

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

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FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 1998

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES ACT OF  
1934

FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NO. 1-13726

CHESAPEAKE ENERGY CORPORATION  
(Exact name of registrant as specified in its charter)

OKLAHOMA  
(State or other jurisdiction of  
incorporation or organization)

73-1395733  
(I.R.S. Employer  
Identification No.)

6100 NORTH WESTERN AVENUE  
OKLAHOMA CITY, OKLAHOMA  
(Address of principal executive offices)

73118  
(Zip Code)

(405) 848-8000  
(Registrant's telephone number, including area code)

-----  
Indicate by check mark whether the registrant (1) has filed all reports  
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of  
1934 during the preceding 12 months (or for such shorter period that the  
registrant was required to file such reports), and (2) has been subject to such  
filing requirements for the past 90 days.

YES  NO

At October 30, 1998, there were 96,710,450 shares of the registrant's \$.01  
par value Common Stock outstanding.

=====

CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES  
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## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

	SEPTEMBER 30, 1998	DECEMBER 31, 1997
	-----	-----
	(UNAUDITED)	
	(\$ IN THOUSANDS)	
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents .....	\$ 20,749	\$ 123,860
Restricted cash .....	4,200	--
Short-term investments .....	--	12,570
Accounts receivable:		
Oil and gas sales .....	11,524	10,654
Oil and gas marketing sales .....	23,120	20,493
Joint interest and other, net of allowance for doubtful accounts of \$1,209,000 and \$691,000.....	30,183	38,781
Related parties .....	16,568	4,246
Inventory .....	6,327	5,493
Other .....	4,618	1,624
	-----	-----
Total current assets .....	117,289	217,721
	-----	-----
PROPERTY AND EQUIPMENT:		
Oil and gas properties, at cost based on full-cost accounting:		
Evaluated oil and gas properties .....	2,054,907	1,095,363
Unevaluated properties .....	92,083	125,155
Less: accumulated depreciation, depletion and amortization.....	(1,176,946)	(602,391)
	-----	-----
Other property and equipment .....	970,044	618,127
Less: accumulated depreciation and amortization .....	78,974	67,633
	(20,537)	(6,573)
	-----	-----
Total property and equipment .....	1,028,481	679,187
	-----	-----
OTHER ASSETS .....	81,504	55,876
	-----	-----
TOTAL ASSETS .....	\$ 1,227,274	\$ 952,784
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable .....	\$ 43,150	\$ 81,775
Accrued liabilities and other .....	55,505	42,733
Revenues and royalties due others .....	20,645	28,972
	-----	-----
Total current liabilities .....	119,300	153,480
	-----	-----
LONG-TERM DEBT, NET .....	919,055	508,992
	-----	-----
REVENUES AND ROYALTIES DUE OTHERS .....	12,524	10,106
	-----	-----
STOCKHOLDERS' EQUITY:		
Preferred stock, \$.01 par value, 10,000,000 shares authorized; 4,600,000 and 0 shares of 7% cumulative convertible stock issued and outstanding at September 30, 1998 and December 31, 1997, respectively, entitled in liquidation to \$230 million.....	230,000	--
Common stock, \$.01 par value, 250,000,000 shares authorized; 96,702,650 and 74,298,061 shares issued and outstanding at..... September 30, 1998 and December 31, 1997, respectively	967	743
Paid-in capital .....	677,453	460,733
Accumulated deficit .....	(702,063)	(181,270)
Less: treasury stock, at cost; 8,503,300 and 0 shares at September 30, 1998 and December 31, 1997, respectively.....	(29,962)	--
	-----	-----
Total stockholders' equity .....	176,395	280,206
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY .....	\$ 1,227,274	\$ 952,784
	=====	=====

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

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	1998	1997	1998	1997
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
<b>REVENUES:</b>				
Oil and gas sales .....	\$ 70,082	\$ 45,667	\$ 195,962	\$ 148,420
Oil and gas marketing sales .....	36,256	26,865	96,451	73,018
Interest and other .....	778	5,878	3,573	14,585
Total revenues .....	107,116	78,410	295,986	236,023
<b>COSTS AND EXPENSES:</b>				
Production expenses .....	14,208	3,894	36,775	11,071
Production taxes .....	1,976	1,286	6,141	3,342
Oil and gas marketing expenses .....	34,720	26,690	94,686	72,282
Impairment of oil and gas properties .....	--	--	466,000	236,000
Impairment of other assets .....	--	--	10,000	--
Oil and gas depreciation, depletion and amortization .....	34,069	28,550	109,311	95,571
Depreciation and amortization of other assets .....	2,518	1,142	5,820	3,088
General and administrative .....	5,197	2,760	14,711	7,823
Interest .....	18,577	8,575	47,930	20,909
Total costs and expenses .....	111,265	72,897	791,374	450,086
INCOME (LOSS) BEFORE INCOME TAX AND EXTRAORDINARY ITEM .....	(4,149)	5,513	(495,388)	(214,063)
INCOME TAX BENEFIT .....	--	--	--	(17,898)
INCOME (LOSS) BEFORE EXTRAORDINARY ITEM .....	(4,149)	5,513	(495,388)	(196,165)
EXTRAORDINARY ITEM:				
Loss on early extinguishment of debt .....	--	--	(13,334)	(177)
NET INCOME (LOSS) .....	(4,149)	5,513	(508,722)	(196,342)
PREFERRED STOCK DIVIDENDS .....	(4,026)	--	(8,051)	--
NET INCOME (LOSS) AVAILABLE TO COMMON SHAREHOLDERS .....	\$ (8,175)	\$ 5,513	\$ (516,773)	\$ (196,342)
<b>EARNINGS PER COMMON SHARE (BASIC AND ASSUMING DILUTION)</b>				
Income (loss) before extraordinary item .....	\$ (0.08)	\$ 0.08	\$ (5.34)	\$ (2.79)
Extraordinary item .....	--	--	(0.14)	--
Net income (loss) .....	\$ (0.08)	\$ 0.08	\$ (5.48)	\$ (2.79)
<b>WEIGHTED AVERAGE COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING</b>				
Basic .....	98,046	70,376	94,355	70,376
Assuming dilution .....	98,046	72,699	94,355	70,376

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

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1998	1997
	----- (\$ IN THOUSANDS)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss .....	\$(508,722)	\$(196,342)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation, depletion and amortization .....	113,449	97,571
Impairment of oil and gas assets .....	466,000	236,000
Impairment of other assets .....	10,000	--
Deferred taxes .....	--	(17,898)
Amortization of loan costs .....	1,682	1,088
Amortization of bond discount .....	77	46
Gain on sale of fixed assets and other .....	(142)	(3,766)
Extraordinary loss .....	13,334	177
Equity in (earnings) losses of equity investees .....	487	(181)
Bad debt expense .....	516	324
	-----	-----
Cash provided by operating activities before changes in current assets and liabilities .....	96,681	117,019
Changes in current assets and liabilities .....	(43,358)	(32,207)
	-----	-----
Cash provided by operating activities .....	53,323	84,812
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Exploration, development and acquisition of oil and gas properties .....	(478,394)	(380,804)
Investment in preferred stock of Gothic Energy Corporation .....	(39,500)	--
Proceeds from sale of assets .....	6,714	1,190
Additions to other property and equipment .....	(9,771)	(40,605)
Long-term loans made to third parties .....	--	(20,000)
Repayment of long-term loan .....	2,000	--
Other investments .....	--	(13,751)
	-----	-----
Cash used in investing activities .....	(518,951)	(453,970)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term borrowings .....	658,750	292,626
Payments on long-term borrowings .....	(474,166)	(12,750)
Proceeds from issuance of preferred stock .....	222,760	--
Purchase of treasury stock .....	(29,962)	--
Dividends paid on common stock .....	(5,592)	(1,405)
Dividends paid on preferred stock .....	(4,025)	--
Cash received from exercise of stock options .....	131	1,340
Other financing .....	--	(210)
	-----	-----
Cash provided by financing activities .....	367,896	279,601
	-----	-----
EFFECT OF EXCHANGE RATE CHANGES ON CASH .....	(5,379)	--
	-----	-----
NET DECREASE IN CASH AND CASH EQUIVALENTS .....	(103,111)	(89,557)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD .....	123,860	140,739
	-----	-----
CASH AND CASH EQUIVALENTS, END OF PERIOD .....	\$ 20,749	\$ 51,182
	=====	=====

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

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

## 1. ACCOUNTING PRINCIPLES

The accompanying unaudited consolidated financial statements of Chesapeake Energy Corporation and subsidiaries (the "Company") have been prepared in accordance with the instructions to Form 10-Q as prescribed by the Securities and Exchange Commission. All material adjustments (consisting solely of normal recurring adjustments) which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods have been reflected. The results for the three and nine months ended September 30, 1998 are not necessarily indicative of the results to be expected for the full fiscal year.

The Company changed its fiscal year end from June 30 to December 31 for the period ended December 31, 1997. This Form 10-Q relates to the three and nine months ended September 30, 1998 (the "Current Quarter" and "Current Period", respectively) and September 30, 1997 (the "Prior Quarter" and "Prior Period", respectively).

## 2. RECENT EVENTS

On July 7, 1998 the Company's Board of Directors authorized management to explore strategic alternatives to enhance shareholder value, including a possible sale or merger of the Company, based upon the Board's opinion that the market was substantially undervaluing the Company's assets and exploration potential. Also on July 7, 1998 Chesapeake's Board of Directors unanimously adopted a shareholder rights plan designed to deter coercive takeover tactics and to prevent a change of control from occurring without all shareholders receiving a fair price.

Pursuant to the decision to explore various alternatives, the Company engaged Donaldson, Lufkin & Jenrette Securities Corporation ("DLJ") to advise the Company. The Company and DLJ are presently evaluating various alternatives, including the potential sale or merger of the Company, sale of certain assets, or alternative financial strategies. This process is underway and is expected to be concluded within the next few months.

On November 2, 1998 the Company announced it had entered into an agreement to tender its 19.9% stake in Pan East Petroleum Corp. ("Pan East") to POCO Petroleum Ltd. and agreed to a property exchange with Pan East. Subject to the successful completion by POCO of its tender offer, the Company anticipates receiving approximately \$26 million in cash and increasing its net reserves by four bcfe. As of September 30, 1998, the Company's net investment in the common stock of Pan East of \$21.3 million has been accounted for using the equity method and is included in Other Assets in the accompanying Consolidated Balance Sheets.

## 3. LEGAL PROCEEDINGS

The Company and certain of its officers and directors are defendants in a consolidated class action suit alleging violations of the Securities Exchange Act of 1934. The plaintiffs assert that the defendants made material misrepresentations and failed to disclose material facts about the success of the Company's exploration efforts in the Louisiana Trend. As a result, the complaint alleges the price of the Company's common stock was artificially inflated from January 25, 1996 until June 27, 1997, when the Company issued a press release announcing disappointing drilling results in the Louisiana Trend and a full-cost ceiling writedown to be reflected in its June 30, 1997 financial statements. The plaintiffs further allege that certain of the named individual defendants sold common stock during the class period when they knew or should have known adverse nonpublic information. The plaintiffs seek a determination that the suit is a proper class action and damages in an unspecified amount, together with interest and costs of litigation, including attorneys' fees. The Company and the individual defendants believe that these claims are without merit, and intend to defend against them vigorously. No estimate of loss or range of estimate of loss, if any, can be made at this time.

A purported class action alleging violations of the Securities Act of 1933 and the Oklahoma Securities Act has been filed against the Company and others on behalf of investors who purchased common stock of Bayard Drilling Technologies, Inc. ("Bayard") in, or traceable to, its initial public offering in November 1997. Total proceeds of the

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

offering were \$254 million, of which the Company received net proceeds of \$90 million as a selling shareholder. Plaintiffs allege that the Company, a major customer of Bayard's drilling services and the owner of 30.1% of Bayard's common stock outstanding prior to the offering, was a controlling person of Bayard. Plaintiffs assert that the Bayard prospectus contained material omissions and misstatements relating to (i) the Company's financial "problems" and their impact on Bayard's operating results, (ii) increased costs associated with Bayard's growth strategy, (iii) undisclosed pending related-party transactions between Bayard and third parties other than the Company, (iv) Bayard's planned use of offering proceeds and (v) Bayard's capital expenditures and liquidity. The alleged defective disclosures are claimed to have resulted in a decline in Bayard's share price following the public offering. Plaintiffs seek a determination that the suit is a proper class action and damages in an unspecified amount or rescission, together with interest and costs of litigation, including attorneys' fees. The Company believes that the claims are without merit and intends to defend against them vigorously. No estimate of loss or range of estimate of loss, if any, can be made at this time.

In October 1996, Union Pacific Resources Company ("UPRC") sued the Company alleging infringement of a patent for a drillbit steering method. Other claims asserted by UPRC have been dismissed. UPRC's infringement claims against the Company are based on services provided to the Company by a third party vendor controlled by former UPRC employees. UPRC is seeking injunctive relief, damages of an unspecified amount, including actual and enhanced damages, interest, costs and attorneys' fees. The Company believes that it has meritorious defenses to UPRC's allegations and that the UPRC patent is invalid. The Company has filed a motion to construe UPRC's patent claims and other dispositive motions are pending. No estimate of loss or range of estimate of loss, if any, can be made at this time; however, in reports filed in the proceeding, experts for UPRC claim that damages could be as much as \$18 million while Company experts state that the amount should not exceed \$25,000, in each case based on a reasonable royalty.

The Company is currently involved in various other routine disputes incidental to its business operations. While it is not possible to determine the ultimate disposition of these matters, management, after consultation with legal counsel, is of the opinion that the final resolution of all such currently pending or threatened litigation is not likely to have a material adverse effect on the consolidated financial position or results of operations of the Company.

## 4. NET LOSS PER SHARE

In February 1997, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 128, Earnings Per Share ("SFAS 128"). SFAS 128 requires presentation of "basic" and "diluted" earnings per share, as defined, on the face of the statement of operations for all entities with complex capital structures. SFAS 128 is effective for financial statements issued for periods ending after December 15, 1997 and requires restatement of all prior period earnings per share amounts. The Company has adopted SFAS 128 and has restated all prior periods presented.

SFAS 128 requires a reconciliation of the numerators and denominators of the basic and diluted EPS computations. For the Current Quarter, the Current Period and the Prior Period, there was no difference between actual weighted average shares outstanding, which are used in computing basic EPS, and diluted weighted average shares outstanding, which are used in computing diluted EPS. Options to purchase 10.6 million and 8.5 million shares of common stock at a weighted average exercise price of \$3.88 and \$5.48 were outstanding at September 30, 1998 and 1997, respectively, but were not included in the computation of diluted EPS because the effect of these outstanding options would be antidilutive. A reconciliation for the Prior Quarter is as follows:

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

	Net Income (Numerator) (in 000's) -----	Shares Outstanding (Denominator) (in 000's) -----	Per-Share Amount -----
For the quarter ended September 30, 1997:			
Basic EPS			
Income available to common stockholders .....	\$5,513	70,376	\$0.08 =====
Effect of Dilutive Securities			
Employee stock options .....	-- -----	2,323 -----	
Diluted EPS			
Income available to common stockholders and assumed conversions .....	\$5,513 =====	72,699 =====	\$0.08 =====

## 5. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENT

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 131 "Disclosures about Segments of an Enterprise and Related Information". This Statement establishes standards for the way that public enterprises report information about operating segments in annual financial statements and requires that those enterprises report selected information about operating segments in interim financial reports issued to shareholders. The Statement is effective for annual financial statements for periods beginning after December 15, 1997 and for interim financial statements issued subsequent to adoption in the annual financial statements. The Company expects that the adoption of this standard will not impact its results of operation or financial position, but may require additional disclosures.

In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities ("FAS 133"). FAS 133 is effective for all fiscal quarters of all fiscal years beginning after June 15, 1999 (January 1, 2000 for the Company). FAS 133 requires that all derivative instruments be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether a derivative is designed as part of a hedge transaction and, if it is, the type of hedge transaction. For fair-value hedge transactions in which the Company is hedging changes in the fair value of an asset, liability, or firm commitment, changes in the fair value of the derivative instrument will generally be offset in the income statement by changes in the hedged item's fair value. For cash-flow hedge transactions, in which the Company is hedging the variability of cash flows related to a variable-rate asset, liability, or a forecasted transaction, changes in the fair value of the derivative instrument will be reported in other comprehensive income. The gains and losses on the derivative instrument that are reported in other comprehensive income will be reclassified as earnings in the periods in which earnings are impacted by the variability of the cash flows of the hedged item. The ineffective portion of all hedges will be recognized in current-period earnings.

The Company has not yet determined the impact that the adoption of FAS 133 will have on its results of operations or its financial position.

## 6. ACQUISITION OF HUGOTON

In March 1998, the Company acquired Hugoton Energy Corporation ("Hugoton") pursuant to a merger by issuing 25.8 million shares of the Company's common stock in exchange for 100% of Hugoton's common stock. The acquisition of Hugoton was accounted for using the purchase method as of March 1, 1998, and the results of operations of Hugoton have been included since that date.

The following unaudited pro forma information has been prepared assuming Hugoton had been acquired as of the beginning of the periods presented. The pro forma information is presented for information purposes only and is not necessarily indicative of what would have occurred if the acquisition had been made as of those dates. In



## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

addition, the pro forma information is not intended to be a projection of future results and does not reflect the efficiencies expected to result from the integration of Hugoton.

## Pro Forma Information (Unaudited)

	Nine Months Ended September 30, 1998	1997
	-----	-----
	(In thousands, except per share data)	
Revenues.....	\$ 305,678	\$ 294,462
Loss before extraordinary item.....	\$ (496,837)	\$ (192,285)
Net Loss.....	\$ (510,171)	\$ (192,462)
Loss before extraordinary item per common share.....	\$ (4.96)	\$ (2.00)
Net loss per common share.....	\$ (5.10)	\$ (2.00)

The Company acquired other businesses and oil and gas properties in the Current Period. The results of operations of these businesses and properties were not material in relation to the Company's consolidated results of operations.

## 7. SENIOR NOTES

## 9.125% Notes

The Company has outstanding \$120 million in aggregate principal amount of 9.125% Senior Notes which mature April 15, 2006. The 9.125% Notes bear interest at an annual rate of 9.125%, payable semiannually on each April 15 and October 15. The 9.125% Notes are senior, unsecured obligations of the Company and are fully and unconditionally guaranteed, jointly and severally, by the Guarantor Subsidiaries (as defined below).

## 7.875% Notes

The Company has outstanding \$150 million in aggregate principal amount of 7.875% Senior Notes which mature March 15, 2004. The 7.875% Notes bear interest at the rate of 7.875%, payable semiannually on each March 15 and September 15. The 7.875% Notes are senior, unsecured obligations of the Company and are fully and unconditionally guaranteed, jointly and severally, by the Guarantor Subsidiaries.

## 8.5% Notes

The Company has outstanding \$150 million in aggregate principal amount of 8.5% Senior Notes which mature March 15, 2012. The 8.5% Notes bear interest at the rate of 8.5%, payable semiannually on each March 15 and September 15. The 8.5% Notes are senior, unsecured obligations of the Company and are fully and unconditionally guaranteed, jointly and severally, by the Guarantor Subsidiaries.

## 9.625% Notes

On April 22, 1998, the Company issued \$500 million aggregate principal amount of 9.625% Senior Notes which mature May 1, 2005. The 9.625% Notes bear interest at an annual rate of 9.625%, payable semiannually on each May 1 and November 1. The 9.625% Notes are senior, unsecured obligations of the Company and are fully and unconditionally guaranteed, jointly and severally, by the Guarantor Subsidiaries.

The Company is a holding company and owns no operating assets and has no significant operations independent of its subsidiaries. The Company's obligations under its Senior Notes have been fully and unconditionally guaranteed, on a joint and several basis, by each of the Company's "Restricted Subsidiaries" (as defined in the respective indentures governing the Senior Notes) (collectively, the "Guarantor Subsidiaries"). Each of the Guarantor Subsidiaries is a direct or indirect wholly-owned subsidiary of the Company.

The Senior Note Indentures contain certain covenants, including covenants limiting the Company and the Guarantor Subsidiaries with respect to asset sales, restricted payments, the incurrence of additional indebtedness and the

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

issuance of preferred stock, liens, sale and leaseback transactions, lines of business, dividend and other payment restrictions affecting Guarantor Subsidiaries, mergers or consolidations, and transactions with affiliates. The Company is obligated to repurchase the 9.125% and 9.625% Notes in the event of a change of control or certain asset sales.

Set forth below are condensed consolidating financial statements of the Guarantor Subsidiaries, the Company's subsidiaries which are not guarantors of the Senior Notes (the "Non-Guarantor Subsidiaries") and the Company. Separate financial statements of each Guarantor Subsidiary have not been provided because management has determined that they are not material to investors.

As of and for the three and nine months ended September 30, 1998, the only Non-Guarantor Subsidiary was Chesapeake Energy Marketing, Inc. As of and for the three and nine months ended September 30, 1997, the Non-Guarantor Subsidiaries were Chesapeake Energy Marketing, Inc. and Chesapeake Canada Corporation. For the 1997 and 1998 periods, the remaining subsidiaries of the Company were Guarantor Subsidiaries.

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

## CONDENSED CONSOLIDATING BALANCE SHEET

AS OF SEPTEMBER 30, 1998  
(\$ IN THOUSANDS)

	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	COMPANY (PARENT)	ELIMINATIONS	CONSOLIDATED
	-----	-----	-----	-----	-----
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents .....	\$ (4,882)	\$ 2,981	\$ 26,850	\$ --	\$ 24,949
Short-term investments .....	--	--	--	--	--
Accounts receivable, net .....	56,930	32,746	276	(8,557)	81,395
Inventory .....	6,189	138	--	--	6,327
Other .....	4,059	43	516	--	4,618
	-----	-----	-----	-----	-----
Total Current Assets .....	62,296	35,908	27,642	(8,557)	117,289
	-----	-----	-----	-----	-----
PROPERTY AND EQUIPMENT:					
Oil and gas properties .....	2,054,907	--	--	--	2,054,907
Unevaluated leasehold .....	92,083	--	--	--	92,083
Other property and equipment .....	59,484	2,572	16,918	--	78,974
Less: accumulated depreciation, depletion and amortization .....	(1,196,120)	(85)	(1,278)	--	(1,197,483)
	-----	-----	-----	-----	-----
Total Property and Equipment .....	1,010,354	2,487	15,640	--	1,028,481
	-----	-----	-----	-----	-----
INVESTMENTS IN SUBSIDIARIES AND INTERCOMPANY ADVANCES .....					
	474,616	--	471,151	(945,767)	--
OTHER ASSETS .....	39,500	580	41,424	--	81,504
	-----	-----	-----	-----	-----
TOTAL ASSETS .....	\$ 1,586,766	\$ 38,975	\$ 555,857	\$ (954,324)	\$ 1,227,274
	=====	=====	=====	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY					
CURRENT LIABILITIES:					
Notes payable and current maturities of long-term debt .....	\$ --	\$ --	\$ --	\$ --	\$ --
Accounts payable and other .....	82,006	14,910	31,240	(8,856)	119,300
	-----	-----	-----	-----	-----
Total Current Liabilities .....	82,006	14,910	31,240	(8,856)	119,300
	-----	-----	-----	-----	-----
LONG-TERM DEBT .....	--	--	919,055	--	919,055
	-----	-----	-----	-----	-----
REVENUES PAYABLE .....	12,524	--	--	--	12,524
	-----	-----	-----	-----	-----
INTERCOMPANY PAYABLES .....	1,346,717	10,524	(1,357,540)	299	--
	-----	-----	-----	-----	-----
STOCKHOLDERS' EQUITY:					
Preferred Stock .....	--	--	230,000	--	230,000
Common Stock .....	27	1	956	(17)	967
Other .....	145,492	13,540	732,146	(945,750)	(54,572)
	-----	-----	-----	-----	-----
Total Stockholders' Equity .....	145,519	13,541	963,102	(945,767)	176,395
	-----	-----	-----	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY .....	\$ 1,586,766	\$ 38,975	\$ 555,857	\$ (954,324)	\$ 1,227,274
	=====	=====	=====	=====	=====

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)

## CONDENSED CONSOLIDATING BALANCE SHEET

AS OF DECEMBER 31, 1997  
(\$ IN THOUSANDS)

	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	COMPANY (PARENT)	ELIMINATIONS	CONSOLIDATED
	-----	-----	-----	-----	-----
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents .....	\$ (589)	\$ 13,999	\$ 110,450	\$ --	\$ 123,860
Short-term investments .....	--	--	12,570	--	12,570
Accounts receivable, net .....	57,476	22,882	1,524	(7,708)	74,174
Inventory .....	4,918	575	--	--	5,493
Other .....	1,613	1	10	--	1,624
	-----	-----	-----	-----	-----
Total Current Assets .....	63,418	37,457	124,554	(7,708)	217,721
	-----	-----	-----	-----	-----
PROPERTY AND EQUIPMENT:					
Oil and gas properties .....	1,056,118	39,245	--	--	1,095,363
Unevaluated leasehold .....	125,155	--	--	--	125,155
Other property and equipment .....	51,868	343	15,422	--	67,633
Less: accumulated depreciation, depletion and amortization .....	(593,359)	(14,650)	(955)	--	(608,964)
	-----	-----	-----	-----	-----
Total Property and Equipment .....	639,782	24,938	14,467	--	679,187
	-----	-----	-----	-----	-----
INVESTMENTS IN SUBSIDIARIES AND INTERCOMPANY ADVANCES .....					
	81,755	49,958	903,713	(1,035,426)	--
	-----	-----	-----	-----	-----
OTHER ASSETS .....					
	10,189	6,918	38,769	--	55,876
	-----	-----	-----	-----	-----
TOTAL ASSETS .....	\$ 795,144	\$ 119,271	\$ 1,081,503	\$(1,043,134)	\$ 952,784
	=====	=====	=====	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY					
CURRENT LIABILITIES:					
Notes payable and current maturities of long-term debt .....	\$ --	\$ --	\$ --	\$ --	\$ --
Accounts payable and other .....	104,259	29,649	27,280	(7,708)	153,480
	-----	-----	-----	-----	-----
Total Current Liabilities .....	104,259	29,649	27,280	(7,708)	153,480
	-----	-----	-----	-----	-----
LONG-TERM DEBT .....					
	--	--	508,992	--	508,992
	-----	-----	-----	-----	-----
REVENUES PAYABLE .....					
	10,106	--	--	--	10,106
	-----	-----	-----	-----	-----
INTERCOMPANY PAYABLES .....					
	853,958	2,959	--	(856,917)	--
	-----	-----	-----	-----	-----
STOCKHOLDERS' EQUITY:					
Common Stock .....	10	3	733	(3)	743
Other .....	(173,189)	86,660	544,498	(178,506)	279,463
	-----	-----	-----	-----	-----
Total Stockholders' Equity .....	(173,179)	86,663	545,231	(178,509)	280,206
	-----	-----	-----	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY .....					
	\$ 795,144	\$ 119,271	\$ 1,081,503	\$(1,043,134)	\$ 952,784
	=====	=====	=====	=====	=====

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS  
(\$ IN THOUSANDS)

	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	COMPANY (PARENT)	ELIMINATIONS	CONSOLIDATED
	-----	-----	-----	-----	-----
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 1998					
REVENUES:					
Oil and gas sales .....	\$ 69,780	\$ (187)	\$ --	\$ 489	\$ 70,082
Oil and gas marketing sales .....	973	64,769	--	(29,486)	36,256
Interest and other .....	966	405	28,024	(28,617)	778
	-----	-----	-----	-----	-----
Total Revenues .....	71,719	64,987	28,024	(57,614)	107,116
	-----	-----	-----	-----	-----
COSTS AND EXPENSES:					
Production expenses and taxes .....	16,184	--	--	--	16,184
Oil and gas marketing expenses .....	1,040	62,677	--	(28,997)	34,720
Impairment of oil and gas properties .....	--	--	--	--	--
Impairment of other assets .....	--	--	--	--	--
Oil and gas depreciation, depletion and amortization .....	34,069	--	--	--	34,069
Other depreciation and amortization .....	1,637	88	793	--	2,518
General and administrative .....	4,514	636	47	--	5,197
Interest .....	26,605	4	20,585	(28,617)	18,577
	-----	-----	-----	-----	-----
Total Costs and Expenses .....	84,049	63,405	21,425	(57,614)	111,265
	-----	-----	-----	-----	-----
INCOME (LOSS) BEFORE INCOME TAXES AND EXTRAORDINARY ITEM .....	(12,330)	1,582	6,599	--	(4,149)
INCOME TAX EXPENSE (BENEFIT) .....	--	--	--	--	--
	-----	-----	-----	-----	-----
NET INCOME (LOSS) BEFORE EXTRAORDINARY ITEM .....	(12,330)	1,582	6,599	--	(4,149)
	-----	-----	-----	-----	-----
EXTRAORDINARY ITEM:					
Loss on early extinguishment of debt, net of applicable income tax .....	--	--	--	--	--
	-----	-----	-----	-----	-----
NET INCOME (LOSS) .....	\$ (12,330)	\$ 1,582	\$ 6,599	\$ --	\$ (4,149)
	=====	=====	=====	=====	=====
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 1997					
REVENUES:					
Oil and gas sales .....	\$ 45,049	\$ --	\$ --	\$ 618	\$ 45,667
Gas marketing sales .....	--	44,326	--	(17,461)	26,865
Interest and other .....	135	487	20,118	(14,862)	5,878
	-----	-----	-----	-----	-----
Total Revenues .....	45,184	44,813	20,118	(31,705)	78,410
	-----	-----	-----	-----	-----
COSTS AND EXPENSES:					
Production expenses and taxes .....	5,180	--	--	--	5,180
Gas marketing expenses .....	--	43,533	--	(16,843)	26,690
Impairment of oil and gas properties .....	--	--	--	--	--
Oil and gas depreciation, depletion and Amortization .....	28,550	--	--	--	28,550
Other depreciation and amortization .....	628	21	493	--	1,142
General and administrative .....	2,578	265	(83)	--	2,760
Interest .....	12,246	33	11,158	(14,862)	8,575
	-----	-----	-----	-----	-----
Total Costs and Expenses .....	49,182	43,852	11,568	(31,705)	72,897
	-----	-----	-----	-----	-----
INCOME (LOSS) BEFORE INCOME TAX .....	(3,998)	961	8,550	--	5,513
INCOME TAX EXPENSE (BENEFIT) .....	--	--	--	--	--
	-----	-----	-----	-----	-----
NET INCOME (LOSS) BEFORE EXTRAORDINARY ITEM .....	(3,998)	961	8,550	--	5,513
	-----	-----	-----	-----	-----
EXTRAORDINARY ITEM:					
Loss on early extinguishment of debt, net of applicable income tax .....	--	--	--	--	--
	-----	-----	-----	-----	-----
NET INCOME (LOSS) .....	\$ (3,998)	\$ 961	\$ 8,550	\$ --	\$ 5,513
	=====	=====	=====	=====	=====

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS  
(\$ IN THOUSANDS)

	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	COMPANY (PARENT)	ELIMINATIONS	CONSOLIDATED
	-----	-----	-----	-----	-----
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1998					
REVENUES:					
Oil and gas sales .....	\$ 193,800	\$ --	\$ --	\$ 2,162	\$ 195,962
Oil and gas marketing sales .....	973	173,405	--	(77,927)	96,451
Interest and other .....	1,471	685	72,007	(70,590)	3,573
	-----	-----	-----	-----	-----
Total Revenues .....	196,244	174,090	72,007	(146,355)	295,986
	-----	-----	-----	-----	-----
COSTS AND EXPENSES:					
Production expenses and taxes .....	42,916	--	--	--	42,916
Oil and gas marketing expenses .....	1,040	169,411	--	(75,765)	94,686
Impairment of oil and gas properties .....	466,000	--	--	--	466,000
Impairment of other assets .....	10,000	--	--	--	10,000
Oil and gas depreciation, depletion and amortization .....	109,311	--	--	--	109,311
Other depreciation and amortization .....	3,698	142	1,980	--	5,820
General and administrative .....	13,122	1,535	54	--	14,711
Interest .....	67,704	4	50,812	(70,590)	47,930
	-----	-----	-----	-----	-----
Total Costs and Expenses .....	713,791	171,092	52,846	(146,355)	791,374
	-----	-----	-----	-----	-----
INCOME (LOSS) BEFORE INCOME TAXES AND EXTRAORDINARY ITEM .....	(517,547)	2,998	19,161	--	(495,388)
INCOME TAX EXPENSE (BENEFIT) .....	--	--	--	--	--
	-----	-----	-----	-----	-----
NET INCOME (LOSS) BEFORE EXTRAORDINARY ITEM .....	(517,547)	2,998	19,161	--	(495,388)
	-----	-----	-----	-----	-----
EXTRAORDINARY ITEM:					
Loss on early extinguishment of debt, net of applicable income tax .....	(2,164)	--	(11,170)	--	(13,334)
	-----	-----	-----	-----	-----
NET INCOME (LOSS) .....	\$(519,711)	\$ 2,998	\$ 7,991	\$ --	\$(508,722)
	=====	=====	=====	=====	=====
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1997					
REVENUES:					
Oil and gas sales .....	\$ 150,416	\$ (3,579)	\$ --	\$ 1,583	\$ 148,420
Gas marketing sales .....	--	131,661	--	(58,643)	73,018
Interest and other .....	746	665	67,564	(54,390)	14,585
	-----	-----	-----	-----	-----
Total Revenues .....	151,162	128,747	67,564	(111,450)	236,023
	-----	-----	-----	-----	-----
COSTS AND EXPENSES:					
Production expenses and taxes .....	14,824	(411)	--	--	14,413
Gas marketing expenses .....	--	129,342	--	(57,060)	72,282
Impairment of oil and gas properties .....	236,000	--	--	--	236,000
Oil and gas depreciation, depletion and amortization .....	96,864	(1,293)	--	--	95,571
Other depreciation and amortization .....	1,737	30	1,321	--	3,088
General and administrative .....	6,348	691	784	--	7,823
Interest .....	49,582	(184)	25,901	(54,390)	20,909
	-----	-----	-----	-----	-----
Total Costs and Expenses .....	405,355	128,175	28,006	(111,450)	450,086
	-----	-----	-----	-----	-----
INCOME (LOSS) BEFORE INCOME TAX .....	(254,193)	572	39,558	--	(214,063)
INCOME TAX EXPENSE (BENEFIT) .....	(19,384)	(967)	2,453	--	(17,898)
	-----	-----	-----	-----	-----
NET INCOME (LOSS) BEFORE EXTRAORDINARY ITEM .....	(234,809)	1,539	37,105	--	(196,165)
	-----	-----	-----	-----	-----
EXTRAORDINARY ITEM:					
Loss on early extinguishment of debt, net of applicable income tax .....	(179)	--	2	--	(177)
	-----	-----	-----	-----	-----
NET INCOME (LOSS) .....	\$(234,988)	\$ 1,539	\$ 37,107	\$ --	\$(196,342)
	=====	=====	=====	=====	=====

## CHESAPEAKE ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 1998  
(UNAUDITED)CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS  
(\$ IN THOUSANDS)

	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	COMPANY (PARENT)	ELIMINATIONS	CONSOLIDATED
	-----	-----	-----	-----	-----
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1998					
CASH FLOWS FROM OPERATING ACTIVITIES: .....	\$ 32,384	\$ (21,068)	\$ 42,007	\$ --	\$ 53,323
	-----	-----	-----	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:					
Oil and gas properties .....	(478,394)	--	--	--	(478,394)
Proceeds from sale of assets .....	3,114	--	3,600	--	6,714
Investment in preferred stock of Gothic .....	(39,500)	--	--	--	(39,500)
Repayment of long-term loan .....	2,000	--	--	--	2,000
Other additions .....	(6,161)	(1,343)	(2,267)	--	(9,771)
	-----	-----	-----	-----	-----
	(518,941)	(1,343)	1,333	--	(518,951)
	-----	-----	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:					
Proceeds from borrowings .....	--	--	658,750	--	658,750
Payments on borrowings .....	--	--	(474,166)	--	(474,166)
Cash received from issuance of preferred stock .....	--	--	222,760	--	222,760
Cash paid for purchase of treasury stock .....	--	--	(29,962)	--	(29,962)
Cash received from exercise of stock options .....	--	--	131	--	131
Cash dividends paid on common and preferred stock .....	--	--	(9,617)	--	(9,617)
Intercompany advances, net .....	465,229	(2,545)	(462,684)	--	--
	-----	-----	-----	-----	-----
	465,229	(2,545)	(94,788)	--	367,896
	-----	-----	-----	-----	-----
Effect of exchange rate changes on cash .....	(5,379)	--	--	--	(5,379)
	-----	-----	-----	-----	-----
Net increase (decrease) in cash .....	(26,707)	(24,956)	(51,448)	--	(103,111)
Cash, beginning of period .....	(284)	13,694	110,450	--	123,860
	-----	-----	-----	-----	-----
Cash, end of period .....	\$ (26,991)	\$ (11,262)	\$ 59,002	\$ --	\$ 20,749
	=====	=====	=====	=====	=====
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1997					
CASH FLOWS FROM OPERATING ACTIVITIES: .....	\$ 76,828	\$ 742	\$ 7,242	\$ --	\$ 84,812
	-----	-----	-----	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:					
Oil and gas properties .....	(380,868)	64	--	--	(380,804)
Proceeds from sale of assets .....	1,190	--	--	--	1,190
Loans to third parties .....	(2,000)	--	(18,000)	--	(20,000)
Other investments .....	--	--	(13,751)	--	(13,751)
Other additions .....	(34,723)	(240)	(5,642)	--	(40,605)
	-----	-----	-----	-----	-----
	(416,401)	(176)	(37,393)	--	(453,970)
	-----	-----	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:					
Proceeds from long-term borrowings .....	--	--	292,626	--	292,626
Payments on borrowings .....	(67,655)	1,710	53,195	--	(12,750)
Cash received from exercise of stock options .....	--	--	1,340	--	1,340
Cash dividends paid on common stock .....	--	--	(1,405)	--	(1,405)
Other financing .....	--	(15)	(195)	--	(210)
Intercompany advances, net .....	396,018	(1,709)	(394,309)	--	--
	-----	-----	-----	-----	-----
	328,363	(14)	(48,748)	--	279,601
	-----	-----	-----	-----	-----
Net increase (decrease) in cash and cash Equivalents .....	(11,210)	552	(78,899)	--	(89,557)
Cash, beginning of period .....	4,865	6,099	129,775	--	140,739
	-----	-----	-----	-----	-----
Cash, end of period .....	\$ (6,345)	\$ 6,651	\$ 50,876	\$ --	\$ 51,182
	=====	=====	=====	=====	=====

## PART I. FINANCIAL INFORMATION

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## RECENT EVENTS

On July 7, 1998 the Company's Board of Directors authorized management to explore strategic alternatives to enhance shareholder value, including a possible sale or merger of the Company, based upon the Board's opinion that the market is substantially undervaluing the Company's assets and exploration potential. Also on July 7, 1998 Chesapeake's Board of Directors unanimously adopted a shareholder rights plan designed to deter coercive takeover tactics and to prevent a change of control from occurring without all shareholders receiving a fair price.

Pursuant to the decision to explore various alternatives, the Company engaged Donaldson, Lufkin & Jenrette Securities Corporation ("DLJ") to advise the Company. The Company and DLJ are presently evaluating various alternatives, including the potential sale or merger of the Company, sale of certain assets, or alternative financial strategies. This process is underway and is expected to be concluded within the next few months.

On November 2, 1998 the Company announced it entered into an agreement to tender its 19.9% stake in Pan East Petroleum Corp. ("Pan East") to POCO Petroleum Ltd. and agreed to a property exchange with Pan East. Subject to the successful completion by POCO of its tender offer, the Company anticipates receiving approximately \$26 million in cash and increasing its net reserves by four billion cubic feet equivalent of natural gas. As of September 30, 1998, the Company's net investment in the common stock of Pan East of \$21.3 million has been accounted for using the equity method and is included in Other Assets in the accompanying Consolidated Balance Sheets.

## RESULTS OF OPERATIONS

Three Months Ended September 30, 1998 vs. September 30, 1997

General. For the three months ended September 30, 1998 (the "Current Quarter"), the Company realized a net loss of \$4.1 million, or a loss of \$0.08 per common share after deducting preferred dividends of \$4.0 million. This compares to net income of \$5.5 million, or income of \$0.08 per common share, for the three months ended September 30, 1997 (the "Prior Quarter").

During the Current Quarter and Prior Quarter, the Company did not record any impairment of its oil and gas properties. Any future impairment is subject to a number of factors, some of which are beyond the control of the Company, including oil and natural gas prices. Lower oil or gas prices could have a material adverse effect on the Company's operations and financial condition and may result in future write-downs of the Company's oil and gas properties due to full-cost ceiling test limitations. As of September 30, 1998, the Company estimates that the present value (SEC-PV10%) of its proved reserves, based on prices at that time of \$15.43 per bbl (NYMEX) and \$2.32 per mcf (NYMEX), adjusted for usual well-head quality and location (basis) variances, was \$929 million. The Company estimates that, as of September 30, 1998, for every \$0.10 per thousand cubic feet ("mcf") reduction in natural gas prices and \$1.00 per barrel of oil ("bbl") reduction in oil prices, the present value of the Company's proved oil and gas reserves would be reduced by approximately \$55 million and \$22 million, respectively.

Oil and Gas Sales. During the Current Quarter, oil and gas sales increased significantly to \$70.1 million from \$45.7 million, an increase of \$24.4 million, or 53%. This increase resulted from significantly higher oil and gas production volumes, which increased from 19.2 bcfe in the Prior Quarter to 36.3 bcfe in the Current Quarter, an increase of 17.1 bcfe, or 89%. The higher production volumes were primarily the result of the Company's acquisitions completed during the first four months of 1998. For the Current Quarter, the Company produced 1.6 million barrels of oil ("mmbo") and 26.8 billion cubic feet of natural gas ("bcf"), compared to 0.9 mmbo and 13.9 bcf in the Prior Quarter. Average oil prices realized were \$12.41 per barrel of oil in the Current Quarter compared



to \$18.48 per barrel in the Prior Quarter, a decrease of 33%. Average gas prices realized were \$1.88 per mcf in the Current Quarter compared to \$2.12 per mcf in the Prior Quarter, a decrease of 11%.

For the Current Quarter, the Company realized an average price of \$1.93 per thousand cubic feet equivalent of natural gas ("mcf"), compared to \$2.38 per mcf in the Prior Quarter. The Company's hedging activities resulted in increased oil and gas revenues of \$6.5 million, or \$0.18 per mcf, in the Current Quarter, compared to increases in oil and gas revenues of \$0.4 million in the Prior Quarter.

The following table shows the Company's production by region for the Current Quarter and the Prior Quarter:

OPERATING AREAS	FOR THE THREE MONTHS ENDED SEPTEMBER 30,			
	1998		1997	
	MMCFE	PERCENT	MMCFE	PERCENT
Mid-Continent .....	17,969	50%	4,277	22%
Gulf Coast .....	13,099	36	13,793	72
Canada .....	2,533	7	--	--
Other areas .....	2,667	7	1,091	6
Total .....	36,268	100%	19,161	100%
	=====	=====	=====	=====

Natural gas production represented approximately 74% of the Company's total production volume on an equivalent basis in the Current Quarter, compared to 73% in the Prior Quarter. The Company anticipates natural gas will represent 70-80% of anticipated 1998 and 1999 production.

Oil and Gas Marketing Sales. The Company realized \$36.3 million in oil and gas marketing sales for third parties in the Current Quarter, with corresponding oil and gas marketing expenses of \$34.7 million, for a gross profit margin of \$1.6 million. This compares to sales of \$26.9 million and expenses of \$26.7 million, resulting in a gross profit margin of \$0.2 million in the Prior Quarter.

Interest and Other. Interest and other revenues for the Current Quarter were \$0.8 million compared to \$5.9 million in the Prior Quarter. The decrease was primarily caused by the Company maintaining lower invested cash balances resulting in reduced interest income during the Current Quarter.

Production Expenses and Taxes. Production expenses increased to \$14.2 million in the Current Quarter, a \$10.3 million increase from \$3.9 million incurred in the Prior Quarter. This significant increase was due to higher production attributable to acquisitions and higher unit-of-production expense. On a production unit basis, production expenses were \$0.39 and \$0.20 per mcf in the Current and Prior Quarters, respectively. Properties acquired in late 1997 and 1998 typically have higher unit-of-production expenses than the Company's historical production base. The Company anticipates production expenses will average \$0.40 per mcf for 1998.

Production taxes, which consist primarily of wellhead severance taxes, were \$2.0 million and \$1.3 million in the Current and Prior Quarters, respectively. This increase was the result of increased production, offset by certain accounting reclassifications. On a per unit basis, production taxes were \$0.05 per mcf in the Current Quarter compared to \$0.07 per mcf in the Prior Quarter. The Company anticipates incurring production taxes at the rate of \$0.07 per mcf for the remainder of 1998 and 1999.

Oil and Gas Depreciation, Depletion and Amortization. Depreciation, depletion and amortization of oil and gas properties ("DD&A") for the Current Quarter was \$34.1 million, compared to \$28.6 million in the Prior Quarter. This increase was caused by significantly increased production, partially offset by a decrease in the DD&A rate per mcf from \$1.49 to \$0.94 in the Prior and Current Quarters, respectively. The Company's DD&A rate is expected to be approximately \$0.95-\$1.00 per mcf for the remainder of 1998.

Depreciation and Amortization of Other Assets. Depreciation and amortization of other assets ("D&A") increased to \$2.5 million in the Current Quarter compared to \$1.1 million in the Prior Quarter. This increase in D&A was caused by increased investments in depreciable buildings and equipment incurred in conjunction with the

acquisitions and increased amortization of debt issuance costs as a result of the issuance of Senior Notes in April 1998. The Company anticipates D&A expense throughout the remainder of 1998 to remain at approximately the same level incurred in the Current Quarter.

General and Administrative. General and administrative expenses ("G&A"), which are net of capitalized internal payroll and non-payroll expenses, were \$5.2 million in the Current Quarter compared to \$2.8 million in the Prior Quarter. This increase was primarily caused by increased employment levels resulting from the Company's acquisitions. The Company capitalized \$0.8 million of internal costs in the Current Quarter directly related to the Company's oil and gas exploration and development efforts, compared to \$1.4 million in the Prior Quarter. The Company anticipates that G&A costs for the remainder of 1998 will not increase significantly and expects G&A costs to trend somewhat lower in 1999.

Interest. Interest expense increased to \$18.6 million in the Current Quarter from \$8.6 million in the Prior Quarter. This increase was a result of additional interest expense in the Current Quarter on the \$500 million principal amount of Senior Notes issued on April 22, 1998. In addition to the interest expense reported, the Company capitalized \$2.0 million of interest during the Current Quarter compared to \$2.6 million capitalized in the Prior Quarter. The Company does not anticipate interest expense will increase significantly during the remainder of 1998.

Provision for Income Taxes. The Company recorded no income tax expense for the Current Quarter or the Prior Quarter. At September 30, 1998, the Company had a net operating loss carryforward of approximately \$525 million for regular federal income taxes which will expire in future years beginning in 2007. Management believes that it cannot be demonstrated at this time that it is more likely than not that the deferred income tax assets, comprised primarily of the net operating loss carryforward, will be realizable in future years, and therefore a valuation allowance has been recorded equaling the net deferred tax asset. The Company does not expect to record any book income tax expense or benefit for the remainder of 1998.

#### Nine Months Ended September 30, 1998 vs. September 30, 1997

General. For the nine months ended September 30, 1998 (the "Current Period"), the Company realized a net loss of \$508.7 million, or a loss of \$5.48 per common share after deducting preferred dividends of \$8.1 million. This compares to a net loss of \$196.3 million, or a loss of \$2.79 per common share, in the nine months ended September 30, 1997 (the "Prior Period"). The loss in the Current Period was primarily caused by a \$466 million asset writedown recorded under the full-cost method of accounting, a \$10 million impairment related to certain of the Company's gas processing and transportation assets located in Louisiana, a \$13.3 million extraordinary loss on the early extinguishment of debt, and a \$19.4 million loss from recurring operations. The asset writedown was partially caused by the acquisitions completed during the Current Period for consideration in excess of the present value (10% discount) of the future net revenues of the acquired proved reserves as of March 31, 1998 or June 30, 1998. See "Impairment of Oil and Gas Properties". The loss in the Prior Period was caused by a \$236 million asset write-down recorded under the full-cost method of accounting. The asset writedown in the Prior Period was primarily caused by poor exploration results in the Company's drilling program, particularly in the Austin Chalk portion of the Louisiana Trend, combined with decreased oil and gas prices, and higher drilling and equipping costs.

Oil and Gas Sales. During the Current Period, oil and gas sales increased significantly to \$196.0 million from \$148.4 million, an increase of \$47.6 million, or 32%. This increase resulted from significantly higher oil and gas production volumes, which increased from 61.0 bcfe in the Prior Period to 96.5 bcfe in the Current Period, an increase of 35.5 bcfe, or 58%. The higher production volumes were primarily the result of the Company's acquisitions completed during the first four months of 1998. For the Current Period, the Company produced 4.6 mmo and 69.0 bcf, compared to 2.5 mmo and 45.9 bcf in the Prior Period. Average oil prices realized were \$13.21 per barrel in the Current Period compared to \$19.66 per barrel in the Prior Period, a decrease of 33%. Average gas prices realized were \$1.96 per mcf in the Current Period compared to \$2.15 per mcf in the Prior Period, a decrease of 9%.

For the Current Period, the Company realized an average price of \$2.03 per mcfe, compared to \$2.43 per mcfe in the Prior Period. The Company's hedging activities resulted in increased oil and gas revenues of \$10.5 million, or

\$0.11 per mcfe, in the Current Period, compared to increases in oil and gas revenues of \$0.1 million in the Prior Period.

The following table shows the Company's production by region for the Current Period and the Prior Period:

OPERATING AREAS	FOR THE NINE MONTHS ENDED SEPTEMBER 30,			
	1998		1997	
	MMCFE	PERCENT	MMCFE	PERCENT
Mid-Continent .....	44,809	46%	12,568	21%
Gulf Coast .....	39,519	41	45,136	74
Canada .....	5,677	6	--	--
Other areas .....	6,457	7	3,291	5
Total .....	96,462	100%	60,995	100%
	=====	=====	=====	=====

Natural gas production represented approximately 72% of the Company's total production volume on an equivalent basis in the Current Period, compared to 75% in the Prior Period.

Oil and Gas Marketing Sales. The Company realized \$96.4 million in oil and gas marketing sales for third parties in the Current Period, with corresponding oil and gas marketing expenses of \$94.7 million, resulting in a gross profit margin of \$1.7 million. This compares to sales of \$73.0 million and expenses of \$72.3 million with a gross profit margin of \$0.7 million in the Prior Period.

Interest and Other. Interest and other revenues for the Current Period were \$3.6 million compared to \$14.6 million in the Prior Period. The decrease was primarily caused by the Company maintaining lower invested cash balances resulting in reduced interest income during the Current Period.

Production Expenses and Taxes. Production expenses increased to \$36.8 million in the Current Period, a \$25.7 million increase from \$11.1 million incurred in the Prior Period, due to the significantly higher production levels and higher per unit costs. On a production unit basis, production expenses were \$0.38 and \$0.18 per mcfe in the Current and Prior Periods, respectively. The primary reason for the increase per mcfe was production from properties acquired in late 1997 and 1998, which typically have higher unit-of-production expenses than the Company's historical production base.

Production taxes, which consist primarily of wellhead severance taxes, were \$6.1 million and \$3.3 million in the Current and Prior Periods, respectively. This increase was primarily the result of increased production. On a per unit basis, production taxes were \$0.06 per mcfe in the Current Period compared to \$0.05 per mcfe in the Prior Period, the result of higher tax rates associated with production from properties acquired in late 1997 and 1998 compared to the Company's historical production base.

Impairment of Oil and Gas Properties. The Company utilizes the full-cost method to account for its investments in oil and gas properties. Under this method, all costs of acquisition, exploration and development of oil and gas reserves (including such costs as leasehold acquisition costs, geological and geophysical expenditures, certain capitalized internal costs, dry hole costs and tangible and intangible development costs) are capitalized as incurred. These oil and gas property costs, including the estimated future capital expenditures to develop proved undeveloped reserves, are depleted and charged to operations using the unit-of-production method based on the ratio of current production to proved oil and gas reserves as estimated by the Company's independent engineering consultants and Company engineers. Costs directly associated with the acquisition and evaluation of unproved properties are excluded from the amortization computation until it is determined whether or not proved reserves can be assigned to the property or whether impairment has occurred. To the extent that capitalized costs of oil and gas properties, net of accumulated depreciation, depletion and amortization and related deferred income taxes, exceed the discounted future net revenues of proved oil and gas properties, such excess costs are charged to operations.

The Company incurred an impairment of oil and gas properties charge of \$466 million in the Current Period (\$250 million recorded during the quarter ended March 31, 1998, and \$216 million recorded during the quarter ended June

30, 1998), compared to an impairment charge of \$236 million in the Prior Period. The writedown in the Current Period was caused by a combination of several factors, including the acquisitions completed by the Company during the Current Period, which were accounted for using the purchase method. The most significant of these acquisitions were Hugoton Energy Corporation and DLB Oil & Gas, Inc. Higher drilling and completion costs, the evaluation of certain leasehold, seismic and other exploration-related costs that were previously unevaluated, together with decreases in oil and gas prices from December 31, 1997 to June 30, 1998, were the remaining contributing factors which led to the writedown in the Current Period. The \$236 million writedown incurred in the Prior Period was due primarily to significant expenditures for acreage acquisition and drilling costs followed by unfavorable exploration and production results in Louisiana, together with increases in drilling and equipment costs and lower oil and gas prices as of June 30, 1997. Future impairment charges, if any, will be dependent upon several factors, primarily oil and gas prices in effect at the date of determination and the results of the Company's exploration activities.

**Impairment of Other Assets.** In the Current Period, the Company incurred an impairment charge of \$10 million as of June 30, 1998 related to certain of the Company's gas processing and transportation assets located in Louisiana. No such charge was recorded in the Prior Period.

**Oil and Gas Depreciation, Depletion and Amortization.** DD&A for the Current Period was \$109.3 million, compared to \$95.6 million in the Prior Period. This increase was caused by significantly increased production offset by a decrease in the DD&A rate per mcfe from \$1.57 to \$1.13 in the Prior and Current Periods, respectively.

**Depreciation and Amortization of Other Assets.** D&A increased to \$5.8 million in the Current Period compared to \$3.1 million in the Prior Period. This increase in D&A was caused by increased investments in depreciable buildings and equipment incurred in conjunction with acquisitions and increased amortization of debt issuance costs as a result of the issuance of Senior Notes in April 1998.

**General and Administrative.** G&A, which is net of capitalized internal payroll and non-payroll expenses, was \$14.7 million in the Current Period compared to \$7.8 million in the Prior Period. This increase was primarily caused by increased employment levels associated with the Company's acquisitions. The Company capitalized \$4.0 million of internal costs in the Current Period directly related to the Company's oil and gas exploration and development efforts, compared to \$4.2 million in the Prior Period.

**Interest.** Interest expense increased to \$47.9 million in the Current Period from \$20.9 million in the Prior Period. This increase was a result of additional interest expense in the Current Period on the \$500 million principal amount of Senior Notes issued on April 22, 1998. In addition to the interest expense reported, the Company capitalized \$5.8 million of interest during the Current Period compared to \$7.9 million capitalized in the Prior Period.

**Provision for Income Taxes.** The Company recorded no income tax expense for the Current Period, and recorded a \$17.9 million tax benefit in the Prior Period.

**Loss on Early Extinguishment of Debt.** During the Current Period and Prior Period, the Company recorded a loss on early extinguishment of debt of \$13.3 million and \$0.2 million, respectively. The loss in the Current Period was due primarily to the early retirement of the Company's 10.5% Senior Notes due 2002. The cost to acquire the \$90 million aggregate principal amount 10.5% Senior Notes of \$99 million, together with the write-off of associated debt issue costs, resulted in an extraordinary charge of \$13.3 million during the Current Period. The Company did not record any such charges in the Current Quarter or Prior Quarter.

## RISK MANAGEMENT ACTIVITIES

Periodically the Company utilizes hedging strategies to hedge the price of a portion of its future oil and gas production. These strategies include (1) swap arrangements that establish an index-related price above which the Company pays the counterparty and below which the Company is paid by the counterparty, (2) the purchase of index-related puts that provide for a "floor" price below which the counterparty pays the Company the amount by which the price of the commodity is below the contracted floor, (3) the sale of index-related calls that provide for a "ceiling" price above which the Company pays the counterparty the amount by which the price of the commodity is above the contracted ceiling, and (4) basis protection swaps, which are arrangements that guarantee the price differential of oil or gas from a specified delivery point or points. The Company only enters into commodity hedging transactions related to the Company's oil and gas production volumes or physical purchase or sale commitments of its oil and gas marketing subsidiaries. Results from commodity hedging transactions are reflected in oil and gas sales to the extent related to the Company's oil and gas production. Gains or losses on crude oil and natural gas hedging transactions are recognized as price adjustments in the months of related production.

As of September 30, 1998, the Company had the following natural gas swap arrangement for periods after September 1998:

MONTHS -----	MONTHLY VOLUME (MMBTU) -----	NYMEX-INDEX STRIKE PRICE (PER MMBTU) -----
October 1998.....	4,960,000	\$ 2.346

The swap arrangement listed above was closed but not settled as of September 30, 1998, resulting in net proceeds to the Company of \$1.1 million in October 1998. The Company has closed transactions for natural gas previously hedged for the period April 1999 through November 1999 and locked in net proceeds of \$3.2 million. Subsequent to September 30, 1998, the Company sold December 1998 natural gas call options with a strike price of \$2.60 on volume of 3.1 bcf for \$0.1325 per mmbtu, and sold January 1999 natural gas call options with a strike price of \$2.70 on volume of 3.1 bcf for \$0.2225 per mmbtu.

As of October 15, 1998, the Company closed transactions for oil previously hedged from January 1999 through December 1999, resulting in a \$0.9 million reduction of revenue. The Company has closed transactions for crude oil previously hedged for the period from September 1998 through February 1999 and has locked in net proceeds of \$0.4 million.

The Company also utilizes hedging strategies to manage fixed-interest rate exposure. Through the use of a swap arrangement, the Company believes that it can benefit from stable or falling interest rates and reduce its upfront interest expense. As of September 30, 1998, the Company's interest rate swap resulted in a \$0.2 million reduction of interest expense for the period August 1998 through October 1998, which settled on November 2, 1998.

## LIQUIDITY AND CAPITAL RESOURCES

In April 1998, the Company completed an offering of \$230 million of 7% Cumulative Convertible Preferred Stock and \$500 million principal amount of 9.625% Senior Notes due 2005. The net proceeds of these offerings were approximately \$711 million, of which \$170 million was used to retire all of the Company's commercial bank debt, approximately \$99 million was used to retire all \$90 million principal amount of the Company's 10.5% Senior Notes due 2002, \$345 million was used to fund certain of the Company's acquisitions, with the balance of the net proceeds increasing the Company's working capital.

As of September 30, 1998, the Company had a working capital deficit of approximately \$2.0 million. The Company, as the result of significantly lower oil and gas prices and a change in the Company's strategy away from higher risk drilling and toward a more balanced acquisition and exploitation strategy, has continued to reduce its capital expenditure plans. The Company currently estimates that it will expend approximately \$50 million for drilling, seismic and leasehold expenditures for the three months ended December 31, 1998 and is currently

budgeting \$195 million in expenditures for 1999. The capital expenditure budget is largely discretionary, and can be adjusted by the Company based on operating results or other factors. The Company believes it has sufficient capital resources from anticipated cash flow from operations, planned asset sales and unused commercial bank facilities to fund the reduced drilling program for the remainder of 1998.

As part of its capital resources plan, the Company has undertaken to sell various non-core assets. The Company expects to realize between \$75 and \$100 million of cash from these asset sales within the six months beginning October 1, 1998, inclusive of the \$26 million transaction announced on November 2, 1998 between Poco Petroleum Ltd. and the Company involving Pan East common stock and oil and gas reserves in the Helmet area of British Columbia. Other completed asset sales combined with offers currently in hand total approximately \$25 million. These asset sales are independent of the Company's strategic alternatives evaluation process.

The Company has a \$50 million secured revolving bank facility with its primary commercial bank. As a result of its reduced capital expenditure plan, reduced acquisition program, and the planned sale of assets, the Company believes this size of bank facility is appropriate for the foreseeable future, although significantly larger secured facilities could be established within the limits of the Company's senior note indentures. The facility contains terms and conditions similar to the bank facilities the Company has had in the past, including collateral-based borrowing limitations. The primary purpose of the facility is to provide standby liquidity for the Company. The Company had no borrowings outstanding under this facility at September 30, 1998.

On May 20, 1998, the Company's Board of Directors approved the expenditure of up to \$25 million to purchase outstanding Company common stock. On July 14, 1998, the Board increased the authorized expenditure to \$30 million. As of August 25, 1998 the Company had purchased approximately 8.5 million shares of common stock for an aggregate amount of \$30.0 million pursuant to such authorization.

The Company's senior note indentures contain restrictions on the Company's ability to make Restricted Payments (as defined), including the payment of preferred stock dividends unless certain tests are met. The Company anticipates that, based on expected production, pricing, and expenses for the twelve months ending December 31, 1998, it may not be able to meet the requirements to incur additional unsecured indebtedness, and consequently would not be able to pay cash dividends on its 7% Cumulative Convertible Preferred Stock as of February 1, 1999. Subsequent payments will be subject to the same restrictions and are dependent upon variables that are beyond the Company's ability to predict, chiefly the future level of oil and gas prices. This restriction does not affect the Company's ability to borrow under or expand its secured commercial bank facility. If the Company fails to pay dividends for six quarterly periods, the holders of preferred stock would be entitled to elect two additional members to the Board.

The Company's cash provided by operating activities before changes in current assets and liabilities decreased 17% to \$96.7 million during the Current Period compared to \$117.0 million during the Prior Period. The decrease was due primarily to reduced operating income as a result of a decrease in average oil and gas prices between periods.

Cash used in investing activities increased to \$518.9 million during the Current Period from \$453.9 million in the Prior Period. The Company completed several acquisitions requiring cash in the Current Period which totaled \$345 million, compared to none in the Prior Period, offset by a significant decrease in drilling activity and leasehold acquisitions in the Current Period compared to the Prior Period. During the Current Period the Company expended approximately \$143.8 million to initiate drilling on 166 gross (91.5 net) wells and invested approximately \$11.1 million in leasehold acquisitions. This compares to \$254.4 million to initiate drilling on 140 gross (78.2 net) wells and \$113.1 million to purchase leasehold in the Prior Period.

Cash provided by financing activities was \$367.9 million in the Current Period, compared to \$279.6 million in the Prior Period. During the Current Period, the Company retired \$465 million of debt consisting of \$85 million of debt assumed at the completion of the DLB acquisition, \$120 million of debt assumed at the completion of the Hugoton acquisition, \$90 million of senior notes, and \$170 million of borrowings made under its commercial bank credit facilities. The Company issued \$500 million in senior notes and \$230 million in preferred stock. During the Prior Period, the Company issued \$300 million in Senior Notes.

The Company is subject to certain routine legal proceedings, none of which are expected to have a material adverse effect upon the Company's financial condition or operations. The Company is also a defendant in other non-routine lawsuits, which are described in Note 3 of the notes to the accompanying financial statements. Also see Part II, Item 1 of this report. An adverse outcome in one or more of such suits could have a material effect on the Company, although management is unable to quantify the Company's exposure to liability. No provision for litigation liability has been recorded for these non-routine lawsuits in the Company's financial statements.

#### YEAR 2000

Project. The Company has placed a high priority on proactively resolving computer or imbedded chip problems related to the "Year 2000" which may have adverse material effects on its continuing operations or cash flow. This problem would be caused by the inability of a component (software, hardware or equipment with embedded microprocessors) to correctly process date data in and between the 20th and 21st centuries and therefore fail to properly perform its intended functions, and/or to exchange correct date data with other components. This problem would most typically be caused by erroneous date calculations, which results from using two digits to signify a year (century implied), handling leap years incorrectly or the use of "special" values that can be confused with legitimate calendar dates. The scope of the Year 2000 project includes conducting an inventory of the Company's software, hardware and "embedded systems" equipment, assessing potential for failure and the associated risk, prioritizing the need for remediation, repairing or replacing significant noncompliant items, and testing. In addition, the Company will take a similar approach to mitigating risks associated with the Year 2000 readiness of material business partners (vendors, suppliers, customers, etc.). The project will also identify contingency plans to cope with unexpected events resulting from Year 2000 issues.

Beginning in mid 1997, the Company began an assessment of its core financial and operational software systems. Three critical systems were identified with date sensitivities: oil and gas financial accounting, production accounting and land/lease administration. A Year 2000 compliant release of the oil and gas financial accounting package in use at the Company is available and has been scheduled for implementation during the first calendar quarter of 1999. The production accounting system in use at the Company is also scheduled for upgrade to a Year 2000 compliant version early in 1999. Both of these upgrades have been scheduled to maintain currency with the respective vendors' support and to take advantage of additional features and performance enhancements. A project has been underway since early 1997 to implement a completely revamped version of the land/lease administration package in use at the Company to provide significantly increased functionality and reliability. The terms of this development arrangement stipulated Year 2000 compliance and is being monitored. Assessment continues for lower priority software systems.

In addition, the Year 2000 compliant AS/400, on which the accounting package resides, was upgraded to provide additional capacity in late 1997. Operating system upgrades will be implemented in the near future for the Windows NT based servers to complete their remediation.

Other activities either already underway or scheduled to start during the balance of 1998 include testing of desktop PC's, assessment of material business partners, and inventory of embedded systems in field locations. The following table summarizes the current overall status of the project with anticipated completion dates:

Component	Phase		
	Inventory	Assessment/Prioritization	Remediation/Contingency
Software	November 30, 1998	December 31, 1998	June 30, 1999
Hardware	December 31, 1998	January 31, 1999	March 31, 1999
Business Partners	December 31, 1998	March 31, 1999	June 30, 1999
Embedded Systems (Non-IT Systems)	March 31, 1999	April 30, 1999	June 30, 1999

In addition to the above, during the second quarter of 1999 the Company will develop an overall contingency plan to assure continued operations which will include precautionary measures.

Cost. To date, the Company has incurred only minor consulting costs for Year 2000 project planning and scope definition. All software packages requiring an upgrade which have been identified will be upgraded within normal maintenance procedures and will not require additional out of pocket expense. In all cases these upgrades had been previously scheduled to maintain desired vendor support and no upgrade project schedule has been accelerated to achieve Year 2000 compliance. An accurate cost cannot be determined prior to conclusion of the Assessment/Prioritization phase, but it is expected total project expenditures including the use of outside consultants should not exceed \$1 million. This does not include any costs which may be assessed by joint venture partners on properties not operated by the Company.

Risks/Contingency. The failure to remediate critical systems (software, hardware or embedded systems), or the failure of a material business partner to resolve critical Year 2000 issues could have serious adverse impact on the ability of the Company to continue operations and meet obligations. At the current time, it is believed that any interruption in operation will be minor and short-lived and will pose no safety or environmental risks. However, until all assessment phases have been completed it is impossible to accurately identify the risks, quantify potential impacts or establish a contingency plan. The Company has not yet clearly identified the most likely worst case scenario if the Company and its material business partners do not achieve Year 2000 compliance on a timely basis. The Company currently intends to complete its contingency planning by June 30, 1999.

#### FORWARD LOOKING STATEMENTS

This Form 10-Q includes "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. All statements other than statements of historical facts included in this Form 10-Q, including without limitation statements under "Management's Discussion and Analysis of Financial Condition and Results of Operations" regarding oil and gas reserve estimates, planned capital expenditures, expected oil and gas production, the Company's financial position, business strategy and other plans and objectives for future operations, capital expenditures plans, expected future expenses, and Year 2000 compliance efforts are forwardlooking statements. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Factors that could cause actual results to differ materially from those expected by the Company, including, without limitation, factors discussed under Risk Factors in the Company's Form 10-K for the period ended December 31, 1997, are concentration of unevaluated leasehold in Louisiana, impairment of asset value, need to replace reserves, substantial capital requirements, ability to supplement capital resources with asset sales, substantial indebtedness, fluctuations in the prices of oil and gas, uncertainties inherent in estimating quantities of oil and gas reserves, projecting future rates of production and the timing of development expenditures, competition, operating risks, acquisition and integration of operation risks, restrictions imposed by lenders, liquidity and capital requirements, the effects of governmental and environmental regulation, patent and securities litigation, adverse changes in the market for the Company's oil and gas production and the Company's ability to successfully address Year 2000 issues. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to release publicly the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in the Company's business strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

- - Not applicable



## PART II. OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

The Company is subject to ordinary routine litigation incidental to its business. In addition, the Company and its officers and directors are defendants in two purported class actions alleging violations of federal and Oklahoma state securities laws. Also the Company is defending a patent infringement claim in another pending action. These matters are described in Item 3 of the Company's Transition Report on Form 10-K for the six-month period ended December 31, 1997, as updated by its Quarterly Reports on Form 10-Q for the first and second quarters of 1998.

On September 11, 1998, the Company and the other named defendants filed a motion to dismiss in Yuan, et al. v. Bayard Drilling Technologies, Inc., et al. pending in the U.S. District Court for the Western District of Oklahoma.

## ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Effective as of September 11, 1998, the Rights Agreement between the Company and UMB Bank, N.A., as rights agent, was amended to add as an "Exempt Person" the pledgee of shares beneficially owned by certain other Exempt Persons as of the date of the amendment, to the extent that such pledgee exercises its rights under the pledge other than the exercise of any voting power or the acquisition of ownership.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

- - Not applicable

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

- - Not applicable

## ITEM 5. OTHER INFORMATION

In July 1998, the Company made a \$5 million secured loan to each of Aubrey K. McClendon and Tom L. Ward, the Company's Chairman and Chief Executive Officer and President, respectively. Each loan is payable on or before December 31, 1998 with interest accruing at an annual rate of 9 1/8%, payable quarterly.

## ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

## (a) Exhibits

The following exhibits are filed as a part of this report:

## Exhibit No.

- |       |  |
|-------|--|
| 4.1.1 | Fourth Supplemental Indenture, dated July 1, 1998, to Indenture dated as of March 15, 1997 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors, and United States Trust Company of New York, as Trustee, with respect to 7-7/8% Senior Notes due 2004. |
| 4.2.1 | Fourth Supplemental Indenture, dated July 1, 1998, to Indenture dated as of March 15, 1997 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors, and United States Trust Company of New York, as Trustee, with respect to 8-1/2% Senior Notes due 2012. |
| 4.3.1 | Fourth Supplemental Indenture, dated July 1, 1998, to Indenture dated as of April 1, 1996 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors,   |

and United States Trust Company of New York, as Trustee, with respect to 9-1/8% Senior Notes due 2006.

- 4.4.1 First Supplemental Indenture, dated July 1, 1998, to Indenture dated as of April 1, 1998 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors, and United States Trust Company of New York, as Trustee, with respect to 9-5/8% Senior Notes due 2005.
- 10.2.1 Amended and Restated Employment Agreement dated July 1, 1998 between Aubrey K. McClendon and Chesapeake Energy Corporation.
- 10.2.2 Amended and Restated Employment Agreement dated July 1, 1998 between Tom L. Ward and Chesapeake Energy Corporation.
- 10.3 Amendment No. 1 dated September 11, 1998 to Rights Agreement dated July 15, 1998 between the Registrant and UMB Bank, N.A., as Rights Agent.
- 12 Schedule of Ratios
- 27 Financial Data Schedule

(b) Reports on Form 8-K

During the quarter ended September 30, 1998, the Company filed the following Current Reports on Form 8-K:

On July 2, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing the declaration of quarterly cash dividends on the Company's common stock and preferred stock.

On July 6, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing that Thomas L. Winton has been named Senior Vice President Information Technology.

On July 9, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing that the Board of Directors authorized management to explore strategic alternatives to enhance shareholder value, involving possible sale or merger of the Company.

On July 16, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing that the Board of Directors adopted a shareholder rights plan on July 7, 1998.

On July 31, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing it had hired Donaldson Lufkin & Jenrette to act as financial advisor in evaluating the Company's various strategic alternatives.

On August 7, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release reporting 1998 second quarter results.

On September 29, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing the declaration of a quarterly cash dividend on the Company's preferred stock and the suspension of cash dividends on its common stock.

On October 7, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release announcing a significant Tuscaloosa discovery.

On October 23, 1998, the Company filed a current report on Form 8-K reporting under Item 5 that the Company issued a press release providing a status report on drilling activity.

On November 9, 1998, the Company filed a current report on Form 8-K announcing that it agreed to tender its 19.9% stake in Pan East Petroleum Corp. to POCO Petroleum Ltd. and agreed to a property exchange with Pan East.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CHESAPEAKE ENERGY CORPORATION  
(Registrant)

November 16, 1998

/s/ Aubrey K. McClendon

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Date

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Aubrey K. McClendon  
Chairman and  
Chief Executive Officer

November 16, 1998

/s/ Marcus C. Rowland

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Date

-----  
Marcus C. Rowland  
Executive Vice President and  
Chief Financial Officer

## Index to Exhibits

Exhibit No. -----	Description -----	Page -----
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4.3.1	Fourth Supplemental Indenture, dated July 1, 1998, to Indenture dated as of April 1, 1996 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors, and United States Trust Company of New York, as Trustee, with respect to 9-1/8% Senior Notes due 2006.	
4.4.1	First Supplemental Indenture, dated July 1, 1998, to Indenture dated as of April 1, 1998 among the Registrant, as issuer, its subsidiaries signatory thereto, as Subsidiary Guarantors, and United States Trust Company of New York, as Trustee, with respect to 9-5/8% Senior Notes due 2005.	
10.2.1	Amended and Restated Employment Agreement dated July 1, 1998 between Aubrey K. McClendon and Chesapeake Energy Corporation.	
10.2.2	Amended and Restated Employment Agreement dated July 1, 1998 between Tom L. Ward and Chesapeake Energy Corporation.	
10.3	Amendment No. 1 dated September 11, 1998 to Rights Agreement dated July 15, 1998 between the Registrant and UMB Bank, N.A., as Rights Agent.	
12	Schedule of Ratios	
27	Financial Data Schedule	

FOURTH SUPPLEMENTAL INDENTURE TO  
INDENTURE DATED MARCH 15, 1997 (7 7/8% SECURITIES)

FOURTH SUPPLEMENTAL INDENTURE dated as of July 1, 1998, among CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), the SUBSIDIARY GUARANTORS listed as signatories hereto, UNITED STATES TRUST COMPANY OF NEW YORK, a New York corporation, as Trustee to the Indenture (as such term is defined in Article I below) and CHESAPEAKE PANHANDLE LIMITED PARTNERSHIP, an Oklahoma limited partnership ("CPLP"), CHESAPEAKE ACQUISITIONS, LTD., an Alberta, Canada corporation ("CAL") and THE AMES COMPANY, INC., an Oklahoma corporation ("TAC").

WHEREAS, the Company, the Subsidiary Guarantors and the Trustee have heretofore entered into the Original Indenture, pursuant to the provisions of which the Company has heretofore issued \$150,000,000 in aggregate principal amount of the Securities;

WHEREAS, CPLP, CAL and TAC are Restricted Subsidiaries of the Company and the parties desire to add CPLP, CAL and TAC as Subsidiary Guarantors under the Indenture;

WHEREAS, Chesapeake Merger Corp., an Oklahoma corporation ("CMC"), Hugoton Energy Corporation, a Kansas corporation ("HEC"), and Hugoton Exploration Corporation, a Kansas corporation ("HEX"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release CMC, HEC and HEX as Subsidiary Guarantors under the Indenture because CMC, HEC and HEX have directly or indirectly merged with and into Chesapeake Mid-Continent Corp., an Oklahoma corporation ("CMCC"), and CMCC is the surviving entity, a Restricted Subsidiary of the Company and a Subsidiary Guarantor under the Indenture;

WHEREAS, HEC Trading Company, a Texas corporation ("HTC"), AmGas Corporation, a Kansas corporation ("AC"), Tiffany Gathering, Inc., a Texas corporation ("TGI"), AnSon Gas Marketing, an Oklahoma general partnership ("AGM"), and Mid-Continent Gas Pipeline Company, an Oklahoma general partnership ("MGPC"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release HTC, AC, TGI, AGM and MGPC as Subsidiary Guarantors under the Indenture because HTC, AC, TGI, AGM and MGPC have directly or indirectly merged with and into Chesapeake Energy Marketing, Inc., an Oklahoma corporation ("CEMI"), and CEMI is the surviving entity and an Unrestricted Subsidiary of the Company and, to the extent required under the Indenture, each such merger has been treated as an Asset Sale under the Indenture;

WHEREAS, Section 9.1 of the Indenture provides, among other things, that the Trustee, the Subsidiary Guarantors and the Company may amend or supplement the Indenture without notice to or consent of any Holder to reflect the addition or release of any Subsidiary Guarantor, as provided for by the Indenture; and

WHEREAS, the execution and delivery of this Fourth Supplemental Indenture have been duly authorized by the Company, the Subsidiary Guarantors, CPLP, CAL and TAC and all actions necessary to make this Fourth Supplemental Indenture a valid and binding instrument according to its terms and the terms of the Original Indenture have been performed.

NOW, THEREFORE, BY THIS FOURTH SUPPLEMENTAL INDENTURE, for and in consideration of the premises and of the mutual covenants herein contained and for other valuable considerations, the receipt whereof is hereby acknowledged, the Company, the Subsidiary Guarantors, CPLP, CAL and TAC covenant and agree with the Trustee, for the equal benefit of all present and future Holders of the Securities, as follows:

#### ARTICLE I

##### DEFINITIONS

SECTION 1.1 The definitions set forth in or incorporated by reference in Article I of the Indenture shall be applicable to this Fourth Supplemental Indenture, as fully and to the same extent as if set forth herein, except as otherwise expressly provided herein. As used in this Fourth Supplemental Indenture, the following terms shall have the following meanings:

"Indenture" means the Original Indenture, as amended by this Fourth Supplemental Indenture, relating to the Securities.

"Original Indenture" means the Indenture dated as of March 15, 1997, among the Company, the Subsidiary Guarantors listed as signatories thereto and the Trustee, relating to the Securities, as amended by: (i) that certain First Supplemental Indenture dated as of December 17, 1997, (ii) that certain Second Supplemental Indenture dated as of February 16, 1998, and (iii) that certain Third Supplemental Indenture dated as of April 22, 1998.

#### ARTICLE II

##### ADDITION OF SUBSIDIARY GUARANTOR

SECTION 2.1 As a Subsidiary Guarantor, each of CPLP, CAL and TAC hereby: (a) jointly and severally, unconditionally guarantees to each Holder and to the Trustee the due and punctual payment of the principal of, premium, if any, and interest on the Securities and all other amounts due and payable under the Indenture and the Securities by the Company, whether at maturity, by acceleration, redemption, repurchase or otherwise including, without

limitation, interest on the overdue principal of, premium, if any, and interest on the Securities to the extent lawful, all in accordance with the terms and subject to the limitations of the Indenture as if each of CPLP, CAL and TAC had been an original party thereto; and (b) subjects each of CPLP, CAL and TAC to the provisions (including the representations and warranties) of the Indenture as a Subsidiary Guarantor.

### ARTICLE III

#### RELEASE OF SUBSIDIARY GUARANTOR

SECTION 3.1 As a result of the direct or indirect merger with CMCC, which constitutes a merger with a Subsidiary Guarantor under Section 10.2(a) of the Indenture, CMC, HEC and HEX shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.4(b) of the Indenture.

SECTION 3.2 As a result of the direct or indirect merger with CEMI, which constitutes an Asset Sale under Section 10.2(b) of the Indenture, HTC, AC, TGI, AGM and MGPC shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.4(b) of the Indenture.

SECTION 3.3 The notation on the Securities relating to the Guarantee shall be deemed to exclude the names of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC and the signature of an Officer on behalf of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC.

### ARTICLE IV

#### ASSUMPTION OF OBLIGATIONS

SECTION 4.1 As the surviving entity in the merger with CMC, HEC and HEX, and as a Subsidiary Guarantor, CMCC hereby agrees to assume all the obligations of CMC, HEC and HEX.

### ARTICLE V

#### MISCELLANEOUS

SECTION 5.1 This Fourth Supplemental Indenture is a supplemental indenture pursuant to Section 9.1 of the Indenture. Upon execution and delivery of this Fourth Supplemental Indenture, the terms and conditions of this Fourth Supplemental Indenture will be part of the terms and conditions of the Indenture for any and all purposes, and all the terms and



conditions of both shall be read together as though they constitute one instrument, except that in case of conflict, the provisions of this Fourth Supplemental Indenture will control.

SECTION 5.2 Except as they have been modified in this Fourth Supplemental Indenture, each and every term and provision of the Indenture shall remain in full force and effect.

SECTION 5.3 This Fourth Supplemental Indenture may be executed in any number of counterparts, each of which when so executed and delivered shall be an original, but such counterparts shall together constitute but one and the same instrument.

SECTION 5.4 This Fourth Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York without giving effect to applicable principals of conflicts of law to the extent that the application of the law of another jurisdiction would be required thereby.

SIGNATURES

IN WITNESS WHEREOF, the parties hereto have caused this Fourth Supplemental Indenture to be duly executed as of the date first written above.

UNITED STATES TRUST COMPANY OF NEW YORK,  
a New York corporation, as Trustee

By /s/ LOUIS P. YOUNG  
-----  
Name: Louis P. Young  
-----  
Title: Vice President  
-----

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive  
Officer

CHESAPEAKE PANHANDLE LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE ACQUISITIONS, LTD., an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

THE AMES COMPANY, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

SUBSIDIARY GUARANTORS

CHESAPEAKE OPERATING, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ENERGY LOUISIANA  
CORPORATION, an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ACQUISITION CORPORATION,  
an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE MID-CONTINENT CORP., an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE GOTHIC CORP., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE CANADA CORPORATION, an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE EXPLORATION LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE LOUISIANA, L.P., an Oklahoma  
limited partnership

By Chesapeake Operating, Inc., an  
Oklahoma corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON

-----  
Aubrey K. McClendon,  
Chief Executive Officer

FOURTH SUPPLEMENTAL INDENTURE TO  
INDENTURE DATED MARCH 15, 1997 (8 1/2% SECURITIES)

FOURTH SUPPLEMENTAL INDENTURE dated as of July 1, 1998, among CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), the SUBSIDIARY GUARANTORS listed as signatories hereto, UNITED STATES TRUST COMPANY OF NEW YORK, a New York corporation, as Trustee to the Indenture (as such term is defined in Article I below) and CHESAPEAKE PANHANDLE LIMITED PARTNERSHIP, an Oklahoma limited partnership ("CPLP"), CHESAPEAKE ACQUISITIONS, LTD., an Alberta, Canada corporation ("CAL") and THE AMES COMPANY, INC., an Oklahoma corporation ("TAC").

WHEREAS, the Company, the Subsidiary Guarantors and the Trustee have heretofore entered into the Original Indenture, pursuant to the provisions of which the Company has heretofore issued \$150,000,000 in aggregate principal amount of the Securities;

WHEREAS, CPLP, CAL and TAC are Restricted Subsidiaries of the Company and the parties desire to add CPLP, CAL and TAC as Subsidiary Guarantors under the Indenture;

WHEREAS, Chesapeake Merger Corp., an Oklahoma corporation ("CMC"), Hugoton Energy Corporation, a Kansas corporation ("HEC"), and Hugoton Exploration Corporation, a Kansas corporation ("HEX"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release CMC, HEC and HEX as Subsidiary Guarantors under the Indenture because CMC, HEC and HEX have directly or indirectly merged with and into Chesapeake Mid-Continent Corp., an Oklahoma corporation ("CMCC"), and CMCC is the surviving entity, a Restricted Subsidiary of the Company and a Subsidiary Guarantor under the Indenture;

WHEREAS, HEC Trading Company, a Texas corporation ("HTC"), AmGas Corporation, a Kansas corporation ("AC"), Tiffany Gathering, Inc., a Texas corporation ("TGI"), AnSon Gas Marketing, an Oklahoma general partnership ("AGM"), and Mid-Continent Gas Pipeline Company, an Oklahoma general partnership ("MGPC"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release HTC, AC, TGI, AGM and MGPC as Subsidiary Guarantors under the Indenture because HTC, AC, TGI, AGM and MGPC have directly or indirectly merged with and into Chesapeake Energy Marketing, Inc., an Oklahoma corporation ("CEMI"), and CEMI is the surviving entity and an Unrestricted Subsidiary of the Company and, to the extent required under the Indenture, each such merger has been treated as an Asset Sale under the Indenture;

WHEREAS, Section 9.1 of the Indenture provides, among other things, that the Trustee, the Subsidiary Guarantors and the Company may amend or supplement the Indenture without notice to or consent of any Holder to reflect the addition or release of any Subsidiary Guarantor, as provided for by the Indenture; and

WHEREAS, the execution and delivery of this Fourth Supplemental Indenture have been duly authorized by the Company, the Subsidiary Guarantors, CPLP, CAL and TAC and all actions necessary to make this Fourth Supplemental Indenture a valid and binding instrument according to its terms and the terms of the Original Indenture have been performed.

NOW, THEREFORE, BY THIS FOURTH SUPPLEMENTAL INDENTURE, for and in consideration of the premises and of the mutual covenants herein contained and for other valuable considerations, the receipt whereof is hereby acknowledged, the Company, the Subsidiary Guarantors, CPLP, CAL and TAC covenant and agree with the Trustee, for the equal benefit of all present and future Holders of the Securities, as follows:

#### ARTICLE I

##### DEFINITIONS

SECTION 1.1 The definitions set forth in or incorporated by reference in Article I of the Indenture shall be applicable to this Fourth Supplemental Indenture, as fully and to the same extent as if set forth herein, except as otherwise expressly provided herein. As used in this Fourth Supplemental Indenture, the following terms shall have the following meanings:

"Indenture" means the Original Indenture, as amended by this Fourth Supplemental Indenture, relating to the Securities.

"Original Indenture" means the Indenture dated as of March 15, 1997, among the Company, the Subsidiary Guarantors listed as signatories thereto and the Trustee, relating to the Securities, as amended by: (i) that certain First Supplemental Indenture dated as of December 17, 1997, (ii) that certain Second Supplemental Indenture dated as of February 16, 1998, and (iii) that certain Third Supplemental Indenture dated as of April 22, 1998.

#### ARTICLE II

##### ADDITION OF SUBSIDIARY GUARANTOR

SECTION 2.1 As a Subsidiary Guarantor, each of CPLP, CAL and TAC hereby: (a) jointly and severally, unconditionally guarantees to each Holder and to the Trustee the due and punctual payment of the principal of, premium, if any, and interest on the Securities and all other amounts due and payable under the Indenture and the Securities by the Company, whether at maturity, by acceleration, redemption, repurchase or otherwise including, without

limitation, interest on the overdue principal of, premium, if any, and interest on the Securities to the extent lawful, all in accordance with the terms and subject to the limitations of the Indenture as if each of CPLP, CAL and TAC had been an original party thereto; and (b) subjects each of CPLP, CAL and TAC to the provisions (including the representations and warranties) of the Indenture as a Subsidiary Guarantor.

### ARTICLE III

#### RELEASE OF SUBSIDIARY GUARANTOR

SECTION 3.1 As a result of the direct or indirect merger with CMCC, which constitutes a merger with a Subsidiary Guarantor under Section 10.2(a) of the Indenture, CMC, HEC and HEX shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.4(b) of the Indenture.

SECTION 3.2 As a result of the direct or indirect merger with CEMI, which constitutes an Asset Sale under Section 10.2(b) of the Indenture, HTC, AC, TGI, AGM and MGPC shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.4(b) of the Indenture.

SECTION 3.3 The notation on the Securities relating to the Guarantee shall be deemed to exclude the names of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC and the signature of an Officer on behalf of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC.

### ARTICLE IV

#### ASSUMPTION OF OBLIGATIONS

SECTION 4.1 As the surviving entity in the merger with CMC, HEC and HEX, and as a Subsidiary Guarantor, CMCC hereby agrees to assume all the obligations of CMC, HEC and HEX.

### ARTICLE V

#### MISCELLANEOUS

SECTION 5.1 This Fourth Supplemental Indenture is a supplemental indenture pursuant to Section 9.1 of the Indenture. Upon execution and delivery of this Fourth Supplemental Indenture, the terms and conditions of this Fourth Supplemental Indenture will be part of the terms and conditions of the Indenture for any and all purposes, and all the terms and

conditions of both shall be read together as though they constitute one instrument, except that in case of conflict, the provisions of this Fourth Supplemental Indenture will control.

SECTION 5.2 Except as they have been modified in this Fourth Supplemental Indenture, each and every term and provision of the Indenture shall remain in full force and effect.

SECTION 5.3 This Fourth Supplemental Indenture may be executed in any number of counterparts, each of which when so executed and delivered shall be an original, but such counterparts shall together constitute but one and the same instrument.

SECTION 5.4 This Fourth Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York without giving effect to applicable principals of conflicts of law to the extent that the application of the law of another jurisdiction would be required thereby.

SIGNATURES

IN WITNESS WHEREOF, the parties hereto have caused this Fourth Supplemental Indenture to be duly executed as of the date first written above.

UNITED STATES TRUST COMPANY OF NEW YORK,  
a New York corporation, as Trustee

By /s/ LOUIS P. YOUNG  
-----  
Name: Louis P. Young  
-----  
Title: Vice President  
-----

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive  
Officer



CHESAPEAKE PANHANDLE LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE ACQUISITIONS, LTD., an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

THE AMES COMPANY, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

SUBSIDIARY GUARANTORS

CHESAPEAKE OPERATING, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ENERGY LOUISIANA  
CORPORATION, an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ACQUISITION CORPORATION,  
an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE MID-CONTINENT CORP., an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE GOTHIC CORP., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE CANADA CORPORATION, an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE EXPLORATION LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE LOUISIANA, L.P., an Oklahoma  
limited partnership

By Chesapeake Operating, Inc., an  
Oklahoma corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON

-----  
Aubrey K. McClendon,  
Chief Executive Officer

FOURTH SUPPLEMENTAL INDENTURE TO  
INDENTURE DATED APRIL 1, 1996

FOURTH SUPPLEMENTAL INDENTURE dated as of July 1, 1998, among CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), the SUBSIDIARY GUARANTORS listed as signatories hereto, UNITED STATES TRUST COMPANY OF NEW YORK, a New York corporation, as Trustee to the Indenture (as such term is defined in Article I below) and CHESAPEAKE PANHANDLE LIMITED PARTNERSHIP, an Oklahoma limited partnership ("CPLP"), CHESAPEAKE ACQUISITIONS, LTD., an Alberta, Canada corporation ("CAL") and THE AMES COMPANY, INC., an Oklahoma corporation ("TAC").

WHEREAS, the Company, the Subsidiary Guarantors and the Trustee have heretofore entered into the Original Indenture, pursuant to the provisions of which the Company has heretofore issued \$120,000,000 in aggregate principal amount of the Securities;

WHEREAS, CPLP, CAL and TAC are Restricted Subsidiaries of the Company and the parties desire to add CPLP, CAL and TAC as Subsidiary Guarantors under the Indenture;

WHEREAS, Chesapeake Merger Corp., an Oklahoma corporation ("CMC"), Hugoton Energy Corporation, a Kansas corporation ("HEC"), and Hugoton Exploration Corporation, a Kansas corporation ("HEX"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release CMC, HEC and HEX as Subsidiary Guarantors under the Indenture because CMC, HEC and HEX have directly or indirectly merged with and into Chesapeake Mid-Continent Corp., an Oklahoma corporation ("CMCC"), and CMCC is the surviving entity, a Restricted Subsidiary of the Company and a Subsidiary Guarantor under the Indenture;

WHEREAS, HEC Trading Company, a Texas corporation ("HTC"), AmGas Corporation, a Kansas corporation ("AC"), Tiffany Gathering, Inc., a Texas corporation ("TGI"), AnSon Gas Marketing, an Oklahoma general partnership ("AGM"), and Mid-Continent Gas Pipeline Company, an Oklahoma general partnership ("MGPC"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release HTC, AC, TGI, AGM and MGPC as Subsidiary Guarantors under the Indenture because HTC, AC, TGI, AGM and MGPC have directly or indirectly merged with and into Chesapeake Energy Marketing, Inc., an Oklahoma corporation ("CEMI"), and CEMI is the surviving entity and an Unrestricted Subsidiary of the Company and, to the extent required under the Indenture, each such merger has been treated as an Asset Sale under the Indenture;

WHEREAS, Section 9.01 of the Indenture provides, among other things, that the Trustee, the Subsidiary Guarantors and the Company may amend or supplement the Indenture without notice to or consent of any Holder to reflect the addition or release of any Subsidiary Guarantor, as provided for by the Indenture; and

WHEREAS, the execution and delivery of this Fourth Supplemental Indenture have been duly authorized by the Company, the Subsidiary Guarantors, CPLP, CAL and TAC and all actions necessary to make this Fourth Supplemental Indenture a valid and binding instrument according to its terms and the terms of the Original Indenture have been performed.

NOW, THEREFORE, BY THIS FOURTH SUPPLEMENTAL INDENTURE, for and in consideration of the premises and of the mutual covenants herein contained and for other valuable considerations, the receipt whereof is hereby acknowledged, the Company, the Subsidiary Guarantors, CPLP, CAL and TAC covenant and agree with the Trustee, for the equal benefit of all present and future Holders of the Securities, as follows:

#### ARTICLE I

##### DEFINITIONS

SECTION 1.1 The definitions set forth in or incorporated by reference in Article I of the Indenture shall be applicable to this Fourth Supplemental Indenture, as fully and to the same extent as if set forth herein, except as otherwise expressly provided herein. As used in this Fourth Supplemental Indenture, the following terms shall have the following meanings:

"Indenture" means the Original Indenture, as amended by this Fourth Supplemental Indenture, relating to the Securities.

"Original Indenture" means the Indenture dated as of April 1, 1996, among the Company, the Subsidiary Guarantors listed as signatories thereto and the Trustee, relating to the Securities, as amended by: (i) that certain First Supplemental Indenture dated as of December 30, 1996, (ii) that certain Second Supplemental Indenture dated as of December 17, 1997, and (iii) that certain Third Supplemental Indenture dated as of April 22, 1998.

#### ARTICLE II

##### ADDITION OF SUBSIDIARY GUARANTOR

SECTION 2.1 As a Subsidiary Guarantor, each of CPLP, CAL and TAC hereby: (a) jointly and severally, unconditionally guarantees to each Holder and to the Trustee the due and punctual payment of the principal of, premium, if any, and interest on the Securities and all other amounts due and payable under the Indenture and the Securities by the Company, whether at maturity, by acceleration, redemption, repurchase or otherwise including, without

limitation, interest on the overdue principal of, premium, if any, and interest on the Securities to the extent lawful, all in accordance with the terms and subject to the limitations of the Indenture as if each of CPLP, CAL and TAC had been an original party thereto; and (b) subjects each of CPLP, CAL and TAC to the provisions (including the representations and warranties) of the Indenture as a Subsidiary Guarantor.

### ARTICLE III

#### RELEASE OF SUBSIDIARY GUARANTOR

SECTION 3.1 As a result of the direct or indirect merger with CMCC, which constitutes a merger with a Subsidiary Guarantor under Section 10.02(a) of the Indenture, CMC, HEC and HEX shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.04 of the Indenture.

SECTION 3.2 As a result of the direct or indirect merger with CEMI, which constitutes an Asset Sale under Section 10.02(b) of the Indenture, HTC, AC, TGI, AGM and MGPC shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.04 of the Indenture.

SECTION 3.3 The notation on the Securities relating to the Guarantee shall be deemed to exclude the names of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC and the signature of an Officer on behalf of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC.

### ARTICLE IV

#### ASSUMPTION OF OBLIGATIONS

SECTION 4.1 As the surviving entity in the merger with CMC, HEC and HEX, and as a Subsidiary Guarantor, CMCC hereby agrees to assume all the obligations of CMC, HEC and HEX.

### ARTICLE V

#### MISCELLANEOUS

SECTION 5.1 This Fourth Supplemental Indenture is a supplemental indenture pursuant to Section 9.01 of the Indenture. Upon execution and delivery of this Fourth Supplemental Indenture, the terms and conditions of this Fourth Supplemental Indenture will be part of the terms and conditions of the Indenture for any and all purposes, and all the terms and

conditions of both shall be read together as though they constitute one instrument, except that in case of conflict, the provisions of this Fourth Supplemental Indenture will control.

SECTION 5.2 Except as they have been modified in this Fourth Supplemental Indenture, each and every term and provision of the Indenture shall remain in full force and effect.

SECTION 5.3 This Fourth Supplemental Indenture may be executed in any number of counterparts, each of which when so executed and delivered shall be an original, but such counterparts shall together constitute but one and the same instrument.

SECTION 5.4 This Fourth Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York without giving effect to applicable principals of conflicts of law to the extent that the application of the law of another jurisdiction would be required thereby.

SIGNATURES

IN WITNESS WHEREOF, the parties hereto have caused this Fourth Supplemental Indenture to be duly executed as of the date first written above.

UNITED STATES TRUST COMPANY OF NEW YORK,  
a New York corporation, as Trustee

By /s/ LOUIS P. YOUNG

-----  
Name: Louis P. Young

-----  
Title: Vice President  
-----

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON

-----  
Aubrey K. McClendon, Chief Executive  
Officer

CHESAPEAKE PANHANDLE LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE ACQUISITIONS, LTD., an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

THE AMES COMPANY, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

SUBSIDIARY GUARANTORS

CHESAPEAKE OPERATING, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ENERGY LOUISIANA  
CORPORATION, an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer



CHESAPEAKE ACQUISITION CORPORATION,  
an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE MID-CONTINENT CORP., an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE GOTHIC CORP., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE CANADA CORPORATION, an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE EXPLORATION LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE LOUISIANA, L.P., an Oklahoma  
limited partnership

By Chesapeake Operating, Inc., an  
Oklahoma corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON

-----  
Aubrey K. McClendon,  
Chief Executive Officer

FIRST SUPPLEMENTAL INDENTURE TO  
INDENTURE DATED APRIL 1, 1998

FIRST SUPPLEMENTAL INDENTURE dated as of July 1, 1998, among CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), the SUBSIDIARY GUARANTORS listed as signatories hereto, UNITED STATES TRUST COMPANY OF NEW YORK, a New York corporation, as Trustee to the Indenture (as such term is defined in Article I below) and CHESAPEAKE PANHANDLE LIMITED PARTNERSHIP, an Oklahoma limited partnership ("CPLP"), CHESAPEAKE ACQUISITIONS, LTD., an Alberta, Canada corporation ("CAL") and THE AMES COMPANY, INC., an Oklahoma corporation ("TAC").

WHEREAS, the Company, the Subsidiary Guarantors and the Trustee have heretofore entered into the Original Indenture, pursuant to the provisions of which the Company has heretofore issued \$500,000,000 in aggregate principal amount of the Securities;

WHEREAS, CPLP, CAL and TAC are Restricted Subsidiaries of the Company and the parties desire to add CPLP, CAL and TAC as Subsidiary Guarantors under the Indenture;

WHEREAS, Chesapeake Merger Corp., an Oklahoma corporation ("CMC"), Hugoton Energy Corporation, a Kansas corporation ("HEC"), and Hugoton Exploration Corporation, a Kansas corporation ("HEX"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release CMC, HEC and HEX as Subsidiary Guarantors under the Indenture because CMC, HEC and HEX have directly or indirectly merged with and into Chesapeake Mid-Continent Corp., an Oklahoma corporation ("CMCC"), and CMCC is the surviving entity, a Restricted Subsidiary of the Company and a Subsidiary Guarantor under the Indenture;

WHEREAS, HEC Trading Company, a Texas corporation ("HTC"), AmGas Corporation, a Kansas corporation ("AC"), Tiffany Gathering, Inc., a Texas corporation ("TGI"), AnSon Gas Marketing, an Oklahoma general partnership ("AGM"), and Mid-Continent Gas Pipeline Company, an Oklahoma general partnership ("MGPC"), are Restricted Subsidiaries of the Company and Subsidiary Guarantors under the Indenture;

WHEREAS, the parties desire to release HTC, AC, TGI, AGM and MGPC as Subsidiary Guarantors under the Indenture because HTC, AC, TGI, AGM and MGPC have directly or indirectly merged with and into Chesapeake Energy Marketing, Inc., an Oklahoma corporation ("CEMI"), and CEMI is the surviving entity and an Unrestricted Subsidiary of the Company and, to the extent required under the Indenture, each such merger has been treated as an Asset Sale under the Indenture;

WHEREAS, Section 9.01 of the Indenture provides, among other things, that the Trustee, the Subsidiary Guarantors and the Company may amend or supplement the Indenture without notice to or consent of any Holder to reflect the addition or release of any Subsidiary Guarantor, as provided for by the Indenture; and

WHEREAS, the execution and delivery of this First Supplemental Indenture have been duly authorized by the Company, the Subsidiary Guarantors, CPLP, CAL and TAC and all actions necessary to make this First Supplemental Indenture a valid and binding instrument according to its terms and the terms of the Original Indenture have been performed.

NOW, THEREFORE, BY THIS FIRST SUPPLEMENTAL INDENTURE, for and in consideration of the premises and of the mutual covenants herein contained and for other valuable considerations, the receipt whereof is hereby acknowledged, the Company, the Subsidiary Guarantors, CPLP, CAL and TAC covenant and agree with the Trustee, for the equal benefit of all present and future Holders of the Securities, as follows:

#### ARTICLE I

##### DEFINITIONS

SECTION 1.1 The definitions set forth in or incorporated by reference in Article I of the Indenture shall be applicable to this First Supplemental Indenture, as fully and to the same extent as if set forth herein, except as otherwise expressly provided herein. As used in this First Supplemental Indenture, the following terms shall have the following meanings:

"Indenture" means the Original Indenture, as amended by this First Supplemental Indenture, relating to the Securities.

"Original Indenture" means the Indenture dated as of April 1, 1998, among the Company, the Subsidiary Guarantors listed as signatories thereto and the Trustee, relating to the Securities.

#### ARTICLE II

##### ADDITION OF SUBSIDIARY GUARANTOR

SECTION 2.1 As a Subsidiary Guarantor, each of CPLP, CAL and TAC hereby: (a) jointly and severally, unconditionally guarantees to each Holder and to the Trustee the due and punctual payment of the principal of, premium, if any, and interest on the Securities and all other amounts due and payable under the Indenture and the Securities by the Company, whether at maturity, by acceleration, redemption, repurchase or otherwise including, without limitation, interest on the overdue principal of, premium, if any, and interest on the Securities to the extent lawful, all in accordance with the terms and subject to the limitations of the

Indenture as if each of CPLP, CAL and TAC had been an original party thereto; and (b) subjects each of CPLP, CAL and TAC to the provisions (including the representations and warranties) of the Indenture as a Subsidiary Guarantor.

### ARTICLE III

#### RELEASE OF SUBSIDIARY GUARANTOR

SECTION 3.1 As a result of the direct or indirect merger with CMCC, which constitutes a merger with a Subsidiary Guarantor under Section 10.02(a) of the Indenture, CMC, HEC and HEX shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.04 of the Indenture.

SECTION 3.2 As a result of the direct or indirect merger with CEMI, which constitutes an Asset Sale under Section 10.02(b) of the Indenture, HTC, AC, TGI, AGM and MGPC shall for all purposes be released as a Subsidiary Guarantor from all of their Guarantee and related obligations in the Indenture, pursuant to Section 10.04 of the Indenture.

SECTION 3.3 The notation on the Securities relating to the Guarantee shall be deemed to exclude the names of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC and the signature of an Officer on behalf of CMC, HEC, HEX, HTC, AC, TGI, AGM and MGPC.

### ARTICLE IV

#### ASSUMPTION OF OBLIGATIONS

SECTION 4.1 As the surviving entity in the merger with CMC, HEC and HEX, and as a Subsidiary Guarantor, CMCC hereby agrees to assume all the obligations of CMC, HEC and HEX.

### ARTICLE V

#### MISCELLANEOUS

SECTION 5.1 This First Supplemental Indenture is a supplemental indenture pursuant to Section 9.01 of the Indenture. Upon execution and delivery of this First Supplemental Indenture, the terms and conditions of this First Supplemental Indenture will be part of the terms and conditions of the Indenture for any and all purposes, and all the terms and conditions of both shall be read together as though they constitute one instrument, except that in case of conflict, the provisions of this First Supplemental Indenture will control.

SECTION 5.2 Except as they have been modified in this First Supplemental Indenture, each and every term and provision of the Indenture shall remain in full force and effect.

SECTION 5.3 This First Supplemental Indenture may be executed in any number of counterparts, each of which when so executed and delivered shall be an original, but such counterparts shall together constitute but one and the same instrument.

SECTION 5.4 This First Supplemental Indenture shall be governed by and construed in accordance with the laws of the State of New York without giving effect to applicable principals of conflicts of law to the extent that the application of the law of another jurisdiction would be required thereby.

SIGNATURES

IN WITNESS WHEREOF, the parties hereto have caused this First Supplemental Indenture to be duly executed as of the date first written above.

UNITED STATES TRUST COMPANY OF NEW YORK,  
a New York corporation, as Trustee

By /s/ LOUIS P. YOUNG  
-----  
Name: Louis P. Young  
-----  
Title: Vice President  
-----

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive  
Officer

CHESAPEAKE PANHANDLE LIMITED  
PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma  
corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE ACQUISITIONS, LTD., an  
Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

THE AMES COMPANY, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

SUBSIDIARY GUARANTORS

CHESAPEAKE OPERATING, INC., an Oklahoma  
corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ENERGY LOUISIANA  
CORPORATION, an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE ACQUISITION CORPORATION,  
an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
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Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE MID-CONTINENT CORP., an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
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Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE GOTHIC CORP., an Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE CANADA CORPORATION, an Alberta, Canada corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer

CHESAPEAKE EXPLORATION LIMITED PARTNERSHIP, an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
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Aubrey K. McClendon,  
Chief Executive Officer

CHESAPEAKE LOUISIANA, L.P., an Oklahoma limited partnership

By Chesapeake Operating, Inc., an Oklahoma corporation, Sole General Partner

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon,  
Chief Executive Officer



AMENDED AND RESTATED  
EMPLOYMENT AGREEMENT

between

AUBREY K. McCLENDON

and

CHESAPEAKE ENERGY CORPORATION

Effective July 1, 1998

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AMENDED AND RESTATED  
EMPLOYMENT AGREEMENT

THIS AGREEMENT is made effective July 1, 1998, between CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), and AUBREY K. McCLENDON, an individual (the "Executive").

W I T N E S S E T H:

WHEREAS, the Company and the Executive entered into that certain employment agreement dated effective July 1, 1997 (the "Prior Agreement");

WHEREAS, the Company has announced that it would explore strategic alternatives to increase shareholder value, and to retain employees during that process the Company adopted a retention program for the Company's key employees other than the senior executive officers;

WHEREAS, for the reasons the Company adopted the retention program for the other employees, the Board of Directors of the Company believes that it is in the best interests of the Company to provide for the retention of the Executive as part of the process of exploring the Company's strategic alternatives; and

WHEREAS, the Company and the Executive desire to amend and restate the Prior Agreement in its entirety.

NOW, THEREFORE, in consideration of the mutual promises herein contained, the Company and the Executive agree as follows:

1. Employment. The Company hereby employs the Executive and the Executive hereby accepts such employment subject to the terms and conditions contained in this Agreement. The Executive is engaged as an employee of the Company, and the Executive and the Company do not intend to create a joint venture, partnership or other relationship which might impose a fiduciary obligation on the Executive or the Company in the performance of this Agreement.

2. Executive's Duties. The Executive is employed on a full-time basis. Throughout the term of this Agreement, the Executive will use the Executive's best efforts and due diligence to assist the Company in achieving the most profitable operation of the Company and the Company's affiliated entities consistent with developing and maintaining a quality business operation.

2.1 Specific Duties. The Executive will serve as Chairman of the Board and Chief Executive Officer for the Company. From time to time, the Executive may be appointed as an officer of one (1) or more of the Company's subsidiaries. During the term of this Agreement, the Executive will be nominated for election or appointed to serve as a director of the Company and one (1) or more of the Company's subsidiaries. The Executive will use the Executive's best efforts to perform all of the services required to fully and faithfully execute the offices and positions to which the Executive is appointed and such other services as may be reasonably directed by the board of directors of the Company in accordance with this Agreement.

- 2.2 Modifications. The precise duties to be performed by the Executive may be extended or curtailed in the discretion of the respective boards of directors of the Company. However, except for termination for cause under paragraph 6.1.2 of this Agreement, the failure of the Executive to be elected, be reelected or serve as a director of the Company during the term of this Agreement, the removal of the Executive as a member of the board of directors of the Company, the withdrawal of the designation of the Executive as Chairman of the Board or Chief Executive Officer of the Company, or the assignment of the performance of duties incumbent on the foregoing offices to other persons without the prior written consent of the Executive will constitute termination without cause by the Company.
- 2.3 Rules and Regulations. The Company currently has an Employment Policies Manual which addresses frequently asked questions regarding the Company. The Executive agrees to comply with the Employment Policies Manual except to the extent inconsistent with this Agreement. The Employment Policies Manual is subject to change without notice in the sole discretion of the Company at any time. In the event of a conflict between the Employment Policies Manual and this Agreement, this Agreement will control over the terms of the Employment Policies Manual.
- 2.4 Stock Investment. For each calendar year during the term of this Agreement the Executive agrees to hold shares of the Company's common stock having an aggregate Investment Value (as hereafter defined) equal to five hundred percent (500%) of the compensation paid to the Executive under paragraphs 4.1 and 4.2 of this Agreement during such calendar year. Any shares of common stock acquired by the Executive prior to the date of this Agreement and still owned by the Executive during the term of this Agreement may be used to satisfy this requirement to own common stock. For purposes of this paragraph, the "Investment Value" of each share of stock will be as follows: (a) for shares purchased in the open market the price paid by the Executive for such shares; (b) for shares acquired through the exercise of stock options, the fair market value of the common stock on the date the option was exercised; and (c) for shares acquired other than through open market purchases or the exercise of options the fair market value of the Company's common stock on the date of the acquisition of such common stock. The stock acquired or owned pursuant to this paragraph 2.4 must be held by the Executive at all times during the Executive's employment by the Company or the Company's affiliated entities. In order to administer this provision, the Executive agrees to deliver to the Company's Chief Executive Officer a semi-annual report of purchases and ownership in a form prepared by the Company. This paragraph will become null and void if the Company's common stock ceases to be listed on the New York Stock Exchange, the National Association of Securities Dealers Automated Quotation System or other national exchange. The Company has no obligation to sell or to purchase from the Executive any of the Company's stock in connection with this paragraph 2.4 and has made no representations or warranties regarding the Company's stock, operations or financial condition.

3. Other Activities. Except for the activities (the "Permitted Activities") expressly permitted by paragraphs 3.1 and 3.2 of this Agreement, or the prior written approval of the board of directors of the Company, the Executive will not: (a) engage in business independent of the Executive's employment by the Company which requires any substantial portion of the Executive's time; (b) serve as an officer or director of any corporation, partnership, company, or firm; (c) except for passive investments that do not violate this Agreement and require a minimal portion of the Executive's time, serve as a general partner or member of any corporation, partnership, company or firm; or (d) directly or indirectly invest in, participate in or acquire an interest in any oil and gas business, including, without limitation, (i) producing oil and gas, (ii) drilling, owning or operating oil and gas leases or wells, (iii) providing services or materials to the oil and gas industry, (iv) marketing or refining oil or gas, or (v) owning any interest in any corporation, partnership, company or entity which conducts any of the foregoing activities. The limitations in this paragraph 3 will not prohibit an investment by the Executive in publicly traded securities. Notwithstanding the foregoing, the Executive will be permitted to participate in the following activities which will be deemed to be approved by the Company, if such activities are undertaken in strict compliance with this Agreement.

3.1 Company's Activities. The Executive or the Executive's designated affiliate will be permitted to acquire a working interest in all of the wells spudded by the Company or the Company's subsidiary corporations, partnerships or entities (the "Program Wells") on the terms and conditions set forth herein in any Calendar Quarter (as hereafter defined) during the Participation Term (as hereafter defined). The Program Wells include any well spudded during such Calendar Quarter in which the Company or the Company's subsidiary corporations, partnerships or entities participate as a nonoperator.

3.1.1 Amount of Participation. On or before the date which is thirty (30) days before the first (1st) day of each Calendar Quarter, the Executive will provide notice to the compensation committee of the Company's board of directors of the Executive's intent to participate in the Program Wells during the succeeding Calendar Quarter and the approximate percentage working interest which the Executive proposes to participate with during such Calendar Quarter (the "Approved Percentage"). The Executive's Approved Percentage working interest participation (determined without consideration of any carried interest) in the Program Wells for any Calendar Quarter will not exceed two and one-half percent (2.5%) on an eight- eighths (8/8ths) basis. On designation of the Approved Percentage for a Calendar Quarter, the Executive will be deemed to have elected to participate in each Program Well spudded during such Calendar Quarter with a working interest equal to the following applicable percentage determined on a well-by-well basis (the "Minimum Participation"): (a) the

Approved Percentage for each Operations Well, each Program Well which does not fall within clause (b) of this paragraph 3.1.1 and any Program Well which does not fall within clause (c) of this paragraph 3.1.1; (b) zero percent (0%) if the combined participation in the Program Well by the Executive, Mr. Tom L. Ward and Mr. Marcus C. Rowland with such individuals' Approved Percentage under their respective employment agreements causes the Company's working interest (determined without consideration of any carried interest) on the spud date for such Program Well to be less than twelve and one-half percent (12.5%) on an eight eighths (8/8ths) basis; or (c) subsequent to a termination under paragraphs 6.1.1 or 6.3 of this Agreement the lowest Approved Percentage elected by the Executive subsequent to such termination. If clause (b) of this paragraph 3.1.1 prohibits the Executive's participation in a Program Well, then Messrs. Ward and Rowland will not be entitled to participate in such Program Well under their employment agreements. An "Operations Well" means a Program Well which falls within the provisions of clause (b) of this paragraph 3.1.1, but for which the Executive's participation is deemed necessary for the Company to retain operations as determined by the disinterested members of the compensation committee of the Company's board of directors. If the Executive fails to provide notice of the Executive's intent to participate and the Executive's proposed participation prior to the specified date as provided herein, the amount of the Approved Percentage for the Calendar Quarter will be deemed to be zero (0).

- 3.1.2 Conditions of Participation. The Participation by the Executive in each Program Well will be on no better terms than the terms agreed to by unaffiliated third party participants in connection with the acquisition of an interest in such Program Well from the Company or its subsidiary corporations, partnerships or entities. The Approved Percentage cannot be changed during any Calendar Quarter without the prior approval of the disinterested members of the compensation committee of the Company's board of directors. Any participation by the Executive under this paragraph 3.1 is also conditioned upon the Executive's participation in each Program Well spudded during such Calendar Quarter in an amount equal to the Minimum Participation. The Executive hereby agrees to execute and deliver any documents reasonably requested by the Company and hereby appoints the Company as the Executive's agent and attorney-in-fact to execute and deliver such documents if the Executive fails or refuses to execute such documents. The Executive further agrees to pay all joint interest billings within one hundred fifty (150) days after receipt. For purposes of this Agreement, the term: (a) "Calendar Quarter" means the three (3) month periods commencing on the first (1st) day of January, April, July and October; and (b) "Participation Term" means the term of this Agreement plus five (5) years after a termination under paragraphs 6.1.1 or 6.3 of this Agreement.

3.2 Other Activities. The Executive currently conducts oil and gas investment activities individually and through Chesapeake Investments, an Oklahoma Limited Partnership ("Investments"), Chesapeake Production Company, an Oklahoma corporation ("Production"), and Chesapeake/Wood Joint Venture ("Venture"). The Executive will be permitted to continue oil and gas activities in such entities but only to the extent such activities are conducted on oil and gas leases or interests owned by the Executive, Investments, Production or Venture as of July 1, 1995, or acquired by Investments, Production or Venture from the Company. The interests acquired by Investments shall be limited by the provisions of paragraph 3.1 of this Agreement. The Company also consents to the Executive serving: (a) as a director of American Bank and Trust Company located in Edmond, Oklahoma; (b) as a director of Pan East Petroleum Corp., an Ontario Canada corporation, pursuant to approval by the board of directors.

4. Executive's Compensation. The Company agrees to compensate the Executive as follows:

- 4.1 Base Salary. A base salary (the "Base Salary"), at the initial annual rate of not less than Three Hundred Fifty Thousand Dollars (\$350,000.00), will be paid to the Executive in equal semi-monthly installments beginning July 15, 1998 during the term of this Agreement.
- 4.2 Bonus. In addition to the Base Salary described at paragraph 4.1 of this Agreement, the Company may periodically pay bonus compensation to the Executive. Any bonus compensation will be at the absolute discretion of the Company in such amounts and at such times as the board of directors of the Company may determine.
- 4.3 Stock Options. In addition to the compensation set forth in paragraphs 4.1 and 4.2 of this Agreement, the Executive may periodically receive grants of stock options from the Company's various stock option plans, subject to the terms and conditions thereof.
- 4.4 Benefits. The Company will provide the Executive such retirement benefits, reimbursement of reasonable expenditures for dues, travel and entertainment and other benefits on terms customarily provided by the Company from time to time. The Company will also provide the Executive the opportunity to apply for coverage under the Company's medical, life and disability plans, if any. If the Executive is accepted for coverage under such plans, the Company will provide such coverage on the same terms as is customarily provided by the Company to the plan participants as modified from time to time. The following specific benefits will also be provided to the Executive at the expense of the Company:



- 4.4.1 Vacation. The Executive will be entitled to take three (3) weeks of paid vacation each calendar year during the term of this Agreement. No additional compensation will be paid for failure to take vacation and no vacation may be carried forward from one calendar year to another.
- 4.4.2 Membership Dues. The Company will reimburse the Executive for: (a) the monthly dues necessary to maintain a full membership in (1) golf and/or country club in the Oklahoma City area selected by the Executive; and (b) the reasonable cost of any qualified business entertainment at such country club. All other costs, including, without implied limitation, any initiation costs, initial membership costs, personal use and business entertainment unrelated to the Company will be the sole obligation of the Executive and the Company will have no liability with respect to such amounts.
- 4.4.3 Automobile and Travel Allowance. The Executive will receive a monthly cash allowance in the amount of One Thousand Five Hundred Dollars (\$1,500.00) to defer a portion of the Executive's cost of acquiring, operating and maintaining an automobile for use in the Executive's employment. Additionally, the Executive will be entitled to utilize any aircraft owned by the Company (whether in whole or in part) for personal use and will not be required to reimburse the Company for any cost related to such use or pay any cost or charge with respect to such use up to an amount during any calendar year equal to the Aircraft Allowance. For purposes of this Agreement the term "Aircraft Allowance" means the variable costs directly identifiable with each use (including fuel, pilot charges, landing fees, hourly charges under co-ownership arrangements and other such costs) but specifically excludes any fixed costs of the aircraft (including acquisition costs and depreciation). The Aircraft Allowance will be equal to \$40,000.00 for the Company's fiscal year ending on June 30, 1998, \$25,000.00 for the six month period ending on December 31, 1998, and \$50,000.00 for each fiscal year thereafter during the term of this Agreement. If the Executive's use of the Company's aircraft exceeds the Aircraft Allowance during any fiscal year the Executive will be required to reimburse the Company for the variable costs directly identified with each such use.
- 4.4.4 Accounting Support. The Executive will be permitted to utilize the Company's office space, computer facilities and the equivalent of one (1) full-time accounting employee of the Company (presently Ms. Linda Peterburs) to maintain books and records for the Executive and the Executive's Permitted Activities. The Executive will not be required to pay any compensation to the Company in connection with such accounting services.

- 4.5 Compensation Review. The compensation of the Executive will be reviewed not less frequently than annually by the board of directors of the Company. The compensation of the Executive prescribed by paragraph 4 of this Agreement may be increased at the discretion of the Company, but may not be reduced without the prior written consent of the Executive.

5. Term. In the absence of termination as set forth in paragraph 6 below, this Agreement will extend for a term of five (5) years commencing on July 1, 1998, and ending on June 30, 2003 (the "Expiration Date") as extended from time to time. Unless the Company provides thirty (30) days prior written notice of nonextension to the Executive, on each June 30 during the term of this Agreement, the term and the Expiration Date will be automatically extended for one (1) additional year so that the remaining term on this Agreement will be not less than four (4) and not more than five (5) years.

6. Termination. This Agreement will continue in effect until the expiration of the term set forth in paragraph 5 of this Agreement unless earlier terminated pursuant to this paragraph 6.

- 6.1 Termination by Company. The Company will have the following rights to terminate this Agreement:

6.1.1 Termination without Cause. The Company may terminate this Agreement without cause at any time by the service of written notice of termination to the Executive specifying an effective date of such termination not sooner than sixty (60) business days after the date of such notice (the "Termination Date"). In the event the Executive is terminated without cause (other than a CC Termination under paragraph 6.3 of this Agreement), the Executive will receive as termination compensation: (a) Base Compensation (as hereafter defined) during the remaining term of this Agreement, but in any event through the Expiration Date; (b) any benefits payable by operation of paragraph 4.4 of this Agreement during the remaining term of this Agreement, but in any event through the Expiration Date; and (c) any vacation pay accrued through the Termination Date. For purposes of this Agreement the term "Base Compensation" means the Executive's current Base Salary under paragraph 4.1 on the Termination Date plus the bonus compensation received by the Executive during the twelve (12) month period preceding the Termination Date.

6.1.2 Termination for Cause. The Company may terminate this Agreement for cause if the Executive: (a) misappropriates the property of the Company or commits any other act of dishonesty; (b) engages in personal misconduct which materially injures the Company; (c) willfully violates any law or regulation relating to the business of the Company which results in injury to the Company; or (d) willfully and repeatedly fails to perform the Executive's duties hereunder. In the event this Agreement is terminated for

cause, the Company will not have any obligation to provide any further payments or benefits to the Executive after the effective date of such termination. This Agreement will not be deemed to have terminated for cause unless a written determination specifying the reasons for such termination is made, approved by a majority of the disinterested members of the board of directors of the Company and delivered to the Executive. Thereafter, the Executive will have the right for a period of twenty (20) days to request a board of directors meeting to be held at a mutually agreeable time and location within thirty (30) days, at which meeting the Executive will have an opportunity to be heard. Failing such determination and opportunity for hearing, any termination of this Agreement will be deemed to have occurred without cause.

- 6.2 Termination by Executive. The Executive may voluntarily terminate this Agreement with or without cause by the service of written notice of such termination to the Company specifying an effective date of such termination sixty (60) days after the date of such notice, during which time Executive may use remaining accrued vacation days, or at the Company's option, be paid for such days. In the event this Agreement is terminated by the Executive, neither the Company nor the Executive will have any further obligations hereunder including, without limitation, any obligation of the Company to provide any further payments or benefits to the Executive after the effective date of such termination.
- 6.3 Termination After Change in Control. If during the term of this Agreement there is a "Change of Control" and within two (2) years thereafter there is a CC Termination (as hereafter defined) then the Executive will be entitled to a severance payment (in addition to any other rights and other amounts payable to the Executive under this Agreement or otherwise) in an amount equal to the sum of the following: (a) five (5) times the Executive's Base Compensation; plus (b) the Gross-up Amount (as hereafter defined). If the foregoing amount is not paid within ten (10) days after the CC Termination, the unpaid amount will bear interest at the per annum rate equal to the prime rate published from time to time in the Wall Street Journal. The interest rate will be adjusted on the date of a change in such prime rate. For purposes of this Agreement the term "Gross-up Amount" means the amount of the payment which will result in the Executive retaining from such payment (after paying all taxes imposed on such payment and any interest or penalties related to such taxes) an amount equal to any excise tax imposed by Section 4999 of the Internal Revenue Code of 1986, as amended, together with any interest and penalties with respect to such excise tax imposed on the all of the payments made to the Executive under this paragraph 6.3.
- 6.3.1 Change of Control. The term "Change of Control" means any action of a nature that would be required to be reported in response to Item 6(e) of Schedule 14A of Regulation 14A under the Securities Exchange Act of 1934

with respect to the Company including, without limitation (i) the direct or indirect acquisition by any person after the date hereof of beneficial ownership of the right to vote or securities of the Company representing the right to vote thirty five percent (35%) or more of the combined voting power of the Company's then outstanding securities having the right to vote for the election of directors, or (ii) within two years of a tender offer or exchange offer for the voting stock of the Company or as a result of a merger, consolidation, sale of assets or contested election (or any combination of the foregoing), a majority of the members of the Company's board of directors is replaced by directors who were not nominated and approved by the board of directors.

6.3.2 CC Termination. The term "CC Termination" means any of the following: (a) this Agreement expires in accordance with its terms; (b) this Agreement is not extended under paragraph 5 of this Agreement and the Executive resigns within one (1) year after such nonextension; (c) the Executive is terminated by the Company other than under paragraphs 6.1.2, 6.4 or 6.5 based on adequate grounds; (d) the Executive resigns as a result of a change in the Executive's duties, a reduction in the Executive's then current compensation, a required relocation more than 25 miles from the Executive's then current place of employment or a default by the Company under this Agreement; (e) the failure by the Company after a Change of Control to obtain the assumption of this Agreement, without limitation or reduction, by any successor to the Company or any parent corporation of the Company; or (f) after a Change of Control has occurred, the Executive agrees to remain employed by the Company for a period of three (3) months to assist in the transition and thereafter resigns.

6.4 Incapacity of Executive. If the Executive suffers from a physical or mental condition which in the reasonable judgment of the Company's board of directors prevents the Executive in whole or in part from performing the duties specified herein for a period of three (3) consecutive months, the Executive may be terminated. Although the termination shall be deemed as a termination with cause, any compensation payable under paragraph 4 of this Agreement will be continued through the remaining term of this Agreement, but in any event through the Expiration Date. Notwithstanding the foregoing, the Executive's Base Salary specified in paragraph 4.1 of this Agreement will be reduced by any benefits payable under any disability plans provided by the Company under paragraph 4 of this Agreement.

6.5 Death of Executive. If the Executive dies during the term of this Agreement, the Company may thereafter terminate this Agreement without compensation to the Executive's estate except: (a) the obligation to continue the Base Salary payments under paragraph 4.1 of this Agreement for twelve (12) months after the effective date of such termination, and (b) the benefits described in paragraph 4.4 of this Agreement accrued through the effective date of such termination.

6.6 Effect of Termination. The termination of this Agreement will terminate all obligations of the Executive to render services on behalf of the Company, provided that the Executive will maintain the confidentiality of all information acquired by the Executive during the term of his employment in accordance with paragraph 7 of this Agreement. In the event of a termination under paragraphs 6.1.1 or 6.3 of this Agreement the Executive's right to participate in Program Wells will continue in accordance with paragraph 3 of this Agreement. Except as otherwise provided in this paragraph 6, no accrued bonus, severance pay or other form of compensation will be payable by the Company to the Executive by reason of the termination of this Agreement. All keys, entry cards, credit cards, files, records, financial information, furniture, furnishings, equipment, supplies and other items relating to the Company will remain the property of the Company. The Executive will have the right to retain and remove all personal property and effects which are owned by the Executive and located in the offices of the Company. All such personal items will be removed from such offices no later than seven (7) days after the effective date of termination, and the Company is hereby authorized to discard any items remaining and to reassign the Executive's office space after such date. Prior to the effective date of termination, the Executive will render such services to the Company as might be reasonably required to provide for the orderly termination of the Executive's employment.

7. Confidentiality. The Executive recognizes that the nature of the Executive's services are such that the Executive will have access to information which constitutes trade secrets, is of a confidential nature, is of great value to the Company or is the foundation on which the business of the Company is predicated. The Executive agrees not to disclose to any person other than the Company's employees or the Company's legal counsel nor use for any purpose, other than the performance of this Agreement, any confidential information ("Confidential Information"). Confidential Information includes data or material (regardless of form) which is: (a) a trade secret; (b) provided, disclosed or delivered to Executive by the Company, any officer, director, employee, agent, attorney, accountant, consultant, or other person or entity employed by the Company in any capacity, any customer, borrower or business associate of the Company or any public authority having jurisdiction over the Company of any business activity conducted by the Company; or (c) produced, developed, obtained or prepared by or on behalf of Executive or the Company (whether or not such information was developed in the performance of this Agreement) with respect to the Company or any assets oil and gas prospects, business activities, officers, directors, employees, borrowers or customers of the foregoing. However, Confidential Information shall not include any information, data or material which at the time of disclosure or use was generally available to the public other than by a breach of this Agreement, was available to the party to whom disclosed on a non-confidential basis by disclosure or access provided by the Company or a third party, or was otherwise developed or obtained independently by the person to whom disclosed without a breach of this Agreement. On request by the Company, the

Company will be entitled to a copy of any Confidential Information in the possession of the Executive. The Executive also agrees that the provisions of this paragraph 7 will survive the termination, expiration or cancellation of this Agreement for a period of five (5) years. The Executive will deliver to the Company all originals and copies of the documents or materials containing Confidential Information. For purposes of paragraphs 7, 8, and 9 of this Agreement, the Company expressly includes any of the Company's affiliated corporations, partnerships or entities.

8. Noncompetition. For a period of twelve (12) months after Executive is no longer employed by the Company as a result of either the resignation by the Executive pursuant to paragraph 6.2 above or termination for cause pursuant to paragraph 6.1.2 above, the Executive will not: (a) acquire, attempt to acquire or aid another in the acquisition or attempted acquisition of an interest in oil and gas assets, oil and gas production, oil and gas leases, mineral interests, oil and gas wells or other such oil and gas exploration, development or production activities within five (5) miles of any operations or ownership interests of the Company or its subsidiary corporations, partnerships or entities (but excluding operations or ownership interests acquired by the Company from a successor entity through a Change of Control as described in paragraph 6.3); and (b) solicit, induce, entice or attempt to entice any employee, contractor, customer, vendor or subcontractor to terminate or breach any relationship with the Company or the Company's affiliates for the Executive's own account or for the benefit of another party. The Executive further agrees that the Executive will not circumvent or attempt to circumvent the foregoing agreements by any future arrangement or through the actions of a third party.

9. Proprietary Matters. The Executive expressly understands and agrees that any and all improvements, inventions, discoveries, processes or know-how that are generated or conceived by the Executive during the term of this Agreement, whether generated or conceived during the Executive's regular working hours or otherwise, will be the sole and exclusive property of the Company. Whenever requested by the Company (either during the term of this Agreement or thereafter), the Executive will assign or execute any and all applications, assignments and or other instruments and do all things which the Company deems necessary or appropriate in order to permit the Company to: (a) assign and convey or otherwise make available to the Company the sole and exclusive right, title, and interest in and to said improvements, inventions, discoveries, processes, know-how, applications, patents, copyrights, trade names or trademarks; or (b) apply for, obtain, maintain, enforce and defend patents, copyrights, trade names, or trademarks of the United States or of foreign countries for said improvements, inventions, discoveries, processes or know-how. However, the improvements, inventions, discoveries, processes or know-how generated or conceived by the Executive and referred to above (except as they may be included in the patents, copyrights or registered trade names or trademarks of the Company, or corporations, partnerships or other entities which may be affiliated with the Company) shall not be exclusive property of the Company at any time after having been disclosed or revealed or have otherwise become available to the public or to a third party on a non-confidential basis other than by a breach of this Agreement, or after they have been independently developed or discussed without a breach of this Agreement by a third party who has no obligation to the Company or its affiliates.

10. Arbitration. The parties will attempt to promptly resolve any dispute or controversy arising out of or relating to this Agreement or termination of the Executive by the Company. Any negotiations pursuant to this paragraph 10 are confidential and will be treated as compromise and settlement negotiations for all purposes. If the parties are unable to reach a settlement amicably, the dispute will be submitted to binding arbitration before a single arbitrator in accordance with the Employment Dispute Resolution Rules of the American Arbitration Association. The arbitrator will be instructed and empowered to take reasonable steps to expedite the arbitration and the arbitrator's judgment will be final and binding upon the parties subject solely to challenge on the grounds of fraud or gross misconduct. Except for damages arising out of a breach of paragraphs 6, 7, 8 or 9 of this Agreement, the arbitrator is not empowered to award total damages (including compensatory damages) which exceed 300% of compensatory damages and each party hereby irrevocably waives any damages in excess of that amount. The arbitration will be held in Oklahoma County, Oklahoma. Judgment upon any verdict in arbitration may be entered in any court of competent jurisdiction and the parties hereby consent to the jurisdiction of, and proper venue in, the federal and state courts located in Oklahoma County, Oklahoma. Each party will bear its own costs in connection with the arbitration and the costs of the arbitrator will be borne by the party who the arbitrator determines did not prevail in the matter. Unless otherwise expressly set forth in this Agreement, the procedures specified in this paragraph 10 will be the sole and exclusive procedures for the resolution of disputes and controversies between the parties arising out of or relating to this Agreement. Notwithstanding the foregoing, a party may seek a preliminary injunction or other provisional judicial relief if in such party's judgment such action is necessary to avoid irreparable damage or to preserve the status quo.

11. Miscellaneous. The parties further agree as follows:

11.1 Time. Time is of the essence of each provision of this Agreement.

11.2 Notices. Any notice, payment, demand or communication required or permitted to be given by any provision of this Agreement will be in writing and will be deemed to have been given when delivered personally or by telefacsimile to the party designated to receive such notice, or on the date following the day sent by overnight courier, or on the third (3rd) business day after the same is sent by certified mail, postage and charges prepaid, directed to the following address or to such other or additional addresses as any party might designate by written notice to the other party:

To the Company: Chesapeake Energy Corporation  
Post Office Box 18496  
Oklahoma City, Oklahoma 73154-0496  
Attn: Mr. Tom L. Ward

To the Executive: Mr. Aubrey K. McClendon  
1214 Larchmont Lane  
Oklahoma City, Oklahoma 73116

- 11.3 Assignment. Neither this Agreement nor any of the parties' rights or obligations hereunder can be transferred or assigned without the prior written consent of the other parties to this Agreement.
- 11.4 Construction. If any provision of this Agreement or the application thereof to any person or circumstances is determined, to any extent, to be invalid or unenforceable, the remainder of this Agreement, or the application of such provision to persons or circumstances other than those as to which the same is held invalid or unenforceable, will not be affected thereby, and each term and provision of this Agreement will be valid and enforceable to the fullest extent permitted by law. This Agreement is intended to be interpreted, construed and enforced in accordance with the laws of the State of Oklahoma and any litigation relating to this Agreement will be conducted in a court of competent jurisdiction sitting in Oklahoma County, Oklahoma.
- 11.5 Entire Agreement. Except as provided in paragraph 2.3 of this Agreement, this Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter herein contained, and no modification hereof will be effective unless made by a supplemental written agreement executed by all of the parties hereto.
- 11.6 Binding Effect. This Agreement will be binding on the parties and their respective successors, legal representatives and permitted assigns. In the event of a merger, consolidation, combination, dissolution or liquidation of the Company, the performance of this Agreement will be assumed by any entity which succeeds to or is transferred the business of the Company as a result thereof.
- 11.7 Attorneys' Fees. If any party institutes an action or proceeding against any other party relating to the provisions of this Agreement or any default hereunder, the unsuccessful party to such action or proceeding will reimburse the successful party therein for the reasonable expenses of attorneys' fees and disbursements and litigation expenses incurred by the successful party.
- 11.8 Supercession. This Agreement is the final, complete and exclusive expression of the agreement between the Company and the Executive and supersedes and replaces in all respects any prior employment agreements (including the Prior Agreement). On execution of this Agreement by the Company and the Executive, the relationship between the Company and the Executive after the effective date of this Agreement will be governed by the terms of this Agreement and not by any other agreements, oral or otherwise.



IN WITNESS WHEREOF, the undersigned have executed this Agreement effective the date first above written.

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ TOM L. WARD

-----  
Tom L. Ward, President

(the "Company")

/s/ AUBREY K. McCLENDON

-----  
Aubrey K. McClendon, individually

(the "Executive")

AMENDED AND RESTATED  
EMPLOYMENT AGREEMENT

between

TOM L. WARD

and

CHESAPEAKE ENERGY CORPORATION

Effective July 1, 1998

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AMENDED AND RESTATED  
EMPLOYMENT AGREEMENT

THIS AGREEMENT is made effective July 1, 1998, between CHESAPEAKE ENERGY CORPORATION, an Oklahoma corporation (the "Company"), and TOM L. WARD, an individual (the "Executive").

## W I T N E S S E T H:

WHEREAS, the Company and the Executive entered into that certain employment agreement dated effective July 1, 1997 (the "Prior Agreement");

WHEREAS, the Company has announced that it would explore strategic alternatives to increase shareholder value, and to retain employees during that process the Company adopted a retention program for the Company's key employees other than the senior executive officers;

WHEREAS, for the reasons the Company adopted the retention program for the other employees, the Board of Directors of the Company believes that it is in the best interests of the Company to provide for the retention of the Executive as part of the process of exploring the Company's strategic alternatives; and

WHEREAS, the Company and the Executive desire to amend and restate the Prior Agreement in its entirety.

NOW, THEREFORE, in consideration of the mutual promises herein contained, the Company and the Executive agree as follows:

1. Employment. The Company hereby employs the Executive and the Executive hereby accepts such employment subject to the terms and conditions contained in this Agreement. The Executive is engaged as an employee of the Company, and the Executive and the Company do not intend to create a joint venture, partnership or other relationship which might impose a fiduciary obligation on the Executive or the Company in the performance of this Agreement.

2. Executive's Duties. The Executive is employed on a full-time basis. Throughout the term of this Agreement, the Executive will use the Executive's best efforts and due diligence to assist the Company in achieving the most profitable operation of the Company and the Company's affiliated entities consistent with developing and maintaining a quality business operation.

2.1 Specific Duties. The Executive will serve as President and Chief Operating Officer for the Company. From time to time, the Executive may be appointed as an officer of one (1) or more of the Company's subsidiaries. During the term of this Agreement, the Executive will be nominated for election or appointed to serve as a director of the Company and one (1) or more of the Company's subsidiaries. The Executive will use the Executive's best efforts to perform all of the services required to fully and faithfully execute the offices and positions to which the Executive is appointed and such other services as may be reasonably directed by the board of directors of the Company in accordance with this Agreement.

- 2.2 Modifications. The precise duties to be performed by the Executive may be extended or curtailed in the discretion of the respective boards of directors of the Company. However, except for termination for cause under paragraph 6.1.2 of this Agreement, the failure of the Executive to be elected, be reelected or serve as a director of the Company during the term of this Agreement, the removal of the Executive as a member of the board of directors of the Company, the withdrawal of the designation of the Executive as President or Chief Operating Officer of the Company, or the assignment of the performance of duties incumbent on the foregoing offices to other persons without the prior written consent of the Executive will constitute termination without cause by the Company.
- 2.3 Rules and Regulations. The Company currently has an Employment Policies Manual which addresses frequently asked questions regarding the Company. The Executive agrees to comply with the Employment Policies Manual except to the extent inconsistent with this Agreement. The Employment Policies Manual is subject to change without notice in the sole discretion of the Company at any time. In the event of a conflict between the Employment Policies Manual and this Agreement, this Agreement will control over the terms of the Employment Policies Manual.
- 2.4 Stock Investment. For each calendar year during the term of this Agreement the Executive agrees to hold shares of the Company's common stock having an aggregate Investment Value (as hereafter defined) equal to five hundred percent (500%) of the compensation paid to the Executive under paragraphs 4.1 and 4.2 of this Agreement during such calendar year. Any shares of common stock acquired by the Executive prior to the date of this Agreement and still owned by the Executive during the term of this Agreement may be used to satisfy this requirement to own common stock. For purposes of this paragraph, the "Investment Value" of each share of stock will be as follows: (a) for shares purchased in the open market the price paid by the Executive for such shares; (b) for shares acquired through the exercise of stock options, the fair market value of the common stock on the date the option was exercised; and (c) for shares acquired other than through open market purchases or the exercise of options the fair market value of the Company's common stock on the date of the acquisition of such common stock. The stock acquired or owned pursuant to this paragraph 2.4 must be held by the Executive at all times during the Executive's employment by the Company or the Company's affiliated entities. In order to administer this provision, the Executive agrees to deliver to the Company's Chief Executive Officer a semi-annual report of purchases and ownership in a form prepared by the Company. This paragraph will become null and void if the Company's common

stock ceases to be listed on the New York Stock Exchange, the National Association of Securities Dealers Automated Quotation System or other national exchange. The Company has no obligation to sell or to purchase from the Executive any of the Company's stock in connection with this paragraph 2.4 and has made no representations or warranties regarding the Company's stock, operations or financial condition.

3. Other Activities. Except for the activities (the "Permitted Activities") expressly permitted by paragraphs 3.1 and 3.2 of this Agreement, or the prior written approval of the board of directors of the Company, the Executive will not: (a) engage in business independent of the Executive's employment by the Company which requires any substantial portion of the Executive's time; (b) serve as an officer or director of any corporation, partnership, company, or firm; (c) except for passive investments that do not violate this Agreement and require a minimal portion of the Executive's time, serve as a general partner or member of any corporation, partnership, company or firm; or (d) directly or indirectly invest in, participate in or acquire an interest in any oil and gas business, including, without limitation, (i) producing oil and gas, (ii) drilling, owning or operating oil and gas leases or wells, (iii) providing services or materials to the oil and gas industry, (iv) marketing or refining oil or gas, or (v) owning any interest in any corporation, partnership, company or entity which conducts any of the foregoing activities. The limitations in this paragraph 3 will not prohibit an investment by the Executive in publicly traded securities. Notwithstanding the foregoing, the Executive will be permitted to participate in the following activities which will be deemed to be approved by the Company, if such activities are undertaken in strict compliance with this Agreement.

3.1 Company's Activities. The Executive or the Executive's designated affiliate will be permitted to acquire a working interest in all of the wells spudded by the Company or the Company's subsidiary corporations, partnerships or entities (the "Program Wells") on the terms and conditions set forth herein in any Calendar Quarter (as hereafter defined) during the Participation Term (as hereafter defined). The Program Wells include any well spudded during such Calendar Quarter in which the Company or the Company's subsidiary corporations, partnerships or entities participate as a nonoperator.

3.1.1 Amount of Participation. On or before the date which is thirty (30) days before the first (1st) day of each Calendar Quarter, the Executive will provide notice to the compensation committee of the Company's board of directors of the Executive's intent to participate in the Program Wells during the succeeding Calendar Quarter and the approximate percentage working interest which the Executive proposes to participate with during such Calendar Quarter (the "Approved Percentage"). The Executive's Approved Percentage working interest participation (determined without consideration of any carried interest) in the Program Wells for any Calendar Quarter will not exceed two and one-half percent (2.5%) on an eight-

eighths (8/8ths) basis. On designation of the Approved Percentage for a Calendar Quarter, the Executive will be deemed to have elected to participate in each Program Well spudded during such Calendar Quarter with a working interest equal to the following applicable percentage determined on a well-by-well basis (the "Minimum Participation"): (a) the Approved Percentage for each Operations Well, each Program Well which does not fall within clause (b) of this paragraph 3.1.1 and any Program Well which does not fall within clause (c) of this paragraph 3.1.1; (b) zero percent (0%) if the combined participation in the Program Well by the Executive, Mr. Tom L. Ward and Mr. Marcus C. Rowland with such individuals' Approved Percentage under their respective employment agreements causes the Company's working interest (determined without consideration of any carried interest) on the spud date for such Program Well to be less than twelve and one-half percent (12.5%) on an eight- eighths (8/8ths) basis; or (c) subsequent to a termination under paragraphs 6.1.1 or 6.3 of this Agreement the lowest Approved Percentage elected by the Executive subsequent to such termination. If clause (b) of this paragraph 3.1.1 prohibits the Executive's participation in a Program Well, then Messrs. Ward and Rowland will not be entitled to participate in such Program Well under their employment agreements. An "Operations Well" means a Program Well which falls within the provisions of clause (b) of this paragraph 3.1.1, but for which the Executive's participation is deemed necessary for the Company to retain operations as determined by the disinterested members of the compensation committee of the Company's board of directors. If the Executive fails to provide notice of the Executive's intent to participate and the Executive's proposed participation prior to the specified date as provided herein, the amount of the Approved Percentage for the Calendar Quarter will be deemed to be zero (0).

- 3.1.2 Conditions of Participation. The Participation by the Executive in each Program Well will be on no better terms than the terms agreed to by unaffiliated third party participants in connection with the acquisition of an interest in such Program Well from the Company or its subsidiary corporations, partnerships or entities. The Approved Percentage cannot be changed during any Calendar Quarter without the prior approval of the disinterested members of the compensation committee of the Company's board of directors. Any participation by the Executive under this paragraph 3.1 is also conditioned upon the Executive's participation in each Program Well spudded during such Calendar Quarter in an amount equal to the Minimum Participation. The Executive hereby agrees to execute and deliver any documents reasonably requested by the Company and hereby appoints the Company as the Executive's agent and attorney-in-fact to execute and deliver such documents if the Executive fails or refuses to



execute such documents. The Executive further agrees to pay all joint interest billings within one hundred fifty (150) days after receipt. For purposes of this Agreement, the term: (a) "Calendar Quarter" means the three (3) month periods commencing on the first (1st) day of January, April, July and October; and (b) "Participation Term" means the term of this Agreement plus five (5) years after a termination under paragraphs 6.1.1 or 6.3 of this Agreement.

- 3.2 Other Activities. The Executive currently conducts oil and gas investment activities individually and through TLW Investments, Inc., ("Investments"). The Executive will be permitted to continue oil and gas activities in such entities but only to the extent such activities are conducted on oil and gas leases or interests owned by the Executive or Investments as of July 1, 1995, or acquired by Investments from the Company. The interests acquired by Investments shall be limited by the provisions of paragraph 3.1 of this Agreement. The Company also consents to the Executive serving as a director of Pan East Petroleum Corp., an Ontario Canada corporation, pursuant to approval by the board of directors.

4. Executive's Compensation. The Company agrees to compensate the Executive as follows:

- 4.1 Base Salary. A base salary (the "Base Salary"), at the initial annual rate of not less than Three Hundred Fifty Thousand Dollars (\$350,000.00), will be paid to the Executive in equal semi-monthly installments beginning July 15, 1998 during the term of this Agreement.
- 4.2 Bonus. In addition to the Base Salary described at paragraph 4.1 of this Agreement, the Company may periodically pay bonus compensation to the Executive. Any bonus compensation will be at the absolute discretion of the Company in such amounts and at such times as the board of directors of the Company may determine.
- 4.3 Stock Options. In addition to the compensation set forth in paragraphs 4.1 and 4.2 of this Agreement, the Executive may periodically receive grants of stock options from the Company's various stock option plans, subject to the terms and conditions thereof.
- 4.4 Benefits. The Company will provide the Executive such retirement benefits, reimbursement of reasonable expenditures for dues, travel and entertainment and other benefits on terms customarily provided by the Company from time to time. The Company will also provide the Executive the opportunity to apply for coverage under the Company's medical, life and disability plans, if any. If the Executive is accepted for coverage under such plans, the Company will provide such coverage on the same terms as is customarily provided by the Company to the plan participants as modified from time to time. The following specific benefits will also be provided to the Executive at the expense of the Company:

- 4.4.1 Vacation. The Executive will be entitled to take three (3) weeks of paid vacation each calendar year during the term of this Agreement. No additional compensation will be paid for failure to take vacation and no vacation may be carried forward from one calendar year to another.
- 4.4.2 Membership Dues. The Company will reimburse the Executive for: (a) the monthly dues necessary to maintain a full membership in (1) golf and/or country club in the Oklahoma City area selected by the Executive; and (b) the reasonable cost of any qualified business entertainment at such country club. All other costs, including, without implied limitation, any initiation costs, initial membership costs, personal use and business entertainment unrelated to the Company will be the sole obligation of the Executive and the Company will have no liability with respect to such amounts.
- 4.4.3 Automobile and Travel Allowance. The Executive will receive a monthly cash allowance in the amount of One Thousand Five Hundred Dollars (\$1,500.00) to defer a portion of the Executive's cost of acquiring, operating and maintaining an automobile for use in the Executive's employment. Additionally, the Executive will be entitled to utilize any aircraft owned by the Company (whether in whole or in part) for personal use and will not be required to reimburse the Company for any cost related to such use or pay any cost or charge with respect to such use up to an amount during any calendar year equal to the Aircraft Allowance. For purposes of this Agreement the term "Aircraft Allowance" means the variable costs directly identifiable with each use (including fuel, pilot charges, landing fees, hourly charges under co-ownership arrangements and other such costs) but specifically excludes any fixed costs of the aircraft (including acquisition costs and depreciation). The Aircraft Allowance will be equal to \$40,000.00 for the Company's fiscal year ending on June 30, 1998, \$25,000.00 for the six month period ending on December 31, 1998, and \$50,000.00 for each fiscal year thereafter during the term of this Agreement. If the Executive's use of the Company's aircraft exceeds the Aircraft Allowance during any fiscal year the Executive will be required to reimburse the Company for the variable costs directly identified with each such use.
- 4.4.4 Accounting Support. The Executive will be permitted to utilize the Company's office space, computer facilities and the equivalent of one (1) full-time accounting employee of the Company (presently Ms. Cheryl Hamilton) to maintain books and records for the Executive and the

Executive's Permitted Activities. The Executive will not be required to pay any compensation to the Company in connection with such accounting services.

- 4.5 Compensation Review. The compensation of the Executive will be reviewed not less frequently than annually by the board of directors of the Company. The compensation of the Executive prescribed by paragraph 4 of this Agreement may be increased at the discretion of the Company, but may not be reduced without the prior written consent of the Executive.

5. Term. In the absence of termination as set forth in paragraph 6 below, this Agreement will extend for a term of five (5) years commencing on July 1, 1998, and ending on June 30, 2003 (the "Expiration Date") as extended from time to time. Unless the Company provides thirty (30) days prior written notice of nonextension to the Executive, on each June 30 during the term of this Agreement, the term and the Expiration Date will be automatically extended for one (1) additional year so that the remaining term on this Agreement will be not less than four (4) and not more than five (5) years.

6. Termination. This Agreement will continue in effect until the expiration of the term set forth in paragraph 5 of this Agreement unless earlier terminated pursuant to this paragraph 6.

- 6.1 Termination by Company. The Company will have the following rights to terminate this Agreement:

- 6.1.1 Termination without Cause. The Company may terminate this Agreement without cause at any time by the service of written notice of termination to the Executive specifying an effective date of such termination not sooner than sixty (60) business days after the date of such notice (the "Termination Date"). In the event the Executive is terminated without cause (other than a CC Termination under paragraph 6.3 of this Agreement), the Executive will receive as termination compensation: (a) Base Compensation (as hereafter defined) during the remaining term of this Agreement, but in any event through the Expiration Date; (b) any benefits payable by operation of paragraph 4.4 of this Agreement during the remaining term of this Agreement, but in any event through the Expiration Date; and (c) any vacation pay accrued through the Termination Date. For purposes of this Agreement the term "Base Compensation" means the Executive's current Base Salary under paragraph 4.1 on the Termination Date plus the bonus compensation received by the Executive during the twelve (12) month period preceding the Termination Date.

- 6.1.2 Termination for Cause. The Company may terminate this Agreement for cause if the Executive: (a) misappropriates the property of the Company or commits any other act of dishonesty; (b) engages in personal misconduct which materially injures the Company; (c) willfully violates any law or regulation relating to the business of the Company which results in injury to the Company; or (d) willfully and repeatedly fails to perform the Executive's duties hereunder. In the event this Agreement is terminated for cause, the Company will not have any obligation to provide any further payments or benefits to the Executive after the effective date of such termination. This Agreement will not be deemed to have terminated for cause unless a written determination specifying the reasons for such termination is made, approved by a majority of the disinterested members of the board of directors of the Company and delivered to the Executive. Thereafter, the Executive will have the right for a period of twenty (20) days to request a board of directors meeting to be held at a mutually agreeable time and location within thirty (30) days, at which meeting the Executive will have an opportunity to be heard. Failing such determination and opportunity for hearing, any termination of this Agreement will be deemed to have occurred without cause.
- 6.2 Termination by Executive. The Executive may voluntarily terminate this Agreement with or without cause by the service of written notice of such termination to the Company specifying an effective date of such termination sixty (60) days after the date of such notice, during which time Executive may use remaining accrued vacation days, or at the Company's option, be paid for such days. In the event this Agreement is terminated by the Executive, neither the Company nor the Executive will have any further obligations hereunder including, without limitation, any obligation of the Company to provide any further payments or benefits to the Executive after the effective date of such termination.
- 6.3 Termination After Change in Control. If during the term of this Agreement there is a "Change of Control" and within two (2) years thereafter there is a CC Termination (as hereafter defined) then the Executive will be entitled to a severance payment (in addition to any other rights and other amounts payable to the Executive under this Agreement or otherwise) in an amount equal to the sum of the following: (a) five (5) times the Executive's Base Compensation; plus (b) the Gross-up Amount (as hereafter defined). If the foregoing amount is not paid within ten (10) days after the CC Termination, the unpaid amount will bear interest at the per annum rate equal to the prime rate published from time to time in the Wall Street Journal. The interest rate will be adjusted on the date of a change in such prime rate. For purposes of this Agreement the term "Gross-up Amount" means the amount of the payment which will result in the Executive retaining from such payment (after paying all taxes imposed on such payment and any interest or penalties related to such taxes) an amount equal to any excise tax imposed by Section 4999 of the Internal Revenue Code of 1986, as amended, together with any

interest and penalties with respect to such excise tax imposed on the all of the payments made to the Executive under this paragraph 6.3.

6.3.1 Change of Control. The term "Change of Control" means any action of a nature that would be required to be reported in response to Item 6(e) of Schedule 14A of Regulation 14A under the Securities Exchange Act of 1934 with respect to the Company including, without limitation (i) the direct or indirect acquisition by any person after the date hereof of beneficial ownership of the right to vote or securities of the Company representing the right to vote thirty five percent (35%) or more of the combined voting power of the Company's then outstanding securities having the right to vote for the election of directors, or (ii) within two years of a tender offer or exchange offer for the voting stock of the Company or as a result of a merger, consolidation, sale of assets or contested election (or any combination of the foregoing), a majority of the members of the Company's board of directors is replaced by directors who were not nominated and approved by the board of directors.

6.3.2 CC Termination. The term "CC Termination" means any of the following: (a) this Agreement expires in accordance with its terms; (b) this Agreement is not extended under paragraph 5 of this Agreement and the Executive resigns within one (1) year after such nonextension; (c) the Executive is terminated by the Company other than under paragraphs 6.1.2, 6.4 or 6.5 based on adequate grounds; (d) the Executive resigns as a result of a change in the Executive's duties, a reduction in the Executive's then current compensation, a required relocation more than 25 miles from the Executive's then current place of employment or a default by the Company under this Agreement; (e) the failure by the Company after a Change of Control to obtain the assumption of this Agreement, without limitation or reduction, by any successor to the Company or any parent corporation of the Company; or (f) after a Change of Control has occurred, the Executive agrees to remain employed by the Company for a period of three (3) months to assist in the transition and thereafter resigns.

6.4 Incapacity of Executive. If the Executive suffers from a physical or mental condition which in the reasonable judgment of the Company's board of directors prevents the Executive in whole or in part from performing the duties specified herein for a period of three (3) consecutive months, the Executive may be terminated. Although the termination shall be deemed as a termination with cause, any compensation payable under paragraph 4 of this Agreement will be continued through the remaining term of this Agreement, but in any event through the Expiration Date. Notwithstanding the foregoing, the Executive's Base Salary specified in paragraph 4.1 of this Agreement will be reduced by any benefits payable under any disability plans provided by the Company under paragraph 4 of this Agreement.

- 6.5 Death of Executive. If the Executive dies during the term of this Agreement, the Company may thereafter terminate this Agreement without compensation to the Executive's estate except: (a) the obligation to continue the Base Salary payments under paragraph 4.1 of this Agreement for twelve (12) months after the effective date of such termination, and (b) the benefits described in paragraph 4.4 of this Agreement accrued through the effective date of such termination.
- 6.6 Effect of Termination. The termination of this Agreement will terminate all obligations of the Executive to render services on behalf of the Company, provided that the Executive will maintain the confidentiality of all information acquired by the Executive during the term of his employment in accordance with paragraph 7 of this Agreement. In the event of a termination under paragraphs 6.1.1 or 6.3 of this Agreement the Executive's right to participate in Program Wells will continue in accordance with paragraph 3 of this Agreement. Except as otherwise provided in this paragraph 6, no accrued bonus, severance pay or other form of compensation will be payable by the Company to the Executive by reason of the termination of this Agreement. All keys, entry cards, credit cards, files, records, financial information, furniture, furnishings, equipment, supplies and other items relating to the Company will remain the property of the Company. The Executive will have the right to retain and remove all personal property and effects which are owned by the Executive and located in the offices of the Company. All such personal items will be removed from such offices no later than seven (7) days after the effective date of termination, and the Company is hereby authorized to discard any items remaining and to reassign the Executive's office space after such date. Prior to the effective date of termination, the Executive will render such services to the Company as might be reasonably required to provide for the orderly termination of the Executive's employment.

7. Confidentiality. The Executive recognizes that the nature of the Executive's services are such that the Executive will have access to information which constitutes trade secrets, is of a confidential nature, is of great value to the Company or is the foundation on which the business of the Company is predicated. The Executive agrees not to disclose to any person other than the Company's employees or the Company's legal counsel nor use for any purpose, other than the performance of this Agreement, any confidential information ("Confidential Information"). Confidential Information includes data or material (regardless of form) which is: (a) a trade secret; (b) provided, disclosed or delivered to Executive by the Company, any officer, director, employee, agent, attorney, accountant, consultant, or other person or entity employed by the Company in any capacity, any customer, borrower or business associate of the Company or any public authority having jurisdiction over the Company of any business activity conducted by the Company; or (c) produced, developed, obtained or prepared by or on behalf of Executive or the

Company (whether or not such information was developed in the performance of this Agreement) with respect to the Company or any assets oil and gas prospects, business activities, officers, directors, employees, borrowers or customers of the foregoing. However, Confidential Information shall not include any information, data or material which at the time of disclosure or use was generally available to the public other than by a breach of this Agreement, was available to the party to whom disclosed on a non-confidential basis by disclosure or access provided by the Company or a third party, or was otherwise developed or obtained independently by the person to whom disclosed without a breach of this Agreement. On request by the Company, the Company will be entitled to a copy of any Confidential Information in the possession of the Executive. The Executive also agrees that the provisions of this paragraph 7 will survive the termination, expiration or cancellation of this Agreement for a period of five (5) years. The Executive will deliver to the Company all originals and copies of the documents or materials containing Confidential Information. For purposes of paragraphs 7, 8, and 9 of this Agreement, the Company expressly includes any of the Company's affiliated corporations, partnerships or entities.

8. Noncompetition. For a period of twelve (12) months after Executive is no longer employed by the Company as a result of either the resignation by the Executive pursuant to paragraph 6.2 above or termination for cause pursuant to paragraph 6.1.2 above, the Executive will not: (a) acquire, attempt to acquire or aid another in the acquisition or attempted acquisition of an interest in oil and gas assets, oil and gas production, oil and gas leases, mineral interests, oil and gas wells or other such oil and gas exploration, development or production activities within five (5) miles of any operations or ownership interests of the Company or its subsidiary corporations, partnerships or entities (but excluding operations or ownership interests acquired by the Company from a successor entity through a Change of Control as described in paragraph 6.3); and (b) solicit, induce, entice or attempt to entice any employee, contractor, customer, vendor or subcontractor to terminate or breach any relationship with the Company or the Company's affiliates for the Executive's own account or for the benefit of another party. The Executive further agrees that the Executive will not circumvent or attempt to circumvent the foregoing agreements by any future arrangement or through the actions of a third party.

9. Proprietary Matters. The Executive expressly understands and agrees that any and all improvements, inventions, discoveries, processes or know-how that are generated or conceived by the Executive during the term of this Agreement, whether generated or conceived during the Executive's regular working hours or otherwise, will be the sole and exclusive property of the Company. Whenever requested by the Company (either during the term of this Agreement or thereafter), the Executive will assign or execute any and all applications, assignments and other instruments and do all things which the Company deems necessary or appropriate in order to permit the Company to: (a) assign and convey or otherwise make available to the Company the sole and exclusive right, title, and interest in and to said improvements, inventions, discoveries, processes, know-how, applications, patents, copyrights, trade names or trademarks; or (b) apply for, obtain, maintain, enforce and defend patents, copyrights, trade names, or trademarks of the United States or of foreign countries for said improvements, inventions, discoveries, processes or

know-how. However, the improvements, inventions, discoveries, processes or know-how generated or conceived by the Executive and referred to above (except as they may be included in the patents, copyrights or registered trade names or trademarks of the Company, or corporations, partnerships or other entities which may be affiliated with the Company) shall not be exclusive property of the Company at any time after having been disclosed or revealed or have otherwise become available to the public or to a third party on a non-confidential basis other than by a breach of this Agreement, or after they have been independently developed or discussed without a breach of this Agreement by a third party who has no obligation to the Company or its affiliates.

10. Arbitration. The parties will attempt to promptly resolve any dispute or controversy arising out of or relating to this Agreement or termination of the Executive by the Company. Any negotiations pursuant to this paragraph 10 are confidential and will be treated as compromise and settlement negotiations for all purposes. If the parties are unable to reach a settlement amicably, the dispute will be submitted to binding arbitration before a single arbitrator in accordance with the Employment Dispute Resolution Rules of the American Arbitration Association. The arbitrator will be instructed and empowered to take reasonable steps to expedite the arbitration and the arbitrator's judgment will be final and binding upon the parties subject solely to challenge on the grounds of fraud or gross misconduct. Except for damages arising out of a breach of paragraphs 6, 7, 8 or 9 of this Agreement, the arbitrator is not empowered to award total damages (including compensatory damages) which exceed 300% of compensatory damages and each party hereby irrevocably waives any damages in excess of that amount. The arbitration will be held in Oklahoma County, Oklahoma. Judgment upon any verdict in arbitration may be entered in any court of competent jurisdiction and the parties hereby consent to the jurisdiction of, and proper venue in, the federal and state courts located in Oklahoma County, Oklahoma. Each party will bear its own costs in connection with the arbitration and the costs of the arbitrator will be borne by the party who the arbitrator determines did not prevail in the matter. Unless otherwise expressly set forth in this Agreement, the procedures specified in this paragraph 10 will be the sole and exclusive procedures for the resolution of disputes and controversies between the parties arising out of or relating to this Agreement. Notwithstanding the foregoing, a party may seek a preliminary injunction or other provisional judicial relief if in such party's judgment such action is necessary to avoid irreparable damage or to preserve the status quo.

11. Miscellaneous. The parties further agree as follows:

- 11.1 Time. Time is of the essence of each provision of this Agreement.
- 11.2 Notices. Any notice, payment, demand or communication required or permitted to be given by any provision of this Agreement will be in writing and will be deemed to have been given when delivered personally or by telefacsimile to the party designated to receive such notice, or on the date following the day sent by overnight courier, or on the third (3rd) business day after the same is sent by certified mail, postage and charges prepaid, directed to the following address or to



such other or additional addresses as any party might designate by written notice to the other party:

To the Company: Chesapeake Energy Corporation  
Post Office Box 18496  
Oklahoma City, OK 73154-0496  
Attn: Aubrey K. McClendon

To the Executive: Mr. Tom L. Ward  
19200 North Rockwell Avenue  
Edmond, Oklahoma 73003-9200

- 11.3 Assignment. Neither this Agreement nor any of the parties' rights or obligations hereunder can be transferred or assigned without the prior written consent of the other parties to this Agreement.
- 11.4 Construction. If any provision of this Agreement or the application thereof to any person or circumstances is determined, to any extent, to be invalid or unenforceable, the remainder of this Agreement, or the application of such provision to persons or circumstances other than those as to which the same is held invalid or unenforceable, will not be affected thereby, and each term and provision of this Agreement will be valid and enforceable to the fullest extent permitted by law. This Agreement is intended to be interpreted, construed and enforced in accordance with the laws of the State of Oklahoma and any litigation relating to this Agreement will be conducted in a court of competent jurisdiction sitting in Oklahoma County, Oklahoma.
- 11.5 Entire Agreement. Except as provided in paragraph 2.3 of this Agreement, this Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter herein contained, and no modification hereof will be effective unless made by a supplemental written agreement executed by all of the parties hereto.
- 11.6 Binding Effect. This Agreement will be binding on the parties and their respective successors, legal representatives and permitted assigns. In the event of a merger, consolidation, combination, dissolution or liquidation of the Company, the performance of this Agreement will be assumed by any entity which succeeds to or is transferred the business of the Company as a result thereof.

- 11.7 Attorneys' Fees. If any party institutes an action or proceeding against any other party relating to the provisions of this Agreement or any default hereunder, the unsuccessful party to such action or proceeding will reimburse the successful party therein for the reasonable expenses of attorneys' fees and disbursements and litigation expenses incurred by the successful party.
- 11.8 Supercession. This Agreement is the final, complete and exclusive expression of the agreement between the Company and the Executive and supersedes and replaces in all respects any prior employment agreements (including the Prior Agreement). On execution of this Agreement by the Company and the Executive, the relationship between the Company and the Executive after the effective date of this Agreement will be governed by the terms of this Agreement and not by any other agreements, oral or otherwise.

IN WITNESS WHEREOF, the undersigned have executed this Agreement effective the date first above written.

CHESAPEAKE ENERGY CORPORATION, an  
Oklahoma corporation

By /s/ AUBREY K. MCCLENDON  
-----  
Aubrey K. McClendon, Chief Executive Officer  
  
(the "Company")

/s/ TOM L. WARD  
-----  
Tom L. Ward, individually  
  
(the "Executive")

AMENDMENT NO. 1 TO RIGHTS AGREEMENT  
BETWEEN  
CHESAPEAKE ENERGY CORPORATION  
AND  
UMB BANK, N.A., AS RIGHTS AGENT

THIS AMENDMENT NO. 1 TO RIGHTS AGREEMENT (this "First Amendment"), dated as of September 11, 1998, is by and between Chesapeake Energy Corporation, and Oklahoma corporation (the "Company"), and UMB Bank, N.A., as Rights Agent (the "Rights Agent").

R E C I T A L S:

WHEREAS, the Company and the Rights Agent have heretofore entered into a Rights Agreement, dated as of July 15, 1998 (the "Rights Agreement"); and

WHEREAS, the Company desires to amend the Rights Agreement to revise Section 1(p) thereof; and

WHEREAS, the Board of Directors of the Company has unanimously approved the amendment to the Rights Agreement effected hereby and in accordance with Section 27 of the Rights Agreement, this First Amendment can be effected without the approval of any holders of the Rights.

NOW, THEREFORE, in consideration of the premises and the mutual agreements herein set forth and in accordance with Section 27 of the Rights Agreement, the parties hereby agree as follows:

1. Section 1(p) of the Rights Agreement is hereby amended, effective as of the date set forth above, by revising such Section to read in its entirety as follows:

"Exempt Person" shall mean (i) the Company or any Subsidiary (as such term is hereinafter defined) of the Company or any employee benefit plan of the Company, (ii) Aubrey K. McClendon, his spouse, lineal descendants and ascendants, heirs, executors or other legal representatives and any trusts established for the benefit of the foregoing, or any other person or entity in which the foregoing persons or entities are at the time of determination the direct record and beneficial owners of all outstanding voting securities (each a "McClendon Stockholder"), (iii) Tom L. Ward, his spouse, lineal descendants and ascendants, heirs, executors or other legal representatives and any trusts established for the benefit of the

foregoing (each a "Ward Stockholder"), (iv) Morgan Guaranty Trust Company of New York in its capacity as pledgee (the "McClendon/Ward Pledgee") of shares ("Pledged Shares") Beneficially Owned by a McClendon Stockholder or Ward Stockholder or both under pledge agreement(s) in effect on the date of this First Amendment, to the extent that upon the exercise by the McClendon/Ward Pledgee of any rights or duties thereunder other than the exercise of any voting power by the McClendon/Ward Pledgee or the acquisition of ownership by the McClendon/Ward Pledgee such McClendon/Ward Pledgee becomes a Beneficial Owner of Pledged Shares, or (v) any Person (other than a McClendon/Ward Pledgee) that is neither a McClendon Stockholder nor a Ward Stockholder but who or which is the Beneficial Owner or Common Stock Beneficially Owned by a McClendon Stockholder or Ward Stockholder (a "Second Tier Stockholder"), but only if the shares of Common Stock otherwise Beneficially Owned by such Second Tier Stockholder ("Second Tier Holder Shares") do not exceed the sum of (A) such holder's Second Tier Holder Shares held on the date hereof and (B) 1% of the shares of Common Stock of the Company then outstanding.

2. Except to the extent amended by this First Amendment, the Rights Agreement shall continue in full force and effect.

3. Capitalized terms used herein but not defined shall have the meanings assigned to such terms in the Rights Agreement.

IN WITNESS WHEREOF, the parties hereto have caused this First Amendment to be duly executed and attested, all as of the day and year first above written.

CHESAPEAKE ENERGY CORPORATION

By:/s/ AUBREY K. MCCLENDON

-----  
Name: Aubrey K. McClendon  
Title: Chairman of the Board and  
Chief Executive Officer

UMB BANK, N.A.  
as Rights Agent

By:/s/ FRANK C. BRAMWELL

-----  
Name: Frank C. Bramwell  
Title: Sr. Vice President

	9 Months Ended Sept. 30, 1997 ----	9 Months Ended Sept. 30, 1998 ----
RATIO OF EARNINGS TO FIXED CHARGES		
Income before income taxes and extraordinary item	(214,063)	(495,388)
Interest	20,909	47,930
Preferred Stock Dividends	-	8,051
Bond discount amortization (a)	-	-
Loan cost amortization	1,088	1,682
	-----	-----
Earnings	(192,066)	(437,725)
Interest expense	20,909	47,930
Capitalized interest	7,944	5,805
Preferred Stock Dividends	-	8,051
Bond discount amortization (a)	-	-
Loan cost amortization	1,088	1,682
	-----	-----
Fixed Charges	29,941	63,468
Ratio	(6.41)	(6.90)
(a) Bond discount excluded since its included in interest expense		
Insufficient coverage	222,007	501,193

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM BALANCE SHEET AS OF SEPTEMBER 30, 1998 AND STATEMENT OF INCOME FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1998.

1,000

9-MOS	DEC-31-1998	JAN-01-1998	SEP-30-1998
			24,949
			0
		82,604	
		1,209	
		6,327	
	117,289		
			2,225,964
	1,197,483		
	1,227,274		
119,300			
			919,055
	0		
		230,000	
			967
1,227,274		(54,572)	
			292,413
	295,986		
			743,444
		791,374	
		0	
		0	
	47,930		
	(495,388)		
			0
(495,388)			
			0
		(13,334)	
			0
		(508,722)	
		(5.48)	
		(5.48)	