

## **The Form 5 LLC Operating Agreement (and related agreements)**

In 2007, Alex Ritchie, Jim Cress and Paul Smith presented a paper at the Rocky Mountain Mineral Law Foundation Annual Institute in Vancouver, British Columbia, called “Form 5 LLC: A Modest Proposal for a Limited Liability Company Agreement Based on Form 5” (the “Modest Proposal”). In that presentation, the authors argued that the Rocky Mountain Mineral Law Foundation’s (the “Foundation”) then existing forms of limited liability company operating agreement and member’s agreement (Form 5A LLC) contained several features that made them less user-friendly than they could be, and that did not reflect the current flexibility offered by the Delaware limited liability statute or the evolution of LLC law and practice. As a result of those and other issues, Form 5A LLC has not been widely used in the mining industry.

Messrs. Ritchie, Cress and Smith proposed in their paper that the Foundation create an updated form of LLC Operating Agreement for use by parties interested in the joint exploration, development and mining of a property, and the Foundation is in the process of doing just that. The Foundation’s Form 5 LLC Committee (the “Committee”), charged with preparing a new form of LLC Operating Agreement to replace Form 5A LLC, includes Alex Ritchie, Jim Cress, Steve Hull, Tom Erwin, Sarah Strunk, Bruce Kirchhoff and Randy Hubbard (addressing mining, LLC and general legal issues), and John Maxfield, Larry Nemirow, Tom Kelly, Doug Scheetz, Noah Baer and Paul Smith (addressing tax issues).

The draft agreements remain a work in progress. The Committee will be making a panel presentation on the status of the various draft agreements at the Rocky Mountain Mineral Law Foundation’s Annual Institute in Banff, Alberta, Canada on July 24, 2010 (the “Institute”). At that presentation, the Committee would like to receive as many questions and comments as possible from practitioners in the audience. The Foundation and the Committee are soliciting comments and questions on those drafts both at this year’s Annual Institute and through written submissions, which we ask be made to the Foundation at [info@rmmlf.org](mailto:info@rmmlf.org) by the end of September of this year. In order to facilitate questions and comments on the draft agreements at this year’s Annual Institute, the Foundation and the Committee have made them available on the website for review in advance of the Institute. The goal of the Foundation and the Committee is to then have the forms finalized by the end of calendar year 2010.

The Committee at this point has decided on an approach based on flexibility. Instead of dictating one transaction structure over another that may never become more widely accepted, the Committee is proposing two different approaches, and will develop five separate documents for use by practitioners. One approach, for parties that are comfortable with the LLC form and willing to incur the negotiation costs up front, is to enter into the LLC Operating Agreement at the start of the exploration/earn-in phase. The other approach is to cover the exploration/earn-in phase with an Exploration Agreement, and to enter into the LLC Operating Agreement only on completion of the earn-in. The documents to be developed by the Committee for the different possible transaction structures are as follows:

- (i) an LLC Operating Agreement to be entered into at the very beginning of the exploration/earn-in phase of a project, for parties that are comfortable with the LLC form and willing to incur the negotiation costs up-front;
- (ii) an LLC Operating Agreement that would not be entered into until after YCO (the funding party) has spent 100% of the exploration dollars required to earn its percentage interest in the project;
- (iii) an Exploration Agreement to cover the earn-in period prior to entering into the LLC Operating Agreement described in item (ii) above;
- (iv) a Contribution Agreement by which the properties and other assets comprising a project would be conveyed by XCO (or XCO and YCO) to the LLC whose activities then would be governed by the LLC Operating Agreement; and
- (v) a set of Alternate Provisions, most derived from Form 5A, that have been used in some contexts but (based entirely on the subjective experience of the Committee) may not be as widely used as the provisions in the base form of LLC Operating Agreement.

Drafts of the agreements described in items (i), (iii), (iv) and (v) above (along with forms of Exhibits for the Accounting Procedure, Tax Matters and Net Proceeds for use in connection with the above forms) are now posted for review on this website. A draft of the agreement described in item (ii) above will be posted on that website by the end of August. As with all of the Rocky Mountain Mineral Law Foundation's forms, practitioners and others should pay close heed to the warning at the beginning of each document that the forms are not meant to simply be taken off the shelf and used once the various blanks are filled in, but rather are intended to be guides for negotiation. That is particularly true with respect to these drafts of the Form 5 LLC agreements, which are not yet finished products and have been made available solely for the purpose of soliciting questions and comments.

For those of you who decide to submit questions or comments, we very much appreciate the input.