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ATTORNEYS FOR HALL PHOENIX/INWOOD, LTD.

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION**

IN RE :)	
)	
HALLWOOD ENERGY, L.P.,)	CASE No. 09-31253
A DELAWARE LIMITED PARTNERSHIP,)	JOINTLY ADMINISTERED
HALLWOOD ENERGY)	
MANAGEMENT, LLC, A DELAWARE)	CHAPTER 11
LIMITED LIABILITY COMPANY,)	
HALLWOOD GATHERING, L.P.,)	
A DELAWARE LIMITED PARTNERSHIP,)	
HG II MANAGEMENT, LLC,)	
A DELAWARE LIMITED LIABILITY COMPANY,)	
HALLWOOD PETROLEUM, LLC,)	
A DELAWARE LIMITED LIABILITY COMPANY,)	
HALLWOOD SWD, LLC)	
A DELAWARE LIMITED LIABILITY COMPANY,)	
)	
DEBTORS.)	

**JOINT PLAN OF REORGANIZATION FOR THE DEBTORS
PROPOSED BY HALL PHOENIX/INWOOD, LTD.
(Dated: July 14, 2009)**

Hall Phoenix/Inwood, Ltd. ("HPI"), the largest secured and unsecured creditor of the Debtors proposes the following Joint Plan of Reorganization for the Debtors (the "**Plan**") pursuant to the United States Bankruptcy Code (the "**Bankruptcy Code**") for Hallwood Energy, L.P., a

Delaware limited partnership; Hallwood Energy Management, LLC, a Delaware limited liability company; Hallwood Gathering, L.P., a Delaware limited partnership; HG II Management, LLC, a Delaware limited liability company; Hallwood Petroleum, LLC, a Delaware limited liability company; and Hallwood SWD, LLC, a Delaware limited liability company, (collectively, “**Hallwood Energy**” or the “**Debtors**”) and their Estates. **THE PLAN HAS THE SUPPORT OF THE OFFICIAL UNSECURED CREDITORS’ COMMITTEE (“COMMITTEE”) FOR THE DEBTORS.**

SUMMARY OVERVIEW

HPI is the largest creditor of the Debtors with Claims in excess of \$118 million secured by Liens on substantially all of the Debtors’ assets. The Bankruptcy Court has permitted HPI to take all action necessary to prepare to foreclose its Liens and take control of the Debtors’ assets including the Debtors’ oil and gas properties. The Debtors’ remaining assets consist primarily of Causes of Action against various parties. HPI and the Committee have reached an agreement regarding the pursuit of the Causes of Action and the terms for treatment of Claims of Creditors, which terms are incorporated in this Plan. The essential terms of the Plan are as follows:

1. The formation of three trusts (Trust I, Trust II and Trust III) for the benefit of Creditors into which certain Causes of Action will be transferred so that such Causes of Action, including claims against the Debtors officers, directors and professionals and The Hallwood Group Incorporated can be pursued for the benefit of Creditors.
2. A settlement between the Debtors’ Estates and HPI and its officers of all claims of the Debtors against such parties, including claims for subordination and breach of fiduciary duty. Under the terms of the settlement the litigation will be dismissed with prejudice and HPI will fulfill its obligations under the Plan including advancing the costs of operating the trusts, releasing its liens on certain Causes of Action and contributing HPI’s Direct Claims to the Trust. HPI will also receive a conveyance of all of its Collateral except those Causes of Action transferred to Trust I.
3. Trade Creditors will receive the following preferred treatment as a result of the agreement reached between the Committee and HPI: from Trust I, the first \$1,000,000 after payment of certain other Claims and administrative costs and then 10% of all Recoveries; from Trust II, 60% of all Recoveries after payment of administrative costs; and from Trust III, 100% of all Recoveries after repayment of any borrowings by Trust III and after payment of administrative costs.
4. Payment of 100% of Allowed Priority M&M Lien Claims as provided in the Plan.

ARTICLE I

DEFINITIONS

Unless the context otherwise requires, the following terms shall have the following meanings when used in initially capitalized form in this Plan. Such meanings shall be equally applicable to both the singular and plural forms of such terms. Any term used in initially capitalized form in this Plan that is not defined herein, but that is defined in the Bankruptcy Code, shall have the meaning assigned to such term in the Bankruptcy Code.

1.01 Administrative Claim means a Claim for payment of an administrative expense under Sections 503(b) or 1114(e)(2) of the Bankruptcy Code and entitled to priority under Section 507(a)(1) of the Bankruptcy Code, including (a) actual, necessary costs and expenses, incurred after the Petition Date, of preserving the Debtors' Estate and operating its business, including wages, salaries or commissions for services rendered after the Petition Date, (b) Fee Claims, (c) all fees and charges assessed against the Estates under 28 U.S.C. Section 1930 and (d) all Allowed Claims that are entitled to be treated as Administrative Claims by virtue of a Final Order entered under Section 546(c)(2)(A) of the Bankruptcy Code.

1.02 Allowed Amount means the amount in lawful currency of the United States of any Allowed Claim, or the number of shares representing any Allowed Interest.

1.03 Allowed Claim and Allowed Interest means, with reference to any Claim or Interest: (i) a Claim against or Interest in the Debtors, proof of which, if required, was Filed on or before the Bar Date, which is not a Contested Claim or Contested Interest, (ii) if no proof of claim or interest was so Filed, a Claim against or Interest in the Debtors that have been or hereafter is listed by the Debtors in their Schedules as liquidated in amount and not disputed or contingent, or (iii) a Claim or Interest allowed hereunder or by Final Order. An Allowed Claim or Allowed Interest does not include any Claim or Interest or portion thereof which is a Disallowed Claim or Disallowed Interest or which has been subsequently withdrawn, disallowed, released or waived by the holder thereof, by this Plan, or pursuant to a Final Order. Unless otherwise specifically provided in this Plan, an Allowed Claim or Allowed Interest shall not include any amount for punitive damages or penalties.

1.04 Avoidance Actions means any claim or cause of action belonging to the Debtors and arising under Chapter 5 of the Bankruptcy Code including, but not limited to, Sections 544, 547, 548 and 550. All Avoidance Actions will be transferred to Trust I except Preference Actions which will be transferred to Trust II and the J. Aron Claims which will be transferred to Trust III.

1.05 Bankruptcy Code means Title 11 of the United States Code, as amended.

1.06 Bankruptcy Court means the United States Bankruptcy Court for the Northern District of Texas, Dallas Division.

1.07 Bar Date means the deadline by which a Claim must have been timely Filed. The Bar Date is July 8, 2009 as to all prepetition Claims.

1.08 Business Day means any day, other than a Saturday, Sunday, or legal holiday (as that term is defined in Bankruptcy Rule 9006(a)).

1.09 Causes of Action means any and all claims, objections to claims, causes of action, cross claims or counterclaims held, or assertable by, the Debtors that have been or could have been brought on or after the Petition Date, including, but not limited to: (i) any claims against competitors, suppliers, customers, employees, independent contractors, consultants, professionals or any other person or entity with whom the Debtors have done business; (ii) any claims, causes of action, cross claims, or counterclaims against any current or former officers, directors, employees, partners, managers or members of the Debtors whether or not covered under a directors and officer policy of liability insurance or otherwise including the D&O Claims; (iii) any claims, causes of action, cross claims, or counterclaims against insurance companies for insurance premium refunds, claims to recover workers' compensation premiums or any similar causes of action; (iv) the Avoidance Actions; (v) the J. Aron Claims; (vi) claims against The Hallwood Group, Inc. and its affiliates, owners, officers and directors including claims for breach of the Equity Support Agreement and damages resulting therefrom; and (vii) any and all claims, causes of action, counterclaims, demands, or controversies, against third parties on account of costs, debts, sums of money, accounts, reckonings, bonds, bills, damages, obligations, liabilities, objections, and executions of any nature, type, or description which the Debtors have or may come to have, including, but not limited to, negligence, gross negligence, usury, fraud, deceit, misrepresentation, conspiracy, unconscionability, duress, economic duress, defamation, control, interference with contractual and business relationships, conflicts of interest, misuse of insider information, concealment, disclosure, secrecy, misuse of collateral, wrongful release of collateral, failure to inspect, environmental due diligence, negligent loan processing and administration, wrongful setoff, violations of statutes and regulations of governmental entities, instrumentalities and agencies (both civil and criminal), racketeering activities, securities and antitrust laws violations, tying arrangements, deceptive trade practices, breach or abuse of fiduciary duty, breach of any alleged special relationship, course of conduct or dealing, obligation of fair dealing, obligation of good faith, whether or not in connection with or related to this Plan, at law or in equity, in contract in tort, or otherwise, known or unknown, suspected or unsuspected. It is the intent of the Plan that this definition of claims shall be as broad as permitted by applicable law and shall include all claims, whether or not disclosed in the Debtors' Schedules, and shall include any claims referenced in any disclosure statement, pleadings or Schedules filed in these Cases.

1.10 Chapter 11 Case means the cases commenced by the Debtors pursuant to the provisions of Chapter 11 of the Bankruptcy Code.

1.11 Claim means and includes: (i) all rights to any legal remedy, including rights of payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured; or (ii) all rights to any equitable remedy, including all rights based upon breach of performance if such breach gives rise to a right of payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured or unsecured.

1.12 Claimant means a holder of a Claim.

1.13 Class means all of the holders of Claims against or Interests with respect to the Debtors that have been designated as a class in Article III hereof.

1.14 Collateral means any property or interest in property of a Debtors' Estate that is subject to a Lien to secure the payment or performance of a Claim, which Lien is not subject to avoidance under the Bankruptcy Code.

1.15 Committee means the Official Committee of Unsecured Creditors' of the Debtors.

1.16 Confirmation means the Bankruptcy Court's confirmation of the Plan.

1.17 Confirmation Date means the date of entry by the Court of an order confirming the Plan.

1.18 Confirmation Hearing means the date of the last hearing to be held before the Bankruptcy Court in which the Plan Proponent shall seek Confirmation of this Plan.

1.19 Confirmation Order means the Order confirming this Plan.

1.20 Consummation shall mean the instant upon which (i) the Trusts are formed, (ii) HPI's Collateral has been transferred to HPI, (iii) all Trust Assets have been transferred to the Trusts and (iv) distribution of cash or property has commenced to any class of Creditors, at which time this Plan shall be deemed fully consummated.

1.21 Contested when used with respect to a Claim or Interest, means a Claim against or Interest in the Debtors that is: (i) listed in the Debtors' Schedules as disputed, contingent, or unliquidated and as to which a proof of claim has been timely Filed; (ii) listed in the Debtors' Schedules as undisputed, liquidated, and not contingent and as to which a proof of Claim or Interest has been Filed with the Bankruptcy Court, to the extent the proof of Claim or Interest amount

exceeds the amount provided for in the Debtors' Schedules; or (iii) the subject of an objection which has been or may be timely Filed and which claim has not been allowed or disallowed by Final Order. Further, except as otherwise provided in this Plan, a Contested Claim shall also include any Claim as to which the holder has retained property of the estate. To the extent an objection relates to the allowance of only a part of a Claim or Interest, such a Claim or Interest shall be a Contested Claim or Contested Interest only to the extent of the objection.

1.22 Creditor means holder of a Claim as of the Petition Date.

1.23 D&O Claims means any claims, causes of action, cross claims or counterclaims against any directors, officers, employees, partners, managers or members of the Debtors or anyone acting in concert therewith, including, but not limited to, claims for breach of fiduciary duty against former officers, directors, partners or managers of the Debtors, including, but not limited to, Anthony Gumbiner, Bill Guzzetti, Russ Meduna, William Marble, and Tony Strehlow.

1.24 Debtors means Hallwood Energy, L.P., a Delaware limited partnership; Hallwood Energy Management, LLC, a Delaware limited liability company; Hallwood Gathering, L.P., a Delaware limited partnership; HG II Management, LLC, a Delaware limited liability company; Hallwood Petroleum, LLC, a Delaware limited liability company; and Hallwood SWD, LLC, a Delaware limited liability company, the Debtors and Debtors-in-Possession in the Chapter 11 Case.

1.25 Deficiency Claims means an Allowed Claim of a Creditor, equal to the amount by which the aggregate Allowed Claims of such Creditor exceed the sum of (a) any set off rights of the Creditor permitted under Section 553 of the Code, plus (b) the Secured Claim of such Creditor; provided, however, that if the holder of a Secured Claim or the Class of which such Claim is a member makes the election provided in Section 1111(b)(2) of the Code, there shall be no Deficiency Claim in respect of such Claim.

1.26 Disallowed Claim or Disallowed Interest means a Claim against, or Interest in, the Debtors, or any portion thereof, (i) that has been disallowed by Final Order, (ii) proof of which has been untimely Filed and as to which no Order of allowance has been entered by the Bankruptcy Court, or (iii) listed as disputed, contingent, or unliquidated and as to which no proof of claim or proof of interest has been timely Filed.

1.27 Disclosure Statement means the written disclosure statement approved by the Bankruptcy Court that relates to this Plan that the Plan Proponent has distributed to solicit acceptances of the Plan.

1.28 Effective Date means the date on which (i) the Trusts are formed, (ii) HPI's Collateral has been transferred to HPI and (iii) all Trust Assets have been transferred to the Trusts; which date shall be not later than 30 days after the date that the Confirmation Order

becomes a Final Confirmation Order. Notice of the occurrence of the Effective Date shall be filed by the Plan Proponent and provided to all professionals retained by the Debtors and the Committee.

1.29 Entity includes any individual, partnership, corporation, estate, trust, governmental unit, person, and the United States Trustee.

1.30 Estate means the estates of the Debtors, being all assets of the Debtors, as created under Section 541 of the Bankruptcy Code upon the commencement of the Chapter 11 Case.

1.31 Estimated Claim means any Contested Claim which is estimated in accordance with Section 502(c) of the Code. For purposes of distribution, the estimated amount of such Contested Claim pursuant to Section 502(c) shall be deemed the Allowed Amount of such Claim, subject to the provisions of Section 502(j) that provide for reconsideration of an allowed claim for cause. For the full satisfaction of its Contested Claim and its Allowed Claim, a Claimant shall have, as its sole and exclusive remedy against the Debtors, the rights to payment provided under this Plan and shall have no other rights or remedies and may not, following Consummation, assert any other right against any of the Debtors, Claimant's estimated and Allowed Claim being fully satisfied by the Debtors' payment obligations described in this Plan, and any amount in excess thereof being fully released, voided and discharged by the Confirmation of this Plan.

1.32 Farmout Agreement means the Acquisition and Farmout Agreement by and among FEI and the Debtors dated June 9, 2008.

1.33 Fee Claim means a Claim for fees and expense reimbursements under Sections 330 or 503(b) of the Bankruptcy Code.

1.34 FEI Shale means FEI Shale L.P.

1.35 Filed means filed with the Bankruptcy Court.

1.36 Final Confirmation Order means the Confirmation Order entered by the Bankruptcy Court confirming this Plan provided that such Confirmation Order has not been amended, modified or reversed in such a manner as is unacceptable to the Plan Proponent and provided that (i) no appeal, petition for certiorari, motion for reargument or rehearing shall then be pending or (ii) in the event that an appeal, writ of certiorari, reargument or rehearing thereof has been sought, no stay has been granted. In the event that an appeal, writ of certiorari, reargument or rehearing thereof has been sought and a stay has been obtained, the Confirmation Order shall become a Final Order after it has been affirmed by the highest court to which such order may be appealed, or certiorari has been denied, and the time to take any further appeal, petition for certiorari or move for reargument or rehearing shall have expired.

1.37 Final Order means an order or judgment, entered by the Bankruptcy Court or other court of competent jurisdiction as to which (i) the time to appeal, petition for certiorari, or move for reargument or rehearing has expired and as to which no appeal, petition for certiorari, or other proceedings for reargument or rehearing, shall then be pending or, (iii) in the event that an appeal, writ of certiorari, reargument or rehearing thereof has been sought, such order shall have been affirmed by the highest court to which such order may be appealed, or certiorari has been denied, and the time to take any further appeal, petition for certiorari or move for reargument or rehearing shall have expired.

1.38 General Unsecured Claims means an Unsecured Claim that is not entitled to priority under Section 507 of the Bankruptcy Code and is not an Administrative Convenience Claim or any Claim relating to Interests.

1.39 Hallwood Group means The Hallwood Group, Inc., a public company that holds Interests in and Claims against Hallwood Energy, L.P.

1.40 HELP/HPI Notes means the \$100,000,000 promissory note issued by Hallwood Energy, L.P. to HPI dated April 19, 2007 and the \$15,000,000 promissory note issued by Hallwood Energy, L.P. to HPI dated January 18, 2008.

1.41 HPE means Hall Phoenix Energy, LLC, an affiliate of HPI that has been formed to own HPI's Claims against the Debtors and HPI's Collateral.

1.42 HPI means Hall Phoenix/Inwood, Ltd, the Plan Proponent and the designee of, and agent for, the Trustees of the Trusts for certain actions and duties related to the Trusts as provided in the Plan.

1.43 HPI Collateral means all of the Debtors' assets in which security or other Lien interests have been granted by any one or more of the Debtors to secure the Claims of HPI including, but not limited to, Accounts; Chattel Paper; Documents; General Intangibles; Goods (including Inventory and Equipment); Instruments; Insurance; Intellectual Property; Investment Related Property (including the equity interests of Hallwood Energy in its subsidiaries Hallwood Petroleum, LLC, HG II Management, LLC, and Hallwood Gathering, LP, and the equity interest of Hallwood Energy Management, LLC in Hallwood Energy); Letter of Credit Rights; Money (including a lien on \$3,200,000.00 cash held by Hallwood Group Incorporated in a segregated account for the benefit of Hallwood Energy, subject to a superior lien held by FEI Shale, L.P.); Receivables and Receivable Records; Commercial Tort Claims; to the extent not otherwise included above, all Collateral Records, Collateral Support and Supporting Obligations relating to any of the foregoing; to extent not otherwise included above, all Proceeds, products, accessions, rents and profits of or in respect to any of the foregoing; all of Hallwood Energy's oil and gas properties, located in the States of Texas, Arkansas, Mississippi and Louisiana; all assets of Hallwood Energy Management, LLC

(Hallwood Energy's general partner), and all the assets of Hallwood Energy's subsidiaries Hallwood Petroleum, LLC, HG II Management, LLC, Hallwood Gathering, LP, and Hallwood SWD, LLC, all Debtors in this jointly-administered case.

1.44 HPI's Direct Claims means any claims by HPI arising out of, or in connection with, its lending relationship with the Debtors, which are assertable directly by HPI against any party other than the Debtors but only to the extent that such claims are legally assignable to Trust I. To the extent such claims are not legally assignable they will remain with HPI. The direct claims will not include any claims arising from HPI's or its affiliates ownership interests in the Debtors or HGI.

1.45 HPI Operating Account means the Debtors' bank accounts on which HPI has a Lien and into which the Debtors deposit proceeds from the sale of gas. Pursuant to the Bankruptcy Court's order on HPI's stay motion, all monies in the HPI Operating Account in excess of \$500,000 have been transferred to HPI. The remaining \$500,000 has been designated for the payment of up to \$50,000 in professional fees of the Committee for each of the months of June, July and August 2009; reservation of \$100,000 to secure the Liens, if any, of Wells Fargo and the balance for payment of other expenses as mutually agreed to by the Committee and HPI with any unused amount to be paid to HPI.

1.46 HPI Secured Lender Collateral means all collateral granted by HPI to secure the HPI Secured Lender Note which includes the HELP/HPI Notes and the HPI Collateral.

1.47 HPI Secured Lender Note means the promissory notes issued under the \$65,000,000 Credit Agreement dated May 10, 2007, as subsequently amended, modified or restated.

1.48 HPI Secured Lenders means the financial institutions which are lenders to HPI under the promissory notes issued under the \$65,000,000 Credit Agreement dated May 10, 2007, as subsequently amended, modified or restated.

1.49 Impaired means the treatment of an Allowed Claim or Allowed Interest under this Plan unless, with respect to such Claim or Interest, either: (i) this Plan leaves unaltered the legal, equitable, and contractual rights to which such Claim or Interest entitles the holder of such Claim or Interest, or (ii) notwithstanding any contractual provision or applicable law that entitles the holder of such Claim or Interest to demand or receive accelerated payment of such Claim or Interest after occurrence of a default, the Debtors (A) cures any default that occurred before, on or after the commencement of the Chapter 11 Case other than default of the kind specified in Section 365(b)(2) of the Bankruptcy Code; (B) reinstates the maturity of such Claim or Interest as such maturity existed before such default; (C) compensates the holder of such Claim or Interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law; and (D) the Plan does not otherwise alter the legal, equitable or contractual rights to which such Claim or Interest entitles the holder of such Claim or Interest.

1.50 Interest means the equity interests in the Debtors represented by shares of issued and outstanding common stock, preferred stock or any options, warrants or rights to purchase or acquire such stock.

1.51 J. Aron Claims means any claims or causes of action of the Debtors against J. Aron and Company, a Goldman Sachs affiliate, which had made a loan to the Debtors pre-petition that was paid off as part of the loans made by HPI.

1.52 Junior M&M Lien Claims means any timely filed and Allowed M&M Liens against the Debtors' properties that are junior in priority to the Liens of HPI.

1.53 Lien means all valid and enforceable liens, security interests, claims and encumbrances against any property of the Estate which are permitted by, or not avoided pursuant to, the Bankruptcy Code.

1.54 M&M Lien means all valid and enforceable liens and security interests arising under any applicable state laws providing for a lien to secure the provision of goods and services in connection with oil and gas properties.

1.55 Net Proceeds means the cash or cash equivalents and any other value, or proceeds arising from the sale or disposition of any Trust Assets, following payment of any (i) reasonable fees and expenses of the Trust, (ii) normal and reasonable expenses of administration of any Trust Assets (including the establishment of such reasonable reserves on behalf of any Trust as the Trustee thereof deems appropriate), and (iii) all reasonable investment banker fees, brokerage commissions, professional fees, legal fees, accounting fees, marketing and sale expenses, title fees, taxes, levies, assessments, other governmental charges, or any other type of expense, fee or cost incurred in connection with the disposition of any Trust Assets.

1.56 Other Priority Claims means and includes all Priority Claims except Administrative Claims, Priority Tax Claims, and Priority Wage Claims.

1.57 Order means an order or judgment of the Bankruptcy Court.

1.58 Person means an individual, corporation, partnership, joint venture, association, joint stock company, limited liability company, limited liability partnership, trust, estate, unincorporated organization or other entity.

1.59 Petition Date means March 1, 2009.

1.60 Plan means this Plan of Reorganization for the Debtors, as it may be amended or modified from time to time as permitted herein or in accordance with Section 1127 of the Bankruptcy Code.

1.61 Plan Proponent means HPI.

1.62 Plan Rate means the prime rate of Bank of America, N.A. in effect at Confirmation, plus one percent (1%) or such other rate of interest as is determined by the Bankruptcy Court.

1.63 Preference Actions means any Cause of Action arising under Section 547 of the Bankruptcy Code.

1.64 Priority Claim means all Claims entitled to priority under section 507(a)(2)-(a)(7) and (a)(9) of the Bankruptcy Code.

1.65 Priority M&M Lien Claim means any timely filed and Allowed M&M Liens against the Debtors' properties that are senior in priority to the Liens of HPI.

1.66 Priority Tax Claim means all Claims for Taxes entitled to priority under section 507(a)(8) of the Bankruptcy Code, and shall include all Tax Claims secured by assets of the Estate.

1.67 Priority Wage Claim means all Claims for wages entitled to priority under section 507(a)(3) of the Bankruptcy Code.

1.68 Project Account means that certain account that was established in accordance with the Farmout Agreement into which were placed the monies funded by FEI Shale to the Debtors. Pursuant to an order of the Bankruptcy Court the Project Account (less certain reserved amounts) has now been transferred to FEI Shale for payment of approved Investment Invoices (as defined in the Farmout Agreement), which primarily consist of Priority M&M Lien Claims and Junior M&M Lien Claims.

1.69 Pro Rata means, with reference to any distribution on account of an Allowed Claim or Allowed Interest, the proportion that an Allowed Claim or Allowed Interest in a particular Class bears, respectively, to the aggregate amount of all Claims or Interests in such Class, including Contested Claims or Contested Interests which are not Disallowed Claims or Disallowed Interests as of the date of such calculation.

1.70 Record Holder means an equity security holder or creditor whose claim is based on a security of record and who is the holder of record of the security on the date the order approving the Disclosure Statement is entered or on another date fixed by the Bankruptcy Court, for cause, after notice and a hearing.

1.71 Recoveries means the cash and cash equivalents and any other value, or proceeds of settlement, litigation or other disposition of the Causes of Action.

1.72 Schedules means those schedules and statements of financial affairs Filed by the applicable Debtors under Federal Rule of Bankruptcy Procedure 1007, as same may be amended from time to time.

1.73 Secured Claim (or Allowed Secured Claim) means an Allowed Claim that is secured by a lien on or security interest in property in which the Estate has an interest, or that is subject to setoff under Section 553 of the Bankruptcy Code, to the extent of the value of a Claimant's interest in such Estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be.

1.74 Sub-Debt Creditors means all Creditors whose Claims arise under any convertible subordinated note agreements with the Debtors. Holders of these Claims have contractually agreed to subordinate their debt to HPI and agreed that HPI will receive any distributions on their Claim until HPI's Claims have been paid in full.

1.75 Subordinated Claim means all Claims (i) arising from fines, penalties or punitive damages, (ii) arising from rescission of a purchase or sale of a security of the Debtors, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under Section 502 of the Bankruptcy Code on account of such a claim, (iii) subordinated to general unsecured claims under Section 510(b) or (c) of the Bankruptcy Code or (iv) contractually subordinated to any secured or general unsecured claim.

1.76 Taxes means and includes all federal, state, county and local income, ad valorem, excise, stamp and other taxes of any type or nature whatsoever.

1.77 Tax Claims means any and all Secured or Priority Claims of any Entity for the payment of any Taxes (a) accorded a priority pursuant to Section 507(a)(8) of the Code (but excluding all Claims for post-petition interest and pre-petition and post-petition penalties all of which interest and penalties, pre-confirmation and post-confirmation, shall be (i) deemed disallowed and (ii) fully discharged on the Confirmation Date), or (b) secured by valid Liens on assets of the Debtors existing on the Confirmation Date (but excluding all Claims for post-petition interest and pre-petition and post-petition penalties, all of which interest and penalties shall be (i) deemed disallowed and (ii) discharged on Confirmation Date). Additionally, all Liens securing Tax Claims shall be deemed and legally treated as released, voided and discharged on the Confirmation Date.

1.78 Trade Creditors means any holder of an Allowed Unsecured Claim in Class 10 other than HPI and Sub-Debt Creditors.

1.79 Trust or Trusts means any of the trusts created on the Effective Date pursuant to its respective Trust Agreement.

1.80 Trust I means the Hallwood Energy I Creditors' Trust as described in Section 6.02 of the Plan.

1.81 Trust II means the Hallwood Energy II Creditors' Trust as described in Section 6.03 of the Plan.

1.82 Trust III means the Hallwood Energy III Creditors' Trust as described in Section 6.04 of the Plan.

1.83 Trust Agreement means the agreement governing any of the respective Trusts and any exhibits, supplements or amendments thereto, filed no later than ten (10) days prior to the Confirmation Hearing.

1.84 Trust Assets means the assets of each of the three Trusts arising under this Plan.

1.85 Trust Related Assets means the Debtors' rights, privileges, interests, books and records and other documents of any kind that relate to, or are necessary to the prosecution of, the Causes of Action transferred to each respective Trust. As to Trust I the Trust Related Assets shall specifically include the Debtor's attorney-client privilege as to all matters.

1.86 Trust Shares means the interests in any of the Debtors issued pursuant to 11 U.S.C. Section 1145 to Trust I for the benefit of the Creditors under this Plan. The Trust Shares shall be issued in the discretion of the Trustee of Trust I subject to the consent of HPI.

1.87 Trustee means the trustee appointed to serve as administrator for each of the three respective Trusts created under this Plan pursuant to the Trust Agreement and appointed by the Confirmation Order as trustee, and any successor trustee selected pursuant to the respective Trust Agreements.

1.88 Unsecured Creditor means the holder of a Claim that is not secured by a Lien and includes General Unsecured Claims, Administrative Convenience Claims, an Administrative Claim, a Priority Claim, or a Priority Tax Claim.

1.89 Wells Fargo means Wells Fargo Bank, N.A., the issuer of two letters of credit on behalf of the Debtors.

ARTICLE II

TREATMENT OF NON-CLASSIFIED CLAIMS

This Plan does not classify Claims against the Debtors having priority as specified in Section 507 of the Bankruptcy Code, which Claims shall be treated as follows:

2.01 Administrative Claims:

- (a) **In General.** Each holder of an Administrative Claim except as otherwise set forth in this Article 2 (and specifically excluding Priority Tax Claims as set forth in Section 2.02 below) shall receive either: (i) with respect to Administrative Claims which are Allowed Claims on the Effective Date, the amount of such holder's Allowed Claim in one cash payment as soon as practicable after the Effective Date; (ii) with respect to Administrative Claims which become Allowed Claims after the Effective Date, the amount of such holder's Allowed Claim in one cash payment, as soon as practicable after such claim becomes an Allowed Administrative Claim; or (iii) such other treatment agreed upon by the Trustee of Trust I and such holder. Allowed Administrative Claims shall be paid first from the Project Account and/or the HPI Operating Account to the extent funds are available for payment of such Claims and then by the Trustee of Trust I.

- (b) **Fee Claims.** Each professional Person whose retention with respect to the Debtors' case has been approved by the Bankruptcy Court or who holds, or asserts, an Administrative Claim that is a Fee Claim shall be required to file with the Bankruptcy Court a final fee application within sixty (60) days after the Effective Date and to serve notice thereof on all parties entitled to such notice including the Plan Proponent. The failure to file timely any such application as required under this Section 2.01(b) of this Plan shall result in the Fee Claim being forever barred and discharged. A Fee Claim, with respect to which a Fee Application has been properly Filed pursuant to this Section 2.01(b) of this Plan, shall become an Administrative Claim only to the extent allowed by a Final Order. Not later than five (5) days after the service of the notice of occurrence of the Effective Date, any Person intending to file a Fee Claim shall file an estimate of such final Fee Claim, including a notice of any retainer received, on counsel for the Debtors, the Committee, the Plan Proponent and the Office of the United States Trustee. Fee Claims shall be paid first from the Project Account and/or the HPI Operating Account to the extent funds are available for payment of such Claims and to the extent permitted by the orders of the Bankruptcy Court regarding such accounts and then from Trust I as soon as practicable after

entry of a Final Order allowing such Claim after giving effect to any claims of setoff by the Debtors' Estates. No payment shall be required to be made on any such Claims if the holder is the subject of a Cause of Action by any of the Trusts until such Cause of Action has been resolved by Final Order.

- (c) **Administrative Claims Bar Date.** Any other Person or Entity who claims to hold an Administrative Claim (other than a Fee Claim) shall be required to file with the Court an application within sixty (60) days after the Effective Date and to serve notice thereof on all parties entitled to such notice. The failure to file timely the application as required under this Section 2.01(c) of this Plan shall result in the Claim being forever barred and discharged. An Administrative Claim with respect to which an application has been properly Filed pursuant to this Section 2.01(c) of this Plan and to which no timely objection has been filed or an objection has been filed but overruled by the Court, shall become an Allowed Administrative Claim to the extent such claim is allowed by Final Order.

2.02 Administrative and Priority Tax Claims:

- (a) **Administrative Tax Claims.** Each holder of an Administrative Claim that is an Allowed Claim for Taxes for which the Debtors are responsible for the period during which the Debtors' Chapter 11 Case is being administered, and any other Taxes of the Debtors payable pursuant to Section 507(a)(1) of the Bankruptcy Code, if any, shall be paid the Allowed Amount of such holder's Claim in cash, in full, by the Trustee of Trust I as soon as practicable after the Effective Date.
- (b) **Priority Tax Claims.** Each Allowed Tax Claim (as defined above) shall be paid by the Trustee of Trust I in accordance with Section 1129(a)(9)(C) of the Bankruptcy Code, over a period not exceeding five years after the Petition Date, commencing as soon as funds are available, with interest accruing thereon from and after the Effective Date at the Plan Rate.

2.03 Other Priority Claims. Each Other Priority Claim, shall be paid by the Trustee of Trust I in accordance with Section 1129(a).

2.04 U.S. Trustee Fees. All fees payable under 28 U.S.C. § 1930 shall be paid in cash in full by the Trustee of Trust I.

ARTICLE III

DESIGNATION OF CLASSES OF CLAIMS AND INTERESTS

For purposes of repayment of the Debtors' indebtedness under the Plan, the Claims and Interests are divided into the following classes:

3.01 Class 1: Priority Wage Claims. This Class consists of Allowed Claims for priority wages under Section 507(a)(3) of the Code including wages, salaries, commissions, vacation, severance, and sick leave pay to the extent incurred within 90 days before the Petition Date and to the extent of \$10,950 per individual.

3.02 Class 2: (HPI's Secured Claims): This Class consists of the Allowed Secured Claims of HPI which Claims are secured by Liens on substantially all of the Debtors' assets.

3.03 Class 3: (FEI Shale's Secured Claims): This Class consists of the Allowed Secured Claims of FEI Shale. FEI Shale asserts a Lien against certain assets of the Debtors including the Project Account, claims arising under the Equity Support Agreement between the Debtors and Hallwood Group and certain of the Debtors' pipe inventory.

3.04 Class 4: (Priority M&M Lien Claims): This Class consists of the Allowed Secured Claims of any Creditor that are secured by M&M Liens on any of the Debtors' assets that are determined to be senior to the Liens of HPI.

3.05 Class 5: (Junior M&M Lien Claims): This Class consists of the Allowed Secured Claims of any Creditor that are secured by M&M Liens that are determined to be junior to the Liens of HPI.

3.06 Class 6: (Wells Fargo's Secured Claims): This Class consists of the Allowed Secured Claims of Wells Fargo represented by two letters of credit in the respective amounts of \$25,000 and \$50,000 and secured by liens on the Debtors' accounts.

3.07 Class 7: (Secured Tax Claims): This Class consists of the Allowed Secured Claims of any states and or relevant municipalities and government entities for sales or property taxes that are entitle to automatic first lien priority pursuant to their state laws or are entitled to secured status by virtue of the value of the collateral that is located in such state.

3.08 Class 8: (Other Secured Claims): This Class consists of any Allowed Secured Claim that has not otherwise been designated in a separate Class.

3.09 Class 9: (Administrative Convenience Claims): This Class consists of Allowed Unsecured Claims of \$10,000 or less against any of the Debtors including any Creditors with Allowed Unsecured Claims in excess of \$10,000 that elect to reduce their claim to \$10,000.

3.10 Class 10:(General Unsecured Claims): This Class consists of Allowed Unsecured Claims in excess of \$10,000, including, but not limited to, the deficiency claim of HPI and claims of holders of convertible notes. Class 10 is further divided into sub-classes comprised of the Allowed Unsecured Claims against each of the Debtors as follows:

Class 10A: Allowed General Unsecured Claims against Hallwood Energy, L.P.

Class 10B: Allowed General Unsecured Claims against Hallwood Energy Management, LLC.

Class 10C: Allowed General Unsecured Claims against Hallwood Gathering, L.P.

Class 10D: Allowed General Unsecured Claims against HG II Management, LLC.

Class 10E: Allowed General Unsecured Claims against Hallwood Petroleum, LLC.

Class 10F: Allowed General Unsecured Claims against Hallwood SWD, LLC.

3.11 Class 11:(Unsecured Subordinated Claims): This Class consists of the Subordinated Claims of any Creditor.

3.12 Class 12:(Interests of Equity Security Holders): This Class consists of: i) the holders of partnership interests in Hallwood Energy, LP and Hallwood Energy Management, LLC; and ii) pursuant to Section 510(b) of the Bankruptcy Code, holders of Claims arising from rescission of a purchase or sale of a security of any of the Debtors or of any affiliate of any of the Debtors, or for reimbursement or contribution allowed under Section 502 on account of such a Claim.

ARTICLE IV

PROVISIONS FOR SATISFACTION OF CLAIMS AND INTERESTS

The Claims and Interests as classified in Article III hereof shall be satisfied in the manner set forth in this Article IV. The treatment of, and the consideration to be received by, Entities holding Allowed Claims against and/or Allowed Interests in the Debtors pursuant to this Plan shall be in full satisfaction of their respective Allowed Claims against and Allowed Interests in the Debtors, but shall not affect the liability of any other Entity on such Claim or Interest.

4.01 Class 1: Priority Wage Claims. Claims in Class 1 will be paid 100% of the Allowed Amount of their Claims by the Trustee of Trust I after giving effect to any claims of setoff by the Debtors' Estates. No payment shall be required to be made on any such Claims if the holder is the subject of a Cause of Action by any of the Trusts until such Cause of Action has been resolved by Final Order.

4.02 Class 2:HPI's Secured Claims. HPI will have an Allowed Claim in the amount of \$118,000,000 of which \$28,000,000 will be an Allowed Secured Claim and \$90,000,000 will be an Allowed Unsecured Claim. The amount of the Allowed Secured Claim is an estimation of the value of HPI's Collateral. HPI's Secured Claim will be treated and fully satisfied in accordance with the terms of the HPI Settlement set forth in Section 6.01 of the Plan. HPI's Allowed Unsecured Claim will be treated as an Unsecured Claim in Class 10. The HPI Secured Claim and HPI Unsecured Claim are currently, and shall continue to be, subject to the security interest and lien of the HPI Secured Lenders and serve as collateral for the HPI Secured Lender Note as described in Section 6.01h of the Plan.

4.03 Class 3:FEI's Secured Claims. FEI Shale's Allowed Claims are secured by Liens on its Collateral as defined in the Farmout Agreement. FEI Shale's Allowed Secured Claim will be treated under Option A or Option B below as elected by FEI Shale on its Ballot:

Option A:

- a. The Allowed Secured Claim of FEI Shale will be determined by Final Order of the Bankruptcy Court.
- b. FEI Shale will retain all of its Liens that existed as of the Petition Date.
- c. Any monies remaining in the Project Account pursuant to the order granting the stay motion of FEI Shale which was entered on June 26, 2009, will be used in accordance with such order to fund health, safety and environmental issues up to \$250,000, June G&A expenses up to \$140,000 and to pay Allowed professional fees of the Debtors and Committee for the months of March, April and May, 2009 up to \$630,953.65. Any unused amounts will be transferred to FEI Shale. All monies received by FEI Shale from the Project Account will be used to satisfy unpaid approved Investment Invoices (as defined in the Farmout Agreement). Any Creditor receiving payment from FEI Shale must release the Estates and FEI Shale from the paid Claim. FEI Shale shall file with the Bankruptcy Court a list of all Creditors paid by FEI Shale within 60 days of June 26, 2009 and update such list every 30 days thereafter.
- d. To the extent FEI Shale has an Allowed Secured Claim that is secured by an interest in the pipe inventory that is senior to HPI's Liens, the pipe inventory in which FEI

Shale has an interest will be relinquished to the possession of FEI Shale at its present location.

- e. To the extent FEI Shale has an Allowed Secured Claim that is secured by an interest in the Equity Support Agreement, FEI Shale shall retain its Lien against any monies recovered by Trust I up to the Allowed Amount of its Secured Claim.

Option B:

- a. FEI Shale agrees to transfer its interests in the Subject Properties and all Related Properties (as defined in the Farmout Agreement) located in Arkansas, Louisiana and Mississippi to HPI and the Debtors and their Estates agree to transfer to FEI Shale all of the Debtors' interests in the Subject Properties and all Related Properties (as defined in the Farmout Agreement) located in Texas;
- b. The above transfers will be without warranty of title or other representations or warranties other than as to corporate authority;
- c. The transfers will include all relevant lease files, land files, well files, and contract files maintained by the Debtors;
- d. Each transferee will assume all liabilities associated with the condition of the Subject Properties to be transferred to it, including with respect to environmental matters, P&A and site restoration obligations, regardless of when such liabilities arise, accrue or accrued;
- e. Any monies remaining in the Project Account pursuant to the order granting the stay motion of FEI Shale which was entered on June 26, 2009, will be used in accordance with such order to fund health, safety and environmental issues up to \$250,000, June G&A expenses up to \$140,000 and to pay Allowed professional fees of the Debtors and Committee for the months of March, April and May, 2009 up to \$630,953.65. Any unused amounts will be transferred to FEI Shale. All monies received by FEI Shale from the Project Account will be used to satisfy unpaid approved Investment Invoices (as defined in the Farmout Agreement) as agreed to by HPI and FEI Shale. Any Creditor receiving payment from FEI Shale must release the Estates and FEI Shale from the paid Claim. FEI Shale shall file with the Bankruptcy Court a list of all Creditors paid by FEI Shale within 60 days of June 26, 2009 and update such list every 30 days thereafter.
- f. FEI Shale will release its Liens and Claims, if any, to the Debtors' pipe inventory;
- g. FEI Shale will assign its Liens and any remaining Allowed Secured Claim to HPI;

- h. All agreements between the Debtors and FEI Shale are rejected upon entry of the Confirmation Order to the extent not previously rejected. FEI Shale will not have any claim for rejection damages.
- i. FEI Shale agrees to provide HPI a right of first refusal on a farmout to HPI and the use of any existing well bores in PSL BLOCK 113 SECTION 13 & 14 AND 23 & 24, and PSL BLOCK 113 SECTION 1 and to all rights from the top of the Devonian formation (or its stratigraphic equivalent) and deeper. The "Devonian" (or its equivalent) is that formation as seen in the electric logs of the American Quasar #1 Bateman well, API# 4210930922000 at a depth of 15,390" upon FEI Shale or its assignees abandoning the subject area wellbores. In the event HPI exercises its right to the above noted farmout and the use of the related well bores, FEI Shale agrees to leave the casing in such well bores and HPI agrees to assume responsibility for the assumed wells including any subsequent abandonment and plugging costs.
- j. The Debtors' Estates will release any claims they may have against FEI Shale.

In the event that FEI Shale elects Option B, HPI will seek the consent of the HPI Secured Lenders. In the event that the HPI Secured Lenders do not approve the proposed exchange of property interests and other terms under Option B, FEI Shale will receive the treatment provided under Option A.

4.04 Class 4: Priority M&M Lien Claims. Claims in Class 4 will be fully satisfied, at the Plan Proponent's option, by one of the following:

a. Cash Option: To the extent not paid by FEI Shale from the transferred balance of the Project Account, Claims in Class 4 will be paid from Trust I 100% of the Allowed Amount of the Claim provided their Allowed Claim is secured by a valid Lien on the Debtors' properties that is senior to HPI's Liens. Payments will be made either (i) in full in cash within 30 days after the later of the Effective Date or after the date of the last payment by FEI Shale of any Claims with the transferred balance of the Project Account or (ii) within 24 months after the Effective Date in quarterly payments with interest at the Plan Rate. Upon the payment in full of the Allowed Claim, the holder of such Class 4 Claim shall execute all instruments and documents necessary to release its Lien securing such Claim. It is the Plan Proponent's intention to exercise this option as to Liens secured by the Debtors' properties in Arkansas and Texas with the exception of certain designated wells as determined by HPI or HPE.

b. Foreclosure Option: The Plan Proponent may also elect, at any time on or before the Effective Date, to fully satisfy a Class 4 Claim by permitting the holder of such Claim to exercise its statutory lien rights and foreclose its Liens on the property securing such Claim. It is the Plan Proponent's intention to exercise this option as to Liens secured by the Debtors' properties in Louisiana and Mississippi and as to certain designated wells in Texas and Arkansas.

4.05 Class 5: Junior M&M Lien Claims. To the extent not paid by FEI Shale from the transferred balance of the Project Account, Claims in Class 5 will be treated as Unsecured Claims in Class 9 or 10 depending on the amount of the Claim.

4.06 Class 6: Wells Fargo's Secured Claims. To the extent the Claims in Class 6 are secured by Liens on the Debtors' cash that are senior to HPI's Liens, the Claims will retain their Liens on the Debtors' cash (whether in the possession of the Debtors, HPI or HPE) until the letter of credit obligations have been terminated. To the extent the Liens are junior to HPI's Liens, the Claims will be treated as Class 10 Claims.

4.07 Class 7: Secured Tax Claims. Claims in Class 7 will be fully satisfied, at the Plan Proponent's option, by one of the following:

a. Cash Option: Payment from Trust I of 100% of the Allowed Amount of the Claim provided their Allowed Claim is secured by a valid Lien on the Debtors' properties. Payments will be made either in full in cash within 30 days after the Effective Date or within five years after the Petition Date in quarterly payments with interest at the Plan Rate. Upon the payment in full of the Allowed Claim, the holder of such Class 7 Claim shall execute all instruments and documents necessary to release its Lien securing such Claim. It is the Plan Proponents intention to exercise this option as to Liens secured by the Debtors' properties in Arkansas and Texas.

b. Foreclosure Option: The Plan Proponent may also elect, at any time on or before the Effective Date, to fully satisfy a Class 7 Claim by permitting the holder of such Claim to exercise its statutory lien rights and foreclose its liens on the property securing such Claim. It is the Plan Proponent's intention to exercise this option as to Liens secured by the Debtors' properties in Louisiana and Mississippi.

4.08 Class 8: Other Secured Claims. Except to the extent that a Class 8 Claimant may otherwise agree, each holder of an Allowed Secured Class 8 Claim shall be fully satisfied, at the Plan Proponent's option, by one of the following:

a. Note Option: Each holder of a Class 8 Claim shall retain all Liens securing such Claim until such Claim is fully paid or until such holder otherwise agrees. The terms and provisions relating to such Liens shall be set forth in appropriate documents agreed to between the parties, or, in the event of disagreement, as directed by the Court. Assuming that the Collateral securing the Class 8 Claim is being transferred to HPE under the Plan, HPE shall execute a note payable to the Class 8 Creditor and deliver it to the holder of such Claim, along with an appropriate mortgage and/or security agreement, no later than the tenth (10th) Business Day after the later of the Effective Date or the date that such Claim becomes an Allowed Claim. The initial principal amount of each Class 8 Claim shall be equal to the lesser of (i) the amount which the Court shall determine is equal to the value of the assets securing such Claim or (ii) the amount of the Class 8 Claim. The term of the note will be five years from the Effective Date; the interest rate will be the Plan Rate; interest

only will be paid quarterly; minimum principal payments of five percent of the principal amount of the Allowed Secured Claim will be paid annually at the end of each year to the extent not already paid from the sale of collateral securing the Allowed Secured Claim with the balance of any unpaid principal being paid at the end of five years. To the extent that any Creditor has a Deficiency Claim in addition to its Class 8 Claim, the Deficiency Claim shall be treated under this Joint Plan as an Unsecured Claim against the Debtors.

b. **Unimpairment Option:** At the option of the Plan Proponent, any Class 8 Claim may be deemed unimpaired. If such election is to be made, it must be made on or before the Effective Date. Any arrearage or other amounts owed by the Debtors as of the Effective Date (and any other payments which may at such date be required to make each such Claim unimpaired) shall be paid in cash, in full, on or before the forty-fifth (45th) Business Day after the Effective Date or as shall otherwise be agreed to in writing by the holder of such Claim, and all other defaults with respect to such Claim required to be cured by Section 1124(2) of the Code shall be cured on or prior to the forty-fifth (45th) Business Day after the Effective Date as shall be agreed to in writing by the holder of such Claim, and from and after the date of such cure any previously accelerated indebtedness shall be reinstated and any default rate of interest shall no longer apply, but shall be deemed waived (not forgiven). Each Class 8 Creditor whose claim is unimpaired pursuant to the terms hereof shall retain such lien as such Creditor held prior to the Petition Date. After the reinstatement of its Class 8 Claim, each Class 8 Creditor will receive payments from HPE in accordance with the instruments governing such Claim or as such Creditor may otherwise in writing agree. Furthermore, after such unimpairment, each Class 8 Creditor will be entitled to exercise all rights, privileges, and remedies available to it under the instruments governing its Class 8 Claim in accordance with the terms for such instruments, without need for any application to or order of the Court.

c. **Cash Option:** The Plan Proponent may also elect, at any time on or before the Effective Date, to have HPE pay a Class 8 Secured Claim in full, in cash, on or promptly after the Effective Date.

d. **Abandonment Option:** The Plan Proponent may also elect, at any time on or before the Effective Date, to fully satisfy a Class 8 Claim by abandoning the collateral securing such Claim to the holder of such Claim.

e. **Release of Lien:** Upon the satisfaction of any note given to any holder of a Class 8 Secured Claim pursuant to any of the methods provided for in this Plan, the holder of such Class 8 Secured Claim shall execute all instruments and documents necessary to release its Lien securing such Claim or note.

4.09 Class 9: Administrative Convenience Claims. Claims in Class 9 will be paid by the Trustee of Trust I 50% of the Allowed Amount of their Claims as soon as practicable after the Effective Date.

4.10 Class 10: General Unsecured Claims. Holders of Allowed Claims in Class 10 will receive a beneficial interest in each of the Trusts (except that only Trade Creditors will receive an interest in Trust III) entitling them to a Pro Rata share of the Trust Assets in each Trust after payment of Allowed Administrative and Priority Claims and Allowed Class 4 Priority M&M Lien Claims up to the Allowed Amount of their Claims unless their Claims are subordinated in which case they shall be treated in Class 11. The Debtors' separate Estates are not being substantively consolidated under this Plan. However, all holders of Unsecured Claims in Class 10 will receive the same treatment by virtue of the settlement with HPI. Claims in Class 11 are subdivided for voting and treatment under this Plan into six (6) sub-Classes representing each of the six (6) Debtors:

Class 10A: Allowed General Unsecured Claims against Hallwood Energy, L.P.

Class 10B: Allowed General Unsecured Claims against Hallwood Energy Management, LLC.

Class 10C: Allowed General Unsecured Claims against Hallwood Gathering, L.P.

Class 10D: Allowed General Unsecured Claims against HG II Management, LLC.

Class 10E: Allowed General Unsecured Claims against Hallwood Petroleum, LLC.

Class 10F: Allowed General Unsecured Claims against Hallwood SWD, LLC.

Contractual subordination provisions between HPI and Sub-Debt Creditors shall be given full force and effect. Any distributions to be made to a Sub-Debt Creditor on account of an Allowed Unsecured Claim shall be paid to HPI until HPI's Allowed Unsecured Claim has been paid in full.

4.11 Class 11: Unsecured Subordinated Claims. Holders of Allowed Claims in Class 11 will receive a beneficial interest in each of the Trusts entitling them to a Pro Rata share of the Trust Assets after payment of all other Allowed Unsecured Claims.

4.12 Class 12: Holders of Equity Security Interests. Holders of Interests will have their Interests canceled and will receive nothing on account of their Interests under the Plan.

ARTICLE V

DESIGNATION OF THE CLASSES OF CLAIMS IMPAIRED UNDER THIS PLAN

5.01 Impairment. For purposes of Plan solicitation, all Classes of Claims except Class 1 are Impaired and are, therefore, entitled to cast ballots on this Plan. Class 12 Interests are deemed to have rejected the Plan.

ARTICLE VI

MEANS FOR IMPLEMENTATION OF PLAN

6.01 HPI Settlement. Confirmation of the Plan shall effect a settlement of any claims of the Debtors against HPI, its affiliated entities, officers and directors on the following terms:

- a. Dismissal of Suit by Debtors: The suit filed by the Debtors against HPI, Craig Hall and Don Braun for subordination and breach of fiduciary duty will be dismissed with prejudice.
- b. Release of HPI: The Debtors' Estates will release HPI, Hall Performance Energy Partners 4, Ltd., Craig Hall, Don Braun, and their affiliated entities, partners, members, shareholders, officers, directors and agents from any and all claims.
- c. Release of Liens on Causes of Action: HPI will release its liens on Causes of Action so that all Causes of Action owned by the Trusts will be free and clear of any liens of HPI.
- d. Transfer of Direct Claims: HPI's Direct Claims will be transferred to Trust I so that all claims can be pursued by its Trustee for the benefit of all beneficiaries of Trust I. Trust I shall have the right to bring such claims in the name of HPI or the Trust.
- e. Funding of Trusts: HPI will advance (i) all costs of Trust I, which are reasonably required, in HPI's judgment, to fund the costs of administering Trust I and (ii) \$200,000 of the costs of administering Trust II.
- f. Allowance of Claims: HPI will have an Allowed Secured Claim in the amount of \$28,000,000 and an Allowed Unsecured Claim in the amount of \$90,000,000. HPI's Allowed Claims and the HPI Collateral will be transferred to, and owned by, HPE prior to Confirmation and will be subject to the continuing security interests and liens of the HPI Secured Lenders as described in paragraph 6.01h below.
- g. HPI's Collateral: HPE will obtain title to HPI's Collateral (except Causes of Action, which are being transferred to the Trusts, and any Collateral located in Mississippi or Louisiana or anywhere else to the extent specifically excluded by HPI or HPE which will remain in the respective Debtor entity subject to HPI's and/or HPE's Liens and the HPI Secured Lenders' Liens) free and clear of all Liens, Claims and

encumbrances except HPI's Liens and except as otherwise provided in the Plan by either (i) the transfer of title to HPE of HPI's Collateral on the Effective Date or (ii) foreclosure by HPE of the Liens transferred to it by HPI. The Confirmation Order will provide all necessary authorization for the implementation of such transfers or foreclosures including authorization for HPI to execute any necessary documentation on behalf of the Debtors. HPE may elect to have some of its Collateral transferred to HPE and some foreclosed by HPE, all at HPE's election. HPE may also elect to exclude specific wells in Texas or Arkansas from the transfer of title to HPE. Any such election shall be subject to approval by the HPI Secured Lenders.

- h. The HPI Secured Lenders hold a security interest and lien in all HPI claims against the Debtors, including the HELP/HPI Notes, and in all of the HPI Collateral to secure the payment of the HPI Secured Lender Note, which security interest and lien shall continue in effect after the transfer of the HELP/HPI Notes and HPI Collateral to HPE. In the event of foreclosure by HPE on any of the HPI Collateral or the transfer of title by the Debtors to HPE of any of the HPI Collateral, HPE shall simultaneously execute a mortgage and security agreement covering such property in favor of the HPI Secured Lenders which mortgage and security agreement shall evidence the existing and continuing security interest and lien of the HPI Secured Lenders in and to such property. Such mortgage and security agreement shall be in form and substance acceptable to the HPI Secured Lenders.

The HPI Secured Lenders shall own and hold a continuing security interest and lien in all amounts payable to HPI or HPE from Trust I and Trust II. HPI and HPE shall execute a security agreement covering such payments in form and substance acceptable to the HPI Secured Lenders.

The continuing security interests and liens of the HPI Secured Lenders in all HPI claims against the Debtors, including the HELP/HPI Notes and the HPI Collateral and all proceeds and products thereof, and the obligation of HPI and/or HPE to execute new mortgages and security agreements as provided herein, shall be acknowledged and confirmed in the Confirmation Order in form and substance acceptable to the HPI Secured Lenders.

6.02 Creation of Trust I. Confirmation of the Plan shall effect the formation of a creditors' trust into which will be conveyed all Causes of Action except Preference Actions and the J. Aron Claims. This trust will be named the Hallwood Energy I Creditors' Trust. The specific terms, conditions, and rules governing this Trust are contained in the Trust Agreement with respect to this Trust. The Trust Assets for this Trust shall consist of the Project Account (subject to use of such monies in accordance with the order granting the stay motion of FEI Shale entered on June 26, 2009); the Causes of Action (except Preference Actions and the J. Aron Claims); the Trust Shares; the Trust Related Assets and HPI's Direct Claims. To the extent necessary as determined by HPI,

HPI and/or HPE agree to fund the costs to pursue Causes of Action belonging to the Trust and any Allowed Claims required to be paid on the Effective Date. The Trustee will be selected by HPI. Any Recoveries from the Trust Assets will be distributed first to fund or reimburse HPI for any monies it has funded for the administration of the Trust, the pursuit of Causes of Action or HPI Direct Claims (whether incurred before or after formation of the Trust), or the payment of any other Allowed Claims required to be paid under the Plan; second, to payment of Allowed Class 4 Senior M&M Liens and any other Allowed Claims that have priority over Unsecured Claims; third, \$1,000,000 to payment of Allowed Claims of Trade Creditors holding Class 10 Claims; and fourth, 90% Pro Rata to HPI and Sub-Debt Creditors and 10% to Trade Creditors; provided, however, that the first \$300,000 of the 10% distribution to Trade Creditors will be paid to HPI. Sub-Debt Creditors are grouped with HPI for purposes of any distributions since they have contractually agreed that any payments they are entitled to will be paid to HPI until HPI has been paid in full.

6.03 Creation of Trust II. Confirmation of the Plan shall effect the formation of a creditors' trust into which will be conveyed all Preference Actions. This trust will be named the Hallwood Energy II Creditors' Trust. The specific terms, conditions, and rules governing this Trust are contained in the Trust Agreement with respect to this Trust. The Trust Assets for this Trust shall consist of the Preference Actions and the Trust Related Assets. HPI agrees to fund \$200,000 in costs of the Trust as requested by the Trustee. The Trustee will be selected by the Committee and named in the Confirmation Order. Any Recoveries from the Trust Assets will be distributed first to fund or reimburse HPI for any costs of the Trust; and second, 40% Pro Rata to HPI and Sub-Debt Creditors and 60% to Trade Creditors. Any excess recoveries in this Trust after payment of Trade Creditors in full will be paid to HPI and Sub-Debt Creditors until their Claims are paid in full. Sub-Debt Creditors are grouped with HPI for purposes of any distributions since they have contractually agreed that any payments they are entitled to will be paid to HPI until HPI has been paid in full.

6.04 Creation of Trust III. Confirmation of the Plan shall effect the formation of a creditors' trust into which will be conveyed the J. Aron Claims. This trust will be named the Hallwood Energy III Creditors' Trust. The specific terms, conditions, and rules governing this Trust are contained in the Trust Agreement with respect to this Trust. The Trust Assets for this Trust shall consist of the J. Aron Claims and the Trust Related Assets. The Trustee may borrow monies from the Hallwood Energy II Creditors' Trust to fund the costs of the Trust. The Trustee will be selected by the Committee and named in the Confirmation Order. Any Recoveries from the Trust Assets will be distributed first to fund or reimburse the Hallwood Energy II Creditors' Trust for any costs of the Trust; and second, 100% to Trade Creditors.

6.04 Trust Assets. On the Effective Date, the Trust Assets shall be conveyed to the respective Trusts free and clear of all Liens, Claims and encumbrances.

6.05 Trust Shares. The existing ownership interests in the Debtors will be canceled effective as of the Effective Date. New ownership interests in each of the Debtors will be issued to

Trust I on the Effective Date. The Trustee of Trust I may sell or dissolve any such entities in his/her sole discretion.

6.06 Amendments to Governing Documents. The governing documents of each Debtor (i.e. articles of incorporation, bylaws, regulations, and partnership agreement) shall be amended by the Trustee of Trust I to eliminate all provisions limiting the liability of the Debtors' officers, directors, employees, managers and partners including any exculpatory and indemnity provisions. Such amendments shall be effective as of the date of organization of each respective Debtor. The Debtors' governing documents may also be amended by the Trustee of Trust I as necessary to implement this Plan.

6.07 Issuance of Shares. All shares issued are issued under Section 1145 (a)(1) and are not subject to securities laws and regulations relative to their transferability and their issuance. Such shares that are issued not on account of a claim or interest, will be issued pursuant to Section 4(2) of the Securities Act of 1933, as amended (the "**Securities Act**").

6.08 Officers and Directors. All existing officers, directors and managers of the Debtors will be removed effective on the date of entry of the Confirmation Order. HPI shall have full authority to manage the Debtors' Assets pending the Effective Date. Following the Effective Date, the Trustee of Trust I shall have the sole authority to govern the affairs of the post-confirmation Debtors, including the power to remove and replace any officer at will; to engage, retain, employ, dismiss or replace professionals; and to take any and all other actions he deems necessary and appropriate. The Trustee of Trust I may assert or waive the attorney-client privilege and any other privileges of the Debtors the same as if the Trustee was the Debtors.

6.09 Authority for Settlement of Causes of Action. The Trustees of the respective Trusts shall be authorized to compromise and settle any of the Causes of Action owned by their respective Trusts, without Court approval, at any time, and for any consideration that they believe to be reasonable and in the Creditors' best interest. Any settlement of a Cause of Action belonging to Trust I or Trust II will require the consent of HPI.

6.10 Termination of the Committee. On the Effective Date, the Committee shall cease to exist and have no further status as a party in interest.

6.11 Consummation. For all purposes, Consummation (and substantial consummation of this Plan) shall occur the instant upon which (i) the Trusts are formed, (ii) HPI's Collateral has been transferred to HPI, (iii) all Trust Assets have been transferred to the Trusts and (iv) distribution of cash or property has commenced to any class of Creditors, at which time this Plan shall be deemed fully consummated.

ARTICLE VII

THE TRUSTS

The Plan provides for the establishment of three Trusts. Each Trust shall be governed by its respective Trust Agreement that shall be substantially consistent with the following provisions:

7.01 Purposes of the Trust. The Trust shall be established for the benefit of Creditors of the Estate and the primary purposes of the Trust shall be:

- (a) to own, hold, pursue, manage and dispose of the Trust Assets for the benefit of the creditors of the Estates.
- (b) to litigate, prosecute, settle or otherwise resolve the Causes of Action belonging to the Trust;
- (c) to defend any counterclaims relating to the Causes of Action belonging to the Trust;
- (d) to own, hold and vote the Trust Shares (if applicable); and
- (e) to do anything necessary, related or incidental to the foregoing.

7.02 Term. The Trust shall terminate upon the earliest to occur of: (a) the fulfillment of the Trust purpose by the prosecution or other resolution of all of the Causes of Action belonging to the Trust, the liquidation of the Trust Assets, and the distribution of the Net Recoveries and Net Proceeds or (b) the term of five (5) years from the Effective Date. The Trustee may terminate the Trust without further Order of the Bankruptcy Court prior to the expiration of the five (5) year term in the event all activities of the Trust are completed or if all of the Causes of Action have been concluded and the Net Recoveries therefrom have been distributed in accordance with this Plan. The Trustee may, without further Order of the Bankruptcy Court, extend the term of the Trust if the conclusion of the Causes of Action and distribution of the Net Recoveries therefrom and Net Proceeds of remaining assets has not been completed, or if other circumstances require such extension.

7.03 Beneficiaries of the Trust. The beneficiaries of the respective Trusts shall be the holders of Allowed Administrative, Priority and Unsecured Claims and Senior M&M Liens, as applicable, who shall receive a beneficial interest in the respective Trust in accordance with their treatment under the terms of this Plan and the Trust Agreement.

7.04 Appointment of the Trustee. The initial Trustee shall be selected by HPI as to Trust I and by the Committee as to Trust II and Trust III. The Trustee shall administer the Trust Assets

and have the authority to initiate or continue all litigation involving the Causes of Action belonging to the respective Trust and make the payments to Creditors as provided in this Plan and the Trust Agreement.

7.05 Powers of Trustee. Except as otherwise provided in this Plan, the Trustee shall have all of the following rights and powers to:

- (a) Receive and hold, to have exclusive possession and control thereof as permissible under applicable law, maintain and administer the Trust Assets;
- (b) Employ, retain or replace professional Persons, including attorneys, accountants, appraisers, investment advisors, expert witnesses, insurance adjustors, or other Persons whose services may be necessary or advisable, in the judgment of the Trustee, to advise or assist him in the discharge of the duties of the Trustee, or otherwise in the exercise of any powers vested in the Trustee or as the Court may direct and, subject to the provisions of the Trust, to pay to such professionals reasonable compensation upon ten days notice to HPI (in this regard, the Trustee may employ professionals employed by HPI or the Committee);
- (c) collect, compromise, settle or discharge any claim of the Trust and pursue, in his discretion, on behalf of the Trust as the designated representative of the Debtors, to either judgment, order, compromise or settlement, any of the Causes of Action, and to defend any counterclaims, cross-actions or other offsets;
- (d) Distribute the cash and proceeds from the sale, liquidation, settlement, prosecution or other distribution of the Trust Assets;
- (e) Seek a determination from the Court of the Allowed Amount of any Claim or Interest against the Trust, including filing objections thereto and pursuing any contest or adversary proceedings with regard thereto and entering into any compromise or settlement thereof, and to execute any contract, including, without limitation, any release in connection with any such compromise or settlement. However, any Claim which is compromised, settled and/or released in connection with any such compromise or settlement agreement set forth in this Plan or the Trust Agreement is excluded;
- (f) Maintain possession of the originals of any and all instruments and documents pertaining to the Trust Assets and any liabilities of the Trust;

- (g) Pay all reasonable expenses incurred in connection with the administration of the Trust;
- (h) Calculate and make distribution to holders of Allowed Claims all as set forth in this Plan;
- (i) Act as the representative of the Estates pursuant to Section 1123(b)(3) of the Bankruptcy Code the same as if such Trustee had been appointed under Section 1104 of the Bankruptcy Code to pursue the Causes of Action in his respective Trust, sue and be sued, including filing and defending contested matters and adversary proceedings in the Court and actions or other proceedings in any other court or before any administrative agency and to pursue or defend any appeal from any judgment or order therefrom, including, without limitation, pursuing claims of the Trust, filing suit or adversary proceedings or contested matters in connection therewith and defending any counterclaims, cross-actions or other offsets in connection therewith and entering into any compromise, settlement, release, discharge or dismissal of any of the claims and asserting any rights, interests, or privileges belonging to the Debtors or their Estates;
- (j) Release, convey or assign any right, title or interest in or about the Trust Assets;
- (k) Enter into contracts binding upon the Trust (but not the Trustee) which are reasonably incident to the administration of the Trust and which the Trustee, in the exercise of his best judgment, believes to be in the best interests of the Trust;
- (l) Enter into real or personal property leases (for the leasing of office space and space for the storage of records) which are reasonably incident to the administration of the Trust and which, in the judgment of the Trustee, will be advantageous to the Trust and will assist the Trustee in the performance of his duties under the Trust Agreement;
- (m) Abandon and charge off as worthless, in whole or in part, those actions which in the judgment of the Trustee, are in whole or in part uncollectible;
- (n) Pay taxes and excises lawfully owing by or chargeable against the Trust or property in the possession or control of the Trustee and to take any action necessary or advisable to obtain the prompt determination of any such tax liability;

- (o) Procure and pay premiums on policies of insurance to protect the Trust, or the Trust Assets, against liability for personal injuries or property damage or against loss or damage by reason of fire, windstorm, collision, theft, embezzlement, breach of fiduciary duty or other hazards against which insurance is normally carried in connection with the activities or on properties such as those with respect to which the Trustee procures such insurance;
- (p) Allocate items, receipts or disbursements either to corpus or income (or partially to corpus and partially to income) of the Trust as the Trustee, in the exercise of his best judgment and discretion, deems to be proper, without thereby doing violence to clearly established and generally recognized principles of accounting;
- (q) Deal with any governmental regulatory authority in obtaining such approvals or exemptions as may, in the opinion of the Trustee, be necessary or desirable with respect to the administration of the Trust;
- (r) Borrow funds from any Person, subject to reasonable commercial terms as agreed upon by the Trustee and prospective lender, with the advice and counsel of HPI; and
- (s) Exercise every power granted to a trustee under the Bankruptcy Code, including the rights and benefits afforded by §§ 108 and 546 of the Bankruptcy Code, which may increase the enumerated powers of the Trustee otherwise granted herein, and engage in any and all other activities, not in violation of any other terms of the Plan and Trust Agreement, which, in the judgment of the Trustee, are necessary or appropriate for the proper liquidation, management, investment and distribution of the assets of the Trust in accordance with the provisions of the Trust Agreement, to effectuate the provisions of the Plan, and to perform such other tasks as the Bankruptcy Court may direct.

7.06 Payment of Trust Fees and Expenses. The Trustee may establish reasonable reserves and accounts at banks and other financial institutions, in a clearly specified fiduciary capacity, into which cash and property may be deposited and checks drawn or withdrawals made to pay or distribute such amounts as permitted or required for reasonable fees, expenses and Trust liabilities pursuant to this Plan and the Trust Agreement. Such funds shall not be subject to any claim by any entity except as provided under this Plan. All reasonable fees and expenses of the Trust, and its agents and employees incurred in connection with (i) the objection to, and settlement, liquidation and payment of claims and interests against the Debtors; (ii) the liquidation or acquisition of assets; or (iii) administering the Trust and completion of the Plan shall, subject to the review and approval of the Trustee, be paid.

7.07 Compensation of Trustee and Persons Employed by the Trust. The Trustee shall be paid reasonable compensation as agreed to by HPI and, in the case of Trusts II and III, the Creditors' Oversight Committee. All Persons or entities employed by the Trustee shall be entitled to reasonable compensation from the Trust and such compensation shall be subject to the review and approval of the Trustee. Any unresolved disputes shall be decided by the Bankruptcy Court.

7.08 Authorization. All Classes of Creditors that vote to accept the Plan hereby authorize the Trustee to act on behalf and in place of such Creditor to the extent provided herein and in any document and instrument delivered hereunder or in connection herewith and to take such other action as may be incidental thereto, including, without limitation, the exercise of any discretion in connection with any determination or decision required for the administration of this Plan and the granting of any waiver, consent, amendment, suspension, supplementation, extension, renewal or other modification with respect to any and all provisions of this Plan on a conditional or unconditional basis.

7.09 Exculpation. The Trustee shall be entitled to rely upon advice and opinions of counsel concerning legal matters, the authenticity of affidavits, letters, telegrams, cablegrams and other methods of communication in general use and usually accepted by businessmen as genuine and what they purport to be, and upon this Plan and any schedule, certificate, statement, report, notice or other writing which it believes to be genuine or to have been presented by a proper entity. Except for its or their own gross negligence or intentional misconduct, neither the Trustee, nor any of his employees or agents shall (a) be responsible for any recitals, representations or warranties contained in, or for the execution, validity, genuineness, effectiveness or enforceability of this Plan, (b) be under any duty to inquire into or pass upon any matter or to make any inquiry concerning the validity of any representation or warranty of the Debtors or the performance by the Debtors of their obligations or (c) in any event, be liable as such for any action taken or omitted by it or them. Each creditor agrees and acknowledges that the Trustee makes no representations or warranties with respect to the legality, validity, sufficiency or enforceability of this Plan.

7.10 Liability of Trustee. No recourse shall ever be had, directly or indirectly, against the Trustee by legal or equitable proceedings or by virtue of any statute or otherwise, or by virtue of any deed of trust, mortgage, pledge or note, or by virtue of any promises, contract, instrument, undertaking, obligation, covenant or agreement whatsoever executed by the Trustee for any purposes authorized, it being expressly understood and agreed that all such liabilities, covenants and agreements of the Trustee, whether in writing or otherwise, shall be enforceable only against and be satisfied only by the Trust, and every undertaking, contract, covenant or agreement entered into in writing by the Trustee may provide expressly against the personal liability of the Trustee. The Trustee shall not be liable for any act he may do or admit to do as the Trustee hereunder while acting in good faith. The Trustee shall not be liable in any event except for his own gross negligence or willful fraud or misconduct. The Trustee shall be indemnified and held harmless by the Trust for any and all loss by reason of his acts or contracts for the Trust except for loss arising out of the Trustee's own gross negligence or willful fraud or misconduct. This provision does not eliminate

the Trustee's responsibilities and obligations regarding the filing of federal tax returns and the payment of any taxes that are due.

7.11 Books and Records. The Trustee shall keep or cause to be kept books containing a description of all Claims, assets, receipts, disbursements and escrows, which records shall be open to inspection at all reasonable times upon reasonable request of any Creditor. All books and records of the Debtors relating to the Trust Assets shall be turned over to the Trustee.

7.12 Delegation of Powers. The Trustee shall be entitled to delegate such authority to his employees and agents as he shall reasonably deem necessary to perform his responsibilities under this Plan.

7.13 Resignation, Death or Removal. The Trustee or any successor trustee may resign upon (thirty) 30 days written notice. In that event, or in the event of the death of the Trustee or a successor trustee, HPI will appoint a substitute or successor Trustee for Trust I and the Creditors' Oversight Committee will appoint a substitute or successor Trustee as to Trust II and Trust III to perform the duties, functions and obligations and to exercise the rights and authority of the Trustee as described in the Plan.

7.14 Investment of Funds. All proceeds and other cash (except for amounts which the Trustee determines, in his sole discretion, are needed for immediate payments and distributions) shall be invested and reinvested by the Trust in United States Treasury Bills or in certificates of deposits, demand deposit or interest-bearing accounts of banking institutions acceptable to the Trust or such other investments as shall be prudent and appropriate under the circumstances, in such amounts and upon such terms as a reasonable and prudent fiduciary would select and with a view toward sufficient liquidity to make the distributions contemplated by this Plan. All interest earned on such proceeds and other cash shall be retained by the Trust and distributed in accordance with this Plan.

7.15 Reserves. Prior to any distribution of cash or proceeds, the Trustee shall establish adequate reserves for the operation of the Trust and Contested Claims that may become Allowed Claims after the Effective Date.

7.16 Interim Distribution. If and when, in the opinion of the Trustee, there are sufficient cash and proceeds to justify an interim distribution to creditors holding Allowed Claims, he may make such interim distributions to Holders of such Allowed Claims as he deems appropriate in his sole and absolute discretion; provided that the Trustee shall maintain an amount deemed necessary by the Trustee to be a sufficient reserve as required in this Section. In any event, however, distributions to creditors holding Allowed Claims will be made at least annually, or, in the event that the Trustee deems the cash and proceeds in the Trust insufficient to justify a distribution, a report on the status of the Trust's activities shall be filed annually with the Bankruptcy Court and served on the U.S. Trustee.

7.17 Unclaimed Distributions. Any proceeds or other cash held for the benefit of any Holder of an Allowed Claim, if unclaimed by the distributee within three months after the distribution, shall be redeposited into the fund and made available for other Allowed Claims and Allowed Interests, and all liability and obligations of the Debtors and the Trust to such distributee with respect thereto shall thereupon cease.

7.18 Termination. Upon termination of the Trust, the powers and responsibilities of the Trustee and his representatives shall terminate.

7.19 Coordination. The Trustees of the three Trusts will coordinate their actions with one another to ensure that they are not duplicating efforts. In particular, the Trustees will coordinate and cooperate with one another in connection with objections to claims. No Trustee shall have authority to release a Cause of Action that belongs to the Trustee of another Trust.

7.20 Appointment of the Creditors' Oversight Committee. The Trustee of Trust II and Trust III shall establish a committee, consisting of no more than three (3) creditors from the existing Creditors' Committee, to consult with the Trustee regarding the Trust Assets. The initial members of the Creditors' Oversight Committee shall be selected by the Committee. The Creditors' Oversight Committee shall only exist so long as there are two (2) creditors willing to serve. No compensation to the members of the Creditors' Oversight Committee shall be paid by the Trustee from the Trust Assets; provided, however, that reasonable expenses of the Creditors' Oversight Committee may be reimbursed by the Trustee at his discretion. The Creditors' Oversight Committee shall have standing as a party in interest to enforce the terms and provisions of the Trust Agreement. The Creditors' Oversight Committee shall have the authority to retain counsel if necessary to resolve a dispute with the Trustee and the reasonable fees and expenses of such counsel shall be a cost of administration of the Trust. The members of the Creditors' Oversight Committee shall not be liable for any act done or omitted to be done as a member of the Creditors' Oversight Committee while acting in good faith. The members of the Creditors' Oversight Committee shall not be liable in any event except for gross negligence or willful fraud or misconduct.

ARTICLE VIII

TREATMENT OF EXECUTORY CONTRACTS AND UNEXPIRED LEASES

8.01 General Treatment of Executory Contracts. The Debtors have previously rejected various executory contracts. The Plan Proponent shall have the power to reject as of the Effective Date additional executory contracts and unexpired leases by motion filed with the Court within ten (10) days after the Effective Date. All executory contracts not rejected shall be deemed assumed.

8.02 Cure of Defaults. HPI or HPE shall cure all defaults existing under any assumed executory contract that it elects to assume pursuant to the provisions of §§ 1123(a)(5)(G) and 365(b) of the Code, by paying the amount, if any, determined by the Court required to be paid in order to assume such executory contract. Payment of such amounts shall be made by HPI or HPE as soon as possible after the Effective Date.

8.03 Claims for Damages. Each Person who is a party to an executory contract rejected pursuant to this Article shall be entitled to file, not later than sixty (60) days after the Effective Date a proof of claim for damages alleged to arise from the rejection of the executory contract to which such Person is a party. A copy of such Claim shall be sent to the Trustee and HPI (or its counsel, if any). The Court shall determine any such objections, unless they are otherwise resolved. All Allowed Claims for rejection damages shall be treated as a Class 9 or Class 10 Claim.

ARTICLE IX

PROVISIONS REGARDING DISTRIBUTIONS AND OBJECTIONS TO CLAIMS

9.01 No Distributions Pending Allowance or Estimation of Claims. No payments or distributions shall be made with respect to all or any portion of a Contested Claim unless and until such Claim becomes an Allowed Claim, or Allowed Interest, as determined by Final Order. No holder of a Claim shall be entitled to any payment under the Plan if such holder has retained property of the Estate.

9.02 Reserve for Certain Distributions. The Trust shall reserve funds adequate to properly treat Contested Claims pending the resolution of any objection to such Claim.

9.03 Distributions After Disallowance. In the event that any amounts held in such reserve remain after all objections to Contested Claims have been resolved, the Trust shall make distributions of funds held in reserve on account of Claim objections on a Pro Rata basis pursuant to the terms of this Plan.

9.04 Treatment of Contingent or Unliquidated Claims. Until such time as a contingent Claim becomes fixed and Allowed, such Claim shall be treated as a Contested Claim for purposes related to voting, allowance, and distributions under this Plan. The Bankruptcy Court upon request by the Debtors or, after the Effective Date, by the Trustee, shall in a summary proceeding for each such contingent Claim or unliquidated Claim, by estimation determine the allowability of each such contingent or unliquidated Claim.

9.05 Form of Payments. Payment to be made by the Trust pursuant to this Plan shall be made by check drawn on a domestic bank or by wire transfer from a domestic bank. The Trustee

may disregard, and elect to not pay, Allowed Claims whose Pro Rata share of a proposed distribution is less than \$100.00. In such case, the Allowed Amount of such Claims shall be reduced to zero and such funds shall be retained as part of the Trust.

ARTICLE X

PROVISIONS FOR THE DISCHARGE, SETTLEMENT, AND ADJUSTMENT OF CLAIMS

10.01 Reservation of Causes of Action. The Causes of Action are hereby preserved and retained for enforcement by and for the benefit of the respective Trusts effective as of the Effective Date. It is the intent of the Plan Proponent that this reservation of claims shall be as broad as permitted by applicable law and shall include all claims, whether or not disclosed in the Debtors' Schedules, and shall include any claims referenced in any pleadings or disclosure statement filed in these Cases. Each Trustee is appointed as the representative of the Estates pursuant to Section 1123(b)(3) of the Bankruptcy Code the same as if such Trustee had been appointed under Section 1104 of the Bankruptcy Code to pursue the Causes of Action in his respective Trust and shall be the only entity authorized to pursue such actions. The Trustee of Trust I shall be deemed to be a "trustee, receiver, liquidator, or rehabilitator (or an assignee thereof)" within the meaning of any insurance policy covering D&O Claims. The Trustee may pursue such Causes of Action in the name of the Trust, HPI or in the name of one or more of the Debtors the same as if such claims were being pursued by the Debtors. Unless the Trustee consents, or unless otherwise ordered by the Bankruptcy Court, no other party shall have the right or obligation to pursue any such actions. Any creditor determined to have received a transfer that is voidable or avoidable under Chapter 5 of the Bankruptcy Code or any other applicable law shall be required to remit to the Trustee the determined amount of the avoided transfer prior to receiving any distribution from the Trust.

10.02 Authority to Pursue HPI's Direct Claims. The Trustee of Trust I is hereby authorized to pursue HPI's Direct Claims in the name of HPI or Trust I for the benefit of Trust I effective as of the Effective Date the same as if such claims were being pursued by HPI. Unless the Trustee consents, or unless otherwise ordered by the Bankruptcy Court, no other party shall have the right or obligation to pursue any such actions.

ARTICLE XI

EFFECT OF CONFIRMATION, DISCHARGE, RELEASES, AND INJUNCTION

11.01 Vesting of Property. Confirmation of the Plan shall vest the Trust Assets in each respective Trust and all other property of the Debtors in HPE and FEI Shale as provided in the Plan.

11.02 Property Free and Clear. Except as otherwise provided in the Plan, all property dealt with by the Plan shall be free and clear of all claims, liens and interests of any party as of the Confirmation of the Plan. This Plan will evidence the release of any and all Liens or encumbrances against all property dealt with by the Plan, unless such Lien or encumbrance is specifically retained in the Plan.

11.03 Legal Binding Effect; Discharge of Claims and Interests. The provisions of this Plan shall: (i) bind all Debtors, Claimants and Interest holders, whether or not they accept this Plan, and (ii) except with respect to Allowed Claims, release the Debtors from liability for all Claims, debts and liabilities that arose before the Petition Date, and from any Claims, debts and liabilities, including, without limitation, any Claims, debts and liabilities of a kind specified in Sections 502(g), 502(h) or 502(i) of the Bankruptcy Code, that arose, or have been asserted against, the Debtors at any time before the entry of the Confirmation Order or that arise from any pre-Confirmation conduct of the Debtors whether or not the Claims, debts and liabilities are known or knowable by the Claimant or Interest holder.

11.04 Effect on Third Parties. Nothing contained in the Plan or in the documents to be executed in connection with the Plan shall affect any Creditor's rights as to any third party.

11.05 Satisfaction of Claims and Interests. Except as otherwise provided by the Plan, the consideration distributed under the Plan shall be in complete satisfaction of all Claims of any Creditor, including Claims arising prior to the Effective Date.

11.06 Permanent Injunction. Except as otherwise expressly provided in, or permitted under, this Plan, the Confirmation Order shall provide, among other things, that all Creditors and Persons who have held, hold or may hold Claims or Interests, are permanently enjoined on and after the Effective Date against the: (i) commencement or continuation of any judicial, administrative, or other action or proceeding against the Debtors, or the Trusts on account of Claims against or Interests in the Debtors; (ii) enforcement, attachment, collection or recovery by any manner or means of any judgment, award, decree, or order against the Debtors or the Trusts, or any assets or property of same; or (iii) creation, perfection or enforcement of any encumbrance of any kind against the Debtors or the Trusts, arising from a Claim.

ARTICLE XII

MISCELLANEOUS PROVISIONS

12.01 Request for Relief under Section 1129(b). In the event any Impaired Class of Claims shall fail to accept this Plan in accordance with Section 1129(a) of the Bankruptcy Code, the Proponent requests the Bankruptcy Court to confirm this Plan in accordance with the provisions of Section 1129(b) of the Bankruptcy Code.

12.02 Headings. All headings utilized in this Plan are for convenience and reference only, and shall not constitute a part of this Plan for any other purpose.

12.03 Securities-Related Claims Based on Common Stock. All Claims asserted based upon or related to ownership of the common stock of the Debtors shall be treated as a Subordinated Claim.

12.04 Due Authorization. Each and every Claimant and Interest holder who elects to participate in the distributions provided for herein warrants that such Claimant or Interest holder is authorized to accept, in consideration of such Claim against or Interest in the Debtors, the distributions provided for in this Plan and that there are not outstanding commitments, agreements, or understandings, expressed or implied, that may or can in any way defeat or modify the rights conveyed or obligations undertaken by such Claimant or Interest holder under this Plan.

12.05 Authorization of Corporate Action. All matters and actions provided for under this Plan involving the organizational structure of the Debtors or corporate or partner action to be taken by or required of the Debtors or the Trusts shall be deemed to have occurred and be effective as provided herein, and shall be deemed to be authorized and approved in all respects without any requirement for further action by the stockholders, directors, members or partners of the Debtors. Specifically, all actions, formal, statutory, legal or equitable, as may be necessary to put into effect or carry out the terms and intent of this Plan and the orders and decrees of the Bankruptcy Court entered in the Chapter 11 Case, may be effected, exercised and taken without further action by the directors or stockholders of the Debtors, as applicable, with like effect as if effected, exercised and taken by unanimous action of the directors, members, partners and stockholders of the Debtors, as applicable.

12.06 Further Assurances and Authorizations. The Debtors or the Trust shall seek such orders, judgments, injunctions, and rulings that may be required to carry out further the intentions and purposes, and to give full effect to the provisions, of this Plan. All terms and provisions of this Plan shall be construed in favor of the Plan Proponent.

12.07 Applicable Law. Except to the extent that the Bankruptcy Code or other federal law is applicable, the rights, duties and obligations arising under this Plan shall be governed by and construed and enforced in accordance with the internal laws of the State of Texas without reference to the laws of other jurisdictions.

12.08 Privileged Communications; Work Product. For purposes of any proprietary, confidential or privileged information or communication, including attorney-client privileged communications, and documents that would otherwise constitute attorney work product, the Trustee of Trust I shall succeed to the interest of the Debtors and the Estate.

12.09 No Interest. Except as expressly stated in this Plan, or allowed by the Court, no interest, penalty or late charge is to be Allowed on any Claim subsequent to the Filing Date.

12.10 Post-Confirmation Actions. After Confirmation, the Plan Proponent or Trustee may, with the approval of the Court, and so long as it does not materially or adversely affect the interest of Creditors, remedy any defect or omission, or reconcile any inconsistencies in the Plan or in the Order of Confirmation, in such manner as may be necessary to carry out the purposes and effect of the Plan.

12.11 Notice of Default. In the event of any alleged default under the Plan, any Creditor or party-in-interest must give a written default notice to the Trustee with copies to counsel of record for the Plan Proponents and such Trustee, as applicable, specifying the nature of the default. Upon receipt of the default notice, the Trustee shall have thirty (30) days to cure such default from the time of receipt of the default notice. If such default has not been cured within the applicable time period, the default may be brought to the attention of the Court or any other court of competent jurisdiction.

12.12 Notices. All notices, requests, elections or demands in connection with the Plan shall be in writing and shall be deemed to have been given when received or, if mailed, five (5) days after the date of mailing provided such writing shall have been sent by registered or certified mail, postage prepaid, return receipt requested.

12.13 Payment Dates. Whenever any payment or distribution to be made under the Plan shall be due on a day other than a Business Day, such payment or distribution shall instead be made, without interest, on the next Business day, except as may be provided in negotiable instruments requiring such payments.

ARTICLE XIII

RETENTION OF JURISDICTION

The Bankruptcy Court shall retain exclusive jurisdiction over this Chapter 11 Case after Confirmation, notwithstanding Consummation or substantial consummation, for the following purposes:

- (a) to consider and effect any modification of this Plan under Section 1127 of the Bankruptcy Code;
- (b) to hear and determine all controversies, suits and disputes that arise in connection with the interpretation, implementation, effectuation, consummation or enforcement of this Plan;

- (c) to hear and determine all requests for compensation and/or reimbursement of expenses for the period commencing on the Petition Date through the Confirmation Date;
- (d) to hear and determine all objections to Claims and Interests, and to determine the appropriate classification of any Claim or Interest, and other controversies, suits and disputes that may be pending at or initiated after the Confirmation Date, except as provided in the Confirmation Order;
- (e) to hear and determine all Causes of Action;
- (f) to consider and act on such other matters consistent with this Plan as may be provided in the Confirmation Order;
- (g) to make such orders as are necessary and appropriate to carry out and implement the provisions of this Plan; including to effect the further assurances provided in Section 12.7 of this Plan;
- (h) to approve the reasonableness of any payments made or to be made, within the meaning of Section 1129(a)(4) of the Bankruptcy Code;
- (i) to exercise the jurisdiction granted pursuant to Section 505(a) and (b) of the Bankruptcy Code to determine any and all federal, state, Commonwealth, local and foreign tax liabilities of, and any and all refunds of such taxes paid by the Debtors;
- (j) to hear and determine any issues or matters in connection with any property not timely claimed as provided in this Plan;
- (k) to determine any and all motions, applications, adversary proceedings and contested matters whether pending in the Case as of the Effective Date or brought subsequently by the Reorganized Debtors or the Trust;
- (l) to determine when the Trustee may destroy business records of the Debtors; and
- (m) to enforce any agreements or contracts executed by the Trustee or in carrying out his responsibilities hereunder or under the Trust Agreement; and
- (n) to determine any disputes with any creditor or party in interest.

Nothing contained in this Article XIII shall be construed so as to limit the rights of the Debtors or the Trust to commence or prosecute any claim in any court of competent jurisdiction.

DATED: July 14, 2009

HALL PHOENIX/INWOOD, LTD.

By: Phoenix Inwood Corporation

By: /s/ Donald Braun
Donald Braun, President

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