorable recommendation;

(ii) the Board of Directors of the Company (or any committee thereof) shall have recommended to the stockholders of the Company any Takeover Proposal or shall have resolved to, or publicly announced an intention to, do so; or

(iii) the Company shall have committed a willful, material breach of Section 5.4.

(f) by the Company, if prior to the Company Meeting, (A) the Company shall not have breached Section 5.4 in any material respect, (B) the Board of Directors of the Company authorizes the Company, subject to complying with the terms of Section 5.4 and Section 7.1(f), to enter into a binding written agreement concerning a transaction that constitutes a Superior Proposal and the Company notifies Parent in writing that it intends to enter into such an agreement, attaching the most current version of such agreement to such notice and (C) the Company prior to such termination pays to Parent in immediately available funds any fees required to be paid pursuant to Section 7.3.

The party desiring to terminate this Agreement shall give written notice of such termination to the other party.

*Section 7.2 Effect of Termination.* If this Agreement is terminated by either the Company or Parent pursuant to the provisions of Section 7.1, this Agreement shall forthwith become void except for, and there shall be no further obligation on the part of any Party or its respective Affiliates, directors, officers or stockholders except pursuant to, the provisions of Section 5.3(c) (but only to the extent of the confidentiality and indemnification provisions contained therein), Section 5.7(c), Section 5.7(d), Section 5.14 and Section 7.3, ARTICLE VIII and the Confidentiality Agreement (which shall continue pursuant to their terms); provided, however, that a termination of this Agreement shall

## Edgar Filing: O'Neill Andrew J - Form 4

not relieve any Party from any liability for damages incurred as a result of a willful breach by such Party of its representations, warranties, covenants, agreements or other obligations hereunder occurring prior to such termination.

Section 7.3 *Fees and Expenses.* If (i) this Agreement is terminated pursuant to Section 7.1(e) or Section 7.1(f) or (ii) (A) a Takeover Proposal in respect of the Company is publicly announced or is proposed or offered or made to the Company or the Company's stockholders prior to this Agreement having been approved by the Required Company Stockholder Vote, (B) this Agreement is terminated by either party, as applicable, pursuant to Section 7.1(b) (solely with respect to the failure to obtain the Required Company Stockholder Vote without breach by the Company of its obligations under Section 5.4) and (C) within 12 months following such termination the Company shall consummate or enter into, directly or indirectly, an agreement with the proponent of such Takeover Proposal or an Affiliate of such proponent, the Company shall promptly, but in no event later than one business day after termination of this Agreement (or on the date of such consummation or, if earlier, entry into such agreement in the case of (ii) above), pay Parent a fee in immediately available funds of \$45,000,000. For purposes of this Section 7.3, the references in the definition of Takeover Proposal to 10% shall be changed to 50%.

### ARTICLE VIII

#### MISCELLANEOUS

Section 8.1 *Nonsurvival of Representations and Warranties.* None of the representations or warranties contained in this Agreement or in any instrument delivered pursuant to this Agreement shall survive the consummation of the Merger.

Section 8.2 *Amendment.* This Agreement may be amended by the Parties at any time before or after the Required Company Stockholder Vote or the Required Parent Stockholder Vote; provided, however, that, after any such approval, no amendment shall be made that by law requires further approval by such stockholders without such further approval. This Agreement may not be amended except by a written instrument signed by an authorized representative of each of the Parties.

Section 8.3 *Notices.* Any notice or other communication required or permitted hereunder shall be in writing and either delivered personally (effective upon delivery), by facsimile transmission (effective on the next day after transmission), by recognized overnight delivery service (effective on the next day after delivery to the service), or by registered or certified mail, postage prepaid and return receipt requested (effective on the third business day after the date of mailing), at the following

A-74

---

## Edgar Filing: O'Neill Andrew J - Form 4

addresses or facsimile transmission numbers (or at such other address(es) or facsimile transmission number(s) for a Party as shall be specified by like notice):

To Parent and/or  
Merger Sub: Cimarex Energy Co.  
1700 Lincoln, Suite 1800  
Denver, Colorado 80203  
Attention: Paul Korus

with a copy to: Holme Roberts & Owen LLP  
1700 Lincoln, Suite 4100  
Denver, Colorado 80203  
Attention: Thomas A. Richardson  
and J. Gregory Holloway

To the Company: Magnum Hunter Resources, Inc.  
600 East Las Colinas Blvd., Suite 1100  
Irving, Texas 75039  
Attention: Jerry Box

with a copy to: Thompson & Knight LLP  
1700 Pacific Avenue, Suite 3300  
Dallas, Texas 75201  
Attention: Andrew B. Derman and Joe Dannenmaier

Section 8.4 *Counterparts.* This Agreement may be executed in one or more counterparts, all of which shall be considered one and the same agreement, and shall become effective when one or more counterparts have been signed by each of the Parties and delivered to the other Parties, it being understood that all Parties need not sign the same counterpart.

Section 8.5 *Severability.* Any term or provision of this Agreement that is invalid or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining terms and provisions of this Agreement or affecting the validity or enforceability of any of the terms or provisions of this Agreement in any other jurisdiction. If any provision of this Agreement is so broad as to be unenforceable, such provision shall be interpreted to be only so broad as is enforceable. This Section shall be subject to Section 8.8.

Section 8.6 *Entire Agreement; No Third Party Beneficiaries.* This Agreement (together with the Confidentiality Agreement and the documents and instruments delivered by the Parties in connection with this Agreement): (a) constitutes the entire agreement and supersedes all other prior agreements and understandings, both written and oral, among the Parties with respect to the subject matter hereof; and (b) except as provided in ARTICLE II and Section 5.3(c), Section 5.3(d), Section 5.15, Section 5.16, and Section 5.18, is solely for the benefit of the Parties and their respective successors, legal representatives and assigns and does not confer on any other Person any rights or remedies hereunder.

Section 8.7 *Applicable Law.* This Agreement shall be governed in all respects, including validity, interpretation and effect, by the laws of the State of Delaware regardless of the laws that might otherwise govern under applicable principles of conflicts of laws thereof.

Section 8.8 *No Remedy in Certain Circumstances.* Each Party agrees that, should any court or other competent authority hold any provision of this Agreement or part hereof to be null, void or unenforceable, or order any Party to take any action inconsistent herewith or not to take an action consistent herewith or required hereby, the validity, legality and enforceability of the remaining

## Edgar Filing: O'Neill Andrew J - Form 4

provisions and obligations contained or set forth herein shall not in any way be affected or impaired thereby, unless the foregoing inconsistent action or the failure to take any action constitutes a material breach of this Agreement or makes this Agreement impossible to perform, in which case this Agreement shall terminate pursuant to ARTICLE VII. Except as otherwise contemplated by this Agreement, to the extent that a Party took an action inconsistent herewith or failed to take action consistent herewith or required hereby pursuant to an order or judgment of a court or other competent Governmental Authority, such Party shall not incur any liability or obligation unless such Party breached its obligations under Section 5.9 or did not in good faith seek to resist or object to the imposition or entering of such order or judgment.

Section 8.9 *Assignment.* Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned by any of the Parties (whether by operation of law or otherwise) without the prior written consent of the other Parties. Subject to the preceding sentence, this Agreement shall be binding upon, inure to the benefit of and be enforceable by the Parties and their respective successors and assigns.

Section 8.10 *Waivers.* At any time prior to the Effective Time, the Parties may, to the extent legally allowed: (a) extend the time for the performance of any of the obligations or other acts of the other Parties, (b) waive any inaccuracies in the representations and warranties contained herein or in any document delivered pursuant hereto, and (c) waive performance of any of the covenants or agreements, or satisfaction of any of the conditions, contained herein. Any agreement on the part of a Party to any such extension or waiver shall be valid only if set forth in a written instrument signed by an authorized representative of such Party. Except as provided in this Agreement, no action taken pursuant to this Agreement, including any investigation by or on behalf of any Party, shall be deemed to constitute a waiver by the Party taking such action of compliance with, or reliance on, any representations, warranties, covenants or agreements contained in this Agreement. The waiver by any Party of a breach of any provision hereof shall not operate or be construed as a waiver of any prior or subsequent breach of the same or any other provisions hereof.

Section 8.11 *Confidentiality Agreement.* The Confidentiality Agreement shall remain in full force and effect following the execution of this Agreement until terminated as described in Section 7.2, is hereby incorporated herein by reference, and shall constitute a part of this Agreement for all purposes; provided, however, that any standstill provisions contained therein shall, effective as of the Closing, be deemed to have been waived to the extent necessary for the Parties to consummate the Merger in accordance with the terms of this Agreement. Any and all information received by Parent and the Company pursuant to the terms and provisions of this Agreement shall be governed by the applicable terms and provisions of the Confidentiality Agreement.

Section 8.12 *Incorporation.* Exhibits and Schedules referred to herein are attached to and by this reference incorporated herein for all purposes.

[Signature Page Follows]

A-76

---

## Edgar Filing: O'Neill Andrew J - Form 4

IN WITNESS WHEREOF, the Parties have caused this Agreement to be executed by their duly authorized representatives, on the date first written above.

"Company"

MAGNUM HUNTER RESOURCES, INC.

By: /s/ JERRY BOX

Name: Jerry Box

Title: Chairman

"Parent"

CIMAREX ENERGY CO.

By: /s/ F. H. MERELLI

Name: F.H. Merelli

Title: Chairman, CEO and President

"Merger Sub"

CIMAREX NEVADA ACQUISITION CO.

By: /s/ GARY C. EVANS

Name: Gary C. Evans

Title: President and CEO

By: /s/ F. H. MERELLI

Name: F.H. Merelli

Title: Chairman, CEO and President

A-77

---

AMENDMENT NO. 1

to

AGREEMENT AND PLAN OF MERGER

This Amendment No. 1 to Agreement and Plan of Merger (this "*Amendment*") is made and entered into as of February 18, 2005, by and among Cimarex Energy Co., a Delaware corporation ("*Parent*"), Cimarex Nevada Acquisition Co., a Nevada corporation and a wholly-owned subsidiary of Parent ("*Merger Sub*"), and Magnum Hunter Resources, Inc., a Nevada corporation (the "*Company*").

WHEREAS, the Company, Parent and Merger Sub entered into an Agreement and Plan of Merger dated as of January 25, 2005 by and among such Parties (the "*Merger Agreement*"); and

WHEREAS, the Parties have differing interpretations of the meaning of Section 5.16(d) of the Merger Agreement; and

WHEREAS, due to information unknown to the Parties at the time the Merger Agreement was entered into, with respect to the Company's representations and warranties under Section 3.15(f) of the Merger Agreement, the Company cannot satisfy the condition to closing set forth in Section 6.3(c) of the Merger Agreement as it is currently written; and

WHEREAS, each of the Parties to the Merger Agreement desires to enter into this Amendment in order to amend the above-referenced provisions of the Merger Agreement;

NOW, THEREFORE, in consideration of the foregoing and the respective representations, warranties, covenants and agreements set forth herein and in the Merger Agreement, the parties hereto agree as follows:

ARTICLE 1  
AMENDMENTS

Section 1.1 *Employees; Employee Benefits*. Section 5.16(d) of the Merger Agreement shall hereby be amended to read in its entirety as follows:

"(d) Parent shall, and shall cause its Subsidiaries to, honor, in accordance with its terms (but without duplication or multiple effect), each severance policy or plan listed on Section 5.16(d) of the Company Disclosure Schedule and all obligations thereunder, including any rights or benefits arising as a result of the transactions contemplated hereby (either alone or in combination with any other event); provided that the end of the Transaction Period under the Company's Extraordinary Transaction Compensation Policy shall be extended from the 180th day following the Closing to the first anniversary of the Closing and the period of time during which severance may be triggered under the Company's Employee Severance Policy shall end on the first anniversary of the Closing (and no severance may be triggered under either such policy or plan after such date). With respect to the Company's Employee Severance Policy, the Parties acknowledge and agree that if a Continuing Employee is involuntarily terminated for any reason other than cause, poor performance or refusal to be reassigned (with respect to duties) or if a Continuing Employee voluntarily terminates employment for the reasons set forth in the specific eligibility provisions related to a change in control as provided in the Employee Severance Policy, then such employee shall be entitled to (i) a severance payment equal to one month's base pay for each year of service (up to a maximum of twelve months) payable in accordance with the terms of the first paragraph of Section III of the Employee Severance Policy, (ii) have his or her COBRA premiums reduced to the amount the employee would be required to pay if he or she were an active employee, for a number of months equal to the same number of months of severance pay received by the employee, (iii) an additional payment equal to the pro-rata share of any annual short-term

## Edgar Filing: O'Neill Andrew J - Form 4

incentive bonus the employee might have been eligible to receive based on Company and individual performance (with the amount of any such bonus received by such employee during fiscal year 2005 as the base for any such proration), and (iv) a payment equal to the amount of accrued but unused vacation pay and commissions earned to the date of termination of employment. The parties further acknowledge and agree that the Termination Payment under the Company's Extraordinary Transaction Compensation Policy is the "revised stay bonus" listed on the attachment to that policy, and that the amount of the revised stay bonus for each covered employee has previously been furnished to Parent. In addition, in the event that a Continuing Employee's employment is involuntarily terminated other than for cause (as determined in accordance with the definition of "cause" set forth in the Company's Extraordinary Transaction Compensation Policy) on or after the Closing Date but before the end of the 6-month period following the Closing Date, then such employee shall be entitled to receive an additional payment equal to the base salary and incentive bonus opportunities (determined, with respect to bonus, as set forth above) and the value of benefits such employee would have received (absent such involuntary termination) during the remainder of such 6-month period. Parent hereby acknowledges that the consummation of the Merger constitutes a change of control, change in control or extraordinary transaction, as the case may be, for all purposes under such Company Employee Benefit Plans. To the extent not specifically otherwise addressed in this Section 5.16(d), the written terms of the Employee Severance Policy and the Extraordinary Transaction Compensation Policy shall continue to apply."

Section 1.2 *Conditions to Obligations of Parent and Merger Sub*. Section 6.3(c) of the Merger Agreement shall hereby be amended to read in its entirety as follows:

"(c) *Tax Opinion*. The Company shall have received an opinion (reasonably acceptable in form and substance to the Company) from counsel selected by the Company, on the date on which the Registration Statement is declared effective by the SEC and on the Closing Date, in each case dated as of such respective date, to the effect that (i) the Merger will be treated for United States federal income tax purposes as a reorganization within the meaning of Section 368(a) of the Code, (ii) each of Parent, the Company and Merger Sub will be a party to the reorganization within the meaning of Section 368(b) of the Code, (iii) no gain or loss will be recognized by Parent, the Company or Merger Sub as a result of the Merger, (iv) no gain or loss will be recognized by U.S. stockholders of the Company with respect to shares of Company Common Stock or Series A Preferred Stock that are exchanged solely for Parent Common Stock in the Merger, except with respect to the amount of cash received instead of fractional shares of Parent Common Stock by U.S. stockholders of Company Common Stock and except with respect to any cash received by any Dissenting Stockholder, and (v) no gain or loss will be recognized by non-U.S. stockholders of the Company with respect to shares of Company Common Stock that are exchanged solely for Parent Common Stock in the Merger, provided such non-U.S. stockholders have not held (either directly or indirectly, after the application of the constructive ownership rules of Section 318 of the Code as modified by Section 897(c)(6)(C) of the Code) more than 5% of the outstanding shares of Company Common Stock at any time during the shorter of (1) the five-year period ending at the Effective Time of the Merger or (2) the period during which such non-U.S. stockholders held such shares of Company Common Stock, and such opinion shall not have been withdrawn, revoked or modified. Such opinion may be based upon customary assumptions and on representations of the Parties and stockholders of the Parties. If the Company does not receive such opinion from such counsel, Parent has the right to provide such opinion from its counsel, and if so provided, then the condition contained in this Section 6.3(c) shall be deemed to have been satisfied."

Section 1.3 *General*. All references to the "Agreement" in the Merger Agreement shall mean the Merger Agreement as amended by this Amendment. Except as expressly modified by this Amendment,

## Edgar Filing: O'Neill Andrew J - Form 4

all provisions of the Merger Agreement remain unmodified and in full force and effect. This Amendment shall be effective as of February 18, 2005.

### **ARTICLE 2 MISCELLANEOUS**

Section 2.1 *Capitalized Terms*. Capitalized terms used but not defined herein shall have the meanings given to such terms in the Merger Agreement.

Section 2.2 *Applicable Law*. This Amendment shall be governed in all respects, including validity, interpretation and effect, by the laws of the State of Delaware regardless of the laws that might otherwise govern under applicable principles of conflicts of laws thereof.

Section 2.3 *Descriptive Headings*. The descriptive headings herein are inserted for convenience of reference only and are not intended to be part of or to affect the meaning or interpretation of this Amendment.

Section 2.4 *Counterparts*. This Amendment may be executed in one or more counterparts, all of which shall be considered one and the same agreement, and shall become effective when one or more counterparts have been signed by each of the Parties and delivered to the other Parties, it being understood that all Parties need not sign the same counterpart.

[Signature Page Follows]

A-80

---

Edgar Filing: O'Neill Andrew J - Form 4

IN WITNESS WHEREOF, the Parties have caused this Amendment to be executed by their duly authorized representatives, on the date first written above.

"Company"  
MAGNUM HUNTER RESOURCES, INC.

By: /s/ GARY C. EVANS  
\_\_\_\_\_

Name: Gary C. Evans  
Title: President and CEO

"Parent"  
CIMAREX ENERGY CO.

By: /s/ F.H. MERELLI  
\_\_\_\_\_

Name: F.H. Merelli  
Title: Chairman, CEO and President

"Merger Sub"  
CIMAREX NEVADA ACQUISITION CO.

By: /s/ F.H. MERELLI  
\_\_\_\_\_

Name: F.H. Merelli  
Title: Chairman, CEO and President

A-81  
\_\_\_\_\_

Edgar Filing: O'Neill Andrew J - Form 4

AMENDMENT NO. 2

TO

AGREEMENT AND PLAN OF MERGER

This Amendment No. 2 to Agreement and Plan of Merger (this "*Amendment*") is made and entered into as of April 20, 2005, by and among Cimarex Energy Co., a Delaware corporation ("*Parent*"), Cimarex Nevada Acquisition Co., a Nevada corporation and a wholly-owned subsidiary of Parent ("*Merger Sub*"), and Magnum Hunter Resources, Inc., a Nevada corporation (the "*Company*").

WHEREAS, the Company, Parent and Merger Sub entered into an Agreement and Plan of Merger dated as of January 25, 2005 by and among such Parties, as amended by Amendment No. 1 thereto among such Parties dated as of February 18, 2005 (the "*Merger Agreement*"); and

WHEREAS, in connection with filing Amendment No. 2 to the Registration Statement, each of the Parties to the Merger Agreement desires to enter into this Amendment in order to amend a condition to closing of the Merger Agreement;

NOW, THEREFORE, in consideration of the foregoing and the respective representations, warranties, covenants and agreements set forth herein and in the Merger Agreement, the parties hereto agree as follows:

ARTICLE 1  
AMENDMENT

Section 1.1 *Conditions to Obligations of Parent and Merger Sub*. Section 6.3(c) of the Merger Agreement shall hereby be amended to read in its entirety as follows:

"(c) *Tax Opinion*. The Company shall have received an opinion (reasonably acceptable in form and substance to the Company) from counsel selected by the Company, on the date on which the Registration Statement is declared effective by the SEC and on the Closing Date, in each case dated as of such respective date, to the effect that (i) the Merger will be treated for United States federal income tax purposes as a reorganization within the meaning of Section 368(a) of the Code, (ii) each of Parent, the Company and Merger Sub will be a party to the reorganization within the meaning of Section 368(b) of the Code, (iii) no gain or loss will be recognized by Parent, the Company or Merger Sub as a result of the Merger, (iv) no gain or loss will be recognized by U.S. stockholders of the Company with respect to shares of Company Common Stock that are exchanged solely for Parent Common Stock in the Merger, except with respect to the amount of cash received instead of fractional shares of Parent Common Stock by U.S. stockholders of Company Common Stock; (v) no gain or loss should be recognized by U.S. stockholders of the Company with respect to shares of Series A Preferred Stock that are exchanged solely for Parent Common Stock in the Merger, except with respect to any cash received by any Dissenting Stockholder, and (vi) no gain or loss will be recognized by non-U.S. stockholders of the Company with respect to shares of Company Common Stock that are exchanged solely for Parent Common Stock in the Merger, provided such non-U.S. stockholders have not held (either directly or indirectly, after the application of the constructive ownership rules of Section 318 of the Code as modified by Section 897(c)(6)(C) of the Code) more than 5% of the outstanding shares of Company Common Stock at any time during the shorter of (1) the five-year period ending at the Effective Time of the Merger or (2) the period during which such non-U.S. stockholders held such shares of Company Common Stock, and such opinion shall not have been withdrawn, revoked or modified. Such opinion may be based upon customary assumptions and on representations of the Parties and stockholders of the Parties. If the Company does not receive such opinion from such

A-82

---

## Edgar Filing: O'Neill Andrew J - Form 4

counsel, Parent has the right to provide such opinion from its counsel, and if so provided, then the condition contained in this Section 6.3(c) shall be deemed to have been satisfied."

Section 1.2 *General*. All references to the "Agreement" in the Merger Agreement shall mean the Merger Agreement as amended by this Amendment. Except as expressly modified by this Amendment, all provisions of the Merger Agreement remain unmodified and in full force and effect. This Amendment shall be effective as of April 20, 2005.

### ARTICLE 2 MISCELLANEOUS

Section 2.1 *Capitalized Terms*. Capitalized terms used but not defined herein shall have the meanings given to such terms in the Merger Agreement.

Section 2.2 *Applicable Law*. This Amendment shall be governed in all respects, including validity, interpretation and effect, by the laws of the State of Delaware regardless of the laws that might otherwise govern under applicable principles of conflicts of laws thereof.

Section 2.3 *Descriptive Headings*. The descriptive headings herein are inserted for convenience of reference only and are not intended to be part of or to affect the meaning or interpretation of this Amendment.

Section 2.4 *Counterparts*. This Amendment may be executed in one or more counterparts, all of which shall be considered one and the same agreement, and shall become effective when one or more counterparts have been signed by each of the Parties and delivered to the other Parties, it being understood that all Parties need not sign the same counterpart.

[Signature Page Follows]

A-83

---

Edgar Filing: O'Neill Andrew J - Form 4

IN WITNESS WHEREOF, the Parties have caused this Amendment to be executed by their duly authorized representatives, on the date first written above.

"Company"  
MAGNUM HUNTER RESOURCES, INC.

By: /s/ RICHARD R. FRAZIER  
\_\_\_\_\_

Name: Richard R. Frazier  
Title: President and CEO

"Parent"  
CIMAREX ENERGY CO.

By: /s/ F.H. MERELLI  
\_\_\_\_\_

Name: F.H. Merelli  
Title: Chairman, CEO and President

"Merger Sub"  
CIMAREX NEVADA ACQUISITION CO.

By: /s/ F.H. MERELLI  
\_\_\_\_\_

Name: F.H. Merelli  
Title: Chairman, CEO and President

A-84  
\_\_\_\_\_

**Annex B**

[LETTERHEAD OF LEHMAN BROTHERS INC.]

January 25, 2005

Board of Directors  
Cimarex Energy Co.  
1700 Lincoln Street  
Suite 1800  
Denver, Colorado 80203

Members of the Board:

We understand that Cimarex Energy Co. ("Cimarex") and Magnum Hunter Resources, Inc. ("Magnum Hunter") are considering entering into a transaction (the "Proposed Transaction") pursuant to which (i) Magnum Hunter will merge with and into a wholly-owned subsidiary of Cimarex (the "Merger") and (ii) upon effectiveness of the Merger, each share of common stock of Magnum Hunter will be converted into the right to receive 0.415 shares of the common stock of Cimarex (the "Exchange Ratio"). We further understand that prior to the Merger, Magnum Hunter will distribute the units of beneficial interests it holds of the publicly-traded TEL Offshore Trust to its shareholders in the form of a dividend. The terms and conditions of the Merger are set forth in more detail in the draft Agreement and Plan of Merger, dated as of January 24, 2005, among Cimarex, Cimarex Nevada Acquisition Co. and Magnum Hunter (the "Agreement").

We have been requested by the Board of Directors of Cimarex to render our opinion with respect to the fairness, from a financial point of view, to Cimarex of the Exchange Ratio to be paid by Cimarex in the Merger. We have not been requested to opine as to, and our opinion does not in any manner address, Cimarex's underlying business decision to proceed with or effect the Proposed Transaction.

In arriving at our opinion, we reviewed and analyzed: (1) the Agreement and its schedules, and the specific terms of the Merger; (2) publicly available information concerning Cimarex and Magnum Hunter that we believe to be relevant to our analysis, including, without limitation, the Annual Reports on Form 10-K for the year ended December 31, 2003 for each of Cimarex and Magnum Hunter, and the Quarterly Reports on Form 10-Q for the nine-months ended September 30, 2004 for each of Cimarex and Magnum Hunter; (3) financial and operating information with respect to the respective businesses, operations and prospects of Cimarex and Magnum Hunter as furnished to us by Cimarex and Magnum Hunter, respectively; (4) estimates of proved and non-proved reserves generated internally at each of Cimarex and Magnum Hunter (the "Internal Reserve Estimates"), third-party reserve reports for each of Cimarex and Magnum Hunter as of December 31, 2003 (the "Third Party Reserve Reports"), and projected future production, revenue, operating costs and capital investments for each of Cimarex and Magnum Hunter provided to us by the managements of Cimarex and Magnum Hunter, respectively (the "Projected Metrics"); (5) the trading histories of Cimarex common stock and Magnum Hunter common stock from January 22, 2004 to January 21, 2005 and a comparison of those trading histories with each other and with those of other companies that we deemed relevant; (6) a comparison of the historical financial results and present financial condition of Cimarex and Magnum Hunter with each other and with those of other companies that we deemed relevant; (7) a comparison of the financial terms of the Merger with the financial terms of certain other transactions that we deemed relevant; (8) the pro forma impact of the Merger on the future financial performance of Cimarex; (9) the relative contributions of Cimarex and Magnum Hunter to the current and future financial performance of the combined company on a pro forma basis; and (10) published estimates of independent equity research analysts (including Lehman Brothers') with respect to the future financial performance of Cimarex and Magnum Hunter. In addition, we have (i) had discussions with the managements of Cimarex and Magnum Hunter concerning (a) their respective businesses, operations,

B-1

---

## Edgar Filing: O'Neill Andrew J - Form 4

assets, financial conditions, reserves, production profiles, hedging levels, exploration programs and prospects and (b) strategic benefits to Cimarex of the Merger and (ii) undertaken such other studies, analyses and investigations as we deemed appropriate.

In arriving at our opinion, we have assumed and relied upon the accuracy and completeness of the financial and other information used by us without assuming any responsibility for independent verification of such information and have further relied upon the assurances of the managements of Cimarex and Magnum Hunter that they are not aware of any facts or circumstances that would make such information inaccurate or misleading. We have not been provided with, and did not have access to, financial projections of Cimarex or Magnum Hunter prepared by the managements of Cimarex and Magnum Hunter, respectively. Accordingly, upon advice of Cimarex, we have assumed that the published estimates of independent equity research analysts are a reasonable basis upon which to evaluate the future financial performance of Cimarex and Magnum Hunter, respectively, and that each of Cimarex and Magnum Hunter will perform substantially in accordance with such estimates. Upon advice of Cimarex and Magnum Hunter, respectively, we have assumed that (i) the Internal Reserve Estimates and the Projected Metrics have been reasonably prepared on a basis reflecting the best currently available estimates and judgments of the managements of Cimarex and Magnum Hunter, respectively, and that the Internal Reserve Estimates and the Projected Metrics will be realized substantially in accordance therewith, and (ii) the Third Party Reserve Reports are a reasonable basis upon which to evaluate the reserve balances at each of Cimarex and Magnum Hunter as of December 31, 2003. In addition, upon the direction of Cimarex, we have not analyzed the merits or the amounts of any actual or potential contingent liabilities of Magnum Hunter or factored them into our analysis in arriving at our opinion. In arriving at our opinion, we have not conducted a physical inspection of the properties and facilities of Cimarex and Magnum Hunter and have not made or obtained from third parties any evaluations or appraisals of the assets or liabilities of Cimarex or Magnum Hunter other than the Third Party Reserve Reports. Upon advice of Cimarex and its legal and accounting advisors, we have assumed that the Merger will qualify as a reorganization within the meaning of Section 368(a) of the Internal Revenue Code of 1986, as amended, and therefore as a tax-free transaction to the stockholders of Cimarex. Our opinion necessarily is based upon market, economic and other conditions as they exist on, and can be evaluated as of, the date of this letter. In addition, we express no opinion as to the price at which shares of common stock of Cimarex or Magnum Hunter actually will trade following announcement of the Merger.

Based upon and subject to the foregoing, we are of the opinion as of the date hereof that, from a financial point of view, the Exchange Ratio to be paid by Cimarex in the Merger is fair to Cimarex.

We have been retained by Cimarex solely to render our opinion in connection with the Proposed Transaction and will receive a fee for our services, a portion of which is contingent upon the consummation of the Merger. In addition, Cimarex has agreed to indemnify us for certain liabilities that may arise out of the rendering of this opinion. We also have performed various investment banking services for Magnum Hunter in the past and have received customary fees for such services. In the ordinary course of our business, we actively trade in the debt and equity securities of Cimarex and Magnum Hunter for our own account and for the accounts of our customers and, accordingly, may at any time hold a long or short position in such securities.

This opinion is for the use and benefit of the Board of Directors of Cimarex and is rendered to the Board of Directors in connection with its consideration of the Merger. This opinion is not intended to be and does not constitute a recommendation to any stockholder of Cimarex or shareholder of Magnum Hunter as to how such stockholder or shareholder should vote with respect to the Merger.

Very truly yours,

/s/ LEHMAN BROTHERS INC.

B-2

---

Annex C

[LETTERHEAD OF DEUTSCHE BANK SECURITIES INC.]

January 25, 2005

Board of Directors  
Magnum Hunter Resources, Inc.  
600 East Las Colinas Blvd  
Dallas, Texas 75039

Gentlemen:

Deutsche Bank Securities Inc. ("Deutsche Bank") has acted as financial advisor to Magnum Hunter Resources, Inc. ("Magnum Hunter" or the "Company") in connection with the proposed combination of Magnum Hunter and Cimarex Energy Co. ("Cimarex") pursuant to the Agreement and Plan of Merger, dated as of January 25, 2005, among Magnum Hunter, Cimarex and Cimarex Nevada Acquisition Co., a wholly owned subsidiary of Cimarex ("Cimarex Merger Sub") (the "Merger Agreement"), which provides, among other things, for the merger of Cimarex Merger Sub with and into Magnum Hunter (the "Transaction"), as a result of which Magnum Hunter will become a wholly owned subsidiary of Cimarex. As set forth more fully in the Merger Agreement, as a result of the Transaction, each share of the Common Stock, par value \$0.002 per share, of the Company ("Company Common Stock") other than Magnum Hunter treasury stock will be converted into the right to receive 0.415 shares (the "Exchange Ratio") of Common Stock, par value \$0.01 per share, of Cimarex ("Cimarex Common Stock"). The terms and conditions of the Transaction are more fully set forth in the Merger Agreement.

You have requested Deutsche Bank's opinion, as investment bankers, as to the fairness, from a financial point of view, to the holders of the Company Common Stock of the Exchange Ratio.

In connection with Deutsche Bank's role as financial advisor to Magnum Hunter, and in arriving at its opinion, Deutsche Bank has reviewed certain publicly available financial and other information concerning the Company and Cimarex and certain internal analyses and other information furnished to it by the Company and Cimarex. Deutsche Bank has also held discussions with members of the senior managements of Magnum Hunter and Cimarex regarding the businesses and prospects of their respective companies and the joint prospects of a combined company. In addition, Deutsche Bank has (i) reviewed the reported prices and trading activity for Magnum Hunter Common Stock and Cimarex Common Stock, (ii) compared certain financial and stock market information for the Company and Cimarex with similar information for certain other companies whose securities are publicly traded, (iii) reviewed the financial terms of certain recent business combinations which it deemed comparable in whole or in part, (iv) reviewed the terms of the Merger Agreement and certain related documents, and (v) performed such other studies and analyses and considered such other factors as it deemed appropriate.

Deutsche Bank has not assumed responsibility for independent verification of, and has not independently verified, any information, whether publicly available or furnished to it, concerning Magnum Hunter or Cimarex, including, without limitation, any financial information, forecasts or projections considered in connection with the rendering of its opinion. Accordingly, for purposes of its opinion, Deutsche Bank has assumed and relied upon the accuracy and completeness of all such information and Deutsche Bank has not conducted a physical inspection of any of the properties or assets, and has not prepared or obtained any independent evaluation or appraisal of any of the assets or liabilities, of Magnum Hunter or Cimarex. With respect to the financial forecasts and projections, including the analyses and forecasts of certain cost savings, operating efficiencies, revenue effects and financial synergies expected by Magnum Hunter and Cimarex to be achieved as a result of the

C-1

---

Transaction (collectively, the "Synergies"), made available to Deutsche Bank and used in its analyses, Deutsche Bank has assumed that they have been reasonably prepared on bases reflecting the best currently available estimates and judgments of the management of Magnum Hunter or Cimarex, as the case may be, as to the matters covered thereby. In rendering its opinion, Deutsche Bank expresses no view as to the reasonableness of such forecasts and projections, including the Synergies, or the assumptions on which they are based. Deutsche Bank's opinion is necessarily based upon economic, market and other conditions as in effect on, and the information made available to it as of, the date hereof.

For purposes of rendering its opinion, Deutsche Bank has assumed that, in all respects material to its analysis, the representations and warranties of Magnum Hunter, Cimarex and Cimarex Merger Sub contained in the Merger Agreement are true and correct, Magnum Hunter, Cimarex and Cimarex Merger Sub will each perform all of the covenants and agreements to be performed by it under the Merger Agreement and all conditions to the obligations of each of Magnum Hunter, Cimarex and Cimarex Merger Sub to consummate the Transaction will be satisfied without any waiver thereof. Deutsche Bank has also assumed that all material governmental, regulatory or other approvals and consents required in connection with the consummation of the Transaction will be obtained and that in connection with obtaining any necessary governmental, regulatory or other approvals and consents, or any amendments, modifications or waivers to any agreements, instruments or orders to which either Magnum Hunter or Cimarex is a party or is subject or by which it is bound, no limitations, restrictions or conditions will be imposed or amendments, modifications or waivers made that would have a material adverse effect on Magnum Hunter or Cimarex or materially reduce the contemplated benefits of the Transaction to Magnum Hunter or the holders of the Company Common Stock. In addition, you have informed Deutsche Bank, and accordingly for purposes of rendering its opinion Deutsche Bank has assumed, that the Transaction will be tax-free to each of Magnum Hunter and Cimarex and their respective stockholders.

Deutsche Bank does not express any opinion as to the price or range of prices at which the Company Common Stock or the Cimarex Common Stock may trade subsequent to the announcement of the Transaction or as to the price or range of prices at which the Cimarex Common Stock may trade subsequent to the consummation of the Transaction.

This opinion is addressed to, and for the use and benefit of, the Board of Directors of Magnum Hunter and is not a recommendation to the stockholders of Magnum Hunter to approve the Transaction. This opinion is limited to the fairness, from a financial point of view, to the holders of the Company Common Stock of the Exchange Ratio, and Deutsche Bank expresses no opinion as to the merits of the underlying decision by Magnum Hunter to engage in the Transaction.

Deutsche Bank will be paid a fee for its services as financial advisor to Magnum Hunter in connection with the Transaction, all of which is contingent upon consummation of the Transaction. We are an affiliate of Deutsche Bank AG (together with its affiliates, the "DB Group"). One or more members of the DB Group have, from time to time, provided investment banking, commercial banking (including extension of credit) and other financial services to Magnum Hunter and Cimarex or their affiliates for which it has received compensation. In the ordinary course of business, members of the DB Group may actively trade in the securities and other instruments and obligations of Magnum Hunter and Cimarex for their own accounts and for the accounts of their customers. Accordingly, the DB Group may at any time hold a long or short position in such securities, instruments and obligations.

Edgar Filing: O'Neill Andrew J - Form 4

Based upon and subject to the foregoing, it is Deutsche Bank's opinion as of the date hereof as investment bankers that the Exchange Ratio is fair, from a financial point of view, to the holders of the Company Common Stock.

Very truly yours,

/s/ DEUTSCHE BANK SECURITIES INC.

DEUTSCHE BANK SECURITIES INC.

C-3

---

**Annex D**

January 25, 2005

Board of Directors  
Magnum Hunter Resources, Inc.  
600 East Las Colinas Blvd, Suite 1100  
Irving, TX 75039

Members of the Board of Directors:

Magnum Hunter Resources, Inc. (the "Company"), Cimarex Energy Co. (the "Acquiror") and Cimarex Nevada Acquisition Co., a wholly owned subsidiary of the Acquiror (the "Acquisition Sub"), have entered into an Agreement and Plan of Merger dated as of January 25, 2005 (the "Agreement") pursuant to which the Acquisition Sub will be merged with the Company in a transaction (the "Merger") in which each outstanding share of the Company's common stock, par value \$.002 per share (the "Company Shares"), will be converted into the right to receive 0.415 shares (the "Exchange Ratio") of the common stock of the Acquiror, par value \$.01 per share (the "Acquiror Shares").

You have asked us whether, in our opinion, the Exchange Ratio is fair from a financial point of view to the holders of the Company Shares.

In arriving at the opinion set forth below, we have, among other things:

- (1) Reviewed certain publicly available business and financial information relating to the Company and the Acquiror that we deemed to be relevant;
- (2) Reviewed certain information, including financial forecasts, relating to the business, earnings, cash flow, assets, liabilities and prospects of the Company and the Acquiror furnished to us by the Company and the Acquiror, respectively;
- (3) Reviewed certain proved reserve data of the Company and the Acquiror as well as information relating to potential future drilling sites and the probable and possible reserves;
- (4) Conducted discussions with members of senior management and representatives of the Company and the Acquiror concerning the matters described in clauses 1, 2 and 3 above, as well as their respective businesses and prospects before and after giving effect to the Merger;
- (5) Reviewed the market prices and valuation multiples for the Company Shares and the Acquiror Shares and compared them with those of certain publicly traded companies that we deemed to be relevant;
- (6) Reviewed the results of operations of the Company and the Acquiror and compared them with those of certain publicly traded companies that we deemed to be relevant;
- (7) Compared the proposed financial terms of the Merger with the financial terms of certain other transactions that we deemed to be relevant;
- (8)

## Edgar Filing: O'Neill Andrew J - Form 4

Participated in certain discussions and negotiations among representatives of the Company and the Acquiror and their financial and legal advisors;

(9)

Reviewed the potential pro forma impact of the Merger;

D-1

---

## Edgar Filing: O'Neill Andrew J - Form 4

- (10) Reviewed the Agreement; and
- (11) Reviewed such other financial studies and analyses and took into account such other matters as we deemed necessary, including our assessment of general economic, market and monetary conditions.

In preparing our opinion, we have assumed and relied on the accuracy and completeness of all information supplied or otherwise made available to us, discussed with or reviewed by or for us, or publicly available, and we have not assumed any responsibility for independently verifying such information or undertaken an independent evaluation or appraisal of any of the assets or liabilities of the Company or the Acquiror or been furnished with any such evaluation or appraisal (other than reserve data referred to herein), nor have we evaluated the solvency or fair value of the Company or the Acquiror under any state or federal laws relating to bankruptcy, insolvency or similar matters. In addition, we have not assumed any obligation to conduct any physical inspection of the properties or facilities of the Company or the Acquiror. With respect to the financial forecast information furnished to or discussed with us by the Company or the Acquiror, we have assumed that they have been reasonably prepared and reflect the best currently available estimates and judgment of the Company's or the Acquiror's management as to the expected future financial performance of the Company or the Acquiror, as the case may be. We have further assumed that the Merger will qualify as a tax-free reorganization for U.S. federal income tax purposes.

Our opinion is necessarily based upon market, economic and other conditions as they exist and can be evaluated on, and on the information made available to us as of, the date hereof. We have assumed that in the course of obtaining the necessary regulatory or other consents or approvals (contractual or otherwise) for the Merger, no restrictions, including any divestiture requirements or amendments or modifications, will be imposed that will have a material adverse effect on the contemplated benefits of the Merger.

We are acting as financial advisor to the Company in connection with the Merger and will receive a fee from the Company for our services contingent upon the consummation of the Merger. In addition, the Company has agreed to indemnify us for certain liabilities arising out of our engagement. We have, in the past, provided financial advisory services to the Company and the Acquiror and may continue to do so and have received, and may receive, fees for the rendering of such services. In addition, in the ordinary course of our business, we may actively trade the Company Shares and other securities of the Company, as well as the Acquiror Shares and other securities of the Acquiror, for our own account and for the accounts of customers and, accordingly, may at any time hold a long or short position in such securities.

This opinion is for the use and benefit of the Board of Directors of the Company. Our opinion does not address the merits of the underlying decision by the Company to engage in the Merger and does not constitute a recommendation to any shareholder as to how such shareholder should vote on the proposed Merger or any matter related thereto. In addition, you have not asked us to address, and this opinion does not address, the fairness to, or any other consideration of, the holders of any class of securities, creditors or other constituencies of the Company, other than the holders of the Company Shares.

We are not expressing any opinion herein as to the prices at which the Company Shares or the Acquiror Shares will trade following the announcement or consummation of the Merger.

On the basis of and subject to the foregoing, we are of the opinion that, as of the date hereof, the Exchange Ratio is fair from a financial point of view to the holders of the Company Shares.

Very truly yours,

MERRILL LYNCH, PIERCE, FENNER & SMITH  
INCORPORATED  
D-2

---

**Annex E**

**STOCKHOLDER VOTING AGREEMENT**

THIS STOCKHOLDER VOTING AGREEMENT (this "**Agreement**") is made, entered into, and effective as of January 25, 2005 by and among Cimarex Energy Co., a Delaware corporation (the "**Cimarex**"), and the persons listed on *Schedule A(Stockholders)* to this Agreement (each, a "**Stockholder**" and, collectively, the "**Stockholders**").

**RECITALS**

WHEREAS, concurrently with the execution and delivery of this Agreement, Cimarex, Cimarex Nevada Acquisition Co., a Nevada corporation and a wholly-owned subsidiary of Cimarex ("**Merger Sub**"), and Magnum Hunter Resources, Inc., a Nevada corporation ("**Magnum**"), are entering into an Agreement and Plan of Merger (the "**Merger Agreement**"), which provides, among other things, for the merger of Merger Sub with and into Magnum (the "**Merger**"), all on the terms and subject to the conditions set forth in the Merger Agreement; and

WHEREAS, as an inducement and a condition to entering into the Merger Agreement, Cimarex has required that each Stockholder agree, and each Stockholder has agreed, to enter into this Agreement;

**AGREEMENT**

NOW, THEREFORE, in and as consideration of and for the foregoing premises and the representations, warranties, agreements, and covenants contained in this Agreement, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto, intending to be legally bound, hereby agree as follows:

1. *Definitions.* Any and all capitalized terms used in this Agreement and not otherwise defined in this Agreement shall have the meaning(s) assigned to such term(s) in the Merger Agreement which is incorporated herein by reference.

2. *Voting.* Unless and until this Agreement is terminated:

(a) Each Stockholder shall, at each meeting of the stockholders of Magnum, if any, however called, or in connection with each written consent of the stockholders of Magnum, if any, vote (or cause to be voted) all shares of Company Common Stock then held of record and/or beneficially owned by such Stockholder (the "**Shares**") (to the extent such Stockholder has the right to vote or direct the voting of such Shares), (i) in favor of the Merger, the execution and delivery by Magnum of the Merger Agreement and the approval of the terms thereof and each of the other actions contemplated by the Merger Agreement and this Agreement and any actions required in furtherance thereof and hereof and (ii) against any proposal relating to a Superior Proposal and against any action or agreement that would impede, frustrate, prevent, or nullify this Agreement, or result in a breach in any respect of any covenant, representation, or warranty or any other obligation or agreement of Magnum under the Merger Agreement or which would result in any of the conditions set forth in Article VI of the Merger Agreement not being fulfilled.

(b) Each Stockholder hereby covenants and agrees that, except as contemplated by this Agreement and/or the Merger Agreement, such Stockholder shall not (i) offer to transfer (which term shall include, without limitation, any sale, tender, gift, pledge, assignment or other disposition), transfer, or consent to any transfer of, any of the Shares beneficially owned by such Stockholder (to the extent such Stockholder has the right to dispose of or direct the disposition of such Shares) or any interest therein without the prior written consent of Cimarex, such consent not to be unreasonably withheld, conditioned, or delayed in the case of a gift or similar estate planning transaction (it being understood that Cimarex may decline to consent to any such transfer if the

person acquiring such Shares does not agree to take such Shares subject to the terms of this Agreement), (ii) enter into any contract, option, or other agreement or understanding with respect to any transfer of any such Shares or any interest therein, (iii) grant any proxy, power-of-attorney, or other authorization or consent in or with respect to any such Shares (other than pursuant to and in accordance with this Agreement), (iv) deposit any such Shares into a voting trust or enter into a voting agreement or arrangement with respect to any such Shares (other than pursuant to and in accordance with this Agreement), or (v) take any other action that would make any representation or warranty of such Stockholder contained herein untrue or incorrect in any material respect or in any way restrict, limit, or interfere in any material respect with the performance of the obligations of such Stockholder hereunder or the transactions contemplated hereby or by the Merger Agreement.

(c) Subject to the terms and conditions of this Agreement, each of the parties hereto agrees to use all commercially reasonable efforts to take, or cause to be taken, all actions, and to do, or cause to be done, all things necessary, proper, and/or advisable under applicable laws to consummate and make effective the transactions contemplated by this Agreement. Each party hereto shall promptly consult with the other parties hereto and provide any necessary information and material with respect to all filings made by any party hereto with any Governmental Authority in connection with this Agreement and the transactions contemplated hereby.

(d) Each Stockholder hereby waives any rights of appraisal or rights to dissent from the Merger that such Stockholder may have.

3. *Representations and Warranties of Each Stockholder.* Each Stockholder hereby represents and warrants, severally and not jointly, to Cimarex as follows:

(a) *Ownership of Shares.* Such Stockholder is the "beneficial owner" (as defined in Rule 13d-3 under the Securities Exchange Act of 1934, as amended, which meaning shall apply for all purposes of this Agreement) of, and has the sole power to vote and dispose of, the number of Shares set forth opposite the name of such Stockholder on *Schedule A (Stockholders)* hereto and is the beneficial owner of options and/or warrants (collectively, the "**Options**") to purchase the number of shares of Company Common Stock set forth opposite the name of such Stockholder on *Schedule A (Stockholders)* hereto, in each case, free and clear of any security interests, liens, charges, encumbrances, equities, claims, options or limitations of whatever nature and free of any other limitation or restriction (including, without limitation, any restriction on the right to vote, sell, or otherwise dispose of such Shares or Options), except, in each case, as may exist by reason of this Agreement or pursuant to applicable law or, in the case of the Options, the restrictions on transferability and/or on exercise or purchase provided for in the applicable option or warrant agreement and/or any related plan, as applicable. The number of Shares and Options set forth opposite the name of such Stockholder on *Schedule A (Stockholders)* hereto represents all of the shares of capital stock of Magnum beneficially owned by such Stockholder as of the date of this Agreement.

(b) Such Stockholder has the power and authority to enter into and perform all of such Stockholder's obligations under this Agreement. This Agreement has been duly and validly executed and delivered by such Stockholder and, assuming due execution and delivery by, and enforceability against, Cimarex, constitutes a legal, valid and binding agreement of such Stockholder, enforceable against such Stockholder in accordance with its terms, except as such enforcement may be limited by any equitable defense. There is no beneficiary or holder of a voting trust certificate or other interest of any trust of which such Stockholder is a trustee, or any party to any other agreement or arrangement, whose consent is required for the execution and delivery of this Agreement or the consummation by such Stockholder of the transactions contemplated thereby.

(c) No filing with, and no permit, authorization, consent or approval of, any Governmental Authority is necessary for the execution and delivery of this Agreement by such Stockholder, the consummation by such Stockholder of the transactions contemplated hereby and the compliance by such Stockholder with the provisions hereof and none of the execution and delivery of this Agreement by such Stockholder, the consummation by such Stockholder of the transactions contemplated hereby or compliance by such Stockholder with any of the provisions hereof, except in cases in which any conflict, breach, default or violation described below would not interfere with the ability of such Stockholder to perform such Stockholder's obligations hereunder, shall (i) conflict with or result in any breach of any organizational documents applicable to such Stockholder, (ii) result in a violation or breach of, or constitute (with or without notice or lapse of time or both) a default (or give rise to any third party right of termination, cancellation, modification or acceleration) under, any of the terms, conditions or provisions of any note, loan agreement, bond, mortgage, indenture, license, contract, commitment, arrangement, understanding, agreement or other instrument or obligation of any kind, including, without limitation, any voting agreement, proxy arrangement, pledge agreement, stockholders agreement or voting trust, to which such Stockholder is a party or by which such Stockholder or any properties or assets of such Stockholder may be bound, or (iii) violate any order, writ, injunction, decree, judgment, order, statute, rule or regulation applicable to such Stockholder or any properties or assets of such Stockholder.

(d) Except as permitted by this Agreement, the Shares beneficially owned by such Stockholder and the certificates representing such Shares are now, and at all times during the term hereof shall be, held by such Stockholder, or by a nominee or custodian for the benefit of such Stockholder, free and clear of all liens, proxies, voting trusts or agreements, understandings or arrangements or any other rights whatsoever, except for any such liens or proxies arising hereunder. The transfer by such Stockholder of the Shares to Cimarex in accordance with the terms of the Merger Agreement shall pass to and unconditionally vest in Cimarex good and valid title to all such Shares, free and clear of all liens, proxies, voting trusts or agreements, understandings or arrangements or any other rights whatsoever.

(e) No broker, investment banker, financial advisor or other person is entitled to any broker's, finder's, financial advisor's or other similar fee or commission in connection with, or as a result of, the execution of this Agreement based upon arrangements made by or on behalf of such Stockholder.

4. *Stop Transfer.* Each Stockholder shall request that Magnum not register the transfer (book-entry or otherwise) of any certificate or uncertificated interest representing any of the Shares beneficially owned by such Stockholder, unless such transfer is made in compliance with this Agreement.

5. *Termination.* This Agreement shall terminate with respect to each Stockholder upon the earliest of (a) the Effective Time, (b) the termination of the Merger Agreement, and (c) July 25, 2005 (which date shall automatically be extended to October 1, 2005 in the event that the SEC has not declared the Registration Statement effective by June 1, 2005).

6. *No Limitation.* Notwithstanding any other provision hereof, nothing in this Agreement shall be construed to prohibit any Stockholder, or any officer or affiliate of any Stockholder that is or has been designated as a member of the Board of Directors of Magnum, from taking any action solely in his or her capacity as a member of the Board of Directors of Magnum or from exercising his or her fiduciary duties as a member of such Board of Directors to the extent specifically permitted by the Merger Agreement.

7. *Miscellaneous.*

(a) This Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter hereof and supersedes all other prior agreements and understandings, both written and oral, between the parties hereto with respect to the subject matter hereof.

(b) This Agreement shall not be assigned by operation of law or otherwise without the prior written consent of each Stockholder (in the case of an assignment by Cimarex) or Cimarex (in the case of an assignment by any Stockholder); *provided, however*, that Cimarex may assign the rights and obligations of Cimarex hereunder to any subsidiary of Cimarex, but no such assignment shall relieve Cimarex of the obligations of Cimarex hereunder.

(c) Without limiting any other rights Cimarex may have hereunder in respect of any transfer of any Shares, each Stockholder agrees that this Agreement and the obligations hereunder shall attach to the Shares beneficially owned by such Stockholder and shall be binding upon any person to which legal or beneficial ownership of such Shares shall pass, whether by operation of law or otherwise, including, without limitation, such Stockholder's heirs, guardians, administrators or successors.

(d) This Agreement may not be amended, changed, supplemented or otherwise modified with respect to any Stockholder except by an instrument in writing signed on behalf of such Stockholder and Cimarex.

(e) All notices, requests, claims, demands and other communications hereunder shall be in writing and shall be given (and shall be deemed to have been duly received if given) by hand delivery or by facsimile transmission with confirmation of receipt, as follows:

If to Cimarex:

Cimarex Energy Co.  
1700 Lincoln, Suite 1800  
Denver, Colorado 80203  
Attention: Paul Korus  
Fax: 303.295.3494

with a copy (which shall not constitute notice) to:

Holme Roberts & Owen LLP  
1700 Lincoln, Suite 4100  
Denver, Colorado 80203  
Attention: Thomas A. Richardson and J. Gregory Holloway  
Fax: 303.866.0200 and 303.866.0200

If to a Stockholder:

At the addresses and facsimile numbers set forth on *Schedule A* hereto.

with a copy (which shall not constitute notice) to:

Haynes and Boone, LLP  
901 Main Street, Suite 3100  
Dallas, Texas 75202-3789  
Attention: Greg R. Samuel, Esq.  
Fax: 214.200.0577

or to such other address or facsimile number as the person to whom notice is given may have previously furnished to the other parties hereto in writing in the manner set forth above.

(f) Whenever possible, each provision or portion of any provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law but if any provision or



portion of any provision of this Agreement is held to be invalid, illegal or unenforceable in any respect under any applicable law or rule in any jurisdiction such invalidity, illegality or unenforceability shall not affect any other provision or portion of any provision in such jurisdiction, and this Agreement shall be reformed, construed and enforced in such jurisdiction as if such invalid, illegal or unenforceable provision or portion of any provision had never been contained herein.

(g) All rights, powers and remedies provided under this Agreement or otherwise available in respect hereof at law or in equity shall be cumulative and not alternative, and the exercise of any thereof by any party shall not preclude the simultaneous or later exercise of any other such right, power or remedy by such party.

(h) The failure of any party hereto to exercise any right, power or remedy provided under this Agreement or otherwise available in respect hereof at law or in equity, or to insist upon compliance by any other party hereto with its obligations hereunder, and any custom or practice of the parties at variance with the terms hereof, shall not constitute a waiver by such party of its right to exercise any such or other right, power or remedy or to demand such compliance.

(i) This Agreement shall be binding upon and inure solely to the benefit of each party hereto, and nothing in this Agreement, express or implied, is intended to confer upon any other person any rights or remedies of any nature whatsoever under or by reason of this Agreement.

(j) This Agreement shall be governed by, and construed in accordance with, the laws of the State of Delaware.

(k) The parties agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions of this Agreement in any Delaware state court located in the City of Wilmington or any Federal court located in the United States District Court for the District of Delaware, Wilmington, Delaware, this being in addition to any other remedy to which they are entitled at law or in equity. In addition, each of the parties hereto (i) consents to submit itself to the personal jurisdiction of any Delaware state court located in the City of Wilmington or any Federal court located in the United States District Court for the District of Delaware, Wilmington, Delaware in the event any dispute arises out of this Agreement or any transaction contemplated by this Agreement, (ii) agrees that it shall not attempt to deny or defeat such personal jurisdiction by motion or other request for leave from any such court and (iii) agrees that it shall not bring any action relating to this Agreement or any transaction contemplated by this Agreement in any court other than any such court. The parties hereto irrevocably and unconditionally waive any objection to the laying of venue of any action, suit or proceeding arising out of this Agreement or the transactions contemplated hereby in the courts of the State of Delaware located in the City of Wilmington or in any Federal court located in the United States District Court for the District of Delaware, Wilmington, Delaware, and hereby further irrevocably and unconditionally waive and agree not to plead or claim in any such court that any such action, suit or proceeding brought in any such court has been brought in a inconvenient forum.

(l) The descriptive headings used herein are inserted for convenience of reference only and are not intended to be part of or to affect the meaning or interpretation of this Agreement.

(m) This Agreement may be executed in counterparts (by fax or otherwise), each of which shall be deemed to be an original, but all of which, taken together, shall constitute one and the same agreement.

(n) Except as otherwise provided herein, each party shall pay its, his or her own expenses incurred in connection with this Agreement.

**Remainder of Page Intentionally Left Blank. Signature Page(s) to Follow.**

Edgar Filing: O'Neill Andrew J - Form 4

IN WITNESS WHEREOF, the parties hereto have executed and delivered this Stockholder Voting Agreement effective as of the date first written above.

**Cimarex:**

Cimarex Energy Co.

By: /s/ PAUL KORUS

---

Name: Paul Korus  
Title: Vice President and CFO

**Stockholders:**

/s/ GARY C. EVANS

---

Gary C. Evans

Jacquelyn Evelyn Enterprises, Inc.

By: /s/ GARY C. EVANS

---

Name: Gary C. Evans  
Title: Secretary

E-6

---

**Annex F**

**Rights of Dissenting Owners**

**NRS 92A.300 Definitions.** As used in NRS 92A.300 to 92A.500, inclusive, unless the context otherwise requires, the words and terms defined in NRS 92A.305 to 92A.335, inclusive, have the meanings ascribed to them in those sections.

(Added to NRS by 1995, 2086)

**NRS 92A.305 "Beneficial stockholder" defined.** "Beneficial stockholder" means a person who is a beneficial owner of shares held in a voting trust or by a nominee as the stockholder of record.

(Added to NRS by 1995, 2087)

**NRS 92A.310 "Corporate action" defined.** "Corporate action" means the action of a domestic corporation.

(Added to NRS by 1995, 2087)

**NRS 92A.315 "Dissenter" defined.** "Dissenter" means a stockholder who is entitled to dissent from a domestic corporation's action under NRS 92A.380 and who exercises that right when and in the manner required by NRS 92A.400 to 92A.480, inclusive.

(Added to NRS by 1995, 2087; A 1999, 1631)

**NRS 92A.320 "Fair value" defined.** "Fair value," with respect to a dissenter's shares, means the value of the shares immediately before the effectuation of the corporate action to which he objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable.

(Added to NRS by 1995, 2087)

**NRS 92A.325 "Stockholder" defined.** "Stockholder" means a stockholder of record or a beneficial stockholder of a domestic corporation.

(Added to NRS by 1995, 2087)

**NRS 92A.330 "Stockholder of record" defined.** "Stockholder of record" means the person in whose name shares are registered in the records of a domestic corporation or the beneficial owner of shares to the extent of the rights granted by a nominee's certificate on file with the domestic corporation.

(Added to NRS by 1995, 2087)

**NRS 92A.335 "Subject corporation" defined.** "Subject corporation" means the domestic corporation which is the issuer of the shares held by a dissenter before the corporate action creating the dissenter's rights becomes effective or the surviving or acquiring entity of that issuer after the corporate action becomes effective.

(Added to NRS by 1995, 2087)

**NRS 92A.340 Computation of interest.** Interest payable pursuant to NRS 92A.300 to 92A.500, inclusive, must be computed from the effective date of the action until the date of payment, at the average rate currently paid by the entity on its principal bank loans or, if it has no bank loans, at a rate that is fair and equitable under all of the circumstances.

(Added to NRS by 1995, 2087)

**NRS 92A.350 Rights of dissenting partner of domestic limited partnership.** A partnership agreement of a domestic limited partnership or, unless otherwise provided in the partnership agreement, an agreement of merger or exchange, may provide that contractual rights with respect to the partnership interest of a dissenting general or limited partner of a domestic limited partnership are available for any class or group of partnership interests in connection with any merger or exchange in which the domestic limited partnership is a constituent entity.

(Added to NRS by 1995, 2088)

**NRS 92A.360 Rights of dissenting member of domestic limited-liability company.** The articles of organization or operating agreement of a domestic limited-liability company or, unless otherwise provided in the articles of organization or operating agreement, an agreement of merger or exchange, may provide that contractual rights with respect to the interest of a dissenting member are available in connection with any merger or exchange in which the domestic limited-liability company is a constituent entity.

(Added to NRS by 1995, 2088)

**NRS 92A.370 Rights of dissenting member of domestic nonprofit corporation.**

1. Except as otherwise provided in subsection 2, and unless otherwise provided in the articles or bylaws, any member of any constituent domestic nonprofit corporation who voted against the merger may, without advance notice, but within 30 days after the effective date of the merger, resign from membership and is thereby excused from all contractual obligations to the constituent or surviving corporations which did not occur before his resignation and is thereby entitled to those rights, if any, which would have existed if there had been no merger and the membership had been terminated or the member had been expelled.

2. Unless otherwise provided in its articles of incorporation or bylaws, no member of a domestic nonprofit corporation, including, but not limited to, a cooperative corporation, which supplies services described in chapter 704 of NRS to its members only, and no person who is a member of a domestic nonprofit corporation as a condition of or by reason of the ownership of an interest in real property, may resign and dissent pursuant to subsection 1.

(Added to NRS by 1995, 2088)

**NRS 92A.380 Right of stockholder to dissent from certain corporate actions and to obtain payment for shares.**

1. Except as otherwise provided in NRS 92A.370 and 92A.390, any stockholder is entitled to dissent from, and obtain payment of the fair value of his shares in the event of any of the following corporate actions:

(a) Consummation of a conversion or plan of merger to which the domestic corporation is a constituent entity:

(1) If approval by the stockholders is required for the conversion or merger by NRS 92A.120 to 92A.160, inclusive, or the articles of incorporation, regardless of whether the stockholder is entitled to vote on the conversion or plan of merger; or

(2) If the domestic corporation is a subsidiary and is merged with its parent pursuant to NRS 92A.180.

(b) Consummation of a plan of exchange to which the domestic corporation is a constituent entity as the corporation whose subject owner's interests will be acquired, if his shares are to be acquired in the plan of exchange.

## Edgar Filing: O'Neill Andrew J - Form 4

(c) Any corporate action taken pursuant to a vote of the stockholders to the extent that the articles of incorporation, bylaws or a resolution of the board of directors provides that voting or nonvoting stockholders are entitled to dissent and obtain payment for their shares.

2. A stockholder who is entitled to dissent and obtain payment pursuant to NRS 92A.300 to 92A.500, inclusive, may not challenge the corporate action creating his entitlement unless the action is unlawful or fraudulent with respect to him or the domestic corporation.

(Added to NRS by 1995, 2087; A 2001, 1414, 3199; 2003, 3189)

### **NRS 92A.390 Limitations on right of dissent: Stockholders of certain classes or series; action of stockholders not required for plan of merger.**

1. There is no right of dissent with respect to a plan of merger or exchange in favor of stockholders of any class or series which, at the record date fixed to determine the stockholders entitled to receive notice of and to vote at the meeting at which the plan of merger or exchange is to be acted on, were either listed on a national securities exchange, included in the national market system by the National Association of Securities Dealers, Inc., or held by at least 2,000 stockholders of record, unless:

- (a) The articles of incorporation of the corporation issuing the shares provide otherwise; or
- (b) The holders of the class or series are required under the plan of merger or exchange to accept for the shares anything except:
  - (1) Cash, owner's interests or owner's interests and cash in lieu of fractional owner's interests of:
    - (I) The surviving or acquiring entity; or
    - (II) Any other entity which, at the effective date of the plan of merger or exchange, were either listed on a national securities exchange, included in the national market system by the National Association of Securities Dealers, Inc., or held of record by at least 2,000 holders of owner's interests of record; or
  - (2) A combination of cash and owner's interests of the kind described in sub-subparagraphs (I) and (II) of subparagraph (1) of paragraph (b).

2. There is no right of dissent for any holders of stock of the surviving domestic corporation if the plan of merger does not require action of the stockholders of the surviving domestic corporation under NRS 92A.130.

(Added to NRS by 1995, 2088)

### **NRS 92A.400 Limitations on right of dissent: Assertion as to portions only to shares registered to stockholder; assertion by beneficial stockholder.**

1. A stockholder of record may assert dissenter's rights as to fewer than all of the shares registered in his name only if he dissents with respect to all shares beneficially owned by any one person and notifies the subject corporation in writing of the name and address of each person on whose behalf he asserts dissenter's rights. The rights of a partial dissenter under this subsection are determined as if the shares as to which he dissents and his other shares were registered in the names of different stockholders.

2. A beneficial stockholder may assert dissenter's rights as to shares held on his behalf only if:

- (a) He submits to the subject corporation the written consent of the stockholder of record to the dissent not later than the time the beneficial stockholder asserts dissenter's rights; and

- (b) He does so with respect to all shares of which he is the beneficial stockholder or over which he has power to direct the vote.

(Added to NRS by 1995, 2089)

**NRS 92A.410 Notification of stockholders regarding right of dissent.**

1. If a proposed corporate action creating dissenters' rights is submitted to a vote at a stockholders' meeting, the notice of the meeting must state that stockholders are or may be entitled to assert dissenters' rights under NRS 92A.300 to 92A.500, inclusive, and be accompanied by a copy of those sections.

2. If the corporate action creating dissenters' rights is taken by written consent of the stockholders or without a vote of the stockholders, the domestic corporation shall notify in writing all stockholders entitled to assert dissenters' rights that the action was taken and send them the dissenter's notice described in NRS 92A.430.

(Added to NRS by 1995, 2089; A 1997, 730)

**NRS 92A.420 Prerequisites to demand for payment for shares.**

1. If a proposed corporate action creating dissenters' rights is submitted to a vote at a stockholders' meeting, a stockholder who wishes to assert dissenter's rights:

(a) Must deliver to the subject corporation, before the vote is taken, written notice of his intent to demand payment for his shares if the proposed action is effectuated; and

(b) Must not vote his shares in favor of the proposed action.

2. A stockholder who does not satisfy the requirements of subsection 1 and NRS 92A.400 is not entitled to payment for his shares under this chapter.

(Added to NRS by 1995, 2089; 1999, 1631)

**NRS 92A.430 Dissenter's notice: Delivery to stockholders entitled to assert rights; contents.**

1. If a proposed corporate action creating dissenters' rights is authorized at a stockholders' meeting, the subject corporation shall deliver a written dissenter's notice to all stockholders who satisfied the requirements to assert those rights.

2. The dissenter's notice must be sent no later than 10 days after the effectuation of the corporate action, and must:

(a) State where the demand for payment must be sent and where and when certificates, if any, for shares must be deposited;

(b) Inform the holders of shares not represented by certificates to what extent the transfer of the shares will be restricted after the demand for payment is received;

(c) Supply a form for demanding payment that includes the date of the first announcement to the news media or to the stockholders of the terms of the proposed action and requires that the person asserting dissenter's rights certify whether or not he acquired beneficial ownership of the shares before that date;

(d) Set a date by which the subject corporation must receive the demand for payment, which may not be less than 30 nor more than 60 days after the date the notice is delivered; and

(e) Be accompanied by a copy of NRS 92A.300 to 92A.500, inclusive.

(Added to NRS by 1995, 2089)

**NRS 92A.440 Demand for payment and deposit of certificates; retention of rights of stockholder.**

1. A stockholder to whom a dissenter's notice is sent must:

(a) Demand payment;

(b) Certify whether he or the beneficial owner on whose behalf he is dissenting, as the case may be, acquired beneficial ownership of the shares before the date required to be set forth in the dissenter's notice for this certification; and

(c) Deposit his certificates, if any, in accordance with the terms of the notice.

2. The stockholder who demands payment and deposits his certificates, if any, before the proposed corporate action is taken retains all other rights of a stockholder until those rights are cancelled or modified by the taking of the proposed corporate action.

3. The stockholder who does not demand payment or deposit his certificates where required, each by the date set forth in the dissenter's notice, is not entitled to payment for his shares under this chapter.

(Added to NRS by 1995, 2090; A 1997, 730; 2003, 3189)

**NRS 92A.450 Uncertificated shares: Authority to restrict transfer after demand for payment; retention of rights of stockholder.**

1. The subject corporation may restrict the transfer of shares not represented by a certificate from the date the demand for their payment is received.

2. The person for whom dissenter's rights are asserted as to shares not represented by a certificate retains all other rights of a stockholder until those rights are cancelled or modified by the taking of the proposed corporate action.

(Added to NRS by 1995, 2090)

**NRS 92A.460 Payment for shares: General requirements.**

1. Except as otherwise provided in NRS 92A.470, within 30 days after receipt of a demand for payment, the subject corporation shall pay each dissenter who complied with NRS 92A.440 the amount the subject corporation estimates to be the fair value of his shares, plus accrued interest. The obligation of the subject corporation under this subsection may be enforced by the district court:

(a) Of the county where the corporation's registered office is located; or

(b) At the election of any dissenter residing or having its registered office in this state, of the county where the dissenter resides or has its registered office. The court shall dispose of the complaint promptly.

2. The payment must be accompanied by:

(a) The subject corporation's balance sheet as of the end of a fiscal year ending not more than 16 months before the date of payment, a statement of income for that year, a statement of changes in the stockholders' equity for that year and the latest available interim financial statements, if any;

(b) A statement of the subject corporation's estimate of the fair value of the shares;

(c) An explanation of how the interest was calculated;

(d) A statement of the dissenter's rights to demand payment under NRS 92A.480; and

(e) A copy of NRS 92A.300 to 92A.500, inclusive.

(Added to NRS by 1995, 2090)

**NRS 92A.470 Payment for shares: Shares acquired on or after date of dissenter's notice.**

1. A subject corporation may elect to withhold payment from a dissenter unless he was the beneficial owner of the shares before the date set forth in the dissenter's notice as the date of the first announcement to the news media or to the stockholders of the terms of the proposed action.

2. To the extent the subject corporation elects to withhold payment, after taking the proposed action, it shall estimate the fair value of the shares, plus accrued interest, and shall offer to pay this amount to each dissenter who agrees to accept it in full satisfaction of his demand. The subject corporation shall send with its offer a statement of its estimate of the fair value of the shares, an explanation of how the interest was calculated, and a statement of the dissenters' right to demand payment pursuant to NRS 92A.480.

(Added to NRS by 1995, 2091)

**NRS 92A.480 Dissenter's estimate of fair value: Notification of subject corporation; demand for payment of estimate.**

1. A dissenter may notify the subject corporation in writing of his own estimate of the fair value of his shares and the amount of interest due, and demand payment of his estimate, less any payment pursuant to NRS 92A.460, or reject the offer pursuant to NRS 92A.470 and demand payment of the fair value of his shares and interest due, if he believes that the amount paid pursuant to NRS 92A.460 or offered pursuant to NRS 92A.470 is less than the fair value of his shares or that the interest due is incorrectly calculated.

2. A dissenter waives his right to demand payment pursuant to this section unless he notifies the subject corporation of his demand in writing within 30 days after the subject corporation made or offered payment for his shares.

(Added to NRS by 1995, 2091)

**NRS 92A.490 Legal proceeding to determine fair value: Duties of subject corporation; powers of court; rights of dissenter.**

1. If a demand for payment remains unsettled, the subject corporation shall commence a proceeding within 60 days after receiving the demand and petition the court to determine the fair value of the shares and accrued interest. If the subject corporation does not commence the proceeding within the 60-day period, it shall pay each dissenter whose demand remains unsettled the amount demanded.

2. A subject corporation shall commence the proceeding in the district court of the county where its registered office is located. If the subject corporation is a foreign entity without a resident agent in the state, it shall commence the proceeding in the county where the registered office of the domestic corporation merged with or whose shares were acquired by the foreign entity was located.

3. The subject corporation shall make all dissenters, whether or not residents of Nevada, whose demands remain unsettled, parties to the proceeding as in an action against their shares. All parties must be served with a copy of the petition. Nonresidents may be served by registered or certified mail or by publication as provided by law.

4. The jurisdiction of the court in which the proceeding is commenced under subsection 2 is plenary and exclusive. The court may appoint one or more persons as appraisers to receive evidence and recommend a decision on the question of fair value. The appraisers have the powers described in the order appointing them, or any amendment thereto. The dissenters are entitled to the same discovery rights as parties in other civil proceedings.

5. Each dissenter who is made a party to the proceeding is entitled to a judgment:
- (a) For the amount, if any, by which the court finds the fair value of his shares, plus interest, exceeds the amount paid by the subject corporation; or
  - (b) For the fair value, plus accrued interest, of his after-acquired shares for which the subject corporation elected to withhold payment pursuant to NRS 92A.470.

(Added to NRS by 1995, 2091)

**NRS 92A.500 Legal proceeding to determine fair value: Assessment of costs and fees.**

1. The court in a proceeding to determine fair value shall determine all of the costs of the proceeding, including the reasonable compensation and expenses of any appraisers appointed by the court. The court shall assess the costs against the subject corporation, except that the court may assess costs against all or some of the dissenters, in amounts the court finds equitable, to the extent the court finds the dissenters acted arbitrarily, vexatiously or not in good faith in demanding payment.

2. The court may also assess the fees and expenses of the counsel and experts for the respective parties, in amounts the court finds equitable:

(a) Against the subject corporation and in favor of all dissenters if the court finds the subject corporation did not substantially comply with the requirements of NRS 92A.300 to 92A.500, inclusive; or

(b) Against either the subject corporation or a dissenter in favor of any other party, if the court finds that the party against whom the fees and expenses are assessed acted arbitrarily, vexatiously or not in good faith with respect to the rights provided by NRS 92A.300 to 92A.500, inclusive.

3. If the court finds that the services of counsel for any dissenter were of substantial benefit to other dissenters similarly situated, and that the fees for those services should not be assessed against the subject corporation, the court may award to those counsel reasonable fees to be paid out of the amounts awarded to the dissenters who were benefited.

4. In a proceeding commenced pursuant to NRS 92A.460, the court may assess the costs against the subject corporation, except that the court may assess costs against all or some of the dissenters who are parties to the proceeding, in amounts the court finds equitable, to the extent the court finds that such parties did not act in good faith in instituting the proceeding.

5. This section does not preclude any party in a proceeding commenced pursuant to NRS 92A.460 or 92A.490 from applying the provisions of N.R.C.P. 68 or NRS 17.115.

(Added to NRS by 1995, 2092)

**Annex G**

**FORM OF AMENDMENT TO  
CIMAREX ENERGY CO.  
2002 STOCK INCENTIVE PLAN**

Cimarex Energy Co., a Delaware corporation (the "Company"), established the Cimarex Energy Co. 2002 Stock Incentive Plan (the "Plan"), effective as of October 1, 2002, and amended the Plan, effective as of March 3, 2003. The Company wishes to amend the Plan as provided below.

***Recitals***

A. The Plan provides for the grant of equity-based compensation awards, including stock options, restricted stock, and stock units. The Company has granted stock options, restricted, stock, and stock units that are subject to vesting and that, as of the date of this Amendment, have not vested and have not become payable.

B. Section 10.4 of the Plan provides that outstanding awards under the Plan will become fully vested and payable or freely transferable upon the occurrence of a "Change in Control Event" as defined in Section 2.5 of the Plan. The award agreements, including stock options, restricted stock and stock units have incorporated by reference the definition of "Change in Control Event" set forth in Section 2.5 of the Plan.

C. The Company has entered into an Agreement and Plan of Merger (the "Merger Agreement") among the Company, a wholly-owned subsidiary of the Company, and Magnum Hunter Resources, Inc. ("MHR") pursuant to which MHR will become a wholly-owned subsidiary of the Company (the "Transaction"). Pursuant to the Merger Agreement and following the closing of the Transaction, the present stockholders of the Company will own approximately 55% of the Company and it is expected that the current management of the Company will continue to manage the Company.

D. In as much as the current stockholders of the Company will continue to own approximately 55% of the Company and it is expected that the current management of the Company will continue to manage the Company, the Company does not believe that (1) the Transaction will result in a change in the actual operational control of the Company and (2) it was ever intended that a transaction like the Transaction would result in accelerated vesting of stock options granted under the Plan, the accelerated vesting and payout of stock units granted under the Plan, or the accelerated vesting and free transferability of restricted stock granted under the Plan.

E. Section 10.1 provides that the Company's Board of Directors can amend the Plan at any time. Section 10.5 provides that the Company may amend outstanding awards under the Plan; provided that if the amendment is adverse to the holder of the award, the amendment will not be effective without the holder's consent.

F. Some of the holders of the outstanding options, units and restricted stock have waived any rights they may have to accelerated vesting of their options, accelerated vesting and payment of their units, or accelerated vesting and free transferability of their restricted stock if the Transaction closes and have consented to the amendment of the definition of "Change in Control Event" to provide that the Transaction will not be deemed to be a Change in Control Event.

G. As a part of the consideration for the waivers and consents given by the holders of options, units and restricted stock, the Company has agreed to amend the option agreements, unit agreements and restricted stock agreements to provide for full vesting of the options, full vesting and payment of units and full vesting and free transferability of restricted stock if the holder dies or terminates employment on account of "disability" as defined in the Plan. A recent change in the law has changed the definition of "disability" that applies for these purposes. The Company wishes to amend the

definition of "disability" to comply with the change in the law and some of the holders of option, units and restricted stock have consented to the amendment.

H. The Company's Board of Directors has determined that it is in the best interests of the Company to increase the number of shares authorized for issuance under the Plan.

***Amendment***

1. Section 1.3 shall be amended in its entirety as follows:

**SECTION 1.3 *Shares Subject to the Plan.*** Subject to the limitations set forth in the Plan, the number of shares of common stock reserved for Awards under the Plan is increased from seven million (7,000,000) to twelve million seven hundred thousand (12,700,000).

2. Section 2.1 shall be amended by the addition of a new subsection (v) at the end to provide as follows:

(v) Notwithstanding the foregoing, the closing of the transaction contemplated by the Agreement and Plan of Merger among the Company, a wholly-owned subsidiary of the Company, and Magnum Hunter Resources, Inc. (the "Transaction") shall not be deemed to be a "Change in Control Event" for purposes of Section 10.4 of this Plan.

3. Section 4.1 shall be amended in its entirety to provide as follows:

**SECTION 4.1 *Committee to Grant Awards.*** The Committee may, from time to time, grant Awards to one or more Participants, provided, however, that:

(i) Subject to Article IX, the aggregate number of shares of Common Stock made subject to the Award of Options to any Participant in any calendar year may not exceed one million (1,000,000).

(ii) Subject to Article IX, in no event shall more than one million (1,000,000) (14%) of the seven million (7,000,000) shares initially subject to the Plan be awarded to Participants as Restricted Stock Awards. Up to one-half of the five million seven hundred thousand (5,700,000) shares added to the Plan upon approval of the stockholders at the meeting held on \_\_\_\_\_, 2005, may be awarded to Participants as Restricted Stock Awards. The limits referred to in this Section 4.1(ii) shall be referred to as the Restricted Stock Award Limit.

(iii) Any shares of Common Stock related to Awards that terminate by expiration, forfeiture, cancellation or otherwise without the issuance of shares of Common Stock or are exchanged in the Committee's discretion for Awards not involving Common Stock, and any shares of Common Stock withheld for the payment of taxes pursuant to Section 9.3 or received by the Company as payment of the exercise price of an Option shall be available again for grant under the Plan; provided, however, that no more than twelve million seven hundred thousand (12,700,000) shares of Common Stock may be issued under Incentive Stock Options. Notwithstanding the foregoing, with respect to the five million seven hundred thousand (5,700,000) shares (the "2005 Additional Share Reserve") added upon approval of the stockholders at the meeting held on \_\_\_\_\_, 2005, a grant of one share as a Restricted Stock Award or a Stock Unit shall reduce the 2005 Additional Share Reserve by two shares and a grant of one share pursuant to an Option shall reduce the 2005 Additional Share Reserve by one share.

(iv) Common Stock delivered by the Company in payment of any Award under the Plan may be authorized and unissued Common Stock or Common Stock held in the treasury of the Company.

Edgar Filing: O'Neill Andrew J - Form 4

(v) The Committee shall, in its sole discretion, determine the manner in which fractional shares arising under the Plan shall be treated.

(vi) Separate certificates representing Common Stock delivered to a Participant upon the exercise of any Option will be issued to such Participant.

4. Section 10.2 shall be amended by the deletion of the parenthetical in the first sentence that reads "(as defined in Section 22(e) of the Code)" and by the addition of the following at the end:

The Grantee shall be disabled if the Grantee

(i) is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, or

(ii) is, by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, receiving income replacement benefits for a period of not less than 3 months under an accident and health plan covering employees of the Company.

5. The Amendments in section 2 and section 4 shall be effective only if the Transaction closes.

6. The Amendments in section 2 and section 4 shall apply only to Participants who have consented to the amendments to the Plan by executing and not revoking a written waiver and amendment or other agreement with the Company.

7. The Amendments in section 1 and section 3 shall become effective upon approval by the Company's stockholders at the meeting scheduled for \_\_\_\_\_, 2005.

IN WITNESS WHEREOF, this Amendment has been signed this \_\_\_\_\_ day of \_\_\_\_\_, 2005 to be effective as provided above.

**CIMAREX ENERGY CO.**

By: \_\_\_\_\_

Name: F. H. Merelli

Title: Chief Executive Officer and President

G-3

---