FORM 10-K

CROSSTEX ENERGY INC - XTXI

Filed: March 26, 2004 (period: December 31, 2003)

Annual report which provides a comprehensive overview of the company for the past year

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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-K

☒ **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2003**

OR

☐ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to**

Commission file number: 000-50536

CROSSTEX ENERGY, INC.

(Exact name of registrant as specified in its charter)

Delaware *(State of organization)*	**52-2235832** *(I.R.S. Employer Identification No.)*
2501 CEDAR SPRINGS, SUITE 600 **DALLAS, TEXAS** *(Address of principal executive offices)*	**75201** *(Zip Code)*

(214) 953-9500
(Registrant's telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Exchange on which Registered
None	Not applicable

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

Title of Class
Common Shares

Indicate by check mark whether registrant has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and has been subject to such filing requirements for the past 90 days. Yes ☐ No ☒

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

There were no Common shares held by non-affiliates of the registrant on June 30, 2003.

At February 28, 2004, there were outstanding 12,079,248 Common shares.

DOCUMENTS INCORPORATED BY REFERENCE: None.

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PART I

Item 1. *Business*

General

Crosstex Energy, Inc. is a Delaware corporation, formed in April 2000. We completed our initial public offering in January 2004. Our shares of common stock are listed on the NASDAQ National Market under the symbol "XTXI". Our executive offices are located at 2501 Cedar Springs, Suite 600, Dallas, Texas 75201, and our telephone number is (214) 953-9500. In this report, the terms "Crosstex Energy, Inc." as well as the terms "our," "we," and "us," or like terms are sometimes used as references to Crosstex Energy, Inc. and its consolidated subsidiaries. References in this report to "Crosstex Energy, L.P.," the "Partnership," or like terms refer to Crosstex Energy, L.P. itself or Crosstex Energy, L.P. and its consolidated subsidiaries.

CROSSTEX ENERGY, INC.

Our assets consist almost exclusively of partnership interests in Crosstex Energy, L.P., a publicly traded limited partnership engaged in the gathering, transmission, treating, processing and marketing of natural gas. These partnership interests consist of the following:

- 333,000 common units and 4,667,000 subordinated units, representing a 54.3% limited partner interest in the Partnership; and
- 100% ownership interest in Crosstex Energy GP, L.P., the general partner of the Partnership, which owns a 2.0% general partner interest and all of the incentive distribution rights in the Partnership.

Our cash flows consist almost exclusively of distributions from the Partnership on the partnership interests we own. The Partnership is required by its partnership agreement to distribute all its cash on hand at the end of each quarter, less reserves established by its general partner in its sole discretion to provide for the proper conduct of the Partnership's business or to provide for future distributions.

The incentive distribution rights entitle us to receive an increasing percentage of cash distributed by the Partnership as certain target distribution levels are reached. Specifically, they entitle us to receive 13.0% of all cash distributed in a quarter after each unit has received $0.50 for that quarter, 23.0% of all cash distributed after each unit has received $0.625 for that quarter and 48.0% of all cash distributed after each unit has received $0.75 for that quarter.

The following table sets forth the distributions we received from the Partnership since its initial public offering in December 2002.

	Cash Distributions to Us				
	IPO to December 31, 2002(1)	Quarter Ended March 31, 2003	Quarter Ended June 30, 2003	Quarter Ended September 30, 2003	Quarter Ended December 31, 2003
Crosstex Energy, L.P. distribution per unit	$ 0.076	$ 0.500	$ 0.550	$ 0.700	$ 0.750
Limited Partner Ownership Interest:					
333,000 common units	$ 25,308	$ 166,500	$ 183,150	$ 233,100	$ 249,750
4,667,000 subordinated units	354,692	2,333,500	2,566,850	3,266,900	3,500,250
Total	380,000	2,500,000	2,750,000	3,500,000	3,750,000
General Partner Ownership Interest:					
2.0% general partner interest	11,322	74,490	83,078	136,686	148,719
Incentive distribution rights	0	0	55,824	380,112	518,495
Total	11,322	74,490	138,902	516,798	667,214
Total	$ 391,322	$ 2,574,490	$ 2,888,902	$ 4,016,798	$ 4,417,214

(1) Reflects the pro rata minimum quarterly distribution covering the period from the closing of the Partnership's initial public offering on December 17, 2002 through December 31, 2002. This distribution was paid to us together with the March 31, 2003 distribution.

We intend to pay to our stockholders, on a quarterly basis, dividends equal to the cash we receive from our Partnership distributions, less reserves for expenses, future dividends and other uses of cash, including:

- federal income taxes, which we are required to pay because we are taxed as a corporation;
- the expenses of being a public company;
- other general and administrative expenses;
- capital contributions to the Partnership upon the issuance by it of additional partnership securities in order to maintain the general partner's 2.0% general partner interest; and
- reserves our board of directors believes prudent to maintain, including reserves equal to the benefit we will receive in 2004 from our existing net operating loss carryforwards.

If the Partnership is successful in implementing its business strategy and increasing distributions to its partners, we would generally expect to increase dividends to our stockholders, although the timing and amount of any such increased dividends will not necessarily be comparable to the increased Partnership distributions.

Our ability to pay dividends is limited by the Delaware General Corporation Law, which provides that a corporation may only pay dividends out of existing "surplus," which is defined as the amount by which a corporation's net assets exceeds its stated capital. While our ownership of the general partner and the common and subordinated units of the Partnership are included in our calculation of net assets, the value of these assets may decline to a level where we have no "surplus," thus prohibiting us from paying dividends under Delaware law.

The Partnership's strategy is to increase distributable cash flow per unit by making accretive acquisitions of assets that are essential to the production, transportation and marketing of natural gas, improving the profitability of its assets by increasing their utilization while controlling costs and pursuing new construction or expansion opportunities in its core operating areas. If the Partnership is successful in implementing this strategy, we believe the total amount of cash distributions it makes will increase and our share of those distributions will also increase. The Partnership announced increases in its quarterly distribution two times since its initial public offering in December 2002. During that time, the Partnership increased the per unit quarterly cash distribution on its common and subordinated units by 40.0%, from $0.50 to $0.70. If the Partnership increased its per unit quarterly distribution to $0.80, its total quarterly distribution would increase $1,504,167 and we would receive $1,101,667, or 73.2%, of that increase. If Crosstex Energy, L.P. then issued an additional 1,000,000 units and maintained its per unit quarterly distribution at $0.80 per unit, its total quarterly distribution would increase another $923,930 and we would receive $123,930, or 13.4%, of that increase, assuming the general partner made a capital contribution to the Partnership sufficient to maintain its 2.0% general partner interest.

So long as we own the general partner, we are prohibited by an omnibus agreement with the Partnership from engaging in the business of gathering, transmitting, treating, processing, storing and marketing natural gas and transporting, fractionating, storing and marketing NGLs, except to the extent that the Partnership, with the concurrence of a majority of its independent directors comprising its conflicts committee, elects not to engage in a particular acquisition or expansion opportunity. The Partnership may elect to forego an opportunity for several reasons, including:

- the nature of some or all of the target's assets or income might affect the Partnership's ability to be taxed as a partnership for federal income tax purposes;
- the board of directors of Crosstex Energy GP, LLC may conclude that some or all of the target assets are not a good strategic opportunity for the Partnership; or
- the seller may desire equity, rather than cash, as consideration and may not want to accept the Partnership's units as consideration.

We have no present intention of engaging in additional operations or pursuing the types of opportunities that we are permitted to pursue under the omnibus agreement, although we may decide to pursue them in the future, either alone or in combination with the Partnership. In the event that we pursue the types of opportunities that we are permitted to pursue under the omnibus agreement, our board of directors, in its sole discretion, may retain all, or a portion of, the cash distributions we receive on our partnership interests in the Partnership to finance all, or a portion of, such transactions, which may reduce or eliminate dividends paid to our stockholders.

CROSSTEX ENERGY, L.P.

Crosstex Energy L.P. is a rapidly growing independent midstream energy company engaged in the gathering, transmission, treating, processing and marketing of natural gas. The Partnership connects the wells of natural gas producers in its market areas to its gathering systems, treats natural gas to remove impurities to ensure that it meets pipeline quality specifications, processes natural gas for the removal of natural gas liquids or NGLs, transports natural gas and ultimately provides an aggregated supply of natural gas to a variety of markets. The Partnership purchases natural gas from natural gas producers and other supply points and sells that natural gas to utilities, industrial consumers, other marketers and pipelines and thereby generates gross margins based on the difference between the purchase and resale prices. In addition, the Partnership purchases natural gas from producers not connected to its gathering systems for resale and sells natural gas on behalf of producers for a fee.

The Partnership's major assets include over 2,500 miles of natural gas gathering and intrastate transmission pipelines, three natural gas processing plants connected to its gathering systems with a total NGL production capacity of 289,800 gallons per day and 61 natural gas treating plants. The Partnership's recently announced acquisition of LIG Pipeline Company (LIG) will add 2,000 miles of pipeline and three major processing plants to the Partnership's assets. The Partnership's gathering systems consist of a network of pipelines that collect natural gas from points near producing wells and transport it to larger pipelines for further transmission. The Partnership's transmission pipelines primarily receive natural gas from its gathering systems and from third party systems and deliver natural gas to industrial end-users, utilities and other pipelines. The Partnership's processing plants remove NGLs from a natural gas stream and fractionate, or separate, the NGLs into separate NGL products, including ethane, propane, mixed butanes and natural gasoline. The Partnership's natural gas treating plants, located largely in the Texas Gulf Coast area, remove impurities from natural gas prior to delivering the gas into pipelines to ensure that it meets pipeline quality specifications.

Set forth in the table below is a list of the Partnership's significant acquisitions since January 2000.

Acquisition	Acquisition Date	Purchase Price	Asset Type	Average Throughput at Time of Acquisition (MMBtu/d)	Average Throughput for Year Ended December 31, 2003 (MMBtu/d)
		(in thousands)			
Provident City Plant	February 2000	$ 350	Treating plants	2,200	23,000
Will-O-Mills (50%)	February 2000	2,000	Treating plants	11,700	8,500
Arkoma Gathering System	September 2000	10,500	Gathering pipeline	12,000	13,000
Gulf Coast System	September 2000	10,632	Gathering and transmission pipeline	117,000	85,000(1)
CCNG Acquisition	May 2001	30,003	Gathering and transmission pipeline and processing plant	272,000	414,000
Pettus Gathering System	June 2001	450	Gathering system	—	—
Millennium Gas Services	October 2001	2,124	Treating assets	—	—
Hallmark Lateral	June 2002	2,300	Pipeline segment	—	57,000
Pandale System	June 2002	2,156	Gathering pipeline	16,000	13,000
KCS McCaskill Pipeline	June 2002	250	Pipeline segment	—	—
Vanderbilt System	December 2002	12,000	Transmission pipeline	32,000	49,000(1)
Will-O-Mills (50%)	December 2002	2,200	Treating plant	9,700	8,500
DEFS Acquisition	June 2003	68,124	Gathering and transmission systems, processing plants and pipeline systems	129,000	127,000(2)

(1)

Certain Gulf Coast customers are now provided service through the Vanderbilt system.

(2)

Represents average throughput from the acquisition date, June 30, 2003, through December 31, 2003.

The Partnership has two operating segments, Midstream and Treating. The Partnership's Midstream division focuses on the gathering, processing, transmission and marketing of natural gas, as well as providing certain producer services, while its Treating division focuses on the removal of carbon dioxide and hydrogen sulfide from natural gas to meet pipeline quality specifications. See Note 15 to the consolidated financial statements for financial information about these operating segments.

The Partnership's general partner interest is held by Crosstex Energy GP, L.P., a Delaware limited partnership. Crosstex Energy GP, LLC, a Delaware limited liability company, is Crosstex

Energy GP, L.P.'s general partner. Crosstex Energy GP, LLC manages the Partnership's operations and activities and employs the Partnership's officers.

References in this report to "Crosstex Energy, L.P.'s predecessor" or the "Partnership's predecessor" refer to Crosstex Energy Services, Ltd., a Texas limited partnership, substantially all of the assets of which were transferred to the Partnership at the closing of its initial public offering in December 2002.

As generally used in the energy industry and in this document, the following terms have the following meanings:

/d = per day
Btu = British thermal units
Mcf = thousand cubic feet
MMBtu = million British thermal units
MMcf = million cubic feet

Business Strategy

The Partnership's strategy is to increase distributable cash flow per unit by making accretive acquisitions of assets that are essential to the production, transportation, and marketing of natural gas; improving the profitability of its owned assets by increasing their utilization while controlling costs; accomplishing economies of scale through new construction or expansion in core operating areas; and maintaining financial flexibility to take advantage of opportunities. The Partnership's strategy is based on its expectation of a continued high level of drilling in its principal geographic areas and a process of ongoing divestitures of gas transportation and processing assets by large industry participants. The Partnership believes these two factors should present opportunities for continued expansion in its existing areas of operation as well as opportunities to acquire assets in new geographic areas that may serve as a platform for future growth. Key elements of the Partnership's strategy include the following:

- *Pursuing accretive acquisitions.* The Partnership intends to use its acquisition and integration experience to continue to make strategic acquisitions of midstream assets that offer the opportunity for operational efficiencies and the potential for increased utilization and expansion of the acquired asset. The Partnership pursues acquisitions that it believes will add to existing core areas in order to capitalize on its existing infrastructure, personnel, and producer and consumer relationships. The Partnership also examines opportunities to establish new core areas in regions with significant natural gas reserves and high levels of drilling activity or with growing demand for natural gas. The Partnership plans to establish new core areas primarily through the acquisition of key assets that will serve as a platform for further growth both through additional acquisitions and the construction of new assets. A recent example of establishing a new core area includes the Mississippi pipeline system acquired as part of the DEFS acquisition. This system provides the Partnership with a platform to develop a significant presence in the south central Mississippi area.

- *Improving existing system profitability.* After the Partnership acquires or constructs a new system, it begins an aggressive effort to market services directly to both producers and end users in order to connect new supplies of natural gas, improve margins, and fully utilize the system's capacity. Many of the Partnership's recently acquired systems have excess capacity that provides it opportunities to increase throughput with minimal incremental cost. As part of this process, the Partnership focuses on providing a full range of services to small and medium size independent producers and end users, including supply aggregation, transportation and hedging, which the Partnership believes provides it with a competitive advantage when it competes for sources of natural gas supply. Additionally, the Partnership emphasizes increasing the percentage of our natural gas sales directly to end users, such as industrial and utility consumers in an effort to increase our operating margins. For the year ended December 31, 2003, approximately 58% of the Partnership's on-system natural gas sales were to industrial end users and utilities.

- *Undertaking construction and expansion opportunities.* The Partnership leverages its existing infrastructure and producer and customer relationships by constructing and expanding systems to meet new or increased demand for its gathering, transmission, treating, processing and marketing services. These projects include expansion of existing systems and construction of new facilities. The Partnership's 2002 acquisition of the Hallmark Lateral facilitated the establishment of connections between its Corpus Christi and its Gulf Coast systems which has increased its flexibility in balancing gas supply and market requirements throughout the regions covered. In August 2003, the Partnership expanded the capacity of its Gregory processing plant from 99,900 MMBtu/d to 166,500 MMBtu/d, a 67% increase over its previous capacity, and began marketing the additional gas through its Corpus Christi and Gulf Coast systems. The Partnership further enhanced the Gregory system by acquiring the Koch Ingleside Pipeline and connecting directly to a major end user customer.

Recent Acquisitions and Expansion

Duke Energy Field Services. In June 2003, the Partnership acquired various midstream assets located in Mississippi, Texas, Alabama and Louisiana from DEFS for $68.1 million in cash. The principal assets acquired were the Mississippi pipeline system, a 638-mile natural gas gathering and transmission system in south central Mississippi that serves utility and industrial customers, and a 12.4% non-operating interest in the Seminole gas processing plant, which provides carbon dioxide separation and sulfur removal services for several major oil companies in West Texas. The acquisition provided the Partnership with a new core area for growth in south central Mississippi, expanded its presence in West Texas, increased the total miles of its pipelines from 1,700 to 2,500 and enabled it to enter the business of carbon dioxide separation. In addition, the Partnership believes that the acquisition has increased the stability of its cash flow as operating profits from the Mississippi pipeline system are generated through purchasing, gathering, transporting and reselling natural gas which generates margins not affected by commodity prices, and a majority of the income it receives from the Seminole gas plant is based on fixed fees for carbon dioxide separation and sulfur removal.

Gregory Expansion. In August 2003, the Partnership completed an expansion of its Gregory processing plant. The expansion increased the plant capacity from approximately 99,900 MMBtu/d to 166,500 MMBtu/d, at a cost of approximately $7.0 million. In addition, the Partnership has significantly reduced its exposure to commodity prices by renegotiating a number of its commodity based contracts, where revenues were subject to fluctuating commodity prices, to fee-based contracts.

Subsequent Event. The Partnership entered into a definitive agreement on February 13, 2004 for the acquisition of the LIG Pipeline Company and its subsidiaries (LIG) from American Electric Power for $76.2 million. The acquisition will increase the Partnership's pipeline miles by approximately 2,000 miles, to a total of 4,500 pipeline miles, and increase pipeline throughput by approximately 600,000 MMBtu/d. The closing, which is subject to completion of certain conditions, is expected to occur within 90 days of the date of the definitive agreement. The Partnership will finance the acquisition through borrowings under our existing bank credit facility, issuance of additional senior notes or other financing alternatives.

Other Developments

Partnership's Follow-on Offering. In September 2003, the Partnership completed a public offering of 1,725,000 common units at a public offering price of $35.97 per common unit. The Partnership received net proceeds of approximately $59.1 million, including an approximate $1.3 million capital contribution by the general partner. The net proceeds were used to repay borrowings outstanding under the bank credit facility of its operating partnership.

Bank Credit Facility. In June 2003, the Partnership's operating partnership, Crosstex Energy Services, L.P., entered into a new $100.0 million senior secured credit facility, which was increased to $120 million in October 2003, consisting of a $70.0 million acquisition facility and a $50.0 million working capital and letter of credit facility. As of December 31, 2003, the operating partnership had $20.0 million of outstanding borrowings under the acquisition facility and $30.3 million of letters of credit issued under the working capital and letter of credit facility. The credit facility matures in June 2006.

Secured Secured Notes. In June 2003, the operating partnership entered into a master shelf agreement with an institutional lender pursuant to which it issued $30.0 million of senior secured notes with an interest rate of 6.95% and a maturity of seven years. In July 2003, the operating partnership issued $10.0 million of senior secured notes pursuant to the master shelf agreement with an interest rate of 6.88% and a maturity of seven years. The senior secured notes are guaranteed by the operating partnership's subsidiaries and us. The operating partnership used the net proceeds from the senior notes offering to repay indebtedness under its bank credit facility.

Midstream Division

Gathering and Transmission. The Partnership's primary Midstream assets include systems located primarily along the Texas Gulf Coast and in south-central Mississippi, which, in the aggregate, consist of approximately 2,500 miles of pipeline and three processing plants and contributed approximately 78% and 72% of our gross profit in 2003 and 2002, respectively.

- *Gulf Coast System*. The Gulf Coast system is an intrastate pipeline system consisting of approximately 484 miles of gathering and transmission pipelines with a mainline from Refugio County in south Texas running northeast along the Gulf Coast to the Brazos River in Fort Bend County near Houston. The system's gathering and transmission pipelines range in diameter from 4 to 20 inches. The Partnership acquired the Gulf Coast system in September 2000 for a purchase price of approximately $10.6 million.

  The Gulf Coast system has two supply pipeline laterals which connect to gathering systems which collect natural gas from approximately 80 receipt points and five treating and processing plants operated by third parties. This system has three delivery laterals which deliver natural gas directly to large industrial and utility consumers along the Gulf Coast. The system interconnects with multiple third party pipelines through which the Partnership may purchase volumes not gathered through its systems for resale or through which it might deliver natural gas to customers which are not connected to its system. The Partnership transports gas on the TXU Lone Star pipeline providing access for its Gulf Coast mainline system in Fort Bend County to the Katy hub, a major natural gas physical exchange that allows access to seven third party pipelines, including Kinder Morgan, TECO and Trunkline. The Gulf Coast system has a capacity of 210,600 MMBtu/d and average throughput on this system was approximately 85,000 MMBtu/d for the year ended December 31, 2003.

  The Partnership generates operating profits in its Gulf Coast system through the margins it earns by purchasing, gathering, transporting and reselling natural gas. The Partnership purchases natural gas from a producer, pipeline or marketing company and then transport and resells the gas. As of December 31, 2003, the Partnership was purchasing gas from over 70 producers primarily pursuant to month-to-month contracts and was reselling the natural gas to approximately 10 customers primarily pursuant to short-term or month-to-month arrangements. For the year ended December 31, 2003, approximately 92% of the natural gas volumes it purchased was purchased at a fixed price relative to an index and the remainder was purchased at a percentage of an index, and all the natural gas volumes it sold was sold at a fixed price relative to an index.

- *Vanderbilt System.* The Partnership's Vanderbilt system consists of approximately 200 miles of gathering and transmission pipelines located in Wharton and Fort Bend Counties near its Gulf Coast system. Natural gas is supplied to the system from over 27 receipt points. The gas had been sold to the Exxon Katy plant and, in June 2003, the Partnership reversed the flow of gas and began deliveries to the Formosa Hydrocarbons processing plant at Point Comfort, Texas. The Partnership's Vanderbilt system has a capacity of 141,700 MMBtu/d and average throughput was approximately 49,000 MMBtu/d for the year ended December 31, 2003. The Partnership acquired the Vanderbilt system in December 2002 for a purchase price of $12.0 million.

  All the gas in the Vanderbilt system is now sold to Formosa Hydrocarbons under a ten year agreement which began in June 2003 to supply up to 60,000 MMBtu/d. The gas is sold to Formosa at a fixed price relative to an index. Gas is purchased from approximately 15 producers, primarily pursuant to month-to-month arrangements, at over 25 receipt points. Approximately 55% percent of the gas is purchased at a percentage of an index, and the remainder is purchased at a fixed price relative to an index. The Partnership generates operating profits in the system through the margins it earns by purchasing gas from producers, then gathering, transporting and reselling the natural gas to Formosa.

- *Corpus Christi System*. The Corpus Christi system is an intrastate pipeline system consisting of approximately 295 miles of gathering and transmission pipelines and extending from supply points in south Texas to markets in the Corpus Christi area. The Partnership's gathering and transmission pipelines range in diameter from four to 20 inches. The Partnership acquired the Corpus Christi system in May 2001 in conjunction with the acquisition of the Gregory gathering system and Gregory processing plant, which it collectively refers to as the CCNG Acquisition, for an aggregate purchase price of approximately $30 million. The Partnership's Corpus Christi system had average throughput of approximately 152,000 MMBtu of gas per day at the time of its acquisition. The main lines comprising the Corpus Christi system were constructed at various times from the 1940's through the 1990's.

  Natural gas is supplied to the Corpus Christi system from approximately 13 receipt points, 16 treating and processing plants and third party gathering systems and pipelines. The system interconnects with multiple third party pipelines through which the Partnership purchases volumes not gathered through its systems for resale and delivers natural gas to customers which are not connected to our system, including the Banquette hub. The Corpus Christi system has a capacity of 355,950 MMBtu/d and average throughput on this system was approximately 213,800 MMBtu/d for the year ended December 31, 2003.

  In June 2002, the Partnership acquired from Florida Gas Transmission approximately 70 miles of 20 inch transmission line which allows it to access new markets within Texas and to interconnect to the Florida Gas system within Texas. The Partnership has constructed an addition to this transmission line creating a connection between its Gulf Coast system and its Corpus Christi system. This connection allows the Partnership to transport gas between our two systems, thereby reducing our dependence on third-party suppliers, move gas supplies to more favorable markets and enhance our margins. In November 2002, the Partnership completed construction of the interconnect between the Hallmark Lateral and the Florida Gas system. With this connection, the Partnership began selling gas into the Florida markets and sold approximately 57,000 MMBtu/d for the year ended December 31, 2003.

The Partnership generates operating profits in its Corpus Christi system through the margins it earns by purchasing, gathering, transporting and reselling natural gas. As of December 31, 2003, the Partnership was purchasing natural gas from approximately 35 producers generally on month-to-month or short-term arrangements. For the year ended December 31, 2003, substantially all of the natural gas volumes the Partnership purchased were purchased at a fixed price relative to an index. The Corpus Christi system transports natural gas to the Corpus Christi area where the Partnership's customers include multiple major refineries and other industrial installations, as well as the local electric utility. As of December 31, 2003, the Partnership was selling gas to over 20 customers primarily pursuant to contracts that expire at various times between 2003 and 2006. For the year ended December 31, 2003, all of the natural gas volumes the Partnership sold were sold at a fixed price relative to an index.

- *Gregory Gathering System*. The Partnership acquired the Gregory processing plant and the Gregory gathering system in May 2001 in connection with the acquisition of the Corpus Christi system. The plant and the gathering system are located north of Corpus Christi, Texas. The gathering system is connected to approximately 70 receipt points in San Patricio County, the Corpus Christi Bay area, Mustang Island, and adjacent coastal areas. The gathering system consists of approximately 297 miles of pipeline ranging in diameter from two inches to 18 inches with a total estimated throughput capacity of 222,000 MMBtu/d. The gathering system had average throughput of approximately 151,000 MMBtu/d for the year ended December 31, 2003 compared to an average throughput of approximately 76,500 MMBtu/d of gas per day at the time of its acquisition. The Gregory Gathering System was constructed in the 1980s.

  The Partnership generates operating profits in its Gregory gathering system through the margins earned by purchasing, gathering, transporting and reselling natural gas. As of December 31, 2003, the Partnership was purchasing gas from over 60 producers primarily pursuant to month-to-month contracts, and for the year ended December 31, 2003, approximately 95% of the natural gas volumes it purchased were purchased at a fixed price relative to an index and the remainder was purchased at percentage of an index.

- *Gregory Processing Plant*. The Partnership's Gregory processing plant is a cryogenic turbo expander with a 210,000 gallon per day fractionator that removes liquid hydrocarbons from the liquids-rich gas produced into the Gregory gathering system. The Partnership's Gregory processing plant inlet capacity was expanded from 99,900 MMBtu/d to approximately 166,500 MMBtu/d during 2003, and average throughput was approximately 106,000 MMBtu/d for the year ended December 31, 2003. At the time of acquisition, the plant was processing approximately 43,400 MMBtu/d of gas per day. The Gregory processing plant was constructed in the 1980s and expanded and upgraded in 1998 and 2003.

  In addition to the margins generated by the Gregory gathering system, the Partnership generates revenues at its Gregory processing plant under two types of arrangements:

  - For the year ended December 31, 2003, the Partnership purchased approximately 16% of the natural gas volumes on its Gregory system under contracts in which it was exposed to the risk of loss or gain in processing the natural gas. Under these contracts, the

Partnership fractionates the NGLs into separate NGL products, which it then sells at prices based upon the market price for NGL products. The processed natural gas is delivered to multiple customers at prices based on a fixed price relative to a monthly index. Since the Partnership extracts Btus from the gas stream in the form of the liquids or consumes it as fuel during processing, the Partnership reduces the Btu content of the natural gas but seek to more than offset this by creating value from the separated NGL products. Accordingly, the Partnership's margins under these arrangements can be negatively affected in periods where the value of natural gas is high relative to the value of NGLs.

- For the year ended December 31, 2003, the Partnership purchased approximately 84% of the natural gas volumes on its Gregory system at a spot or market price less a discount that includes a conditioning fee for processing and marketing the natural gas and NGLs at its Gregory processing plant with no risk of loss or gain in processing the natural gas. Under these contracts, the producer retains ownership of the fractionated NGLs, and accordingly bears the risk and retains the benefits associated with processing the natural gas.

- *Arkoma Gathering System*. The Partnership acquired the Arkoma gathering system, located in the Southeastern region of Oklahoma, in September 2000 for $10.5 million. In addition, since acquiring this system, the Partnership has acquired the Shawnee extension, consisting of 15 miles of gathering pipelines extending through additional supply areas in this region. The Arkoma gathering system when acquired was approximately 84 miles in length and included a 3,700 horsepower compressor station. With the addition of the Shawnee extension and additional well connections, the system is now approximately 100 miles in length and ranges in diameter from 2 to 10 inches. This low-pressure system gathers gas from approximately 170 wells to three compressor stations for discharge to a mainline transmission pipeline. This system has a capacity of 21,400 MMBtu/d and average throughput was approximately 13,000 MMBtu/d for the year ended December 31, 2003.

  The Partnership generates a margin for gathering and transporting gas in the Arkoma gathering system equal to a percentage of the proceeds from the sale of the natural gas to the mainline transmission pipeline into which it delivers. The Partnership takes title to the gas at the point of receipt into the gathering system, with payment based upon an allocation of the metered volume sold into the mainline transmission facilities of our customer with the producer sharing their pro rata portion of the fuel costs for the compression and the removal of water from the natural gas stream.

- *Mississippi Pipeline System.* The Partnership acquired the Mississippi pipeline system from DEFS in June 2003 in connection with the DEFS acquisition. The Mississippi pipeline system is located in 15 counties of south Mississippi spanning from the city of Jackson in the northwest to Hattiesburg in the southeast. The system has wellhead supply connections in most of the gas fields in the counties of operation—primarily Jasper, Jefferson Davis, Lawrence, Marion and Simpson counties. The system delivers natural gas through direct market connections to utilities and industrial end users. The pipeline system consists of approximately 638 miles of pipeline ranging in diameter from four to 20 inches with a total estimated capacity of 198,500 MMBtu/d. Average throughput on this system was approximately 79,000 MMBtu/d for the year ended December 31, 2003. The system was constructed in the 1970s.

  The Partnership generates operating profits in our Mississippi pipeline system by purchasing, gathering, transporting and reselling natural gas. The Partnership purchases gas from approximately 50 producers at the delivery points into the system and gas is sold to approximately 15 customers. The majority of contracts provide that natural gas volumes are purchased at a fixed price relative to an index.

- *Seminole Gas Processing Plant.* The Partnership owns an undivided 12.4% interest in the Seminole gas processing plant, which is located in Gaines County, Texas. The Seminole plant has dedicated long-term reserves from the Seminole San Andres unit, to which it also supplies carbon dioxide under a long-term arrangement. Revenues at the plant are derived from a fee it charges producers, including those at the Seminole San Andres unit, for each Mcf of carbon dioxide returned to the producer for reinjection. The fees currently average approximately $0.59 for each Mcf of carbon dioxide returned. The plant also receives 50% of the NGLs produced by the plant. The Partnership has entered into a one-year contract with Duke Energy NGL Services, L.P. to market its NGLs on its behalf. The Partnership receives its share of proceeds from the sale of carbon dioxide from the plant operator. The Partnership is separately billed by the plant operator for its share of expenses. The plant had capacity of 150,000 Mcf/d at the time of acquisition. The recently completed expansion increased capacity by 60,000 Mcf/d, increasing total capacity to 210,000 Mcf/d. Average throughput for the plant was approximately 144,000 Mcf/d for the last six months of 2003. The plant was constructed in the 1980s.

- *Conroe Gas Plant And Gathering System.* The Partnership acquired the Conroe gas plant and gathering system in June 2003 in connection with the DEFS asset acquisition. Located in Montgomery County, Texas, the Conroe gas plant is a cryogenic gas processing plant with 10 miles of gathering pipelines located within the Conroe Field Unit, which is operated by ExxonMobil. The plant gathers low pressure and high pressure natural gas through contracts with over 20 producers. The plant has outlet natural gas connections to Kinder Morgan Texas Pipeline, L.P. and Copano Field Services. Recovered NGLs are delivered into the Chaparral NGL pipeline. The plant has a capacity of 70,265 MMBtu/d and average throughput on this system was approximately 26,000 MMBtu/d for the year ended December 31, 2003. The Conroe gas plant was constructed in the 1930s.

  The Partnership generates operating profits at our Conroe gas plant from one customer primarily from compression and processing fees and from retaining 40% of the NGLs from the recycled lift gas.

- *Alabama Pipeline System.* The Partnership acquired the Alabama pipeline system in June 2003 in connection with the DEFS asset acquisition. The system is located in Fayette, Lamar, Picken and Tuscaloosa Counties in west-central Alabama. The system gathers coalbed methane gas from the Black Warrior Basin and other conventional wells. The system is a series of three natural gas gathering and transmission systems consisting of approximately 125 miles of four to twelve inch pipeline with an estimated capacity of 72,300 MMBtu/d. One supplier to the system accounted for over half of the gas gathered. The gas is delivered primarily to industrial end users. Average throughput on this system was approximately 14,000 MMBtu/d for the year ended December 31, 2003. The system was constructed in the 1970's.

  The Partnership generates operating profits in its Alabama pipeline system by gathering, transporting and reselling natural gas. All gas is purchased at the delivery points into the system. The majority of the contracts are priced at a fixed basis to an area index and the Partnership sells gas to approximately five customers.

- *Other Systems.* The Partnership owns several small gathering systems totaling approximately 135 miles, including the Manziel system in Wood County, Texas, the San Augustine system in

San Augustine County, Texas, the Freestone Rusk system in Freestone County, Texas, the Jack Starr and North Edna systems in Jackson County, Texas and the Cadeville and Aurora Centana systems in Louisiana. Through Crosstex Pipeline Partners, a limited partnership of which the Partnership is the co-general partner, the Partnership owns a 28% interest in five gathering systems in east Texas, totaling 64 miles with a combined capacity of 119,000 MMBtu/d. The Partnership also owns five industrial bypass systems each of which supplies natural gas directly from a pipeline to a dedicated customer. The combined volumes for these five industrial bypass systems was approximately 4,200 MMBtu/d for the year ended December 31, 2003. In addition to these systems, the Partnership owns various smaller gathering and transmission systems located in Texas, New Mexico and Louisiana.

Producer Services. The Partnerhip currently purchases for resale volumes of natural gas that do not move through its gathering, processing or transmission assets from over 50 independent producers. The Partnership engages in such activities on more than 20 interstate and intrastate pipelines with a major emphasis on Gulf Coast pipelines. The Partnership focuses on supply aggregation transactions in which it either purchases and resells gas and thereby eliminates the need of the producer to engage in the marketing activities typically handled by in-house marketing or supply departments of larger companies, or act as agent for the producer. Profits from energy trading activities for the year ended December 31, 2003 and 2002 were $1.9 million and $2.7 million, respectively.

The Partnership's business strategy includes developing relationships with natural gas producers to facilitate the purchase of its production on a long-term basis. The Partnership believes that this business also provides it with strategic insights and valuable market intelligence which may impact its expansion and acquisition strategy.

The Partnership offers to its customers the ability to hedge their purchase or sale price by agreeing to sell to it or to purchase from it volumes of natural gas. This risk management tool enables its customers to reduce pricing volatility associated with the sale and purchase of natural gas. When the Partnership agrees to purchase or sell natural gas from a customer, it contemporaneously executes a contract for the sale or purchase of such natural gas or the Partnerhip enters into an offsetting obligation using futures contracts on the New York Mercantile Exchange or by using over-the-counter derivative instruments with third parties.

Treating Division

The Partnership operates treating plants which remove carbon dioxide and hydrogen sulfide from natural gas before it is delivered into transportation systems to ensure that it meets pipeline quality specifications. The Partnership's treating division contributed approximately 22% and 27% of our gross margin in 2003 and 2002, respectively. The Partnership's treating business has grown from 35 plants in operation at December 31, 2002 to 52 plants in operation at December 31, 2003.

As of December 31, 2003, the Partnership owned 61 treating plants, 41 of which were operated by its personnel, 11 of which were operated by producers, and 9 of which were held in inventory. The Partnership entered the treating business in 1998 with the acquisition of WRA Gas Services and it is now one of the largest gas treating operations in the Texas Gulf Coast. The treating plants remove carbon dioxide and hydrogen sulfide from natural gas before it is introduced to transportation systems to ensure that it meets pipeline quality specifications. Natural gas from certain formations in the Texas Gulf Coast, as well as other locations, is high in carbon dioxide. The majority of the Partnership's active plants are treating gas from the Wilcox and Edwards formations in the Texas Gulf Coast, both of which are deeper formations that are high in carbon dioxide. The

Partnership's active treating facilities include 47 amine plants and five hydrogen sulfide scavenger installations. In cases where producers pay the Partnership to operate the treating facilities, the Partnership either charges a fixed rate per Mcf of natural gas treated or charges a fixed monthly fee.

In addition to the Partnership's treating plants, it has three gathering systems with an aggregate of 43 miles of gathering pipeline located in Val Verde, Crockett, Dewitt and Live Oak counties, Texas that are connected to approximately 73 producing wells. These gathering systems are connected to three of the Partnership's treating plants. The diameter of these gathering pipelines ranges from two to six inches. These gathering assets in the aggregate have a capacity of 61,000 MMBtu/d and average throughput was approximately 20,800 MMBtu/d for the year ended December 31, 2003. In cases where the Partnership both gathers and treats natural gas, its fee is generally based on throughput.

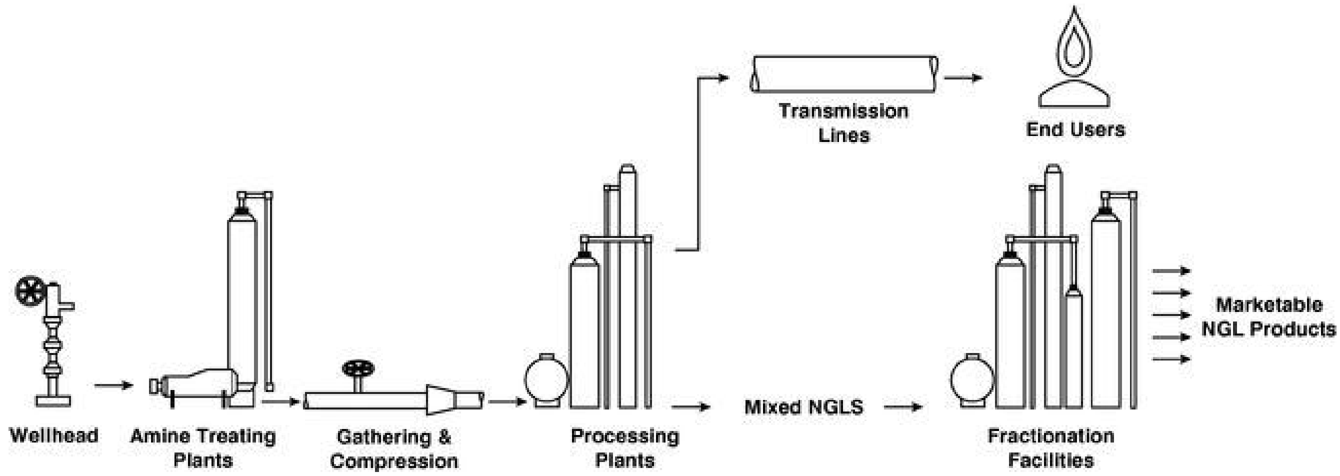
A component of the Partnership's strategy is to purchase used plants and then refurbish and repair them at its shop and seven-acre yard in Victoria, Texas and its 14-acre yard in Odessa, Texas. The Partnership believes that it can purchase used plants and recondition them at a significant cost savings to purchasing new plants. The Partnership has an inventory of plants of varying sizes which can be deployed after refurbishment. The Partnership also mounts most of the plant equipment on skids allowing them to be moved in a timely and cost efficient manner. At such time as the Partnership's active plants come offline, the Partnership will put them in its inventory pending redeployment. The Partnership believes its plant inventory gives it an advantage of several weeks in the time required to respond to a producer's request for treating services.

Treating process. The amine treating process involves a continuous circulation of a liquid chemical called amine that physically contacts with the natural gas. Amine has a chemical affinity for hydrogen sulfide and carbon dioxide that allows it to absorb the impurities from the gas. After mixing, gas and amine are separated and the impurities are removed from the amine by heating. Treating plants are sized by the amine circulation capacity in terms of gallons per minute. The size range of the 52 plants in operation is 3.5 to 300 gallons per minute, and the size range of the 9 plants in inventory is 3.5 to 1,000 gallons per minute.

Hydrogen sulfide scavenger facilities use a liquid or solid chemical that reacts with hydrogen sulfide thereby removing it from the gas. Used chemicals are disposed of and cannot be regenerated as amine can. The facilities are primarily vertical towers mounted on concrete foundations. As of December 31, 2003, the Partnership had two such facilities which were operated by the producer.

Industry Overview

The following diagram illustrates the natural gas treating, gathering, processing, fractionation and transmission process.



The midstream natural gas industry is the link between exploration and production of natural gas and the delivery of its components to end-use markets. The midstream industry is generally characterized by regional competition based on the proximity of gathering systems and processing plants to natural gas producing wells.

Natural gas gathering. The natural gas gathering process begins with the drilling of wells into gas bearing rock formations. Once a well has been completed, the well is connected to a gathering system. Gathering systems typically consist of a network of small diameter pipelines and, if necessary, compression systems that collect natural gas from points near producing wells and transport it to larger pipelines for further transmission.

Natural gas treating. Natural gas has a varied composition depending on the field, the formation and the reservoir from which it is produced. Natural gas from certain formations in the Texas Gulf Coast is high in carbon dioxide. Treating plants are placed at or near a well and remove carbon dioxide and hydrogen sulfide from natural gas before it is introduced into gathering systems to ensure that it meets pipeline quality specifications.

Natural gas processing and fractionation. The principal components of natural gas are methane and ethane, but most natural gas also contains varying amounts of NGLs and contaminants, such as water, sulfur compounds, nitrogen or helium. Most natural gas produced by a well is not suitable for long-haul pipeline transportation or commercial use and must be processed to remove the heavier hydrocarbon components and contaminants. Natural gas in commercial distribution systems is composed almost entirely of methane and ethane, with moisture and other contaminants removed to very low concentrations. Natural gas is processed not only to remove unwanted contaminants that would interfere with pipeline transportation or use of the natural gas, but also to separate from the gas those hydrocarbon liquids that have higher value as NGLs. The removal and separation of individual hydrocarbons by processing is possible because of differences in weight, boiling point, vapor pressure and other physical characteristics. Natural gas processing involves the separation of natural gas into pipeline quality natural gas and a mixed NGL stream, as well as the removal of contaminants. NGL fractionation facilities separate mixed NGL streams into discrete NGL products: ethane, propane, isobutane, normal butane and natural gasoline.

Natural gas transmission. Natural gas transmission pipelines receive natural gas from mainline transmission pipelines, plant tailgates, and gathering systems and deliver it to industrial end-users, utilities and to other pipelines. All of our transmission pipelines are intrastate systems.

Risk Management

As the Partnership purchases natural gas, it establishes a margin by selling natural gas for physical delivery to third party users, using over-the-counter derivative instruments or by entering into a future delivery obligation under futures contracts on the New York Mercantile Exchange. Through these transactions, the Partnership seeks to maintain a position that is substantially balanced between purchases, on the one hand, and sales or future delivery obligations, on the other hand. The Partnership's policy is not to acquire and hold natural gas future contracts or derivative products for the purpose of speculating on price changes.

Competition

The business of providing natural gas gathering, transmission, treating, processing and marketing services is highly competitive. The Partnership faces strong competition in acquiring new natural gas supplies. The Partnership's competitors in obtaining additional gas supplies and in treating new natural gas supplies include major integrated oil companies, major interstate and intrastate pipelines, and other natural gas gatherers that gather, process and market natural gas. Competition for natural gas supplies is primarily based on the reputation, efficiency and reliability of the gatherer and the pricing arrangements offered by the gatherer. The main difference between the Partnership and its competitors is that the Partnership offers most midstream services, while its competitors typically offer only a few select services. Many of its competitors have substantially greater capital resources and control substantially greater supplies of natural gas. The Partnership's major competitors in the Texas Gulf Coast area for natural gas supplies and markets include El Paso Field Services, Kinder Morgan Inc., Houston Pipeline Company and Duke Energy Field Services. The Partnership's major competitors in Mississippi for natural gas supplies and markets include Southern Natural Gas and Gulf South Pipeline Company.

The Partnership's gas treating operations face competition from manufacturers of new treating plants and from a small number of regional operators that provide plant and operations similar to ours. The Partnership also faces competition from vendors of used equipment that occasionally operate plants for producers. The Partnership's primary competitor for natural gas treating services in our principal market area is The Hanover Company.

In marketing natural gas, the Partnership has numerous competitors, including marketing affiliates of interstate pipelines, major integrated oil companies, and local and national natural gas gatherers, brokers and marketers of widely varying sizes, financial resources and experience. Local utilities and distributors of natural gas are, in some cases, engaged directly, and through affiliates, in marketing activities that compete with its marketing operations.

Natural Gas Supply

The Partnership's end-user pipelines have connections with major interstate and intrastate pipelines, which the Partnership believes have ample supplies of natural gas in excess of the volumes required for these systems. In connection with the construction and acquisition of the Partnership's gathering systems, it evaluated well and reservoir data furnished by producers to determine the availability of natural gas supply for the systems. Based on those evaluations, the Partnership believes that there should be adequate natural gas supply to recoup its investment with an adequate rate of return. The Partnership does not routinely obtain independent evaluations of reserves dedicated to its systems due to the cost of such evaluations. Accordingly, the Partnership does not have estimates of total reserves dedicated to its systems or the anticipated life of such producing reserves.

Credit Risk and Significant Customers

The Partnership is diligent in attempting to ensure that it issues credit to only credit-worthy customers. However, the Partnership's purchase and resale of gas exposes it to significant credit risk, as the margin on any sale is generally a very small percentage of the total sale price. Therefore, a credit loss can be very large relative to the Partnership's overall profitability.

During the year ended December 31, 2003, the Partnership had one customer that individually accounted for more than 10% of consolidated revenues. During the year ended December 31, 2003, Kinder Morgan Tejas accounted for 20.5% of our consolidated revenue. While this customer represents a significant percentage of consolidated revenues, the loss of this customer would not have a material impact on our results of operations.

Regulation

Regulation by FERC of Interstate Natural Gas Pipelines. Under the Natural Gas Act ("NGA"), the Federal Energy Regulatory Commission ("FERC") generally regulates the transportation of natural gas in interstate commerce. The Partnership does not own any interstate natural gas pipelines, so FERC does not directly regulate any of its facilities or operations. However, as discussed below, the Partnership does perform some interstate transmission service that is incidental to its intrastate business, and this interstate transmission is subject to FERC rate regulation. Also, FERC's regulation of interstate transportation by others indirectly influences certain aspects of the Partnership's business and the market for its products. In recent years, FERC has pursued pro-competitive policies in its regulation of interstate natural gas pipelines. However, we cannot assure you that FERC will continue this approach as it considers matters such as pipelines' rates and rules and policies that may affect rights of access to natural gas transportation capacity.

Intrastate Pipeline Regulation. The Partnership's intrastate natural gas pipeline operations are not subject to regulation by FERC, but they are subject to regulation by various agencies of the states in which they are located, principally the Texas Railroad Commission, or TRRC. However, to the extent that the Partnership's intrastate pipeline systems provide incidental transportation of natural gas in interstate commerce, the rates, terms and conditions of such transportation services are subject to FERC jurisdiction under Section 311 of the Natural Gas Policy Act ("NGPA"). Section 311 applies to, among other things, the providing of transportation services by an intrastate natural gas pipeline on behalf of a local distribution company or an interstate natural gas pipeline. Most states have agencies that possess the authority to review and authorize natural gas transportation transactions and the construction, acquisition, abandonment and interconnection of physical facilities. Some states also have state agencies that regulate transportation rates, service terms and conditions and contract pricing to ensure their reasonableness and to ensure that the intrastate pipeline companies that they regulate do not discriminate among similarly situated customers.

The Partnership's operations in Texas are subject to the Texas Gas Utility Regulatory Act, as implemented by the TRRC. Generally the TRRC is vested with authority to ensure that rates charged for natural gas sales or transportation services are just and reasonable. The rates the Partnership charges for transportation services are deemed just and reasonable under Texas law unless challenged in a complaint. The Partnership cannot predict whether such a complaint will be filed against it or whether the TRRC will change its regulation of these rates.

A twelve-mile section of the Partnership's Mississippi gathering system is regulated by the Mississippi Oil and Gas Board as it transports gas not owned by the Partnership for a fee. The Partnership's one hundred twenty-five mile gathering system in Oklahoma is not regulated by the Oklahoma Corporation Commission. Similarly, gathering systems the Partnership owns in Alabama and Louisiana are not subject to regulation by the Alabama State Oil and Gas Board and the Louisiana Office of Conservation respectively. While it is possible that Alabama, Louisiana, Oklahoma, Mississippi and New Mexico may try to assert or expand jurisdiction on those lines, it is not likely that the assertion or expansion of that jurisdiction would have a significant effect on the Partnership's operations in those states because all tend to apply Federal regulations to natural gas pipeline facilities without numerous additional state-specific requirements.

Gathering Pipeline Regulation. Section 1(b) of the NGA exempts natural gas gathering facilities from the jurisdiction of FERC under the NGA. The Partnership owns a number of natural gas pipelines that it believes meet the traditional tests FERC has used to establish a pipeline's status as a gatherer not subject to FERC jurisdiction. However, the distinction between FERC-regulated transmission services and federally unregulated gathering services is the subject of substantial, on-going litigation, so the classification and regulation of the Partnership's gathering facilities, for purposes of rate regulation to the extent it provides NGPA Section 311 services over such facilities, are subject to change based on future determinations by FERC and the courts. State regulation of gathering facilities generally includes various safety, environmental and, in some circumstances, nondiscriminatory take requirements, and in some instances complaint-based rate regulation.

The Partnership is subject to state ratable take and common purchaser statutes. The ratable take statutes generally require gatherers to take, without undue discrimination, natural gas production that may be tendered to the gatherer for handling. Similarly, common purchaser statutes generally require gatherers to purchase without undue discrimination as to source of supply or producer. These statutes are designed to prohibit discrimination in favor of one producer over another producer or one source of supply over another source of supply. These statutes have the effect of restricting our right as an owner of gathering facilities to decide with whom the Partnership contracts to purchase or transport natural gas.

Natural gas gathering may receive greater regulatory scrutiny at both the state and federal levels since FERC has less extensively regulated the gathering activities of interstate pipeline transmission companies and a number of such companies have transferred gathering facilities to unregulated affiliates. For example, the TRRC has approved changes to its regulations governing transportation and gathering services performed by intrastate pipelines and gatherers, which prohibit such entities from unduly discriminating in favor of their affiliates. The Partnership's gathering operations could be adversely affected should they be subject in the future to the application of state or federal regulation of rates and services. The Partnership's gathering operations also may be or become subject to safety and operational regulations relating to the design, installation, testing, construction, operation, replacement and management of gathering facilities. Additional rules and legislation pertaining to these matters are considered or adopted from time to time. The Partnership cannot predict what effect, if any, such changes might have on its operations, but the industry could be required to incur additional capital expenditures and increased costs depending on future legislative and regulatory changes.

Sales of Natural Gas. The price at which the Partnership sells natural gas currently is not subject to federal regulation and, for the most part, is not subject to state regulation. The Partnership's sales of natural gas are affected by the availability, terms and cost of pipeline transportation. As noted above, the price and terms of access to pipeline transportation are subject to extensive federal and state regulation. FERC is continually proposing and implementing new rules and regulations affecting those segments of the natural gas industry, most notably interstate natural gas transmission companies, that remain subject to FERC's jurisdiction. These initiatives also may affect the intrastate transportation of natural gas under certain circumstances. The stated purpose of many of these regulatory changes is to promote competition among the various sectors of the natural gas industry and these initiatives generally reflect less extensive regulation. The Partnership cannot predict the ultimate impact of these regulatory changes on its natural gas marketing operations, and we note that some of FERC's more recent proposals may adversely affect the availability and reliability of interruptible transportation service on interstate pipelines. The Partnership does not believe that it will be affected by any such FERC action materially differently than other natural gas marketers with whom it competes.

Environmental Matters

General. The Partnership's operation and the Partnership's possible future operation of processing and fractionation plants, pipelines and associated facilities in connection with the gathering and processing of natural gas and the transportation, fractionation and storage of NGLs is subject to stringent and complex federal, state and local laws and regulations relating to release of hazardous substances or wastes into the environment or otherwise relating to protection of the environment. As with the industry generally, compliance with existing and anticipated environmental laws and regulations increases the Partnership's overall costs of doing business, including cost of planning, constructing, and operating plants, pipelines, and other facilities. Included in the Partnership's construction and operation costs are capital cost items necessary to maintain or upgrade equipment and facilities. The Partnership will likely incur similar costs upon its acquisition of assets if it acquires operating assets.

Any failure to comply with applicable environmental laws and regulations, including those relating to obtaining required governmental approvals, may result in the assessment of administrative, civil, or criminal penalties, imposition of investigatory or remedial activities and, in less common circumstances, issuance of injunctions or construction bans or delays. While the Partnership believes that it currently holds material governmental approvals required to operate its major facilities, the Partnership is currently evaluating and updating permits for certain of its facilities that primarily were obtained in recent acquisitions. As part of the regular overall evaluation of its operations, the Partnership has implemented procedures to and are presently working to ensure that all governmental approvals, for both recently acquired facilities and existing operations, are updated as may be necessary. The Partnership believes that its operations and facilities are in substantial compliance with applicable environmental laws and regulations and that the cost of compliance with such laws and regulations will not have a material adverse effect on its operating results or financial condition.

The clear trend in environmental regulation is to place more restrictions and limitations on activities that may affect the environment, and thus there can be no assurance as to the amount or timing of future expenditures for environmental compliance or remediation, and actual future expenditures may be different from the amounts we currently anticipate. Moreover, risks of process upsets, accidental releases or spills are associated with the Partnership's possible future operations, and the Partnership cannot assure you that it will not incur significant costs and liabilities including those relating to claims for damage to property and persons as a result of such upsets, releases, or spills. In the event of future increases in costs, the Partnership may be unable to pass on those cost increases to our customers. A discharge of hazardous substances or wastes into the environment could, to the extent the event is not insured, subject the Partnership to substantial expense, including both the cost to comply with applicable laws and regulations and the cost related to claims made by neighboring landowners and other third parties for personal injury or damage to property. The

Partnership will attempt to anticipate future regulatory requirements that might be imposed and plan accordingly in order to remain in compliance with changing environmental laws and regulations and in order to minimize the costs of such compliance.

Hazardous Substance and Waste. To a large extent, the environmental laws and regulations affecting the Partnership's possible future operations relate to the release of hazardous substances or solid wastes into soils, groundwater, and surface water, and include measures to control environmental pollution of the environment. These laws and regulations generally regulate the generation, storage, treatment, transportation, and disposal of solid and hazardous wastes, and may require investigatory and corrective actions at facilities where such waste may have been released or disposed. For instance, the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, also known as the "Superfund" law, and comparable state laws, impose liability without regard to fault or the legality of the original conduct, on certain classes of persons that contributed to a release of "hazardous substance" into the environment. These persons include the owner or operator of the site where a release occurred and companies that disposed or arranged for the disposal of the hazardous substances found at the site. Under CERCLA, these persons may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources, and for the costs of certain health studies. CERCLA also authorizes the EPA and, in some cases, third parties to take actions in response to threats to the public health or the environment and to seek to recover from the responsible classes of persons the costs they incur. It is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by hazardous substances or other wastes released into the environment. Although "petroleum" as well as natural gas and NGLs are excluded from CERCLA's definition of a "hazardous substance," in the course of future, ordinary operations, we may generate wastes that may fall within the definition of a "hazardous substance." We may be responsible under CERCLA for all or part of the costs required to clean up sites at which such wastes have been disposed. We have not received any notification that we may be potentially responsible for cleanup costs under CERCLA or any analogous state laws.

The Partnership also generates, and may in the future generate, both hazardous and nonhazardous solid wastes that are subject to requirements of the federal Resource Conservation and Recovery Act, or RCRA, and comparable state statutes. From time to time, the Environmental Protection Agency, or EPA, has considered the adoption of stricter disposal standards for nonhazardous wastes, including crude oil and natural gas wastes. The Partnership is not currently required to comply with a substantial portion of the RCRA requirements because its operations generate minimal quantities of hazardous wastes. However, it is possible that some wastes generated by the Partnership that are currently classified as nonhazardous may in the future be designated as "hazardous wastes," resulting in the wastes being subject to more rigorous and costly disposal requirements. Changes in applicable regulations may result in an increase in our capital expenditures or plant operating expenses.

The Partnership currently owns or leases, and has in the past owned or leased, and in the future the Partnership may own or lease, properties that have been used over the years for natural gas gathering and processing and for NGL fractionation, transportation and storage. Solid waste disposal practices within the NGL industry and other oil and natural gas related industries have improved over the years with the passage and implementation of various environmental laws and regulations. Nevertheless, some hydrocarbons and other solid wastes have been disposed of on or under various properties owned or leased by the Partnership during the operating history of those facilities. In addition, a number of these properties may have been operated by third parties over whom we had no control as to such entities' handling of hydrocarbons or other wastes and the manner in which such substances may have been disposed of or released. These properties and wastes disposed thereon may be subject to CERCLA, RCRA, and analogous state laws. Under these laws, the Partnership could be required to remove or remediate previously disposed wastes or property contamination, including groundwater contamination or to perform remedial operations to prevent future contamination.

The Partnership recently acquired two assets from DEFS that have environmental contamination, including a gas plant in Montgomery County, near Conroe, Texas and a compressor station near Cadeville, Louisiana. At both of these sites, contamination from historical operations has been identified at levels that exceed the applicable state action levels. Consequently, site investigation and/or remediation are underway to address those impacts. The estimated remediation cost for the Conroe plant site is currently estimated to be approximately $3.2 million, and the remediation cost for the Cadeville site is currently estimated to be approximately $1.2 million. Under the Partnership's purchase agreement, Duke has retained liability for cleanup of both the Conroe and Cadeville sites. Moreover, the remediation costs associated with the Conroe site will be covered by agreements with TRC Companies and AIG. Therefore, the Partnership does not expect to incur any material environmental liability associated with the Conroe or Cadeville sites.

Air Emissions. The Partnership's operations are, and the Partnership's possible future operations will likely be, subject to the Clean Air Act and comparable state statutes. Amendments to the Clean Air Act were enacted in 1990. Moreover, recent or soon to be adopted changes to state implementation plans for controlling air emissions in regional, non-attainment areas require or will require most industrial operations in the United States to incur capital expenditures in order to meet air emission control standards developed by the EPA and state environmental agencies. As a result of these amendments, the Partnership's processing and fractionating plants, pipelines, and storage facilities or any of its future assets that emit volatile organic compounds or nitrogen oxides may become subject to increasingly stringent regulations, including requirements that some sources install maximum or reasonably available control technology. Such requirements, if applicable to our operations, could cause the Partnership to incur capital expenditures in the next several years for air pollution control equipment in connection with maintaining or obtaining governmental approvals addressing air emission related issues. In addition, the 1990 Clean Air Act Amendments established a new operating permit for major sources, which applies to some of the Partnership's facilities and which may apply to some of its possible future facilities. Failure to comply with applicable air statutes or regulations may lead to the assessment of administrative, civil or criminal penalties, and may result in the limitation or cessation of construction or operation of certain air emission sources. Although the Partnership can give no assurances, the Partnership believes implementation of the 1990 Clean Air Act Amendments will not have a material adverse effect on its financial condition or operating results.

Clean Water Act. The Federal Water Pollution Control Act, also known as the Clean Water Act, and similar state laws impose restrictions and strict controls regarding the discharge of pollutants, including natural gas liquid related wastes, into state waters or waters of the United States. Regulations promulgated pursuant to these laws require that entities that discharge into federal and state waters obtain National Pollutant Discharge Elimination System, or NPDES, and/or state permits authorizing these discharges. The Clean Water Act and analogous state laws assess administrative, civil and criminal penalties for discharges of unauthorized pollutants into the water and impose substantial liability for the costs of removing spills from such waters. In addition, the Clean Water Act and analogous state laws require that individual permits or coverage under general permits be obtained by covered facilities for discharges of storm water runoff. We believe that the Partnership is in substantial compliance with Clean Water Act permitting requirements as well as the conditions imposed thereunder, and that continued compliance with such existing permit conditions will not have a material effect on its results of operations.

Employee Safety. The Partnership is subject to the requirements of the Occupational Safety and Health Act, referred to as OSHA, and comparable state laws that regulate the protection of the health and safety of workers. In addition, the OSHA hazard communication standard requires that information be maintained about hazardous materials used or produced in operations and that this information be provided to employees, state and local government authorities and citizens. We believe that the Partnership's operations are in substantial compliance with the OSHA requirements, including general industry standards, record keeping requirements, and monitoring of occupational exposure to regulated substances.

Endangered Species Act. The Endangered Species Act restricts activities that may affect endangered species or their habitats. Presently, the Partnership operates in only one area that is designated as a critical habitat for a certain species of beetle. This area consists of 29 counties in eastern and central Oklahoma into which part of the Partnership's gathering system extends. A coalition of oil and gas industry and regulatory agencies are currently working together to minimize impacts on future construction and operation activities for oil and gas production and transportation. This designated area has had no material effect on the Partnership's operations in Oklahoma to date. While the Partnership has no reason to believe that the Partnership operates in any other area that is currently designed as habitat for endangered or threatened species, the discovery of previously unidentified endangered species could cause the Partnership to incur additional costs or become subject to operating restrictions or bans in the affected areas.

Safety Regulations. The Partnership's pipelines are subject to regulation by the U.S. Department of Transportation under the Hazardous Liquid Pipeline Safety Act, as amended, or HLPSA, and the Pipeline Integrity Management in High Consequence Areas (Gas Transmission Pipelines) amendment to 49 CFR Part 192, effective February 14, 2004 relating to the design, installation, testing, construction, operation, replacement and management of pipeline facilities. The HLPSA covers crude oil, carbon dioxide, NGL and petroleum products pipelines and requires any entity which owns or operates pipeline facilities to comply with the regulations under the HLPSA, to permit access to and allow copying of records and to make certain reports and provide information as required by the Secretary of Transportation. The Pipeline Integrity Management in High Consequence Areas (Gas Transmission Pipelines) amendment to 49 CFR Part 192 (PIM) requires operators of gas transmission pipelines and segments of gathering lines in certain populated areas to ensure the integrity of their pipelines through hydrostatic pressure testing, the use of in-line inspection tools or through risk-based direct assessment techniques. The Partnership believes that its pipeline operations are in substantial compliance with applicable HLPSA and PIM requirements; however, due to the possibility of new or amended laws and regulations or reinterpretation of existing laws and regulations, there can be no assurance that future compliance with the HLPSA or PIM requirements will not have a material adverse effect on the Partnership's results of operations or financial positions.

Office Facilities

In addition to the Partnership's gathering and treating facilities discussed above, we, together with the Partnership, occupy approximately 21,000 square feet, increasing up to approximately 40,000 square feet over the next two years, of space at our executive offices in Dallas, Texas under a lease expiring in March 2010.

Employees

As of December 31, 2003, the Partnership's operating Partnership, had approximately 189 full-time employees. Approximately half of the Partnership's employees were general and administrative, engineering, accounting and commercial personnel and the remainder were operational employees. Neither we nor the Partnership is party to any collective bargaining agreements, and neither we nor the Partnership had any significant labor disputes in the past. We believe that we have good relations with our employees.

Item 2. *Properties*

A description of our properties is contained in "Item 1. Business."

Title to Properties

Substantially all of the Partnership's pipelines are constructed on rights-of-way granted by the apparent record owners of the property. Lands over which pipeline rights-of-way have been obtained may be subject to prior liens that have not been subordinated to the right-of-way grants. The Partnership has obtained, where necessary, easement agreements from public authorities and railroad companies to cross over or under, or to lay facilities in or along, watercourses, county roads, municipal streets, railroad properties and state highways, as applicable. In some cases, property on which the Partnership's pipeline was built was purchased in fee. The Partnership's Gregory processing plant is on land that it owns in fee.

The Partnership believes that it has satisfactory title to all of its assets. Title to property may be subject to encumbrances. The Partnership believes that none of such encumbrances should materially detract from the value of its properties or from our interest in these properties or should materially interfere with their use in the operation of its business.

Item 3. *Legal Proceedings*

We are not currently a party to any material litigation. The Partnership operations are subject to a variety of risks and disputes normally incident to its business. As a result, at any given time the Partnership may be a defendant in various legal proceedings and litigation arising in the ordinary course of business. The Partnership maintains insurance policies with insurers in amounts and with coverage and deductibles as its managing general partner believes are reasonable and prudent. However, we cannot assure that this insurance will be adequate to protect the Partnership from all material expenses related to potential future claims for personal and property damage or that these levels of insurance will be available in the future at economical prices.

Item 4. *Submission of Matters to a Vote of Security Holders*

No matters were submitted to security holders during the fourth quarter of the year ended December 31, 2003.

PART II

Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

Our common stock is listed on the NASDAQ National Market under the symbol "XTXI". Our common stock began trading on January 13, 2004, at an initial public offering price of $19.50 per share. On March 12, 2004, there were approximately 2,522 record holders and beneficial owners (held in street name) of our common stock.

We have not paid any cash dividend as of the date of this report, however, we intend to pay to our stockholders, on a quarterly basis, dividends equal to the cash we receive from our Partnership distributions, less reserves for expenses, future dividends and other uses of cash, including:

- federal income taxes, which we are required to pay because we are taxed as a corporation;
- the expenses of being a public company;
- other general and administrative expenses;
- capital contributions to the Partnership upon the issuance by it of additional partnership securities in order to maintain the general partner's 2.0% general partner interest; and
- reserves our board of directors believes prudent to maintain, including reserves equal to the benefit we will receive in 2004 from our existing net operating loss carryforwards.

If the Partnership is successful in implementing its business strategy and increasing distributions to its partners, we would generally expect to increase dividends to our stockholders, although the timing and amount of any such increased dividends will not necessarily be comparable to the increased Partnership distributions.

The determination of the amount of cash dividends, including the quarterly dividend referred to above, if any, to be declared and paid will depend upon our financial condition, results of operations, cash flow, the level of our capital expenditures, future business prospects and any other matters that our board of directors deems relevant. The Partnership's debt agreements contain restrictions on the payment of distributions and prohibit the payment of distributions if the Partnership is in default. If the Partnership cannot make incentive distributions to the general partner or limited partner distributions to us, we will be unable to pay dividends on our common stock.

Recent Sales of Unregistered Securities

In January 2003, we issued: (i) 239,745 shares of our Series A $7\,^1/_2$% Cumulative Convertible Preferred Stock to Yorktown Energy Partners IV, L.P., Barry E. Davis, A. Chris Aulds, James R. Wales, Lisa M. Brecht, John W. Daugherty, William W. Davis, Mark E. Huff, Mike W. Hopkins, Jack M. Lafield, Rodney A. Madden and Michael P. Scott as a dividend paid pursuant to the terms of the Series A $7\,^1/_2$% Cumulative Convertible Preferred Stock; and (ii) 22,236 shares of our Series B $7^1/_2$% Cumulative Convertible Preferred Stock to Yorktown Energy Partners IV, L.P., Lubar Nominees, Barry E. Davis, A. Chris Aulds and James R. Wales as a dividend paid pursuant to the terms of the Series B $7\,^1/_2$% Cumulative Convertible Preferred Stock.

In August 2003, we sold in a private placement: (i) 10,000 of our Series B $7^1/_2$% Cumulative Convertible Preferred Stock to Marc Lyons and Stewart McCorkle, each of whom is an employee of a subsidiary of the registrant, for an aggregate purchase price of $120,000, consisting of $12,000 in cash and $108,000 in the form of full recourse promissory notes secured by the shares purchased by such individuals; and (ii) 20,000 shares of our Series C $7^{1}/_{2}$% Cumulative Convertible Preferred Stock to Dale Wilson, an employee of a subsidiary of the registrant, for an aggregate purchase price of $280,000, consisting of $28,000 in cash and $252,000 in the form of a full recourse promissory note secured by the shares purchased by such individual.

Upon the completion of our initial public offering in January 2004, all of the above shares of preferred stock were converted into common stock. The sales and issuances of securities in all of the above transactions were deemed to be exempt from registration under the Securities Act of 1933, in reliance upon Section 4(2) thereof, or Regulation D or Rule 701 promulgated thereunder, as transactions by an issuer not involving a public offering. Recipients of the securities in each such transaction represented their intentions to acquire such securities for investment purposes only and not with a view to or for sale in connection with any distribution thereof and appropriate legends were affixed to the instruments issued in such transactions. All recipients either received adequate information about the registrant or had access, through employment relationships or otherwise, to such information. In addition, the foregoing transactions were consummated without the use of underwriters.

Use of Proceeds from Registered Securities

On January 12, 2004, our registration statement on Form S-1 (Registration No. 333-110095) was declared effective by the Securities and Exchange Commission in connection with the public offering of 2,306,000 shares of common stock (plus up to 345,900 additional shares of common stock upon the exercise of the underwriters' over-allotment option), which commenced on January 13, 2004. The initial public offering did not terminate prior to the sale of all the securities registered. The underwriters of the offering were A.G. Edwards & Sons, Inc., Raymond James & Associates, Inc., and RBC Dain Rauscher Inc. The initial public offering consisted solely of one class of common stock. The number of securities registered, including the shares of common stock subject to the underwriters' over-allotment option, was 2,651,900, all of which have been sold to the public.

The price to public, underwriting discounts and commissions, and proceeds to the Partnership are set forth in the following table:

		Price to Public	Underwriting Discounts and Commissions	Proceeds to the Selling Stockholders	Proceeds Received by Us
Per share	$	19.50	1.26	18.24	18.24
Total upon initial public offering	$	44,967,000	2,905,560	42,061,440	0
Total upon exercise of over-allotment	$	51,712,050	3,341,394	42,061,440	6,309,216(1)

(1) Before deducting expenses of approximately $1.5 million paid by us.

The net proceeds that we received from the initial public offering of the shares of common stock, after deducting expenses of approximately $1.5 million and underwriting discounts and commissions, was approximately $4.8 million. We plan to use the net proceeds received by us from the initial public offering for general corporate expenses, but have not done so as of the date of this report. We did not receive any of the net proceeds from any sale of shares of common stock by any selling stockholder. The selling stockholders used approximately $5.0 million of the net proceeds received by them to retire outstanding notes from the selling stockholders held by us.

Item 6. *Selected Financial Data*

The following table sets forth selected historical financial and operating data of Crosstex Energy, Inc. and our predecessor, Crosstex Energy Services, Ltd., as of and for the dates and periods indicated. The selected historical financial data are derived from the audited financial statements of Crosstex Energy, Inc. or our predecessor, Crosstex Energy Services, Ltd. The investment in our predecessor by Yorktown Energy Partners IV, L.P. in May 2000 resulted in the dissolution of the predecessor partnership and the creation of a new partnership with the same organization, purpose, assets and liabilities. Accordingly, the financial statements of our predecessor for 2000 are divided into the four months ended April 30, 2000 and the eight months ended December 31, 2000 because a new basis of accounting was established effective May 1, 2000 to give effect to the Yorktown transaction. In addition, our summary historical financial and operating data includes the results of operations of the Arkoma system beginning in September 2000, the Gulf Coast system beginning in September 2000, the CCNG system, which includes the Corpus Christi system, the Gregory gathering system and the Gregory processing plant, beginning in May 2001, the Vanderbilt system beginning in December 2002 and the DEFS assets beginning in June 2003.

The table should be read together with "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Crosstex Energy, Inc.				Crosstex Energy Services, Ltd.(1)	
	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001	Eight Months Ended December 31, 2000	Four Months Ended April 30, 2000	Year Ended December 31, 1999
Statement of Operations Data:						
Revenues:						
Midstream	$ 993,140	$ 437,676	$ 362,673	$ 88,008	$ 3,591	$ 7,896
Treating	20,523	14,817	24,353	17,392	5,947	9,770
Total revenues	1,013,663	452,493	387,026	105,400	9,538	17,666
Operating costs and expenses:						
Midstream purchased gas	946,412	413,982	344,755	83,672	2,746	5,154
Treating purchased gas	7,568	5,767	18,078	14,876	4,731	8,110
Operating expenses	17,758	11,420	7,761	1,796	544	986
General and administrative	11,593	7,663	5,583	2,010	810	2,078
Stock based compensation	5,345	41	—	—	8,802	—
Impairments	—	4,175	2,873	—	—	538
(Profit) loss on energy trading contracts	(1,905)	(2,703)	3,714	(1,253)	(638)	(1,764)
Depreciation and amortization	13,542	7,745	6,208	2,333	522	1,286
Total operating costs and expenses	1,000,313	448,090	388,972	103,434	17,517	16,388
Operating income (loss)	13,350	4,403	(1,946)	1,966	(7,979)	1,278
Other income (expense):						
Interest expense, net	(3,103)	(2,381)	(2,253)	(530)	(79)	(638)
Other income (expense)	179	56	174	115	381	(138)
Total other income (expense)	(2,924)	(2,325)	(2,079)	(415)	302	(776)
Income (loss) before gain on issuance of units by the partnership, income taxes and interest of non-controlling partners in the partnership's net income	10,426	2,078	(4,025)	1,551	(7,677)	502
Gain on issuance of partnership units(2)	18,360	11,054	—	—	—	—
Income tax (provision) benefit	(10,157)	(7,451)	1,294	(679)	—	—
Interest of non-controlling partners in the partnership's net income	(5,181)	(99)	—	—	—	—
Net income (loss)	$ 13,448	$ 5,582	($ 2,731)	$ 872	($ 7,677)	$ 502
Net income (loss) per common share—basic(3)	$ 2.83	$ 0.68	$ (1.25)	$ 0.05	N/A	N/A
Net income (loss) per common share—diluted(3)	$ 1.10	$ 0.49	$ (1.25)	$ 0.05	N/A	N/A

Balance Sheet Data:						
Working capital surplus (deficit)	$ (6,047)	$ (9,483)	$ (1,555)	$ 5,763	$ (4,005)	$ (3,483)
Property and equipment, net	204,890	111,203	84,951	37,242	10,540	8,072
Total assets	369,738	240,676	171,369	202,909	45,051	36,497
Long-term debt	60,750	22,550	60,000	22,000	7,000	5,389
Interest of non-controlling partners in the partnership	67,882	27,540	—	—	—	—
Stockholders' equity	69,619	57,749	42,241	39,808	3,608	3,242
Cash Flow Data:						
Net cash flow provided by (used in):						
Operating activities	$ 42,103	$ (5,650)	$ (10,686)	$ 7,634	$ 7,380	$ 1,404
Investing activities	(110,288)	(33,240)	(52,535)	(25,643)	(2,849)	(1,342)
Financing activities	65,856	41,746	44,918	36,664	198	(857)
Other Financial Data:						
Midstream gross margin	$ 46,728	$ 23,694	$ 17,918	$ 4,336	$ 845	$ 2,742
Treating gross margin	12,955	9,050	6,275	2,516	1,216	1,660
Total gross margin(4)	$ 59,683	$ 32,744	$ 24,193	$ 6,852	$ 2,061	$ 4,402
Operating Data:						
Pipeline throughput (MMBtu/d)	626,000	392,000	313,000	104,000	23,000	20,000
Natural gas processed (MMBtu/d)	132,000	86,000	61,000	16,000	31,000	23,000
Treating volumes (MMBtu/d)(5)	90,000	98,000	63,000	36,000	27,000	13,000

(1) We, through our ownership interest in the Partnership, are the successor to Crosstex Energy Services, Ltd. Results of operations and balance sheet data prior to May 1, 2000 represent historical results of the predecessor to Crosstex Energy Services, Ltd. These results are not necessarily comparable to the results of Crosstex Energy Services, Ltd. subsequent to May 2000 due to the new basis of accounting. There are no income tax provisions for these predecessor periods because Crosstex Energy Services, Ltd. was a limited partnership not subject to federal income taxes.

(2) We recognized gains of $11.1 million in 2002 and $18.4 million in 2003 as a result of the Partnership issuing additional units to the public in public offerings at prices per unit greater than our equivalent carrying value.

(3) Per share amounts have been adjusted for the two-for-one stock split made in conjunction with an initial public offering in January 2004.

(4) Gross margin is defined as revenue less related cost of purchased gas.

(5) Represent volumes for treating plants operated by the Partnership whereby it receives a fee based on the volumes treated.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

You should read the following discussion of our financial condition and results of operations in conjunction with the financial statements and notes thereto included elsewhere in this report. For more detailed information regarding the basis of presentation for the following information, you should read the notes to the financial statements included in this report.

Overview

Crosstex Energy, Inc. is a Delaware corporation formed on April 28, 2000 to engage, through its subsidiaries, in the gathering, transmission, treating, processing and marketing of natural gas. On July 12, 2002, we formed Crosstex Energy, L.P., a Delaware limited partnership, to acquire indirectly substantially all of the assets, liabilities and operations of its predecessor, Crosstex Energy Services, Ltd. Our assets consist almost exclusively of partnership interests in Crosstex Energy, L.P., a publicly traded limited partnership engaged in the gathering, transmission, treating, processing and marketing of natural gas. These partnership interests consist of (i) 333,000 common units and 4,667,000 subordinated units, representing a 54.3% limited partner interest in Crosstex Energy, L.P. and (ii) 100% ownership interest in Crosstex Energy GP, L.P., the general partner of Crosstex Energy, L.P., which owns a 2.0% general partner interest and all of the incentive distribution rights in Crosstex Energy, L.P.

Since we control the general partner interest in the Partnership, we reflect our ownership interest in the Partnership on a consolidated basis, which means that our financial results are combined with the Partnership's financial results and the results of our other subsidiaries. The interest owned by non-controlling partner's share of income is reflected as an expense in our results of operations. We have no separate operating activities apart from those conducted by the Partnership, and our cash flows consist almost exclusively of distributions from the Partnership on the partnership interests we own. Our consolidated results of operations are derived from the results of operations of the Partnership, and also include our gains on the issuance of units in the Partnership, deferred taxes, interest of non-controlling partners in the Partnership's net income, interest income (expense) and general and administrative expenses not reflected in the Partnership's results of operations. Accordingly, the discussion of our financial position and results of operations in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" primarily reflects the operating activities and results of operations of the Partnership.

The Partnership has two industry segments, Midstream and Treating, with a geographic focus along the Texas Gulf Coast. The Partnership's Midstream division focuses on the gathering, processing, transmission and marketing of natural gas, as well as providing certain producer services, while its Treating division focuses on the removal of carbon dioxide and hydrogen sulfide from natural gas to meet pipeline quality specifications. For the year ended December 31, 2003, 78% of the Partnership's gross margin was generated in the Midstream division, with the balance in the Treating division, and approximately 71% of its gross margin was generated in the Texas Gulf Coast region. The Partnership focuses on gross margin to manage its business because its business is generally to gather, process, transport, market or treat gas for a fee or a buy-sell margin. The Partnership buys and sells most of its gas at a fixed relationship to the relevant index price so its margins are not significantly affected by changes in gas prices. As explained under "Commodity Price Risk" below, the Partnership enters into financial instruments to reduce volatility in its gross margin due to price fluctuations.

Since the Partnership's formation, it has grown significantly as a result of its construction and acquisition of gathering and transmission pipelines and treating and processing plants. From January 1, 2000 through December 31, 2003, the Partnership had invested approximately $222.0 million to develop or acquire new assets. The purchased assets were acquired from numerous sellers at different periods and were accounted for under the purchase method of accounting. Accordingly, the results of operations for such acquisitions are included in the Partnership's financial statements only from the applicable date of the acquisition. As a consequence, the historical results of operations for the periods presented may not be comparable.

The Partnership's results of operations are determined primarily by the volumes of natural gas gathered, transported, purchased and sold through its pipeline systems, processed at its processing facilities or treated at its treating plants as well as fees earned from recovering carbon dioxide and natural gas liquids at a non-operated processing plant. The Partnership generates revenues from four primary sources:

- gathering and transporting natural gas on the pipeline systems it owns;
- processing natural gas at its processing plants;
- treating natural gas to remove carbon dioxide and other impurities at its treating plants; and
- providing producer services.

The bulk of the Partnership's operating profits are derived from the margins it realizes for gathering and transporting natural gas through its pipeline systems. Generally, the Partnership buys gas from a producer, plant tailgate, or transporter at either a fixed discount to a market index or a percentage of the market index. The Partnership then transports and resells the gas. The resale price is based on the same index price at which the gas was purchased, and, if the Partnership is to be profitable, at a smaller discount or larger premium to the index than it was purchased. The Partnership attempts to execute all purchases and sales substantially concurrently, or it enters into a future delivery obligation, thereby establishing the basis for the margin it will receive for each natural gas transaction. The Partnership's gathering and transportation margins related to a percentage of the index price can be adversely affected by declines in the price of natural gas. See "Commodity Price Risk" below for a discussion of how the Partnership manages its business to reduce the impact of price volatility.

The Partnership generates producer services revenues through the purchase and resale of natural gas. The Partnership currently purchases for resale volumes of natural gas that do not move through its gathering, processing or transmission assets from over 50 independent producers. The Partnership engages in such activities on more than 20 interstate and intrastate pipelines with a major emphasis on Gulf Coast pipelines. The Partnership focuses on supply aggregation transactions in which it either purchases and resells gas and thereby eliminates the need of the producer to engage in the marketing activities typically handled by in-house marketing or supply departments of larger companies, or acts as agent for the producer.

The Partnership generates treating revenues under three arrangements:

- a volumetric fee based on the amount of gas treated, which accounted for approximately 55% and 66% of the operating income in its Treating division for the years ended December 31, 2003 and 2002, respectively;
- a fixed fee for operating the plant for a certain period, which accounted for approximately 38% and 22% of the operating income in its Treating division for the years ended December 31, 2003 and 2002, respectively; or
- a fee arrangement in which the producer operates the plant, which accounted for approximately 7% and 12% of the operating income in its Treating division for the years ended December 31, 2003 and 2002, respectively.

Typically, the Partnership incurs minimal incremental operating or administrative overhead costs when gathering and transporting additional natural gas through its pipeline assets. Therefore, the Partnership recognizes a substantial portion of incremental gathering and transportation revenues as operating income.

Operating expenses are costs directly associated with the operations of a particular asset. Among the most significant of these costs are those associated with direct labor and supervision and associated transportation and communication costs, property insurance, ad valorem taxes, repair and maintenance expenses, measurement and utilities. These costs are normally fairly stable across broad volume ranges, and therefore, do not normally decrease or increase significantly in the short term with decreases or increases in the volume of gas moved through the asset.

We modified certain terms of certain outstanding options in the first quarter of 2003 which allowed the option holders to elect to be paid in cash for the modified options based on the fair value of the options. These modifications resulted in variable award accounting for the modified options until the option holders elect to cash out the options or the election to cash out the options lapses. December 31, 2003 was the last valuation date that a holder of modified options could elect the cash-out alternative. Accordingly, effective January 1, 2004, the remaining modified options will be accounted for as fixed options. We recognized total compensation expense of approximately $5.0 million related to these modified options in the year ended December 31, 2003.

The Partnership has grown significantly through asset purchases in recent years, which creates many of the major differences when comparing operating results from one period to another. The most significant asset purchases are the acquisitions of the Partnership's CCNG system, Vanderbilt system and DEFS assets.

The Partnership acquired the CCNG system in May 2001 for a purchase price of approximately $30.0 million. The CCNG system included four principal assets: the Corpus Christi system, the Gregory gathering system, the Gregory processing plant and the Rosita treating plant.

- The Corpus Christi system consists of approximately 295 miles of gathering and transmission lines extending from supply points in south Texas to markets in Corpus Christi Texas, with average throughput of approximately 152,000 MMBtu of gas per day at the time of the acquisition.

- The Gregory gathering system consists of approximately 297 miles of gathering lines located primarily in the Corpus Christi Bay area, with average throughput of approximately 76,500 MMBtu of gas per day at the time of the acquisition.

- The Gregory processing plant processes most of the gas gathered by the Gregory gathering system, extracting the liquids, fractionating them into NGLs, and selling the remaining residue gas. At the time of the acquisition, the plant was processing approximately 43,400 MMBtu of gas per day.

- The Rosita treating plant was treating approximately 25,000 MMBtu of gas per day at the time of its acquisition. The Rosita treating plant is operated in the Partnership's Treating Division, whereas all of the other assets in the CCNG acquisition are included in the Partnership's Midstream Division.

The Partnership acquired the Vanderbilt system in December 2002 for a purchase price of $12.0 million. The Vanderbilt system consists of approximately 200 miles of gathering lines in the same approximate geographic area as the Gulf Coast System. At the time of its acquisition, the Vanderbilt system was transporting approximately 32,000 MMBtu of gas per day.

The Partnership acquired the DEFS assets in June 2003 for $68.1 million in cash. The principal assets acquired were the Mississippi pipeline system, a 638-mile natural gas gathering and transmission system in south central Mississippi that serves utility and industrial customers, and a 12.4% non-operating interest in the Seminole gas processing plant, which provides carbon dioxide separation and sulfur removal services for several major oil companies in West Texas. The acquisition provided the Partnership with a new core area for growth in south central Mississippi, expanded its presence in West Texas, increased the total miles of its pipelines from 1,700 to 2,500 and enabled it to enter the business of carbon dioxide separation.

Other Assets. We own two inactive gas plants and a receivable associated with the Enron Corp. bankruptcy in addition to our limited and general partner interests in the Partnership. The Enron receivable is discussed below under "—Results of Operations—Year Ended December 31, 2002 Compared to Year Ended December 31, 2001—Profit (Loss) on Energy Trading Activities." The two gas plants are the Jonesville processing plant, which had been largely inactive since the beginning of 2001, and the Clarkson plant, acquired shortly before the Partnership's initial public offering. Our management has not yet determined whether we will elect to activate or liquidate these plants. The activation or liquidation of one or both of these plants will not have a material impact on our business or results of operations.

Impact of Federal Income Taxes. Crosstex Energy, Inc. is a corporation for federal income tax purposes. As such, our federal taxable income is subject to tax at a maximum rate of 35.0% under current law. We expect to have significant amounts of taxable income allocated to us as a result of our investment in the Partnership units particularly because of remedial allocations that will be made among the unitholders and because of the general partner's incentive distribution rights, which we will benefit from as the sole owner of the general partner. Taxable income allocated to us by the Partnership will increase over the years as the ratio of income to distributions increases for all of the unitholders.

We currently have a net operating loss carryforward. We estimate that we will be able to use our net operating loss carryforward to offset most of the income allocated to us in fiscal 2004 by the Partnership. In future years, however, we do not expect to have this net operating loss carryforward to offset our income. As a result, we will have to pay tax on our federal taxable income at a maximum rate of 35.0% under current law. Thus, the amount of money available to make cash distributions to our stockholders will decrease markedly after we use all of our net operating loss carryforward.

Our use of this net operating loss carryforward will be limited if there is a greater than 50.0% change in our stock ownership over a three year period. However, we do not expect such a change in ownership to occur before we fully utilize our loss carryforward.

Commodity Price Risk

The Partnership's profitability has been and will continue to be affected by volatility in prevailing NGL product and natural gas prices. Changes in the prices of NGL products correlate closely with changes in the price of crude oil. NGL product and natural gas prices have been subject to significant volatility in recent years in response to changes in the supply and demand for NGL products and natural gas market uncertainty.

Profitability under the Partnership's gas processing contracts is impacted by the margin between NGL sales prices and the cost of natural gas and may be negatively affected by decreases in NGL prices or increases in natural gas prices.

Changes in natural gas prices impact the Partnership's profitability since the purchase price of a portion of the gas it buys (approximately 8.4% in 2003) is based on a percentage of a particular natural gas price index for a period, while the gas is resold at a fixed dollar relationship to the same index. Therefore, during periods of low gas prices, these contracts can be less profitable than during periods of higher gas prices. However, on most of the gas the Partnership buys and sells, margins are not affected by such changes because the gas is bought and sold at a fixed relationship to the relevant index. Therefore, while changes in the price of gas can have very large impacts on revenues and cost of revenues, the changes are equal and offsetting.

Set forth in the table below is the volume of the natural gas purchased and sold at a fixed discount or premium to the index price and at a percentage discount or premium to the index price for the Partnership's principal gathering and transmission systems and for its producer services business for the year ended December 31, 2003. The Partnership's gathering and transportation margins related to a percentage of the index price can be adversely affected by declines in the price of natural gas.

	Year ended December 31, 2003			
	Gas Purchased		Gas Sold	
Asset or Business	**Fixed Amount to Index**	**Percentage of Index**	**Fixed Amount to Index**	**Percentage of Index**
	(in billions of MMBtus)			
Gulf Coast system	28.5	2.5	31.1	—
CCNG transmission system	59.5	0.7	60.2	—
Gregory gathering system(1)	52.5	2.5	45.8	—
Vanderbilt system(1)	10.2	12.4	20.0	—
Conroe system(1)	0.1	0.3	0.3	
Arkoma gathering system	0.3	4.4	4.7	—
Mississippi system	13.5	0.5	14.0	
Producer services(2)	94.2	0.4	94.6	—

(1) Gas sold is less than gas purchased due to production of natural gas liquids.

(2) These volumes are not reflected in revenues or purchased gas cost, but are presented net as a component of profit (loss) on energy trading activities.

The Partnership estimates that, due to the gas that it purchases at a percentage of index price, for each $0.50 per MMBtu increase or decrease in the price of natural gas, its gross margins increase or decrease by approximately $0.7 million on an annual basis (before consideration of the hedges discussed below). As of December 31, 2003, the Partnership has hedged a portion of its exposure to such fluctuations in natural gas prices as follows for future periods:

Period	Volume Hedged (MMBtu per month)	Weighted-Average Price per MMBtu
1st quarter of 2004	90,000	5.11
2nd quarter of 2004	70,000	4.97
3rd quarter of 2004	30,000	4.85
4th quarter of 2004	30,000	4.85

The Partnership expects to continue to hedge its exposure to gas production which it purchases at a percentage of index when market opportunities appear attractive.

In addition to the margins generated by the Gregory gathering system, the Partnership generates revenues at its Gregory processing plant under two types of arrangements:

- For the year ended December 31, 2003, the Partnership purchased approximately 16% the natural gas volumes on its Gregory system under contracts in which it was exposed to the risk of loss or gain in processing the natural gas. Under these contracts, the Partnership fractionates the NGLs into separate NGL products, which it then sells at prices based upon the market price for NGL products. All of the processed natural gas, up to 100,000 MMcf/d, is delivered to two customers at a price based on a fixed price relative to a monthly index. Since the Partnership extracts Btu's from the gas stream in the form of the liquids or consume it as fuel during processing, it reduces the Btu content of the natural gas but seeks to more than offset this by creating value from the separated NGL products. Accordingly, the Partnership's margins under these arrangements can be negatively affected in periods where the value of natural gas is high relative to the value of NGLs.

- For the year ended December 31, 2003, the Partnership purchased approximately 84% of the natural gas volumes on its Gregory system at a spot or market price less a discount that includes a fixed margin for gathering, processing and marketing the natural gas and NGLs at its Gregory processing plant with no risk of loss or gain in processing the natural gas. Under these contracts, the producer retains ownership of the fractionated NGLs, and accordingly bears the risk and retains the benefits associated with processing the natural gas. The Partnership anticipates purchasing increasing percentages of gas under fixed fee arrangements as opposed to contracts under which the processing economics are for its account.

The Partnership's Conroe gas plant and gathering system generates revenues based on fees it charges to producers for gathering and compression services, and it retains 40% of the NGLs produced from a portion of the gas processed at the facility.

The Partnership owns an undivided 12.4% interest in the Seminole gas processing plant, which is located in Gaines County, Texas. The Seminole plant has dedicated long-term reserves from the Seminole San Andres unit, to which it also supplies carbon dioxide under a long-term arrangement. Revenues at the plant are derived from a fee it charges producers, including those at the Seminole San Andres unit, for each Mcf of carbon dioxide returned to the producer for reinjection. The fees currently average approximately $0.59 for each Mcf of carbon dioxide returned. Reinjected carbon dioxide is used in a tertiary oil recovery process in the field. The plant also receives 50% of the NGLs produced by the plant. Therefore, the Partnership has commodity price exposure due to variances in the prices of NGLs. In the last half of 2003, the Partnership's share of NGLs totaled 2,824,000 gallons at an average price of $0.5154 per gallon. The Partnership has entered into a one-year contract with Duke Energy NGL Services, L.P. to market the Partnership's NGLs on its behalf, and to receive its share of proceeds from the sale of carbon dioxide from the plant operator. The Partnership is separately billed by the plant operator for its share of expenses.

Gas prices can also affect the Partnership's profitability indirectly by influencing drilling activity and related opportunities for gas gathering, treating and processing.

Results of Operations

Set forth in the table below is certain financial and operating data for the Midstream and Treating divisions for the periods indicated.

	Year Ended December 31,		
	2003	2002	2001
		(in millions)	
Midstream revenues	$ 993.1	$ 437.7	$ 362.7
Midstream purchased gas	946.4	414.0	344.8
Midstream gross margin	46.7	23.7	17.9
Treating revenues	20.5	14.8	24.4
Treating purchased gas	7.5	5.8	18.1
Treating gross margin	13.0	9.0	6.3
Total gross margin	$ 59.7	$ 32.7	$ 24.2
Midstream Volumes (MMBtu/d):			
Gathering and transportation	626,000	392,000	313,000
Processing	132,000	86,000	61,000
Producer services	259,000	230,000	283,000
Treating Volumes (MMBtu/d)	90,000	98,000	63,000

Year Ended December 31, 2003 Compared to Year Ended December 31, 2002

Gross Margin. Midstream gross margin was $46.7 million for the year ended December 31, 2003 compared to $23.7 million for the year ended December 31, 2002, an increase of $23.0 million, or 97%. The largest increase in gross margin was due to the acquisition of assets from Duke Energy Field Services on June 30, 2003. These assets added gross margin of $9.4 million. The CCNG system had significant growth due to an increase in on-system volume and the addition of the Hallmark lateral, resulting in an increase in margin of $4.7 million. The Partnership acquired the Vanderbilt Gathering system on December 31, 2002; this system added gross margin of $4.4 million. Gregory gathering system and Gregory processing plant had increased margin of $2.6 million. These systems had significant growth in volume due to producer drilling activity in the area, to which the Partnership responded with the Gregory plant expansion during 2003. The Gulf Coast system had increased margin of $1.2 million despite the fact that volumes declined. The reason for the decline in volumes was because the Partnership sourced two markets from Vanderbilt the last half of 2003 that were previously sourced from the Gulf Coast system. The Partnership had an increase in volume and increase in margin due to a large customer taking gas from its system for 12 months in 2003 and only 6 months in 2002, and it had increased margin due to renegotiation of producer contracts. The Arkoma system also had increased volume, creating an increase in margin of $0.8 million.

Treating gross margin was $13.0 million for the year ended December 31, 2003 compared to $9.0 million in the same period in 2002, an increase of $4.0 million, or 44%. The increase was due to 27 new plants placed in service in 2003, which generated $3.7 million offset by 10 plants removed from service in 2003, which decreased margin by $0.8 million (a net increase of $2.9 million). In addition, an increase in volume at two plants with throughput-based contracts accounted for $1.1 million of the increase in treating margin.

Operating Expenses. Operating expenses were $17.8 million for the year ended December 31, 2003, compared to $11.4 million for the year ended December 31, 2002, an increase of $6.4 million, or 55%. An increase of $3.1 million was associated with the acquisition of assets from Duke Energy Field Services in June 2003. Costs for the Partnership's technical services support increased by approximately $0.8 million due to staff additions to operate the assets acquired in December 2002 and in June 2003 from DEFS and to manage other construction projects. The Vanderbilt system added $1.1 million to operating expenses, new treating plants increased operating expenses by $0.6 million and the Gregory Plant expansion added $0.4 million in operating expenses.

General and Administrative Expenses. General and administrative expenses were $11.6 million for the year ended December 31, 2003 compared to $7.5 million for the year ended December 31, 2002, an increase of $3.9 million, or 51%. The increase was primarily due to increases in staffing associated with the requirements of the Duke Energy Field Services acquisition and associated with the Partnership being a public entity in 2003. We also recognized an additional bad debt reserve of $1.2 million related to the Company's Enron receivable based on current recovery estimates from Enron's bankruptcy proceedings.

Impairments. The Partnership had no impairment expense in 2003 compared to $4.2 million in 2002. See "Year Ended December 31, 2002 Compared to Year Ended December 31, 2001" for a discussion of the 2002 charge.

(Profit) Loss on Energy Trading Activities. The profit on energy trading activities was $1.9 million for the year ended December 31, 2003 compared to $2.7 million for the year ended December 31, 2002, a decrease of $0.8 million, or 30%. Included in these amounts are realized margins on delivered volumes in the producer services "off-system" gas marketing operations of $2.2 million in 2003 and $1.8 million in 2002, an increase of $0.4 million, or 22%. This increase is primarily due to an increase in our producer services volumes. In addition, losses of $0.3 million and gains of $0.9 million relating primarily to options bought and/or sold in the management of the company's Enron position were booked in 2003 and 2002, respectively.

Depreciation and Amortization. Depreciation and amortization expenses were $13.5 million for the year ended December 31, 2003 compared to $7.7 million for the year ended December 31, 2002, an increase of $5.8 million, or 75%. The increase related to the Duke assets purchased in June 2003 was $2.3 million. The Vanderbilt system, purchased in December 2002 added $1.0 million of depreciation, new treating plants placed in service in 2003 resulted in an increase of $0.9 million and the Hallmark system added $0.3 million. The remaining $1.3 million increase in depreciation and amortization is a result of expansion projects and other new assets, such as the expansion of the Gregory Plant.

Interest Expense. Interest expense was $3.1 million for the year ended December 31, 2003 compared to $2.4 million for the year ended December 31, 2002, an increase of $0.7 million, or 29%. The increase relates primarily to bank debt incurred in the acquisition of the Duke assets in June, 2003 and by higher interest rates (weighted average rate of 5.35% in 2003 compared to 4.67% in 2002).

Income Tax Expense. We provide for income taxes using the liability method. Accordingly, deferred taxes are recorded for the differences between the tax and book basis of assets and liabilities that will reverse in future periods. Our income tax provision was $10.2 million in 2003 compared to $7.5 million in 2002, an increase of approximately $2.7 million. This increase was primarily due to the increase in the gain on issuance of units of the Partnership and the increase in operating income. We estimate that we will not have a current tax liability in 2003 due to the availability of our net operating loss carryforward. This tax provision is reflected as an increase in our deferred tax liability.

Interest of Non-controlling Partners in the Partnership's Net Income. We recorded an expense of $5.2 million in 2003 and $99,000 in 2002 associated with the interests of non-controlling partners' in the Partnership. We owned all of the interests in the Partnership and its predecessors until its December 2002 initial public offering.

Net Income (Loss). Net income for the year ended December 31, 2003 was $13.4 million compared to $5.6 million for the year ended December 31, 2002, an increase of $7.8 million. This increase in net income was principally the result of the increase of $7.3 million in gains on issuance of units in the Partnership and the increase in gross margin of $26.9 million from 2002 to 2003, offset by increases in ongoing cash costs for operating expenses, general and administrative expenses, interest expense and income taxes as discussed above. Non-cash charges for depreciation and amortization expenses and stock based compensation also increased.

Year Ended December 31, 2002 Compared to Year Ended December 31, 2001

Gross Margin. Midstream gross margin was $23.7 million for the year ended December 31, 2002 compared to $17.9 million for the year ended December 31, 2001, an increase of $5.8 million, or 32%. The Corpus Christi system, the Gregory gathering system and the Gregory processing plant were acquired in May 2001. The gross margin from these assets for the 12-month period of 2002 exceeded that of the 8-month period in 2001 by $6.9 million. This was offset by lower margin of $0.8 million at the Arkoma system and $0.4 million at the Gulf Coast system due to lower prices in 2002.

Treating gross margin was $9.0 million for the year ended December 31, 2002 compared to $6.3 million for the same period in 2001, an increase of $2.7 million, or 43%. The increase was primarily due to 14 new plants placed in service in 2002, which generated $1.6 million. In addition, margin of $1.0 million was generated at two plants due to increased volume and additional margin of $0.9 million from six plants in service the entire year 2002, but were in operation only a few months in 2001. This was offset by $0.3 million decrease in margin from four plants being removed from service and another $0.3 million from contract restructuring at one treating facility.

Operating Expenses. Operating expenses were $11.4 million for the year ended December 31, 2002, compared to $7.8 million for the year ended December 31, 2001, an increase of $3.0 million, or 47%. $1.8 million of the increase was associated with the CCNG assets purchased in May 2001 and another $1.0 million was associated with growth in the treating division.

General and Administrative Expenses. General and administrative expenses were $7.7 million for the year ended December 31, 2002 compared to $5.6 million for the year ended December 31, 2001, an increase of $2.1 million, or 37%. The increases were associated with increases in staffing associated with the requirements of the CCNG assets and in preparation for the Partnership's initial public offering.

Impairments. Impairment expense was $4.2 million in 2002 compared to $2.9 million in 2001. Intangible assets were booked associated with the contract values of certain treating plants and other assets in conjunction with the Yorktown investment in May 2000. Impairment charges in 2002 and 2001 are associated with writing off certain of these intangible contract values. The charges in 2001 relate to intangible contract values associated with the Jonesville processing plant, which was transferred out of the partnership in conjunction with the initial public offering. Impairment charges in 2002 are primarily associated with intangible contract values at 4 specific treating plants. Two of the plants are still working at the location where they were sited at the time of the Yorktown investment, but had experienced declines in cash flows. As the operator of the wells behind these plants had recently told the company that it was canceling its drilling plans in the area, the declines were expected to continue until the plants was relocated. The other two treating plants were removed from service during 2002 at the locations where they were sited at the time of the Yorktown investment, and therefore the intangible contract values associated with that particular location were deemed impaired. (One of the plants was immediately contracted at another location at a higher rental rate than previously in effect. The other plant is currently in inventory.)

(Profit) Loss on Energy Trading Activities. The profit on energy trading activities was $2.7 million for the year ended December 31, 2002 compared to a loss of $3.7 million for the year ended December 31, 2001, an increase of $6.4 million. Included in these amounts are realized margins on delivered volumes in the producer services "off-system" gas marketing operations of $1.8 million in 2002 and $1.9 million in 2001. In addition, gains of $0.9 million relating primarily to options bought and/or sold in the management of the company's Enron position were booked in 2002. Offsetting the gains from the producer services off-system gas marketing operations in 2001 was the $5.7 million reserve booked against the company's Enron receivable due to Enron Corporation's December 2001 bankruptcy.

Depreciation and Amortization. Depreciation and amortization expenses were $7.7 million for the year ended December 31, 2002 compared to $6.2 million for the year ended December 31, 2001, an increase of $1.5 million, or 25%. The increase is primarily related to additional depreciation expense associated with the CCNG assets purchased in May 2001, partially offset by a decrease in amortization expense due to goodwill no longer being amortized in 2002 in accordance with SFAS 142.

Interest Expense. Interest expense was $2.4 million for the year ended December 31, 2002 compared to $2.3 million for the year ended December 31, 2001, an increase of $0.1 million, or 6%. The increase relates primarily to bank debt incurred in the acquisitions of the CCNG assets in May 2001, offset by lower interest rates.

Gain on issuance of units in the Partnership. In conjunction with the Partnership's December 2002 initial public offering of common units, we conveyed to the Partnership our entire interest in the Partnership's predecessor in exchange for (1) a 2.0% general partner interest in the Partnership, (2) 333,000 common units and (3) 4,667,000 subordinated units of the Partnership. As a result of the Partnership issuing additional units to the public in its initial public offering at a price per unit greater than our equivalent carrying value, our share of the net assets of the Partnership increased by $11.1 million. Accordingly, we recognized an $11.1 million gain in 2002.

Income Taxes. Our income tax expense was $7.5 million for the year ended December 31, 2002, primarily due to the gain on the issuance of units in the Partnership, compared to a tax benefit of $1.3 million for the year ended December 31, 2001. As a result of the remedial allocations of Partnership deductions that will be made in favor of the holders who purchased their units on the open market, we will be allocated more taxable income relative to our distributions than other unitholders. The remedial income allocations will result in an additional current income tax provision for the year in which the allocations are made, but should correspondingly reduce the differences between the tax and book basis of the assets with respect to which remedial allocations are made, thereby reducing our deferred tax liability. At December 31, 2002, the difference in our book and tax basis in our Partnership units was less than our share of the difference in the book and tax basis of the Partnership's assets, after considering the remedial allocations. The resulting deferred tax asset of $2.6 million can only be realized upon liquidation of the Partnership and only to the extent of capital gains. Accordingly, we have fully reserved this deferred tax asset at December 31, 2002. The amount of the deferred tax asset will change in the future when the Partnership sells additional units. The amount of future changes is dependent on the amounts of future remedial allocations and gains or losses recorded by us on the Partnership's sale of additional units.

At December 31, 2002, we had a net operating loss carry-forward of approximately $9.2 million. This carry-forward can be utilized to offset future taxable income and does not expire until 2022.

Interest of Non-controlling Partners in the Partnership's Net Income. We recorded an expense of $0.1 million during the year ended December 31, 2002 associated with the interests of non-controlling partners' in the Partnership.

Net Income (Loss). Our net income (loss) for the year ended December 31, 2002 was $5.6 million compared to ($2.7) million for the year ended December 31, 2001, an increase of $8.3 million. Gross margin increased by $8.6 million from 2001 to 2002, offset by increases in ongoing cash costs for operating expenses, general and administrative expenses, and interest expense as discussed above. The gain on issuance of units in the Partnership of $11.1 million and the profit on energy trading contracts also contributed to the increase in net income partially offset by increases in non-cash charges for depreciation and amortization expense, impairment expense and tax expense.

Critical Accounting Policies and Estimates

The selection and application of accounting policies is an important process that has developed as our business activities have evolved and as the accounting rules have developed. Accounting rules generally do not involve a selection among alternatives, but involve an implementation and interpretation of existing rules, and the use of judgment to the specific set of circumstances existing in our business. Compliance with the rules necessarily involves reducing a number of very subjective judgments to a quantifiable accounting entry or valuation. We make every effort to properly comply with all applicable rules on or before their adoption, and we believe the proper implementation and consistent application of the accounting rules is critical. Our critical accounting policies are discussed below. For further details on our accounting policies and a discussion of new accounting pronouncements. See Note 2 of the Notes to Combined Financial Statements.

Revenue Recognition and Commodity Risk Management. We recognize revenue for sales or services at the time the natural gas or natural gas liquids are delivered or at the time the service is performed.

The Partnership engages in price risk management activities in order to minimize the risk from market fluctuations in the price of natural gas and natural gas liquids. The Partnership also manages its price risk related to future physical purchase or sale commitments by entering into either corresponding physical delivery contracts or financial instruments with an objective to balance its future commitments and significantly reduce its risk to the movement in natural gas prices.

Prior to January 1, 2001, we used the deferral method of accounting to account for financial instruments which qualified for hedge accounting, whereby unrealized gains and losses were generally not recognized until the physical delivery required by the contracts was made.

Effective January 1, 2001, we adopted Statement of Financial Accounting Standards No. 133 ("SFAS No. 133"), *Accounting for Derivative Instruments and Hedging Activities*. In accordance with SFAS No. 133, all derivatives and hedging instruments are recognized as assets or liabilities at fair value. If a derivative qualifies for hedge accounting, changes in the fair value can be offset against the change in the fair value of the hedged item through earnings or recognized in other comprehensive income until such time as the hedged item is recognized in earnings.

The Partnership conducts "off-system" gas marketing operations as a service to producers on systems that it does not own. The Partnership refers to these activities as part of producer services. In some cases, the Partnership earns an agency fee from the producer for arranging the marketing of the producer's natural gas. In other cases, the Partnership purchases the natural gas from the producer and enters into a sales contract with another party to sell the natural gas. Where the Partnership takes title to the natural gas, the purchase contract is recorded as cost of gas purchased and the sales contract is recorded as revenue upon delivery.

The Partnership manages its price risk related to future physical purchase or sale commitments for producer services activities by entering into either corresponding physical delivery contracts or financial instruments with an objective to balance its future commitments and significantly reduce its risk to the movement in natural gas prices. However, the Partnership is subject to counterparty risk for both the physical and financial contracts. Prior to October 26, 2002, the Partnership accounted for its producer services natural gas marketing activities as energy trading contracts in accordance with EITF 98-10, *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*. EITF 98-10 required energy-trading contracts to be recorded at fair value with changes in fair value reported in earnings. In October 2002, the EITF reached a consensus to rescind EITF No. 98-10. Accordingly, derivative contracts held for trading purposes entered into subsequent to October 25, 2002, should be accounted for under accrual-basis accounting rather than mark-to-market accounting unless the contracts meet the requirements of a derivative under SFAS No. 133. The Partnership's energy trading contracts qualify as derivatives, and accordingly, it continues to use mark-to-market accounting for both physical and financial contracts of its producer services business. Accordingly, any gain or loss associated with changes in the fair value of derivatives and physical delivery contracts relating to its producer services natural gas marketing activities are recognized in earnings as profit or loss on energy trading contracts immediately and are reflected net in the statements of operations.

For each reporting period, the Partnership records the fair value of open energy trading contracts based on the difference between the quoted market price and the contract price. Accordingly, the change in fair value from the previous period in addition to the realized gains or losses on settled activities are reported as profit or loss on energy trading activities in the statements of operations.

Sales of Securities by Subsidiaries. We recognize gains and losses in the consolidated statements of operations resulting from subsidiary sales of additional equity interest, including the Partnership's limited partnership units, to unrelated parties.

Impairment of Long-Lived Assets. In accordance with Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we evaluate the long-lived assets, including related intangibles, of identifiable business activities for impairment when events or changes in circumstances indicate, in management's judgment, that the carrying value of such assets may not be recoverable. The determination of whether impairment has occurred is based on management's estimate of undiscounted future cash flows attributable to the assets as compared to the carrying value of the assets. If impairment has occurred, the amount of the impairment recognized is determined by estimating the fair value for the assets and recording a provision for loss if the carrying value is greater than fair value.

When determining whether impairment of one of our long-lived assets has occurred, we must estimate the undiscounted cash flows attributable to the asset. Our estimate of cash flows is based on assumptions regarding the purchase and resale margins on natural gas, volume of gas available to the asset, markets available to the asset, operating expenses, and future natural gas prices and NGL product prices. The amount of availability of gas to an asset is sometimes based on assumptions regarding future drilling activity, which may be dependent in part on natural gas prices. Projections of gas volumes and future commodity prices are inherently subjective and contingent upon a number of variable factors, including but not limited to:

- changes in general economic conditions in regions in which the Partnership's markets are located;
- the availability and prices of natural gas supply;
- the Partnership's ability to negotiate favorable sales agreements;
- the risks that natural gas exploration and production activities will not occur or be successful;
- the Partnership's dependence on certain significant customers, producers, and transporters of natural gas; and
- competition from other midstream companies, including major energy producers.

Any significant variance in any of the above assumptions or factors could materially affect our cash flows, which could require us to record an impairment of an asset.

Liquidity and Capital Resources

Cash Flows. Our net cash provided by operating activities was $42.1 million for the year ended December 31, 2003 compared to cash used by operations of $5.1 million for the year ended December 31, 2002. Income before non-cash income and expenses was $27.7 million in 2003 and $14.1 million in 2002. Changes in working capital provided $14.4 million in cash flows from operating activities in 2003 and used $19.1 million in cash flows from operating activities in 2002. Income before non-cash income and expenses increased between years primarily due to asset acquisitions as discussed in "Results of Operations—Year Ended December 31, 2003 compared to year ended December 31, 2002." Changes in working capital provided $14.4 million in cash flows in 2003 primarily due to $3.5 million in prepayments by certain customers in December 2003 combined with $3.8 million due to delays in collecting from a few large customers in December 2002 until January 2003. In addition, property cost accruals increased by approximately $1.5 million due to an increase in capital projects late in 2003 as compared to 2002. The remaining changes in working capital were due to timing of receipts and disbursements in the ordinary course of business.

Our net cash used in investing activities was $110.3 million and $33.2 million for the year ended December 31, 2003 and 2002, respectively. Net cash used in investing activities during 2003 related to the Duke acquisition ($68.1 million) as well as internal growth projects, and during 2002 primarily related to internal growth projects and the acquisitions of the Vanderbilt system ($12.0 million) and the Hallmark Lateral ($2.3 million). The primary internal growth projects referred to during 2003 were the Gregory plant expansion ($7.4 million), improvements to the Vanderbilt system ($4.7 million), and buying, refurbishing and installing treating plants ($9.9 million). The main projects in the 2002 period were the acquisition and connection of the Hallmark system ($4.3 million), the Calpine interconnect ($1.1 million), buying, refurbishing and installing treating plants ($7.3 million), and a line extension at the Gregory plant ($0.9 million).

Our net cash provided by (used in) financing activities was $65.9 million and $41.7 million for the years ended December 31, 2003 and 2002, respectively. Financing activities in 2003 relate principally to the funding of the Duke assets acquisition and internal growth projects discussed above from bank borrowings and proceeds from the sale of common units discussed below. Financing activities during 2002 primarily represented funding or refunding of the partnership's debt and working capital needs through bank borrowings and net proceeds from our initial public offering in December 2002 and partner contributions. Financing activities also included a decrease in drafts payable of $17.1 million for the year ended December 31, 2003 and an increase in drafts payable of $25.6 million for the year ended December 31, 2002. In order to reduce our interest costs, we borrow money to fund outstanding checks as they are presented to the bank. Fluctuations in drafts payable are caused by timing of disbursements, cash receipts and draws on our revolving credit facility.

Off-Balance Sheet Arrangements. We had no off-balance sheet arrangements as of December 31, 2003 and 2002.

September 2003 Sale of Common Units. In September 2003, the Partnership completed a public offering of 1,725,000 common units at a public offering price of $35.97 per common unit. We received net proceeds of approximately $58.0 million, excluding an approximate $1.3 million capital contribution by our general partner. The net proceeds were used to repay borrowings outstanding under the bank credit facility of the Partnership's operating partnership.

Distributions Received from the Partnership. The following table sets forth the distributions we received from the Partnership since its initial public offering in December 2002.

	Cash Distributions to Us				
	IPO to December 31, 2002(1)	**Quarter Ended March 31, 2003**	**Quarter Ended June 30, 2003**	**Quarter Ended September 30, 2003**	**Quarter Ended December 31, 2003**
Crosstex Energy, L.P. distribution per unit	$ 0.076	$ 0.500	$ 0.550	$ 0.700	$ 0.75
Limited Partner Ownership Interest:					
333,000 common units	$ 25,308	$ 166,500	$ 183,150	$ 233,100	$ 249,750
4,667,000 subordinated units	354,692	2,333,500	2,566,850	3,266,900	3,500,250
Total	380,000	2,500,000	2,750,000	3,500,000	3,750,000
General Partner Ownership Interest:					
2.0% general partner interest	11,322	74,490	83,078	136,686	148,719
Incentive distribution rights	0	0	55,824	380,112	518,495
Total	11,322	74,490	138,902	516,798	667,214
Total	$ 391,322	$ 2,574,490	$ 2,888,902	$ 4,016,798	$ 4,417,214

(1) Reflects the pro rata minimum quarterly distribution covering the period from the closing of the Partnership's initial public offering on December 17, 2002 through December 31, 2002. This distribution was paid to us together with the March 31, 2003 distribution.

Capital Requirements. The natural gas gathering, transmission, treating and processing businesses are capital-intensive, requiring significant investment to maintain and upgrade existing operations. The Partnership's capital requirements have consisted primarily of, and we anticipate will continue to be:

- maintenance capital expenditures, which are capital expenditures made to replace partially or fully depreciated assets in order to maintain existing operating capacity of our assets and to extend their useful lives, or other capital expenditures which do not increase the Partnership's cash flows; and
- growth capital expenditures such as those to acquire additional assets to grow its business, to expand and upgrade gathering systems, transmission capacity, processing plants or treating plants, and to construct or acquire new pipelines, processing plants or treating plants.

Given the Partnership's objective of growth through acquisitions, the Partnership anticipates that it will continue to invest significant amounts of capital to grow and acquire assets. The Partnership actively considers a variety of assets for potential acquisitions.

The Partnership believes that cash generated from operations will be sufficient to meet its present quarterly distribution level of $0.75 per quarter and to fund a portion of its anticipated capital expenditures through December 31, 2004. The Partnership expects to fund the remaining capital expenditures from the proceeds of borrowings under the revolving credit facility discussed below. Total capital expenditures are budgeted to be approximately $17 million in 2004. The Partnership's ability to pay distributions to its unit holders and to fund planned capital expenditures and to make acquisitions will depend upon its future operating performance, which will be affected by prevailing economic conditions in its industry and financial, business and other factors, some of which are beyond its control.

Subsequent Event. The Partnership entered into a definitive agreement on February 13, 2004 for the acquisition of the LIG Pipeline Company and its subsidiaries (LIG) from American Electric Power for $76.2 million. The acquisition will increase the Partnership's pipeline miles by approximately 2,000 miles, to a total of 4,500 pipeline miles, and increase pipeline throughput by approximately 600,000 MMBtu/d. The closing, which is subject to completion of certain conditions, is expected to occur within 90 days of the date of the definitive agreement. The Partnership will finance the acquisition through borrowings under its existing bank credit facility, issuance of additional senior notes or other financing alternatives.

Total Contractual Cash Obligations. A summary of our total contractual cash obligations as of December 31, 2003, is as follows:

	Payments due by period					
Contractual Obligations	**Total**	**2004**	**2005**	**2006**	**2007-2008**	**Thereafter**
	(in millions)					
Long-Term Debt	$ 60.8	$ .1	$ .1	$ 28.8	$ 19.4	$ 12.4
Capital Lease Obligations	—	—	—	—	—	—
Operating Leases	$ 5.6	$ 1.2	$ 1.1	$ 1.0	$ 1.4	$ .9
Unconditional Purchase Obligations	—	—	—	—	—	—
Other Long-Term Obligations	—	—	—	—	—	—
Total Contractual Obligations	$ 66.4	$ 1.3	$ 1.2	$ 29.8	$ 20.8	$ 13.3

The above table does not include any physical or financial contract purchase commitments for natural gas.

Other Obligations. The Partnership receives notices from pipeline companies from time to time of gas volume allocation corrections related to gas deliveries on their pipeline systems. Since the Partnership balances its purchases and sales in the pipelines, these allocation corrections normally have little impact to its gross margin since both the purchase and sale on the pipeline system require corrections. At December 31, 2003, the Partnership had a dispute related to one such allocation correction with a pipeline company and a customer on that pipeline. In reallocating previous settled deliveries, the pipeline company has billed the Partnership for approximately $1.2 million of gas deliveries, which occurred in the period from December 2000 through February 2001. The Partnership has, in turn, billed its customer who was over paid due to the allocation error. The Partnership's customer is disputing the timeliness of this corrected billing. The allocation error occurred prior to the acquisition by the Partnership of the subsidiary involved in the dispute. The Partnership has an indemnity from the seller for liabilities prior to the acquisition date. As of December 31, 2003, the Partnership has recorded a receivable of $1.2 million in other current receivables and a liability of $1.2 million in other current liabilities related to this allocation correction. The Partnership believes the dispute of the receivable by its customer is without merit, and further believe that the Partnership is protected against loss by its potential indemnity claim.

Description of Indebtedness

Bank Credit Facility. In June 2003 the Partnership's operating partnership, Crosstex Energy Services, L.P., entered into a $100 million senior secured credit facility with Union Bank of California, N.A. (as a lender and as administrative agent) and other lenders which was increased to $120 million in October 2003, consisting of the following two facilities:

- a $70.0 million senior secured revolving acquisition facility; and

- a $50.0 million senior secured revolving working capital and letter of credit facility.

The acquisition facility was used for the DEFS acquisition and will be used to finance the acquisition and development of gas gathering, treating and processing facilities, as well as general partnership purposes. At December 31, 2003, $20.0 million was outstanding under the acquisition facility, leaving approximately $50.0 available for future borrowings. The acquisition facility will mature in June 2006, at which time it will terminate and all outstanding amounts shall be due and payable. Amounts borrowed and repaid under the acquisition credit facility may be re-borrowed.

The working capital and letter of credit facility will be used for ongoing working capital needs, letters of credit, distributions to partners and general partnership purposes, including future acquisitions and expansions. At December 31, 2003, the Partnership had $30.3 million of letters of credit issued under the $50 million working capital and letter of credit facility, leaving approximately $19.7 million available for future issuances of letters of credit and/or cash borrowings. The aggregate amount of borrowings under the working capital and letter of credit facility is subject to a borrowing base requirement relating to the amount of the Partnership's cash and eligible receivables (as defined in the credit agreement), and there is a $25.0 million sublimit for cash borrowings. This facility will mature in June 2006, at which time it will terminate and all outstanding amounts shall be due and payable. Amounts borrowed and repaid under the working capital and letter of credit facility may be re-borrowed. The Partnership is required to reduce all working capital borrowings to zero for a period of at least 15 consecutive days once each year.

The obligations under the bank credit facility are secured by first priority liens on all of the Partnership's material pipeline, gas gathering and processing assets, all material working capital assets and a pledge of all of its equity interests in certain of its subsidiaries, and ranks *pari passu* in right of payment with the senior secured notes. The bank credit facility is guaranteed by certain of the Partnership's subsidiaries and by us. The Partnership may prepay all loans under the bank credit facility at any time without premium or penalty (other than customary LIBOR breakage costs), subject to certain notice requirements.

Indebtedness under the acquisition facility and the working capital and letter of credit facility bear interest at the Partnership's operating partnership's option at the administrative agent's reference rate plus 0.25% to 1.50% or LIBOR plus 1.75% to 3.00%. The applicable margin varies quarterly based on the Partnership's leverage ratio. The fees charged for letters of credit range from 1.50% to 2.00% per annum, plus a fronting fee of 0.125% per annum. The operating partnership will incur quarterly commitment fees based on the unused amount of the credit facilities.

The credit agreement prohibits the Partnership from declaring distributions to unitholders if any event of default, as defined in the credit agreement, exists or would result from the declaration of distributions. In addition, the bank credit facility contains various covenants that, among other restrictions, limit the operating partnership's ability to:

- incur indebtedness;

- grant or assume liens;
- make certain investments;
- sell, transfer, assign or convey assets, or engage in certain mergers or acquisitions;
- make distributions;
- change the nature of its business;
- enter into certain commodity contracts;
- make certain amendments to the operating partnership's partnership agreement; and
- engage in transactions with affiliates.

The bank credit facility also contains covenants requiring us to maintain:

- a maximum ratio of total funded debt to consolidated EBITDA (each as defined in the bank credit facility), measured quarterly on a rolling four-quarter basis, of 3.75 to 1 through March 31, 2004, declining to 3.5 to 1 beginning June 30, 2004, pro forma for any asset acquisitions;
- a minimum interest coverage ratio (as defined in the credit agreement), measured quarterly on a rolling four quarter basis, equal to 3.50 to 1;
- minimum current ratio (as defined in the credit agreement), measured quarterly, of 1 to 1; and
- a minimum tangible net worth (as defined in the credit agreement) of $60 million, plus one-half of certain equity contribution proceeds received after December 31, 2002.

Each of the following will be an event of default under the Partnership's bank credit facility:

- failure to pay any principal, interest, fees, expenses or other amounts when due;
- failure to observe any agreement, obligation, or covenant in the credit agreement, subject to cure periods for certain failures;
- certain judgments against the Partnership or any of its subsidiaries, in excess of certain allowances;
- certain ERISA events involving the Partnership or its subsidiaries;
- cross defaults to certain material indebtedness;
- certain bankruptcy or insolvency events involving the Partnership or its subsidiaries;
- a change in control (as defined in the credit agreement); and
- the failure of any representation or warranty to be materially true and correct when made.

Senior Secured Notes. In June 2003, the operating partnership of the Partnership entered into a master shelf agreement with an institutional lender pursuant to which it issued $30.0 million aggregate principal amount of senior secured notes with an interest rate of 6.95% and a maturity of seven years. In July 2003, the operating partnership issued $10.0 million aggregate principal amount of senior secured notes pursuant to the master shelf agreement with an interest rate of 6.88% and a maturity of seven years.

The following is a summary of the material terms of the senior secured notes.

The notes represent senior secured obligations of the operating partnership and will rank at least *pari passu* in right of payment with the bank credit facility. The notes are secured, on an equal and ratable basis with the obligations of the Partnership's operating partnership under the credit facility, by first priority liens on all of its material pipeline, gas gathering and processing assets, all material working capital assets and a pledge of all of its equity interests in certain of its subsidiaries. The senior secured notes are guaranteed by the Partnership, the operating partnership's subsidiaries and us.

The senior secured notes are redeemable, at the operating partnership's option and subject to certain notice requirements, at a purchase price equal to 100% of the principal amount together with accrued interest, plus a make-whole amount determined in accordance with the master shelf agreement.

The master shelf agreement relating to the notes contains substantially the same covenants and events of default as the Partnership's bank credit facility.

If an event of default resulting from bankruptcy or other insolvency events occurs, the senior secured notes will become immediately due and payable. If any other event of default occurs and is continuing, holders of more than 50.1% in principal amount of the outstanding notes may at any time declare all the notes then outstanding to be immediately due and payable. If an event of default relating to nonpayment of principal, make-whole amounts or interest occurs, any holder of outstanding notes affected by such event of default may declare all the notes held by such holder to be immediately due and payable.

The operating partnership was in compliance with all debt covenants at December 31, 2003 and 2002.

Intercreditor and Collateral Agency Agreement. In connection with the execution of the master shelf agreement in June 2003, the lenders under the bank credit facility and the initial purchasers of the senior secured notes entered into an Intercreditor and Collateral Agency Agreement, which was acknowledged and agreed to by the Partnership's operating partnership and its subsidiaries. This agreement appointed Union Bank of California, N.A. to act as collateral agent and authorized Union Bank to execute various security documents on behalf of the lenders under the bank credit facility and the initial purchases of the senior secured notes. This agreement specifies various rights and obligations of lenders under the bank credit facility, holders of senior secured notes and the other parties thereto in respect of the collateral securing Crosstex Energy Services, L.P.'s obligations under the bank credit facility and the master shelf agreement.

Credit Risk and Significant Customers

The Partnership is diligent in attempting to ensure that it issues credit to only credit-worthy customers. However, the Partnership's purchase and resale of gas exposes it to significant credit risk, as the margin on any sale is generally a very small percentage of the total sale price. Therefore, a credit loss can be very large relative to the Partnership's overall profitability.

During the year ended December 31, 2003, the Partnership had one customer that individually accounted for more than 10% of consolidated revenues. During the year ended December 31, 2003, Kinder Morgan Tejas accounted for 20.5% of the Partnership's consolidated revenue. While this customer represents a significant percentage of consolidated revenues, the loss of this customer would not have material impact on the Partnership's results of operations.

Inflation

Inflation in the United States has been relatively low in recent years and did not have a material impact on the Partnership's results of operations for the years ended December 31, 2001, 2002, or 2003. Although the impact of inflation has been insignificant in recent years, it is still a factor in the United States economy and may increase the cost to acquire or replace property, plant and equipment and may increase the costs of labor and supplies. To the extent permitted by competition, regulation and the Partnership's existing agreements, it has and will continue to pass along increased costs to its customers in the form of higher fees.

Environmental

The Partnership's operations are subject to environmental laws and regulations adopted by various governmental authorities in the jurisdictions in which these operations are conducted. The Partnership believes it is in material compliance with all applicable laws and regulations. For a more complete discussion of the environmental laws and regulations that impact the Partnership. See Item 1. "Business—Environmental Matters."

Recent Accounting Pronouncements

In June 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. This statement establishes standards for accounting for obligations associated with the retirement of tangible long-lived assets. This standard was adopted by us on January 1, 2003. We do not presently have any significant legal asset retirement obligations, and accordingly, the adoption of SFAS No. 143 had no impact on our results of operations or financial condition.

SFAS No 148, *Accounting for Stock-Based Compensation—Transition and Disclosure, an amendment of FASB Statement No. 123*, SFAS No. 148 amends SFAS No. 123 and provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 also requires prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. SFAS No. 148 permits two additional transition methods for entities that adopt the fair value based method, these methods allow companies to avoid the ramp-up effect arising from prospective application of the fair value based method. This Statement is effective for financial statements for fiscal years ending after December 15, 2002. We have complied with the disclosure provisions of the Statement in our financial statements.

In January 2003, the FASB issued Interpretation (FIN) No. 45, *Guarantor's Accounting and Disclosure Requirement for Guarantees, including Indirect Guarantees of Indebtedness of Others*. FIN No. 45 requires an entity to recognize a liability for the obligations it has undertaken in issuing a guarantee. This liability would be recorded at the inception of a guarantee and would be measured at fair value. Certain guarantees are excluded from the measurement and disclosure provisions while certain other guarantees are excluded from the measurement provisions of the interpretation. The measurement provisions of this statement apply prospectively to guarantees issued or modified after December 31, 2002. The disclosure provisions of the statement apply to financial statements for periods ended after December 15, 2002. The adoption of this statement had no impact on our results of operations or financial condition.

In January 2003, the FASB issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*, *an interpretation of ARB No 51*. In December 2003, the FASB issued FIN No. 46R which clarified certain issues identified in FIN 46. FIN No. 46R requires an entity to consolidate a variable interest entity if it is designated as the primary beneficiary of that entity even if the entity does not have a majority of voting interests. A variable interest entity is generally defined as an entity where its equity is unable to finance its activities or where the owners of the entity lack the risk and rewards of ownership. The provisions of this statement apply at inception for any entity created after January 31, 2003. For an entity created before February 1, 2003, the provisions of this interpretation must be applied at the beginning of the first interim or annual period beginning after March 15, 2004. We are currently evaluating our ownership interests in joint ventures and limited partnerships that are currently accounted for using the equity method of accounting to determine whether FIN No. 46R will require the consolidation of any of these investments, however, we currently believe that one of the Partnership's joint venture interests, as described in Note 5 to the financial statements, will be consolidated in our financial statements when FIN No. 46R is adopted in March 2004.

The FASB issued Statement of Financial Accounting Standards No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity," ("SFAS No. 150") in May 2003. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. We have no financial instruments which are subject to SFAS No. 150.

Disclosure Regarding Forward-Looking Statements

This report on Form 10-K includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 31E of the Securities Exchange Act of 1934, as amended. Statements included in this report which are not historical facts (including any statements concerning plans and objectives of management for future operations or economic performance, or assumptions or forecasts related thereto), including, without limitation, the information set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations," are forward-looking statements. These statements can be identified by the use of forward-looking terminology including "forecast," "may," "believe," "will," "expect," "anticipate," "estimate," "continue" or other similar words. These statements discuss future expectations, contain projections of results of operations or of financial condition or state other "forward-looking" information. In addition to specific uncertainties discussed elsewhere in this Form 10-K, the following risks and uncertainties may affect our performance and results of operations:

- our only cash-generating assets are our partnership interests in the Partnership, and our cash flow is therefore completely dependent upon the ability of the Partnership to make distributions to its partners;

- the value of our investment in the Partnership depends largely on the Partnership's being treated as a partnership for federal income tax purposes;

- the amount of cash distributions from the Partnership that we will be able to distribute to you will be reduced by our expenses, including federal corporate income taxes and the costs of being a public company, and reserves for future dividends;

- so long as we own the general partner of the Partnership, we are prohibited by an omnibus agreement with the Partnership from engaging in the business of gathering, transmitting, treating, processing, storing and marketing natural gas and transporting, fractionating, storing and marketing NGLs, except to the extent that the Partnership, with the concurrence of its independent directors comprising its conflicts committee, elects not to engage in a particular acquisition or expansion opportunity;

- in our corporate charter, we have renounced business opportunities that may be pursued by the Partnership or by affiliated stockholders that hold a majority of our common stock;

- substantially all of our partnership interest in the Partnership are subordinated to the common units, and during the subordination period, our subordinated units will not receive any distributions in a quarter until the Partnership has paid the minimum quarterly distribution of $0.50 per unit, plus any arrearages in the payment of the minimum quarterly distribution from prior quarters, on all of the outstanding common units;

- the Partnership may not have sufficient cash after the establishment of cash reserves and payment of its general partner's fees and expenses to pay the minimum quarterly distribution each quarter;

- if the Partnership is unable to contract for new natural gas supplies, it will be unable to maintain or increase the throughput levels in its natural gas gathering systems and asset utilization rates at its treating and processing plants to offset the natural decline in reserves;

- the Partnership's profitability is dependent upon the prices and market demand for natural gas and NGLs, which are beyond its control and have been volatile;

- the Partnership's future success will depend in part on its ability to make acquisitions of assets and businesses at attractive prices and to integrate and operate the acquired business profitably;

- since the Partnership is not the operator of certain of our assets, the success of the activities conducted at such assets are outside its control;

- the Partnership operates in very competitive markets and encounters significant competition for natural gas supplies and markets;

- the Partnership is subject to risk of loss resulting from nonpayment or nonperformance by its customers or counterparties;

- the Partnership may not be able to retain existing customers, especially key customers, or acquire new customers at rates sufficient to maintain its current revenues and cash flows;
- the construction of gathering, processing and treating facilities requires the expenditure of significant amounts of capital and subjects the Partnership to construction risks and risks that natural gas supplies will not be available upon completion of the facilities;
- the Partnership's business is subject to many hazards and operational risks, some of which may not be covered by insurance; and
- the Partnership is subject to extensive and changing federal, state and local laws and regulations designed to protect the environment, and these laws and regulations could impose liability for remediation costs and civil or criminal penalties for non-compliance.

Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may differ materially from those in the forward-looking statements. We disclaim any intention or obligation to update or review any forward-looking statements or information, whether as a result of new information, future events or otherwise.

Except as required by applicable securities laws, we do not intend to update these forward-looking statements and information.

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

Market risk is the risk of loss arising from adverse changes in market rates and prices. The Partnership faces market risk from commodity price variations, primarily due to fluctuations in the price of a portion of the natural gas it sells; and for the portion of the natural gas it processes and for which it has taken the processing risk, it is at risk for the difference in the value of the NGL products it produces versus the value of the gas used in fuel and shrinkage in their production. The Partnership also incurs credit risks and risks related to interest rate variations.

Commodity Price Risk. Approximately 8.4% of the natural gas the Partnership markets is purchased at a percentage of the relevant natural gas index price, as opposed to a fixed discount to that price. As a result of purchasing the gas at a percentage of the index price, the Partnership's resell margins are higher during periods of higher natural gas prices and lower during periods of lower natural gas prices. In addition, of the gas the Partnership processes at its Gregory Processing Plant, the Partnership was exposed to the processing risk on 16% of the gas it purchased during the year ended December 31, 2003. The Partnership's processing margins on this portion of the gas will be higher during periods when the price of gas is low relative to the value of the liquids produced and its margins will be lower during periods when the value of gas is high relative to the value of liquids. For the year ended December 31, 2003, a $0.01 per gallon change in NGL prices offset by a change of $0.10 per MMBtu in the price of natural gas would have changed the Partnership's processing margin by $170,000. Changes in natural gas prices indirectly may impact the Partnership's profitability since prices can influence drilling activity and well operations and thus the volume of gas it can gather, transport, process and treat.

The Partnership's primary commodity risk management objective is to reduce volatility in its cash flows. The Partnership maintains a Risk Management Committee, including members of senior management, which oversees all hedging activity. The Partnership enters into hedges for natural gas using NYMEX futures or over-the-counter derivative financial instruments with only certain well-capitalized counterparties which have been approved by its Risk Management Committee. Hedges to protect the Partnership's processing margins are generally for a more limited time frame than is possible for hedges in natural gas, as the financial markets for NGLs are not as developed as the markets for natural gas. Such hedges generally involve taking a long position with regard to the relevant liquids and a short position in the required volume of natural gas.

The use of financial instruments may expose the Partnership to the risk of financial loss in certain circumstances, including instances when (1) sales volumes are less than expected requiring market purchases to meet commitments, or (2) the Partnership's counterparties fail to purchase the contracted quantities of natural gas or otherwise fail to perform, as happened in the case of the Enron loss discussed above. To the extent that the Partnership engages in hedging activities it may be prevented from realizing the benefits of favorable price changes in the physical market. However, the Partnership is similarly insulated against decreases in such prices.

The Partnership manages its price risk related to future physical purchase or sale commitments for its producer services activities by entering into either corresponding physical delivery contracts or financial instruments with an objective to balance its future commitments and significantly reduce its risk to the movement in natural gas prices. However, the Partnership is subject to counterparty risk for both the physical and financial contracts. The Partnership accounts for certain of our producer services natural gas marketing activities as energy trading contracts or derivatives. These energy-trading contracts are recorded at fair value with changes in fair value reported in earnings. Accordingly, any gain or loss associated with changes in the fair value of derivatives and physical delivery contracts relating to the Partnership's producer services natural gas marketing activities are recognized in earnings as profit or loss on energy trading contracts immediately.

For each reporting period, the Partnership records the fair value of open energy trading contracts based on the difference between the quoted market price and the contract price. Accordingly, the change in fair value from the previous period is reported as profit or loss on energy trading contracts in the statement of operations. In addition, realized gains and losses from settled contracts are also recorded in profit or loss on energy trading contracts.

Set forth below is the summarized notional amount and terms of all instruments held by the Partnership for price risk management purposes at December 31, 2003 (all quantities are expressed in British Thermal Units). The remaining term of the contracts extend no later than December 2004, with no single contract longer than 6 months. The Partnership's counterparties to hedging contracts include Williams Energy Services Company, Sempra Energy Trading Corp., Morgan Stanley Capital Group, BP Corporation, Duke Field Services, and Duke Energy Trading and Marketing. Changes in the fair value of the Partnership's derivatives related to Producer Services gas marketing activities are recorded in earnings. The effective portion of changes in the fair value of cash flow hedges is recorded in accumulated other comprehensive income until the related anticipated future cash flow is recognized in earnings.

December 31, 2003

Transaction type	Total volume	Pricing terms	Remaining term of contracts	Fair value (in thousands)	
Cash Flow Hedge:					
Natural gas swaps Cash flow hedge	(2,630,000)	Fixed prices ranging from $4.01 to $6.545 settling against the various Inside FERC Index prices	January - December 2004	$	(563)
Natural gas swaps Cash flow hedge	8,314,000		January - December 2004		2,391
Total natural gas swaps Cash flow hedge				$	1,828
Producer Services:					
Marketing trading financial swaps	910,000	Fixed prices ranging from $3.14 to $6.24 settling against the various Inside FERC Index prices	January - December 2004	$	284
Marketing trading financial swaps	(723,000)		January - December 2004		(522)
Total marketing trading financial swaps				$	(238)
Physical offset to marketing trading transactions	(910,000)	Fixed prices ranging from $3.59 to $6.155 settling against the various Inside FERC Index prices	January - December 2004	$	(282)
Physical offset to marketing trading transactions	723,000		January - December 2004		494
Total physical offset to marketing trading transactions swaps				$	212

On all transactions where the Partnership is exposed to counterparty risk, the Partnership analyzes the counterparty's financial condition prior to entering into an agreement, establishes limits, and monitors the appropriateness of these limits on an ongoing basis.

Credit Risk. The Partnership is diligent in attempting to ensure that it issues credit to only credit-worthy customers. However, the Partnership's purchases and resales of gas exposes it to significant credit risk, as the margin on any sale is generally a very small percentage of the total sale price. Therefore, a credit loss can be very large relative to the Partnership's overall profitability.

Interest Rate Risk. The Partnership is exposed to changes in interest rates, primarily as a result of its long-term debt with floating interest rates. At December 31, 2003, the Partnership had $20.0 million of indebtedness outstanding under floating rate debt. The Partnership has interest rate swap agreements to adjust the ratio of fixed and floating rates in the debt portfolio, wherein the Partnership has swapped floating rates for fixed rates of 2.29% and the applicable margin through November 1, 2004. The impact of a 100 basis point increase in interest rates on the Partnership's debt level as of December 31, 2003 would result in an increase in interest expense and a decrease in income before taxes of approximately $41,000 per year. This amount has been determined by considering the impact of such hypothetical interest rate increase on the Partnership's non-hedged, floating rate debt outstanding at December 31, 2003.

Item 8. *Financial Statements and Supplementary Data*

The Report of Independent Public Accountants, Consolidated Financial Statements and supplementary financial data required by this Item are set forth on pages F-1 through F-35 and S-1 of this Report and are incorporated herein by reference.

Item 9. *Changes in and Disagreements With Accountants on Accounting and Financial Disclosure*

None.

Item 9A. *Controls And Procedures*

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2003 to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

There has been no change in our internal controls over financial reporting that occurred during the three months ended December 31, 2003 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

PART III

Item 10. *Directors and Executive Officers of the Registrant*

Crosstex Energy, Inc.

The following table shows information for our executive officers and members of our board of directors. Directors are elected for three-year staggered terms. Barry E. Davis and Robert F. Murchison are in the class whose term expires in 2005; Sheldon B. Lubar and Frank M. Burke are in the class whose term expires in 2006; Bryan H. Lawrence is in the class whose term expires in 2007. Executive officers are elected for one year terms.

Name	Age	Position with Us
Barry E. Davis	42	President, Chief Executive Officer and Director
James R. Wales	50	Executive Vice President
A. Chris Aulds	42	Executive Vice President
Jack M. Lafield	53	Executive Vice President
William W. Davis	50	Executive Vice President and Chief Financial Officer
Michael P. Scott	49	Senior Vice President
Frank M. Burke	64	Director
Bryan H. Lawrence	61	Chairman of the Board
Sheldon B. Lubar	74	Director
Robert F. Murchison	50	Director

Barry E. Davis, President, Chief Executive Officer and Director, led the management buyout of the midstream assets of Comstock Natural Gas, Inc. in December 1996, which transaction resulted in our formation. He has also served as President, Chief Executive Officer and Director of Crosstex Energy GP, LLC since July 2002. Mr. Davis was President and Chief Operating Officer of Comstock Natural Gas and founder of Ventana Natural Gas, a gas marketing and pipeline company that was purchased by Comstock Natural Gas. Mr. Davis started Ventana Natural Gas in June 1992. Prior to starting Ventana, he was Vice President of Marketing and Project Development for Endevco, Inc. Before joining Endevco, Mr. Davis was employed by Enserch Exploration in the marketing group. Mr. Davis holds a B.B.A. in Finance from Texas Christian University.

James R. Wales, Executive Vice President, joined us in December 1996. He has also served as Executive Vice President—Southern Division of Crosstex Energy GP, LLC since July 2002. As one of the founders of Sunrise Energy Services, Inc., he helped build Sunrise into a major national independent natural gas marketing company, with sales and service volumes in excess of 600,000 MMBtu/d. Mr. Wales started his career as an engineer with Union Carbide. In 1981, he joined Producers Gas Company, a subsidiary of Lear Petroleum Corp., and served as manager of its Mid-Continent office. In 1986, he joined Sunrise as Executive Vice President of Supply, Marketing and Transportation. From 1993 to 1994, Mr. Wales was the Chief Operating Officer of Triumph Natural Gas, Inc., a private midstream business. Prior to joining Crosstex, Mr. Wales was Vice President for Teco Gas Marketing Company. Mr. Wales holds a B.S. degree in Civil Engineering from the University of Michigan, and a Law degree from South Texas College of Law.

A. Chris Aulds, Executive Vice President, together with Barry E. Davis, participated in the management buyout of Comstock Natural Gas in December 1996, which transaction resulted in our formation. He has also served as Executive Vice President—Northern and Treating Divisions of

Crosstex Energy GP, LLC since July 2002. Mr. Aulds joined Comstock Natural Gas, Inc. in October 1994 as a result of the acquisition by Comstock of the assets and operations of Victoria Gas Corporation. Mr. Aulds joined Victoria in 1990 as Vice President responsible for gas supply, marketing and new business development and was directly involved in the providing of risk management services to gas producers. Prior to joining Victoria, Mr. Aulds was employed by Mobil Oil Corporation as a production engineer before being transferred to Mobil's gas marketing division in 1989. There he assisted in the creation and implementation of Mobil's third-party gas supply business segment. Mr. Aulds holds a B.S. degree in Petroleum Engineering from Texas Tech University.

Jack M. Lafield, Executive Vice President, joined us in August 2000. He joined Crosstex Energy GP, LLC in July 2002 and serves as its Executive Vice President—Corporate Development. For five years prior to joining us, Mr. Lafield was Managing Director of Avia Energy, an energy consulting group, and was involved in all phases of acquiring, building, owning and operating midstream assets and natural gas reserves. He also provided project development and consulting in domestic and international energy projects to major industry and financing organizations, including development, engineering, financing, implementation and operations. Prior to consulting, Mr. Lafield held positions of President and Chief Executive Officer of Triumph Natural Gas, a private midstream business he founded, President and Chief Operating Officer of Nagasco, Inc. (a joint venture with Apache Corporation), President of Producers' Gas Company, and Senior Vice President of Lear Petroleum Corp. Mr. Lafield holds a B.S. degree in Chemical Engineering from Texas A&M University, and is a graduate of the Executive Program at Stanford University.

William W. Davis, Executive Vice President and Chief Financial Officer, joined us in September 2001, and has 25 years of finance and accounting experience. He joined Crosstex Energy GP, LLC in July 2002 and serves as its Executive Vice President and Chief Financial Officer. Prior to joining us, Mr. Davis held various positions with Sunshine Mining and Refining Company from 1983 to September 2001, including Vice President—Financial Analysis from 1983 to 1986, Senior Vice President and Chief Accounting Officer from 1986 to 1991 and Executive Vice President and Chief Financial Officer from 1991 to 2001. In addition, Mr. Davis served as Chief Operating Officer in 2000 and 2001. Mr. Davis graduated magna cum laude from Texas A&M University with a B.B.A. in Accounting and is a Certified Public Accountant. Mr. Davis is not related to Barry E. Davis.

Michael P. Scott, Senior Vice President, joined us in July 2001. He has also served as Senior Vice President—Technical Services of Crosstex Energy GP, LLC since July 2002. Before joining us, Mr. Scott held various positions at Aquila Gas Pipeline Corporation, including Director of Engineering from 1992 to 2001, Director of Operations from 1990 to 1992, and Director of Project Development from 1989 to 1990. Prior to Aquila, Mr. Scott held various project development and engineering positions at Cabot Corporation/Cabot Transmission, Perry Gas Processors and General Electric. Mr. Scott holds a B.S. degree in Mechanical Engineering from Oklahoma State University.

Frank M. Burke joined as a director for us in February 2004 and has served as a director for Crosstex Energy GP, LLC since August 2003. Mr. Burke has served as Chairman, Chief Executive Officer and Managing General Partner of Burke, Mayborn Company Ltd., a private investment company located in Dallas, Texas, since 1984. Prior to that, Mr. Burke was a partner in Peat, Marwick, Mitchell & Co. (now KPMG). He is a member of the National Petroleum Council and also serves as a director of Arch Coal, Inc., Dorchester Minerals, L.P., Kaneb Pipe Line Partners, L.P., Xanser Corporation and Kaneb Services LLC. Mr. Burke received his Bachelor of Business Administration and Master of Business Administration from Texas Tech University and his Juris

Doctor from Southern Methodist University. He is a Certified Public Accountant and member of the State Bar of Texas.

Bryan H. Lawrence, Chairman of the Board, joined in May 2000 and has served as a director for Crosstex Energy GP, LLC since the completion of its initial public offering in December 2002. Mr. Lawrence is a founder and senior manager of Yorktown Partners LLC, the manager of the Yorktown group of investment partnerships, which make investments in companies engaged in the energy industry. The Yorktown partnerships were formerly affiliated with the investment firm of Dillon, Read & Co. Inc., where Mr. Lawrence had been employed since 1966, serving as a Managing Director until the merger of Dillon Read with SBC Warburg in September 1997. Mr. Lawrence also serves as a director of D&K Healthcare Resources, Inc., Hallador Petroleum Company, TransMontaigne Inc., and Vintage Petroleum, Inc. (each a United States publicly traded company) and Cavell Energy Corp. (a Canadian publicly traded company) and certain non-public companies in the energy industry in which Yorktown partnerships hold equity interests including PetroSantander Inc., Savoy Energy, L.P., Athanor B.V., Camden Resources, Inc., ESI Energy Services Inc., Ellora Energy Inc., Dernick Resources Inc. Cinco Natural Resources Corp., Peak Energy Resources, Inc., Approach Resources, Inc., Nytis Exploration Co., and Compass Petroleum Ltd. Mr. Lawrence is a graduate of Hamilton College and also has an M.B.A. from Columbia University.

Sheldon B. Lubar joined us as a director in May 2001 and has served as a director for Crosstex Energy GP, LLC since the completion of its initial public offering in December 2002. Mr. Lubar has been Chairman of the Board of Lubar & Co. Incorporated, a private investment and venture capital firm he founded, since 1977. He was Chairman of the Board of Christiana Companies, Inc., a logistics and manufacturing company, from 1987 until its merger with Weatherford International in 1995. Mr. Lubar has also been a Director of C2, Inc., a logistics and manufacturing company, since 1995, MGIC Investment Corporation, a mortgage insurance company, since 1991, Grant Prideco, Inc., an energy services company, since 2000, and Weatherford International, Inc., an energy services company, since 1995. Mr. Lubar holds a bachelor's degree in Business Administration and a Law degree from the University of Wisconsin—Madison. He was awarded an honorary Doctor of Commercial Science degree from the University of Wisconsin—Milwaukee.

Robert F. Murchison joined us as a director in February 2004 and has served as a director for Crosstex Energy GP, LLC since the completion of its initial public offering in December 2002. Mr. Murchison has been the President of the general partner of Murchison Capital Partners, L.P., a private equity investment partnership since 1992. Prior to founding Murchison Capital Partners, L.P., Mr. Murchison held various positions with Romacorp, Inc., the franchisor and operator of Tony Roma's restaurants, including Chief Executive Officer from 1984 to 1986 and Chairman of the board of directors from 1984 to 1993. He served as a director of Cenergy Corporation, an oil and gas exploration and production company, from 1984 to 1987, Conquest Exploration Company from 1987 to 1991 and has served as a director of TNW Corporation, a short line railroad holding company, since 1981 and Tecon Corporation, a holding company with holdings in real estate development, investor owned water utilities, rail car repair and the fund of funds management business, since 1978. Mr. Murchison holds a bachelor's degree in history from Yale University.

"Independent" Directors

Messrs. Burke, Lubar and Murchison qualify as "independent" in accordance with the published listing requirements of The NASDAQ Stock Market (NASDAQ). The NASDAQ independence definition includes a series of objective tests, such as that the director is not an employee of the company and has not engaged in various types of business dealings with the company. In addition, as further required by the NASDAQ rules, the board of directors has made a subjective determination as to each independent director that no relationships exist which, in the opinion of the board, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.

In addition, the members of our Audit Committee of the board of directors will each qualify as "independent" under standards established by the Securities and Exchange Commission (SEC) for members of audit committees, and the Audit Committee will include at least one member who is determined by the board of directors to meet the qualifications of an "audit committee financial expert" in accordance with SEC rules, including that the person meets the relevant definition of an "independent" director. Because we recently completed our initial public offering, we have one-year from the date of our initial listing on the Nasdaq National Market to have three members on our Audit Committee. We currently have one member, Mr. Burke, on our Audit Committee and he qualifies as "independent." Mr. Burke has been determined to be an audit committee financial expert. Shareholders should understand that this designation is a disclosure requirement of the SEC related to Mr. Burke's experience and understanding with respect to certain accounting and auditing matters. The designation does not impose on Mr. Burke any duties, obligations or liability that are greater than are generally imposed on him as a member of the Audit Committee and board of directors, and his designation as an audit committee financial expert pursuant to this SEC requirement does not affect the duties, obligations or liability of any other member of the Audit Committee or board of directors.

Board Committees

Our board of directors currently has, and appoints the members of, standing Audit and Compensation Committees. Each member of the Audit and Compensation Committees is an independent director in accordance with NASDAQ standards described above. Each of the board committees has a written charter approved by the board. Copies of the charter will be provided to any person, without charge, upon request. Contact Kathie Keller at 214-721-9327 to request a copy of a charter or send your request to Crosstex Energy, Inc., Attn: Kathie Keller, 2501 Cedar Springs, Suite 600, Dallas, Texas 75201.

Our Audit Committee, currently comprised of Mr. Burke, assists the board of directors in its general oversight of our financial reporting, internal controls and audit functions, and is directly responsible for the appointment, retention, compensation and oversight of the work of our independent auditors. Mr. Burke is the Chairman of our Audit Committee. Because we recently completed our initial public offering, we have one-year from the date of our initial listing on the Nasdaq National Market to have three members on our Audit Committee.

Our Compensation Committee, comprised of Messrs. Lubar and Murchison, oversees compensation decisions for our officers as well as the compensation plans described herein.

Code of Ethics

We adopted a Code of Business Conduct and Ethics applicable to all officers, and our independent directors who are not employees, with regard to company-related activities. The Code of Business Conduct and Ethics incorporates guidelines designed to deter wrongdoing and to promote honest and ethical conduct and compliance with applicable laws and regulations. It also incorporates our expectations of our employees that enable us to provide accurate and timely disclosure in our filings with the Securities and Exchange Commission and other public communications. A copy of our Code of Business Conduct and Ethics will be provided to any person, without charge, upon request. Contact Kathie Keller at 214-721-9327 to request a copy of a charter or send your request to Crosstex Energy, Inc., Attn: Kathie Keller, 2501 Cedar Springs, Suite 600, Dallas, Texas 75201. If any substantive amendments are made to the Code of Business Conduct and Ethics or if we grant any waiver, including any implicit waiver, from a provision of the code to any of our executive officers and directors, we will disclose the nature of such amendment or waiver in a report on Form 8-K.

Section 16(a)—Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires our directors and certain officers and any 10% beneficial owners of our common stock to send reports of their beneficial ownership of common stock and changes in beneficial ownership to the Securities and Exchange Commission. We were not a public company in fiscal 2003 and therefore no Section 16(a) filings were required.

Item 11. *Executive Compensation*

The following table sets forth information concerning the compensation by us and the Partnership (and its predecessor) for our chief executive officer and the five other most highly compensated executive officers in 2002 and 2003.

Summary Compensation Table

		Annual Compensation			Long Term Compensation Awards(1)		
Name and Principal Position	**Year**	**Salary ($)**	**Bonus ($)**	**Other Annual Compensation ($)**	**Restricted Unit Awards ($)**	**Units Underlying Options (#)**	**All Other Compensation ($)**
Barry E. Davis	2003	$ 210,000	$ 177,000	—	$ 285,670	—	—
President and Chief Executive Officer	2002	201,500	100,750	—	—	30,000	—
James R. Wales	2003	180,000	108,000	—	181,790	—	—
Executive Vice President—Southern Division	2002	171,064	59,872	—	—	20,000	—
A. Chris Aulds	2003	180,000	108,000	—	181,790	—	—
Executive Vice President-Northern and Treating Divisions	2002	171,064	59,872	—	—	20,000	—
Jack M. Lafield	2003	170,000	108,000	—	181,790	—	—
Executive Vice President—Business Development	2002	160,875	56,306	—	—	17,500	—
William W. Davis	2003	170,000	108,000	—	181,790	—	—
Executive Vice President and Chief Financial Officer	2002	160,875	93,306	—	—	17,500	—
Michael P. Scott	2003	150,000	90,000	—	103,880	—	—
Senior Vice President-Technical Services	2002	134,304	47,007	—	—	12,500	—

(1) Executive officers received equity-based awards received under the Crosstex Energy GP, LLC Long-Term Incentive Plan.

Employment Agreements

The executive officers of Crosstex Energy GP, LLC, including Barry E. Davis, James R. Wales, A. Chris Aulds, Jack M. Lafield, William W. Davis and Michael P. Scott, have entered into employment agreements with Crosstex Energy, L.P. The following is a summary of the material provisions of those employment agreements. All of these employment agreements are substantially similar, with certain exceptions as set forth below.

Each of the employment agreements has an initial term that expires two years from the effective date, but will automatically be extended such that the remaining term of the agreements will not be less than one year. The employment agreements provide for a base annual salary of $218,400, $187,200, $187,200, $176,00, $176,000 and $156,000 for Barry E. Davis, James R. Wales, A. Chris Aulds, Jack M. Lafield, William W. Davis and Michael P. Scott, respectively, for 2004.

Except in the event of Crosstex Energy, L.P.'s becoming bankrupt or ceasing operations, termination for cause or termination by the employee other than for good reason, the employment agreements provide for continued salary payments, bonus and benefits following termination of employment for the remainder of the employment term under the agreement. If a change in control occurs during the term of an employee's employment and either party to the agreement terminates the employee's employment as a result thereof, the employee will be entitled to receive salary payments, bonus and benefits following termination of employment for the remainder of the employment term under the agreement.

The employment agreements also provide for a noncompetition period that will continue until the later of one year after the termination of the employee's employment or the date on which the employee is no longer entitled to receive severance payments under the employment agreement. During the noncompetition period, the employees are generally prohibited from engaging in any business that competes with us or our affiliates in areas in which we conduct business as of the date of termination and from soliciting or inducing any of our employees to terminate their employment with us or accept employment with anyone else or interfere in a similar manner with our business.

Long-Term Incentive Plan

We adopted a long-term incentive plan for our employees, directors and affiliates who perform services for us.

The plan provides for the discretionary grant of incentive stock options, within the meaning of Section 422 of the Internal Revenue Code of 1986, to employees and for the grant of nonqualified stock options, stock appreciation rights, dividend equivalents, restricted stock and other incentive awards to employees, outside directors and consultants. The 2004 plan provides that we cannot issue incentive stock options after ten years from the date of the board's adoption of the plan. The plan was an amendment and restatement of our 2000 Stock Option Plan.

The compensation committee of our board of directors administers the plan. The administrator has the power to determine the terms of the options or other awards granted, including the exercise price of the options or other awards, the number of shares subject to each option or other award (up to 100,000 per year per participant), the exercisability thereof and the form of consideration payable upon exercise. In addition, the administrator has the authority to amend, suspend or terminate the plan, provided that no such action may affect any share of common stock previously issued and sold or any option previously granted under the plan without the consent of the holder.

The exercise price of all incentive stock options granted under the plan must be at least equal to 100% of the fair market value of the common stock on the date of grant. The exercise price of nonqualified stock options and other awards granted under the plan is determined by the administrator, but the exercise price must be at least 50% of the fair market value of the common stock on the date of grant. The term of all options granted under the plan may not exceed ten years.

Each option and other award is exercisable during the lifetime of the optionee only by such optionee. Options granted under the plan must generally be exercised within three months after the end of optionee's status as an employee, director or consultant, or within one year after such optionee's termination by disability or death, respectively, but in no event later than the expiration of the option's term.

The plan provides that in the event of a merger of our company (other than a merger whereby Yorktown Partners LLC or its affiliates cease to own a controlling interest in us) all options and other awards shall, in the discretion of the administrator, be subject to adjustment to reflect any changes in our outstanding common stock. In addition, the plan provides that a "change of control" shall be deemed to have occurred if (i) Yorktown Partners LLC or its affiliates including any funds under its management no longer directly or indirectly owns a controlling interest in us, other than as a result of a firm commitment underwritten public offering, (ii) any sale or other disposition of all or substantially all of our assets to any person, other than our affiliates, or (iii) any merger, reorganization, consolidation or other transaction pursuant to which more than 50% of the combined voting power of the equity interests in us ceases to be owned by persons owning such interests as of the closing of this offering. Immediately prior to a change of control, all awards granted under the plan shall automatically vest and become payable or exercisable, as the case may be, in full. In this regard, all restriction periods shall terminate and all performance criteria, if any, shall be deemed to have been achieved at the maximum level. To the extent that certain awards are not exercised upon a change of control, the administrator may, in its discretion, cancel such award without payment or provide for a replacement award with respect to such property and on such terms as it deems appropriate.

Options granted under our 2000 Stock Option Plan prior to its amendment and restatement provide that if the holder of an option voluntarily terminates his or her employment with us due to the occurrence of a "change of control," such holder will be entitled to exercise the portion of the option that would have vested through the date of such voluntary termination. Under the 2000 Stock Option Plan, a "change of control" is defined as: (i) a sale of all or substantially all of our assets, (ii) a sale of all or more than 50% of our outstanding equity interests or (iii) any merger, consolidation, or reorganization where we are not the surviving corporation and, after the merger, more than 50% of the combined voting power of the equity interests in us ceases to be owned by persons owning such interests immediately prior to the merger.

Option Grants

There were no stock options granted to the named executive officers in 2003.

Option Exercises and Year-End Option Values

Crosstex Energy, Inc. The following table provides information about the number of shares issued upon option exercises by our named executive officers during 2003, and the value realized by our executive officers. The table also provides information about the number and value of options that were held by our named executive officers at December 31, 2003.

Aggregated Option Exercise in Last Fiscal Year and Fiscal Year End Option Values

Name	Shares Acquired on Exercise	Value Realized	Number of Securities Underlying Unexercised Options at December 31, 2003(1)		Value of Unexercised In-the-Money Options at December 31, 2003(2)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Barry E. Davis	—	—	40,000	—	$ 580,000	—
A. Chris Aulds	—	—	60,000	—	870,000	—
James R. Wales	—	—	85,000	—	1,232,500	—
Jack M. Lafield	—	—	31,003	15,501	449,539	224,769
William W. Davis	—	—	33,333	16,667	450,000	225,000
Michael P. Scott	—	—	26,667	13,333	360,000	180,000

(1) The options expire on May 5, 2005. The options for Messrs. Barry E. Davis, Aulds and Wales have vested. The options for Mr. William W. Davis vest at a rate of one-third per year on each anniversary of October 1, 2001. The options for Mr. Lafield vest at a rate of one-third per year on each anniversary of May 1, 2001. The options for Mr. Scott vest at a rate of one-third per year on each anniversary of July 23, 2001.

(2) Based on the $19.50 per share initial public offering price of our common stock on January 13, 2004, less the option exercise price. The option exercise price for Messr.'s Barry E. Davis, Aulds, Wales and Lafield is $5.

Crosstex Energy, L.P. The following table provides information about the number of units issued upon option exercises by Crosstex Energy, L.P.'s named executive officers during 2003, and the value realized by the Partnership's named executive officers. The table also provides information about the number and value of options that were held by the named executive officers at December 31, 2003.

Aggregated Option Exercise in Last Fiscal Year and Fiscal Year End Option Values

Name	Shares Acquired on Exercise (#)	Value Realized ($)	Number of Securities Underlying Unexercised Options at 12/31/03 (#)		Value of Unexercised In-the-Money Options at 12/31/03 ($)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Barry E. Davis	—	—	10,000	20,000	$ 213,000	$ 426,000
James R. Wales	—	—	6,667	13,333	142,000	284,000
A. Chris Aulds	—	—	6,667	13,333	142,000	284,000
Jack M. Lafield	—	—	5,833	11,667	124,250	248,500
William W. Davis	—	—	5,833	11,667	124,250	248,500
Michael P. Scott	—	—	4,167	8,333	88,750	177,500

The closing price for the Crosstex Energy, L.P. common units was $41.30 on December 31, 2003, the last trading day of 2003.

Compensation of Directors

Prior to 2004, our directors generally did not receive compensation for services provided as a director. Beginning in 2004, each non-employee director will be paid an annual retainer fee of $25,000. Directors may elect to receive their annual retainer in cash or in shares of restricted stock or options to purchase shares of common stock. If a director elects to receive shares of restricted stock, each share will be valued at the average of the closing prices of our common stock in the first quarter of 2004. If a director elects to receive options, the director will receive options to acquire 2.5 times the number of restricted shares that the director would have been eligible to receive at an exercise price equal to the average closing price of the stock in the first quarter of 2004. Directors will not receive an attendance fee for each board meeting, but an attendance fee of $1,000 will be paid to each director for each committee meeting he attends, except the audit committee members who will receive $1,250 for each audit committee meeting; provided that with respect to directors who are members of the same committees for both our board directors and the board of directors of Crosstex Energy GP, LLC, such director will receive 150% of the normal meeting fee for meetings for both companies' committees that occur on the same date and the cost will be split evenly between both companies. Each committee chairman will receive $2,500 annually except for the audit committee chairman who will receive $3,500 annually; provided that with respect to directors who are the chair of the same committees for both our board of directors and the board of directors of Crosstex Energy GP, LLC, such director will receive 150% of the chairman's annual fee and the cost will be split evenly between both companies. Each of our independent directors received a one-time grant of options to acquire 10,000 shares of common stock at an exercise price of $19.50. Further, we have entered into indemnity agreements with each of our directors.

Compensation Committee Interlocks And Insider Participation

The Compensation Committee of our board of directors determines compensation of the executive officers. Sheldon B. Lubar and Robert F. Murchison have served as members of the Compensation Committee of our board of directors since the completion of our initial public offering.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

The following table shows the beneficial ownership of our common stock as of February 28, 2004, held by:

- each person who beneficially owns 5% or more of the shares of common stock then outstanding;
- each of our directors;
- each of our executive officers; and

- all of our directors and executive officers as a group.

Name of Beneficial Owner(1)	Shares of Common Stock Beneficially Owned	Percent
Yorktown Energy Partners IV, L.P.(2)	5,817,748	48.16%
Yorktown Energy Partners V, L.P.(2)	1,457,000	12.06%
Lubar Nominees(3)	697,498	5.77%
Barry E. Davis(4)	643,916	5.31%
James R. Wales(4)	306,762	2.52%
A. Chris Aulds(4)	383,268	3.16%
Jack M. Lafield(4)	59,305	*
William W. Davis(4)	58,269	*
Michael P. Scott(4)	48,917	*
Frank M. Burke	10,000	*
C. Roland Haden	—	—
Bryan H. Lawrence(5)	—	—
Sheldon B. Lubar(3)	697,498	5.77%
Stephen A. Wells	—	—
Robert F. Murchison	30,000	*
All directors and executive officers as a group (11 persons)(4)	2,237,895	18.11%

* Less than 1%.

(1) Unless otherwise indicated, the address of each person listed above is 2501 Cedar Springs, Suite 600, Dallas, Texas 75201.

(2) The address for Yorktown Energy Partners IV, L.P. and Yorktown Energy Partners V, L.P. is 410 Park Avenue, New York, New York 10022.

(3) Sheldon B. Lubar is a general partner of Lubar Nominees, and may be deemed to beneficially own the shares held by Lubar Nominees.

(4) Ownership percentage for such individual or group includes shares issuable pursuant to stock options which are presently exercisable or exercisable within 60 days including 40,000 shares for Mr. Barry E. Davis, 85,000 shares for Mr. Wales, 60,000 shares for Mr. Aulds, 31,003 shares for Mr. Lafield, 33,333 shares for Mr. William W. Davis, 26,667 shares for Mr. Scott and 276,003 shares for all directors and executive officers as a group.

(5) Bryan H. Lawrence is a member and a manager of the general partner of both Yorktown Energy Partners IV, L.P. and Yorktown Energy Partners V, L.P.

Equity Compensation Plan Information

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants, And Rights (1)	Weighted-Average Price Of Outstanding Options, Warrants And Rights (2)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected In Column (1))
Equity Compensation Plans Approved By Security Holders(3)	1,200,000(1)	$ 5.42(2)	337,610(3)
Equity Compensation Plans Not Approved By Security Holders	N/A	N/A	N/A

(1)
We adopted and maintain a Long Term Incentive Plan for our officers, employees and directors. See Item 11. "Executive Compensation—Long-Term Incentive Plan."

(2)
The exercise prices for outstanding stock options under the plan as of December 31, 2003 range from $5.00 to $7.00.

(3)
Our Long Term Incentive Plan for our officers, employees and directors was approved by our security holders prior to our initial public offering.

Item 13. *Certain Relationships and Related Transactions*

Relationship with Crosstex Energy, L.P.

General. We indirectly own 333,000 common units and 4,667,000 subordinated units representing an aggregate 54.3% limited partnership interest in the Partnership. The Partnership's general partner owns a 2% general partner interest in the Partnership and the incentive distribution rights. The general partner's ability, as general partner, to manage and operate Crosstex Energy, L.P. and our ownership of an aggregate 54.3% limited partner interest in the Partnership effectively gives the general partner the ability to veto some of the Partnership's actions and to control the Partnership's management.

Omnibus Agreement. Concurrent with the closing of the Partnership's initial public offering, we entered into an agreement with the Partnership, Crosstex Energy GP, LLC and the general partner which governs potential competition among us and the other parties to the agreement. We agreed, and caused our controlled affiliates to agree, for so long as management, Yorktown Energy Partners IV, L.P. and Yorktown Energy Partners V, L.P. and its affiliates, or any combination thereof, control the Partnership's general partner, not to engage in the business of gathering, transmitting, treating, processing, storing and marketing of natural gas and the transportation, fractionation, storing and marketing of NGLs unless it first offers the Partnership the opportunity to engage in this activity or acquire this business, and the board of directors of Crosstex Energy GP, LLC, with the concurrence of its conflicts committee, elects to cause the Partnership not to pursue such opportunity or acquisition. In addition, we have the ability to purchase a business that has a competing natural gas gathering, transmitting, treating, processing and producer services business if the competing business does not represent the majority in value of the business to be acquired and we offer the Partnership the opportunity to purchase the competing operations following their acquisition. The noncompetition restrictions in the omnibus agreement do not apply to the assets retained and business conducted by us at the closing of the Partnership's initial public offering. Except as provided above, our controlled affiliates are not prohibited from engaging in activities in which they compete directly with the Partnership. In addition, Yorktown Energy Partners IV, L.P., Yorktown Energy Partners V, L.P. and any affiliated Yorktown funds are not prohibited from owning or engaging in businesses which compete either with us or the Partnership.

Renunciation of Opportunities

In our restated charter and in accordance with the Delaware law, we have renounced any interest or expectancy we may have in, or being offered an opportunity to participate in, any business opportunities, including any opportunities within those classes of opportunity currently pursued by the Partnership, presented:

- to persons who are officers or directors of the company or who, on October 1, 2003, were, and at the time of presentation are, stockholders of the company (or to persons who are affiliates or associates of such officers, directors or stockholders), if the company is prohibited from participating in such opportunities by the omnibus agreement; or

- to two affiliated stockholders with a controlling interest in our company, Yorktown Energy Partners IV, L.P. and Yorktown Energy Partners V, L.P., or any other investment fund sponsored or managed by Yorktown Partners, LLC, including any fund still to be formed, or to any of our directors who is an affiliate or designate of these entities.

As a result of this renunciation, these officers, directors and stockholders should not be deemed to be breaching any fiduciary duty to us if they or their affiliates or associates pursue opportunities presented as described above.

Crosstex Energy, LP.'s General Partner

The Partnership's general partner does not receive any management fee or other compensation in connection with its management of the Partnership's business, but it is reimbursed for all direct and indirect expenses incurred on its behalf. These expenses include the costs of employee, officer and director compensation and benefits properly allocable to the Partnership, and all other expenses necessary or appropriate to the conduct of the business of, and allocable to, the Partnership. The partnership agreement provides that the general partner will determine the expenses that are allocable to the Partnership in any reasonable manner determined by the general partner in its sole discretion. For the twelve months ended December 31, 2003, the amount which the Partnership reimbursed the general partner and its affiliates for costs incurred with respect to the general and administrative services performed on its behalf could not exceed $6.0 million. This reimbursement cap did not apply to the cost of any third-party legal, accounting or advisory services received, or the direct expenses of management incurred, in connection with acquisition or business development opportunities evaluated on behalf of the partnership. The $6.0 million limit on such reimbursements expired in December 2003 and future expenses reimbursed by the Partnership wil be higher.

The Partnership's general partner owns a 2% general partner interest in the Partnership and all of the incentive distribution rights. The Partnership's general partner is entitled to receive incentive distributions if the amount the Partnership distributes with respect to any quarter exceeds levels specified in the partnership agreement. Under the quarterly incentive distribution provisions, generally the general partner is entitled to 13% of amounts the Partnership distributes in excess of $0.50 per unit, 23% of the amounts the Partnership distributes in excess of $0.625 per unit and 48% of amounts the Partnership distributes in excess of $0.75 per unit.

Indemnification of Directors and Officers

Section 145 of the Delaware General Corporation Law permits indemnification of officers, directors and other corporate agents under specific circumstances and subject to specific limitations. Our restated certificate of incorporation and restated bylaws provide that we shall indemnify our directors and officers to the full extent permitted by the Delaware General Corporation Law, including in circumstances in which indemnification is otherwise discretionary under Delaware law.

We have entered into indemnification agreements with our directors and executive officers that provide the maximum indemnity allowed to directors and executive officers by Section 145 of the Delaware General Corporation Law, as well as certain additional procedural protections. The indemnity agreements provide that directors will be indemnified to the fullest extent not prohibited by law against all expenses (including attorney's fees) and settlement amounts paid or incurred by them in any action or proceeding as our directors or executive officers, including any action on account of their services as executive officers or directors of any other company or enterprise when they are serving in such capacities at our request, and including any action by us or in our right. In addition, the indemnity agreements provide for reimbursement of expenses incurred in conjunction with being a witness in any proceeding to which the indemnitee is not a party. We must pay in advance of a final disposition of a proceeding or claim the expenses incurred by the indemnitee no later than 10 days after our receipt of an undertaking by or on behalf of the indemnitee, to repay the amount of the expenses to the extent that it is ultimately determined that the indemnitee is not entitled to be indemnified by us. The indemnity agreements also provide the indemnitee with remedies in the event that we do not fulfill our obligations under the indemnity agreements.

Section 102(b)(7) of the Delaware General Corporation Law permits a corporation to provide in its certificate of incorporation that a director of the corporation shall not be personally liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, except for liability (i) for any breach of the director's duty of loyalty to the corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) for payments of unlawful dividends or unlawful stock repurchases or redemptions, or (iv) for any transaction from which the director derived an improper personal benefit. Our restated certificate of incorporation provides for that limitation of liability.

We maintain policies of insurance under which our directors and officers are insured, within the limits and subject to the limitations of the policies, against specific expenses in connection with the defense of, and specific liabilities which might be imposed as a result of, actions, suits or proceedings to which they are parties by reason of being or having been directors or officers.

Option Cancellation

In 2003, Jack M. Lafield received $93,236 as consideration for the cancellation of 13,496 options to purchase our common stock which had been previously granted under our 2000 Stock Option Plan.

Registration Rights

In October 2003, we entered into an Agreement Regarding 2003 Registration Statement and Waiver and Termination of Stockholders' Agreement whereby we granted certain registration rights to our stockholders, including certain of our directors and all of our officers, for shares of our common stock.

According to the terms of a registration rights agreement effective upon our initial public offering, Yorktown Energy Partners V, L.P., Lubar Nominees and all of our officers will be entitled to demand registration rights for the 9,427,348 shares of our capital stock outstanding prior to our initial public offering and any shares acquired by such persons in connection with the exercise of stock options. The stockholders must exercise their demand for registration by delivering a written request to us. We shall not be required to effect more than two registration statements for our officers, and we shall not be required to effect more than four registration statements for Yorktown Energy Partners IV, L.P., Yorktown Energy Partners V, L.P. and Lubar Nominees. If our board of directors determines a demand registration would have an adverse effect on us, we may delay any demand registration for a period not to exceed 90 days. We are also not required to effect more than two registrations in any 12-month period. In addition, these stockholders may participate in any public offering by us of our common stock, other than this offering or an offering under a registration statement on Form S-4 or Form S-8 or any other forms not available for registering capital stock for the sale to the public, subject to marketing considerations as determined by our managing underwriter for that offering. We will pay all expenses in connection with any registration under this agreement. This agreement terminates to each stockholder when all of the stockholders' shares have been registered pursuant to the Securities Act of 1933 and sold or sold under Rule 144 to the Securities Act of 1933.

Other Related Party Transactions

Camden Resources, Inc. The Partnership treats gas for, and purchases gas from, Camden Resources, Inc. Yorktown Energy Partners IV, L.P. has made equity investments in both Camden and us. The gas treating and gas purchase agreements the Partnership has entered into with Camden are standard industry agreements containing terms substantially similar to those contained in the Partnership's agreements with other third parties. During the year ended December 31, 2003, the Partnership purchased natural gas from Camden Resources, Inc. in the amount of approximately $8.4 million and received approximately $190,000 in treating fees from Camden Resources, Inc.

Crosstex Pipeline Partners, L.P. The Partnership indirectly owns general and limited partner interests in Crosstex Pipeline Partners, L.P. that represent a 28% economic interest. The Partnership has entered into various transactions with Crosstex Pipeline Partners, and it believes that the terms of these transactions are comparable to those that it could have negotiated with unrelated third parties. During the year ended December 31, 2003, the Partnership's predecessor: (1) purchased natural gas from Crosstex Pipeline Partners in the amount of approximately $8.2 million and paid Crosstex Pipeline Partners approximately $41,000 for transportation of natural gas, (2) received a management fee from Crosstex Pipeline Partners in the amount of approximately $125,000 and (3) received approximately $104,000 in distributions from Crosstex Pipeline Partners

Crosstex Denton County Gathering J.V. The Partnership owns a 50% interest in Crosstex Denton County Gathering, J.V. (CDC). CDC was formed to build, own and operate a natural gas gathering system in Denton County, Texas. The Partnership manages the business affairs of CDC. The other 50% joint venture partner (the CDC Partner) is an unrelated third party who owns and operates the natural gas field in Denton County.

In connection with the formation of CDC, the Partnership agreed to loan the CDC Partner up to $1.5 million for their initial capital contribution. The loan bears interest at an annual rate of prime plus 2%. CDC makes payments directly to the Partnership attributable to CDC Partner's 50% share of distributable cash flow to repay the loan. Any balance remaining on the note is due in August 2007.

The Partnership's investment in CDC is $2.3 million as of December 31, 2003. The Partnership also has $635,000 in receivables from affiliates for cash advances to CDC for current disbursements that are generally repaid on a month-to-month basis in the normal course of business.

During the year ended December 31, 2003, the Partnership received a management fee from CDC of $110,000.

Item 14. *Principal Accountant Fees and Services*

Audit Fees

The fees for professional services rendered for the audit of our annual financial statements for the fiscal year ended December 31, 2003 and services that are normally provided by KPMG in connection with statutory or regulatory filings or engagement for the fiscal year were $317,000. This amount also included fees associated with comfort letters and consents related to debt and equity offerings. For the fiscal year ended December 31, 2002, we did not have any similar fees to those described above. The fees for professional services rendered for the audit of Crosstex Energy, L.P.'s annual financial statements for each of the fiscal years ended December 31, 2003 and December 31, 2002, and the reviews of the financial statements included in Crosstex Energy, L.P.'s Quarterly Reports on Forms 10-Q or services that are normally provided by KPMG in connection with statutory or regulatory filings or engagement for each of those fiscal years, were $411,500 and $354,123, respectively. These amounts also included fees associated with comfort letters and consents related to debt and equity offerings of Crosstex Energy, L.P.

Audit-Related Fees

KPMG did not perform any assurance and related services related to the performance of the audit or review of our financial statements for the fiscal years ended December 31, 2003 and December 31, 2002 that were not included in the audit fees listed above.

Tax Fees

Aggregate fees billed or expected to be billed by KPMG, for tax compliance, tax advice and tax planning for each of the fiscal years ended December 31, 2003 and December 31, 2002, were $34,090 and $3,500, respectively. These fees include fees relating to reviews of tax returns, tax consulting and planning. Aggregate fees billed or expected to be billed by KPMG to Crosstex Energy, L.P. for tax compliance, tax advice and tax planning for each of the fiscal years ended December 31, 2003 and December 31, 2002, were $103,725 and $50,875, respectively. These fees include fees relating to reviews of tax returns, tax consulting and planning for Crosstex Energy, L.P.

All Other Fees

KPMG did not render services to us, other than those services covered in the sections captioned "Audit Fees," and "Tax Fees" for the fiscal years ended December 31, 2003 and December 31, 2002.

Audit Committee Approval of Audit and Non-Audit Services

We were not a public company in 2003 and did not have an Audit Committee. For 2004, the Audit Committee has pre-approved the use of KPMG for specific tax-related services. In such case, the Audit Committee has also set a specific annual limit on the amount of such tax-related services which we will obtain from KPMG, and has required management to report the specific engagements to the Audit Committee. All other non-audit services other than the pre-approved services set forth above and any services that exceed the annual limits set forth in the policy must be pre-approved by the Audit Committee. The Chairman of the Audit Committee is authorized by the Audit Committee to pre-approve additional KPMG audit and non-audit services between Audit Committee meetings; provided that the additional services do not affect KPMG's independence under applicable Securities and Exchange Commission rules and any such pre-approval is reported to the Audit Committee at its next meeting.

PART IV

Item 15. *Exhibits, Financial Statement Schedules and Reports on Form 8-K*

(a) Financial Statements and Schedules

(1) See the Index to Financial Statements on page F-1.

(2) See Schedule II—Valuation and Qualifying Accounts on Page S-1.

(3) Exhibits

The exhibits filed as part of this report are as follows (exhibits incorporated by reference are set forth with the name of the registrant, the type of report and registration number or last date of the period for which it was filed, and the exhibit number in such filing):

Number		Description
3.1*	—	Restated Certificate of Incorporation of Crosstex Energy, Inc.
3.2*	—	Restated Bylaws of Crosstex Energy, Inc.
3.3	—	Certificate of Limited Partnership of Crosstex Energy, L.P (incorporated by reference from Exhibit 3.1 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.4	—	Amended and Restated Agreement of Limited Partnership of Crosstex Energy, L.P., dated as of December 17, 2002 (incorporated by reference from Exhibit 3.2 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
3.5	—	Certificate of Limited Partnership of Crosstex Energy Services, L.P. (incorporated by reference from Exhibit 3.3 to Amendment No. 2 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed November 4, 2002)
3.6	—	Amended and Restated Agreement of Limited Partnership of Crosstex Energy Services, L.P., dated as of December 17, 2002 (incorporated by reference from Exhibit 3.4 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
3.7	—	Certificate of Limited Partnership of Crosstex Energy GP, L.P. (incorporated by reference from Exhibit 3.5 to Crosstex Energy, L.P.'s Registration Statement, file No. 333-97779, filed August 7, 2002)
3.8	—	Agreement of Limited Partnership of Crosstex Energy GP, L.P., dated as of July 12, 2002 (incorporated by reference from Exhibit 3.6 to Crosstex Energy L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.9	—	Certificate of Formation of Crosstex Energy GP, LLC (incorporated by reference from Exhibit 3.7 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.10	—	Amended and Restated Limited Liability Company Agreement of Crosstex Energy GP, LLC, dated as of December 17, 2002 (incorporated by reference from Exhibit 3.8 from Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
3.11	—	Amended and Restated Certificate of Formation of Crosstex Holdings GP, LLC (incorporated by reference from Exhibit 3.11 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.12	—	Limited Liability Company Agreement of Crosstex Holdings GP, LLC, dated as of October 27, 2003 (incorporated by reference from Exhibit 3.12 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.13	—	Certificate of Formation of Crosstex Holdings LP, LLC (incorporated by reference from Exhibit 3.13 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.14	—	Limited Liability Company Agreement of Crosstex Holdings LP, LLC, dated as of November 4, 2003 (incorporated by reference from Exhibit 3.14 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.15	—	Amended and Restated Certificate of Limited Partnership of Crosstex Holdings, L.P. (incorporated by reference from Exhibit 3.15 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.16	—	Agreement of Limited Partnership of Crosstex Holdings, L.P., dated as of November 4, 2003 (incorporated by reference from Exhibit 3.16 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
4.1	—	Specimen Certificate representing shares of common stock (incorporated by reference from Exhibit 4.1 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)

10.1	—	Omnibus Agreement, dated December 17, 2002, among Crosstex Energy, Inc. and certain other parties (incorporated by reference from Exhibit 10.5 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.2*	—	Form of Indemnity Agreement, entered into with directors and/or officers on December 31, 2003
10.3+	—	Crosstex Energy GP, LLC Long-Term Incentive Plan dated July 12, 2002 (incorporated by reference from Exhibit 10.4 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.4*	—	Agreement Regarding 2003 Registration Rights Agreement and Termination of Stockholders' Agreement, dated October 27, 2003
10.5*+	—	Crosstex Energy, Inc. Long-Term Incentive Plan, dated December 31, 2003
10.6*	—	Registration Rights Agreement, dated December 31, 2003
10.7	—	Second Amended and Restated Credit Agreement, dated November 26, 2002, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated reference from Exhibit 10.1 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.8	—	First Amendment to Second Amended and Restated Credit Agreement dated as of June 3, 2003, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated by reference from Exhibit 10.2 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
10.9	—	Second Amendment to Second Amended and Restated Credit Agreement, dated as of June 3, 2003, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 10, 2004)
10.10	—	$50,000,000 Senior Secured Notes Master Shelf Agreement as of June 3, 2003 (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
10.11	—	First Contribution, Conveyance and Assumption Agreement dated November 27, 2002, among Crosstex Energy, L.P. and certain other parties (incorporated by reference from Exhibit 10.2 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.12	—	Closing Contribution, Conveyance and Assumption Agreement dated December 11, 2002, among Crosstex Energy, L.P. and certain other parties (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.13	—	Crosstex Energy Holdings Inc. 2000 Stock Option Plan (incorporated by reference from Exhibit 10.14 to Amendment No. 2 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed December 30, 2003)
21.1	—	List of Subsidiaries (incorporated by reference from Exhibit 21.1 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
31.1*	—	Certification of the principal executive officer
31.2*	—	Certification of the principal financial officer
32.1*	—	Certification of the principal executive officer and the principal financial officer of the Company pursuant to 18 U.S.C. Section 1350

* Filed herewith.

\+ Compensatory benefit plan or arrangement in which directors and executive officers are eligible to participate.

(b) Reports on Form 8-K.

Registrant did not file any Current Reports on Form 8-K during the fourth quarter of 2003.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 26 day of March 2004.

CROSSTEX ENERGY, INC.

By: /s/ BARRY E. DAVIS

Barry E. Davis,
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on the dates indicated by the following persons on behalf of the Registrant in the capacities indicated.

Signature	Title	Date
/s/ BARRY E. DAVIS Barry E. Davis	President, Chief Executive Officer and Director (Principal Executive Officer)	March 26, 2004
/s/ FRANK M. BURKE Frank M. Burke	Director	March 26, 2004
/s/ BRYAN H. LAWRENCE Bryan H. Lawrence	Chairman of the Board	March 26, 2004
/s/ SHELDON B. LUBAR Sheldon B. Lubar	Director	March 26, 2004
/s/ ROBERT F. MURCHISON Robert F. Murchison	Director	March 26, 2004
/s/ WILLIAM W. DAVIS William W. Davis	Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 26, 2004

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Independent Auditors' Report

To the Stockholders of
Crosstex Energy, Inc.:

We have audited the accompanying consolidated balance sheets of Crosstex Energy, Inc. (a Delaware corporation) and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of operations, changes in stockholders' equity, comprehensive income and cash flows for each of the years in the three-year period ended December 31, 2003. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedules as listed in the accompanying index. These financial statements and financial statement schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Crosstex Energy, Inc. and subsidiaries as of December 31, 2003 and 2002, and the consolidated results of their operations, comprehensive income and their cash flows for each of the years in the three-year period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects, the information set forth therein.

As explained in Note 2 to the consolidated financial statements, effective January 1, 2001, the Partnership changed its method of accounting for derivatives. Also, as explained in note 2 to the financial statements, effective January 1, 2002, the Company changed its method of amortizing goodwill.

/s/ KPMG LLP

Dallas, Texas,
February 26, 2004

CROSSTEX ENERGY, INC.
Consolidated Balance Sheets December 31, 2003 and 2002
(In thousands, except share data)

	December 31, 2003	December 31, 2002
Assets		
Current assets:		
Cash and cash equivalents	$ 1,479	$ 3,808

Accounts receivable:		
Trade	9,491	26,302
Accrued revenues	124,517	78,500
Imbalances	447	79
Related party	617	—
Other	2,628	1,037
Note receivable	535	—
Fair value of derivative assets	4,080	2,947
Prepaid expenses and other	2,013	1,256
Total current assets	145,807	113,929
Property and equipment:		
Transmission assets	99,650	50,391
Gathering systems	27,990	22,624
Gas plants	88,395	40,730
Other property and equipment	3,743	2,754
Construction in process	9,863	6,935
Total property and equipment	229,641	123,434
Accumulated depreciation	(24,751)	(12,231)
Total property and equipment, net	204,890	111,203
Account receivable from Enron (net of allowance of $6,931 and $5,776 in 2003 and 2002, respectively)	1,312	2,467
Fair value of derivative assets	—	155
Intangible assets, net	5,366	5,340
Goodwill, net	6,164	6,458
Investment in limited partnerships	2,560	346
Other assets, net	3,639	778
Total assets	$ 369,738	$ 240,676
Liabilities and Stockholders' Equity		
Current liabilities:		
Drafts payable	$ 10,446	$ 27,546
Accounts payable	4,064	9,200
Accrued gas purchases	119,756	74,768
Accounts payable-related party	448	—
Preferred dividends payable	3,471	3,021
Accrued imbalances payable	212	149
Fair value of derivative liabilities	2,487	4,006
Current portion of long-term debt	50	50
Other current liabilities	10,920	4,672
Total current liabilities	151,854	123,412
Fair value of derivative liabilities	—	452
Deferred tax liability	19,683	9,023
Long-term debt	60,700	22,500
Interest of non-controlling partners in the Partnership	67,882	27,540
Stockholders' equity:		
Convertible preferred stock (7,500,000 authorized shares, $.01 par value, 4,123,642 and 4,093,642 issued and outstanding in 2003 and 2002, respectively, $50,740 liquidation value in 2003)	42	42
Common stock (4,000,000 shares authorized, $.01 par value, 1,743,032 and 1,882,772 issued and outstanding in 2003 and 2002, respectively)	19	19
Additional paid-in capital	68,934	64,913
Retained earnings	7,902	(1,962)
Treasury stock, at cost (139,740 common shares)	(2,500)	—
Accumulated other comprehensive income	506	(528)
Notes receivable from stockholders	(5,284)	(4,735)
Total stockholders' equity	69,619	57,749
Total liabilities and stockholders' equity	$ 369,738	$ 240,676

See accompanying notes to consolidated financial statements

CROSSTEX ENERGY, INC.
Consolidated Statements of Operations
(In thousands, except share data)

	Years Ended December 31, 2003	2002	2001
Revenues:			
Midstream	$ 993,140	$ 437,676	$ 362,673
Treating	20,523	14,817	24,353
Total revenues	1,013,663	452,493	387,026
Operating costs and expenses:			
Midstream purchased gas	946,412	413,982	344,755
Treating purchased gas	7,568	5,767	18,078
Operating expenses	17,758	11,420	7,761
General and administrative	11,593	7,663	5,583
Stock based compensation	5,345	41	—
Impairments	—	4,175	2,873
(Profit) loss on energy trading activities	(1,905)	(2,703)	3,714
Depreciation and amortization	13,542	7,745	6,208
Total operating costs and expenses	1,000,313	448,090	388,972
Operating (loss) income	13,350	4,403	(1,946)
Other income (expense):			
Interest expense, net	(3,103)	(2,381)	(2,253)
Other income (expense)	179	56	174
Total other income (expense)	(2,924)	(2,325)	(2,079)
Income before gain on issuance of units by the Partnership, income taxes and interest of non-controlling partners in the Partnership's net income	10,426	2,078	(4,025)
Gain on issuance of units of the Partnership	18,360	11,054	—
Income tax (provision) benefit	(10,157)	(7,451)	1,294
Interest of non-controlling partners in the Partnership's net income	(5,181)	(99)	—
Net income (loss)	$ 13,448	$ 5,582	$ (2,731)
Preferred stock dividends	$ 3,584	$ 3,021	$ 1,970
Net income (loss) available to common	$ 9,864	$ 2,561	$ (4,701)
Basic earnings (loss) per common share	$ 2.83	$ 0.68	$ (1.25)
Diluted earnings (loss) per common share	$ 1.10	$ 0.49	$ (1.25)
Weighted-average shares outstanding:			
Basic	3,486	3,766	3,766
Diluted	12,271	1,361	3,766

See accompanying notes to consolidated financial statements.

CROSSTEX ENERGY, INC.

Consolidated Statements of Changes in Stockholders' Equity

(In thousands, except share data)

Preferred Stock	Common Stock	Accumulated other Compre- hensive	Total Stock- holders'

	Shares	Amt	Shares	Amt	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Income	Notes Receivable	Equity
Balance, December 31, 2000	2,319,375	$ 24	1,882,772	$ 19	41,980	$ —	178	$ —	$ (2,393)	$ 39,808
Issuance of preferred stock	581,663	6	—	—	6,934	—	—	—	(1,920)	5,020
Preferred dividends	192,604	2	—	—	1,968	—	(1,970)	—	—	—
Change in notes receivable	—	—	—	—	—	—	—	—	52	52
Net loss	—	—	—	—	—	—	(2,731)	—	—	(2,731)
Cumulative adjustment from adoption of accounting standard	—	—	—	—	—	—	—	(654)	—	(654)
Hedging gains or losses reclassified to earnings	—	—	—	—	—	—	—	654	—	654
Adjustment in fair value of derivatives	—	—	—	—	—	—	—	92	—	92
Balance, December 31, 2001	3,093,642	32	1,882,772	19	50,882	—	(4,523)	92	(4,261)	42,241
Issuance of preferred stock	1,000,000	10	—	—	13,990	—	—	—	—	14,000
Preferred dividends	—	—	—	—	—	—	(3,021)	—	—	(3,021)
Change in notes receivable	—	—	—	—	—	—	—	—	(474)	(474)
Stock based compensation	—	—	—	—	41	—	—	—	—	41
Net income	—	—	—	—	—	—	5,582	—	—	5,582
Non-controlling partners' share of other comprehensive income in the Partnership	—	—	—	—	—	—	—	236	—	236
Hedging gains or losses reclassified to earnings	—	—	—	—	—	—	—	(116)	—	(116)
Adjustment in fair value of derivatives	—	—	—	—	—	—	—	(740)	—	(740)
Balance, December 31, 2002	4,093,642	42	1,882,772	19	64,913	—	(1,962)	(528)	(4,735)	57,749
Issuance of preferred stock	30,000	—	—	—	400	—	—	—	(360)	40
Treasury stock purchased	—	—	(139,740)	—	—	(2,500)	—	—	—	(2,500)
Non-cash stock based compensation	—	—	—	—	3,621	—	—	—	—	3,621
Preferred dividends	—	—	—	—	—	—	(3,584)	—	—	(3,584)
Change in notes receivable	—	—	—	—	—	—	—	—	(189)	(189)
Net income	—	—	—	—	—	—	13,448	—	—	13,448
Non-controlling partners' share of other comprehensive income in the Partnership	—	—	—	—	—	—	—	298	—	298
Hedging gains or losses reclassified to earnings	—	—	—	—	—	—	—	1,725	—	1,725
Adjustment in fair value of derivatives	—	—	—	—	—	—	—	(989)	—	(989)
Balance, year ended December 31, 2003	4,123,642	$ 42	1,743,032	$ 19	$ 68,934	$ (2,500)	$ 7,902	$ 506	$ (5,284)	$ 69,619

See accompanying notes to consolidated financial statements.

CROSSTEX ENERGY, INC.

Consolidated Statements of Comprehensive Income December 31, 2003, 2002 and 2001

(In thousands)

	Years Ended December 31,		
	2003	2002	2001
Net income (loss)	$ 13,448	$ 5,582	$ (2,731)
Cumulative adjustment from adoption of accounting standard	—	—	(654)
Non-controlling partners' share of other comprehensive income in the Partnership	298	236	—
Hedging gains or losses reclassified to earnings	1,725	(116)	654
Adjustment in fair value of derivatives	(989)	(740)	92
Comprehensive income (loss)	$ 14,482	$ 4,962	$ (2,639)

CROSSTEX ENERGY, INC.

Consolidated Statements of Cash Flows

(In thousands)

	Years Ended December 31,		
	2003	2002	2001
Cash flows from operating activities:			
Net income (loss)	$ 13,448	$ 5,582	$ (2,731)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	13,542	7,745	6,208
Impairments	—	4,175	2,873
(Income) loss on investment in affiliated partnerships	(208)	41	(35)
Gain on issuance of units of the Partnership	(18,360)	(11,054)	—
Interest of non-controlling partners in the Partnership net income	5,181	99	—
Deferred tax	10,103	7,451	(994)
Non-cash stock based compensation	3,967	41	—
Changes in assets and liabilities:			
Accounts receivable	(31,782)	(46,554)	47,165
Prepaid expenses	(1,292)	239	(1,814)
Accounts payable, accrued gas purchased, and other accrued liabilities	40,363	29,521	(65,133)
Fair value of derivatives	(389)	(4,668)	4,573
Other	7,530	2,332	(798)
Net cash provided by (used in) operating activities	42,103	(5,050)	(10,686)
Cash flows from investing activities:			
Additions to property and equipment	(39,003)	(14,545)	(22,685)
Asset purchases	(68,124)	(18,785)	(30,003)
Additions to intangibles and other non-current assets	(1,027)	—	—
Distributions from (contributions to) affiliated partnerships	(2,134)	90	153
Net cash used in investing activities	(110,288)	(33,240)	(52,535)
Cash flows from financing activities:			
Proceeds from bank borrowings	320,100	384,050	267,131
Payments on bank borrowings	(281,900)	(421,500)	(229,150)
Drafts payable	(17,100)	25,628	1,918
Distribution to non-controlling partners in the Partnership	(5,408)	—	—
Deferred dividends paid	(3,134)	—	—
Debt refinancing and offering costs	(2,200)	—	—
Net proceeds from issuance of units of the Partnership	57,958	39,568	—
Purchase of treasury stock	(2,500)	—	—
Proceeds from sale of common and preferred stock	40	14,000	5,019
Net cash provided by (used in) financing activities	65,856	41,746	44,918
Net increase (decrease) in cash and cash equivalents	(2,329)	3,456	(18,303)
Cash and cash equivalents, beginning of period	3,808	352	18,655
Cash and cash equivalents, end of period	$ 1,479	$ 3,808	$ 352
Cash paid for interest	$ 3,394	$ 2,558	$ 2,720
Cash paid for income taxes	—	—	300
Contributions of assets and liabilities of predecessor	—	—	—
Notes receivable from management for stock issuances	—	—	1,920

See accompanying notes to consolidated financial statements.

CROSSTEX ENERGY, INC.

Notes to Consolidated Financial Statements December 31, 2003 and 2002

(1) Organization and Summary of Significant Agreements:

(a)

Description of Business

Crosstex Energy, Inc. (the "Company" and formerly Crosstex Energy Holdings Inc.), a Delaware corporation formed on April 28, 2000, is engaged, through its subsidiaries, in the gathering, transmission, treating, processing and marketing of natural gas. The Company connects the wells of natural gas producers in the geographic areas of its gathering systems in order to purchase the gas production, treats natural gas to remove impurities to ensure that it meets pipeline quality specifications, processes natural gas for the removal of natural gas liquids or NGLs, transports natural gas and ultimately provides an aggregated supply of natural gas to a variety of markets. In addition, the Company purchases natural gas from producers not connected to its gathering systems for resale and sells natural gas on behalf of producers for a fee.

(b)

Organization, Public Offering of Units in CELP and Public Offering of the Company

On July 12, 2002, the Company formed Crosstex Energy, L.P. (herein referred to as "the Partnership" or "CELP"), a Delaware limited partnership. On December 17, 2002, the Partnership completed an initial public offering of common units representing limited partner interests in the Partnership. Prior to its initial public offering, the Partnership was an indirect wholly owned subsidiary of the Company. The Company conveyed to the Partnership its indirect wholly owned ownership interest in Crosstex Energy Services, Ltd. (CES) in exchange for (i) a 2% general partner interest (including certain Incentive Distribution Rights) in the Partnership, (ii) 333,000 common units and (iii) 4,667,000 subordinated units of the Partnership, together representing a 67.1% limited partner interest. Prior to the conveyance of CES to the Partnership, CES distributed certain assets to the Company including (i) the Jonesville and Clarkson gas plants, (ii) the Enron receivable, and (iii) the right to receive a cash distribution of $2.5 million. As a result of CELP issuing additional units to unrelated parties, the Company's share of net assets of CELP increased by $11.1 million. Accordingly, the Company recognized a $11.1 million gain in 2002. See Note 3 for a discussion of the Partnership's September 2003 sale of additional common units.

CES constitutes the Partnership's predecessor. The transfer of ownership interests in CES to the Partnership represented a reorganization of entities under common control and was recorded at historical cost. Accordingly, the accompanying financial statements include the historical results of operations of CES prior to transfer to the Partnership.

As of December 31, 2003, Yorktown Energy Partners IV, L.P. and Yorktown Energy Partners V, L.P. (collectively, Yorktown) owned 77% of CEI and CEI management and directors owned 23% of CEI. In January 2004, CEI completed an initial public offering of its common stock. In conjunction with the public offering, the Company converted all of its preferred stock to common stock, cancelled its treasury stock and made a two-for-one stock split, effected in the form of a stock dividend. CEI's existing shareholders sold 2,306,000 common shares (on a post-split basis) and CEI issued 345,900 common shares (on a post-split basis) at a public offering price of $19.50 per common share. The Company received net proceeds of approximately $4.8 million from the common stock issuance. CEI's existing stockholders also repaid approximately $4.9 million in stockholder notes receivable in connection with the public offering. After giving effect to this public offering,

Yorktown owns 60.2% of CEI's outstanding common shares, CEI management and directors own 17.8% of CEI's common shares and the remaining 22.0% is held publicly.

(c)

Basis of Presentation

The accompanying consolidated financial statements include the assets, liabilities and results of operations of the Company and its majority owned subsidiaries, including the Partnership. The consolidated operations are hereafter referred to collectively as the "Company." All material intercompany balances and transactions have been eliminated. Certain reclassifications have been made to the consolidated financial statements for the prior years to conform to the current presentation.

(2) Significant Accounting Policies

(a)

Management's Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management of the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates. See discussion of Enron account receivable in Note 10.

(b)

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

(c)

Property, Plant, and Equipment

Property, plant and equipment consists of intrastate gas transmission systems, gas gathering systems, industrial supply pipelines, natural gas processing plants, an undivided 12.4% interest in a carbon dioxide processing plant, and gas treating plants..

Other property and equipment is primarily comprised of furniture, fixtures, and office equipment. Such items are depreciated over their estimated useful life of five years. Property, plant and equipment is recorded at cost.. Repairs and maintenance are charged against income when incurred. Renewals and betterments, which extend the useful life of the properties, are capitalized. Depreciation is provided using the straight-line method based on the estimated useful life of each asset, as follows:

	Useful Lives
Transmission assets	15 years
Gathering systems	7-15 years
Gas treating, gas processing and carbon dioxide plants	10-15 years
Other property and equipment	5 years

Statement of Financial Accounting Standards ("SFAS") No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, requires long-lived assets to be reviewed whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. In order to determine whether an impairment has occurred, the Company compares the net book value of the asset to the undiscounted expected future net cash flows. If an impairment has occurred, the amount of such impairment is determined based on the expected future net cash flows discounted using a rate commensurate with the risk associated with the asset. Impairments of approximately $4.2 million and $2.9 million associated with certain assets and the related intangible assets were recorded in the years ended December 31, 2002 and 2001, respectively. The impairments recorded in 2002 and 2001 relate primarily to customer relationships recorded as intangible assets as part of CES's formation. Due to changes impacting the expected future cash flows of the related assets, the Company determined the intangible assets were impaired under SFAS No. 121 or SFAS No. 144.

When determining whether impairment of one of our long-lived assets has occurred, we must estimate the undiscounted cash flows attributable to the asset. Our estimate of cash flows is based on assumptions regarding the purchase and resale margins on natural gas, volume of gas available to the asset, markets available to the asset, operating expenses, and future natural gas prices and NGL product prices. The amount of availability of gas to an asset is sometimes based on assumptions regarding future drilling activity, which may be dependent in part on natural gas prices. Projections of gas volumes and future commodity prices are inherently subjective and contingent upon a number of variable factors. Any significant variance in any of the above assumptions or factors could materially affect our cash flows, which would require us to record an impairment of an asset.

(d)

Amortization of Intangibles

Until January 1, 2002, goodwill was amortized on a straight-line basis over 15 years.. Such amortization was $390,000 for the year ended December 31, 2001. The Company discontinued the amortization of goodwill effective January 1, 2002 with the adoption of SFAS No. 142. As of December 31, 2003, accumulated amortization of goodwill was $674,000.

The following table shows the Company's net earnings excluding goodwill amortization for the year ended December 31, 2001 (in thousands except per share data).

		Year Ended December 31, 2001
Reported net loss	$	(2,731)
Goodwill amortization		390
Pro forma net loss	$	(2,341)
Pro forma net loss per common share (adjusted for the two-for-one stock split made in conjunction with the Company's January 2004 initial public offering):		
Basic	$	(1.15)
Diluted	$	(1.15)

The Company has approximately $6.2 million of goodwill at December 31, 2003 which resulted from the Company's formation in May 2000. The goodwill has been allocated to the Midstream segment and is assessed at least annually for impairment. During the fourth quarter of 2003, the Company completed the annual impairment testing of goodwill and no impairment was required.

Intangible assets are amortized on a straight-line basis over the expected benefits of the customer relationships, which average six years. Such amortization was $896,000, $454,000 and $772,000 for the years ended December 31, 2003, 2002 and 2001, respectively. See impairment of intangibles discussed in note 2(d). As of December 31, 2003, accumulated amortization of intangible assets was $2,089,000.

(e)

Other Assets

Unamortized debt issuance costs totaling $2.1 million as of December 31, 2003 are included in other non-current assets. Debt issuance costs are amortized into interest expense over the term of the related debt. Other non-current assets as of December 31, 2003 also include the non-current portion of the note receivable from Adkins discussed in Note 5.

(f)

Gas Imbalance Accounting

Quantities of natural gas over-delivered or under-delivered related to imbalance agreements are recorded monthly as receivables or payables using weighted average prices at the time of the imbalance. These imbalances are typically settled with deliveries of natural gas. The Company had an imbalance payable of $212,000 and $149,000 and an imbalance receivable of $447,000 and $79,000 at December 31, 2003 and 2002, respectively. Imbalance receivables are carried at the lower of costs or market value.

(g)

Revenue Recognition

The Company recognizes revenue for sales or services at the time the natural gas or NGLs are delivered or at the time the service is performed. See discussion of accounting for energy trading activities in note 2(i).

(h)

Commodity Risk Management

The Company engages in price risk management activities in order to minimize the risk from market fluctuations in the price of natural gas, oil and NGLs. To qualify as a hedge, the price movements in the commodity derivatives must be highly correlated with the underlying hedged commodity. Gains and losses related to commodity derivatives, which qualify as hedges, are recognized in income when the underlying hedged physical transaction closes and are included in the consolidated statements of operations as a cost of gas purchased.

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133 ("SFAS 133"), *Accounting for Derivative Instruments and Hedging Activities*. This standard requires recognition of all derivative and hedging instruments in the statements of financial position as either assets or liabilities and measures them at fair value. If a derivative does not qualify for hedge accounting, it must be adjusted to fair value through earnings. However, if a derivative does

qualify for hedge accounting, depending on the nature of the hedge, changes in fair value can be offset against the change in fair value of the hedged item through earnings or recognized in other comprehensive income until such time as the hedged item is recognized in earnings.

To qualify for cash flow hedge accounting, the cash flows from the hedging instrument must be highly effective in offsetting changes in cash flows due to changes in the underlying item being hedged. In addition, all hedging relationships must be designated, documented, and reassessed periodically. The impact of adopting SFAS 133 on January 1, 2001, was to record the fair value of derivatives as a liability in the amount of $1,006,000 ($654,000 net of taxes).

Currently, all derivative financial instruments that qualify for hedge accounting are designated as cash flow hedges. These instruments hedge the exposure of variability in expected future cash flows that is attributable to a particular risk. The effective portion of the gain or loss on these derivative instruments is recorded in other comprehensive income in stockholders' equity and reclassified into earnings in the same period in which the hedged transaction affects earnings. The asset or liability related to the derivative instruments is recorded on the balance sheet in fair value of derivative assets or liabilities. Any ineffective portion of the gain or loss is recognized in earnings immediately.

(i)

Producer Services

The Company conducts "off-system" gas marketing operations as a service to producers on systems that the Company does not own. The Company refers to these activities as part of Producer Services. In some cases, the Company earns an agency fee from the producer for arranging the marketing of the producer's natural gas. In other cases, the Company purchases the natural gas from the producer and enters into a sales contract with another party to sell the natural gas.

The Company manages its price risk related to future physical purchase or sale commitments for its natural gas marketing activities by entering into either corresponding physical delivery contracts or financial instruments with an objective to balance the Company's future commitments and significantly reduce its risk to the movement in natural gas prices. However, the Company is subject to counterparty risk for both the physical and financial contracts. Prior to October 26, 2002, the Company accounted for its Producer Services natural gas marketing activities as energy trading contracts in accordance with EITF 98-10, *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*. EITF 98-10 required energy-trading contracts to be recorded at fair value with changes in fair value reported in earnings. In October 2002, the EITF reached a consensus to rescind EITF No. 98-10. Accordingly, energy trading contracts entered into subsequent to October 25, 2002, should be accounted for under accrual accounting rather than mark-to-market accounting unless the contracts meet the requirements of a derivative under SFAS No. 133. The Company's energy trading contracts qualify as derivatives, and accordingly, the Company continues to use mark-to-market accounting for both physical and financial contracts of its Producer Services business. Accordingly, any gain or loss associated with changes in the fair value of derivatives and physical delivery contracts relating to the Company's Producer Services natural gas marketing activities are recognized in earnings as profit or loss on energy trading immediately.

For each reporting period, the Company records the fair value of open energy trading contracts based on the difference between the quoted market price and the contract price. Accordingly, the change in fair value from the previous period in addition to the realized gains or losses on settled contracts are reported as profit or loss on energy trading in the statements of operations.

Margins earned on settled contracts from its producer services activities included in profit (loss) on energy trading contracts in the consolidated statement of operations was $2,231,000, $1,791,000, and $1,946,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

Energy trading contract volumes that were physically settled were as follows (in MMBTUs):

	Years Ended December 31,		
	2003	2002	2001
Volumes purchased and sold	94,572,000	84,069,000	103,331,000

(j)

Comprehensive Income (Loss)

During 1998, the Company adopted SAFS No. 130 ("SFAS 130"), *Reporting Comprehensive Income*, which establishes standards for reporting and display of comprehensive income and its components in a full set of general purpose financial statements. Comprehensive income includes net income and other comprehensive income, which includes, but is not limited to, unrealized gains and losses on marketable securities, foreign currency translation adjustments, minimum pension liability adjustments, and effective January 1, 2001, unrealized gains and losses on derivative financial instruments.

With the adoption of SFAS No. 133 on January 1, 2001, the Company began recording deferred hedge gains and losses on its derivative financial instruments that qualify as hedges as other comprehensive income.

(k)

Concentrations of Credit Risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist primarily of trade accounts receivable and derivative financial instruments. Management believes the risk is limited as the Company's customers represent a broad and diverse group of energy marketers and end users. In addition, the Company continually monitors and reviews credit exposure to its marketing counterparties and letters of credit or other appropriate security are obtained as considered necessary to limit the risk of loss. As of December 31, 2003 and 2002, the reserve for doubtful accounts was approximately $6.9 million and $5.8 million, respectively. See further discussion at Note 12.

During the years ended December 31, 2003, 2002 and 2001, the Company had 1, 1, and 3 customers, respectively, which accounted for more than 10% of consolidated revenues. The relevant percentages for these customers were: (i) for the year ended December 31, 2003—20.5%; (ii) for the year ended December 31, 2002—27.5%; and (iii) for the year ended December 31, 2001—23.9%, 13.4%, and 11.5%. While these customers represent a significant percentage of revenues, the loss of any of these would not have a material adverse impact on the Company's results of operations.

(l)

Environmental Costs

Environmental expenditures are expensed or capitalized as appropriate, depending on the nature of the expenditures and their future economic benefit. Expenditures that related to an existing condition caused by past operations that do not contribute to current or future revenue generation are expensed. Liabilities for these expenditures are recorded on an undiscounted basis (or a discounted basis when the obligation can be settled at fixed and determinable amounts) when environmental assessments or clean-ups are probable and the costs can be reasonably estimated. For the years ended December 31, 2003, 2002 and 2001, such expenditures were not significant.

(m)

Option Plans

The Company applies the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB No. 25), and the related interpretations in accounting for the plan. In accordance with APB No. 25 for fixed rate stock and unit options, compensation is recorded to the extent the fair value of the stock or unit exceeds the exercise price of the option at the measurement date. In addition, compensation expense is recorded on variable options based on the difference between fair value of the stock or unit and the exercise price of the options at the end of the period. Compensation expense of $5,345,000, $41,000 and $0 was recognized in 2003, 2002 and 2001, respectively. The portion of compensation expense for 2003 related to operating activities was $2,122,000 and the remaining expense of $3,223,000 related to general and administrative activities.

Had compensation cost for the Company been determined based on the fair value at the grant date for awards in accordance with SFAS No. 123, *Accounting for Stock Based Compensation*, the Company's net income (loss) would have been as follows (in thousands except per share amounts):

	Year Ended December 31,		
	2003	2002	2001
Net income (loss), as reported	$ 13,448	$ 5,582	$ (2,731)
Add: Stock-based employee compensation expense included in reported net income, net of tax	3,474	27	—
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of tax	(3,636)	(213)	(147)
Pro forma net income (loss)	$ 13,286	$ 5,396	$ (2,878)

Pro forma net income (loss) per common share (adjusted for the two-for-one stock split made in conjunction with the Company's January 2004 initial public offering):			
Basic	$ 2.78	$ 0.63	$ (1.29)
Diluted	$ 1.08	$ 0..48	$ (1.29)

The fair value of each option is estimated on the date of grant using the Black Scholes option-pricing model with the following weighted-average assumptions used for grants in 2002 and 2001:

	Crosstex Energy, Inc.		Crosstex Energy, L.P.	
	2002	2001	2003	2002
Dividend yield	0%	0%	9.8%	10%
Expected volatility	0%	0%	24%	24%
Risk free interest rate	4.1%	5.8%	2.65%	2.2%
Expected life	3 years	3 years	4.3 years	3 years
Contractual life	3	3.6	10	10
Weighted average of fair value of options granted	$ —	$ —	$ 2.56	$ 1.15
Fair value of $5 options granted*	1.59	1.64	—	—
Fair value of $6 options granted*	0.70	0.76	—	—
Fair value of $7 options granted*	0.46	—	—	—

* Fair values and option prices have been adjusted for the two-for-one stock split made in conjuntion with the Company's January 2004 initial public offering.

No Company options were granted in 2003.

(n) Sales of Securities by Subsidiaries

The Company recognizes gains and losses in the consolidated statements of operations resulting from subsidiary sales of additional equity interest, including CELP limited partnership units, to unrelated parties.

(o) New Accounting Pronouncements

In June 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. This statement establishes standards for accounting for obligations associated with the retirement of tangible long-lived assets. This standard was adopted by the Company on January 1, 2003. The Company does not presently have any significant asset retirement obligations, and accordingly, the adoption of SFAS No. 143 had no impact on the Company's results of operations or financial condition.

SFAS No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure*, an amendment of FASB Statement No. 123, provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 also requires prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. SFAS No. 148 permits two additional transition methods for entities that adopt the fair value based method, these methods allow companies to avoid the ramp-up effect arising from prospective application of the fair value based method. This Statement is effective for financial

statements for fiscal years ending after December 15, 2002. The Company has complied with the disclosure provisions of the Statement in its financial statements.

In January 2003, the FASB issued FASB Interpretation (FIN) No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. FIN No. 45 requires an entity to recognize a liability for the obligations it has undertaken in issuing a guarantee. This liability would be recorded at the inception of a guarantee and would be measured at fair value. Certain guarantees are excluded from the measurement provisions of the Interpretation. The measurement provisions of this statement apply prospectively to guarantees issued or modified after December 31, 2002. The disclosure provisions of the statement apply to financial statements for periods ending after December 15, 2002. The adoption of the statement had no material effect on the Company's financial statements.

In January 2003, the FASB issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities, an interpretation of ARB No. 51*. In December 2003, the FASB issued FIN No. 46R which clarified certain issues identified in FIN 46. FIN No. 46R requires an entity to consolidate a variable interest entity if it is designated as the primary beneficiary of that entity even if the entity does not have a majority of voting interests. A variable interest entity is generally defined as an entity where its equity is unable to finance its activities or where the owners of the entity lack the risk and rewards of ownership. The provisions of this statement apply at inception for any entity created after January 31, 2003. For an entity created before February 1, 2003, the provisions of this

Interpretation must be applied at the beginning of the first interim or annual period ending after March 15, 2004. The Company is evaluating its ownership interests in joint ventures and limited partnerships that are currently accounted for using the equity method of accounting to determine whether FIN No. 46R will require the consolidation of any of these investments, however, the Company currently believes that one of its joint venture interests, as described in Note 5 to the financial statements, will be consolidated in the financial statements when FIN No. 46R is adopted in March 2004.

The FASB issued Statement of Financial Accounting Standards No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity," ("SFAS No. 150") in May 2003. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. The Company has no financial instruments which are subject to SFAS No. 150.

(3) Public Offerings of Units by CELP and Certain Provisions of the Partnership Agreement

(a)

Initial Public Offering

On December 17, 2002, the Partnership completed its initial public offering of 2,300,000 common units representing limited partner interests at a price of $20.00 per common unit. Total proceeds from the sale of the 2,300,000 units were $46.0 million, before offering costs and underwriting commissions.

A summary of the proceeds received from the offering and the use of those proceeds is as follows (in thousands):

Proceeds received:		
Sale of common units	$	46,000
Use of proceeds:		
Underwriters' fees	$	3,220
Professional fees and other offering costs		2,590
Repayment of debt		33,000
Distribution to Crosstex Holdings		2,500
Working capital		4,690
Total use of proceeds	$	46,000

The Crosstex Energy, L.P. partnership agreement contains specific provisions for the allocation of net earnings and losses to the partners for purposes of maintaining the partner capital accounts. Net income is allocated to the general partner based on incentive distributions earned for the period plus 2% of remaining net income.

(b)

Sale of Additional Common Units

In September 2003, the Partnership completed a public offering of 1,725,000 common units at a public offering price of $35.97 per common unit. The Partnership received net proceeds of approximately $58.0 million. The net proceeds were used to repay borrowings outstanding under the bank credit facility of our operating partnership.

(c)

Limitation of Issuance of Additional Common Units

During the subordination period, the Partnership may issue up to 1,316,500 additional common units or an equivalent number of securities ranking on a parity with the common units without obtaining unit-holder approval. The Partnership may also issue an unlimited number of common units during the subordination period for acquisitions, capital improvements or debt repayments that increase cash flow from operations per unit on a pro forma basis.

(d)

Subordination Period

The subordination period will end once the Partnership meets the financial tests in the partnership agreement, but it generally cannot end before December 31, 2007. When the subordination period ends, each remaining subordinated unit will convert into one common unit and the common units will no longer be entitled to arrearages.

(e)

Early Conversion of Subordinated Units

If the Partnership meets the applicable financial tests in the partnership agreement for any three consecutive four-quarter periods ending on or after December 31, 2005, 25% of the subordinated units will convert to common units. If the Partnership meets these tests for any three consecutive four-quarter periods ending on or after December 31, 2006, an additional 25% of the subordinated units will convert to common units. The early conversion of the second 25% of the subordinated units may not occur until at least one year after the early conversion of the first 25% of the subordinated units.

(f)

Cash Distributions

In accordance with the partnership agreement, the Partnership must make distributions of 100% of available cash, as defined in the partnership agreement, within 45 days following the end of each quarter commencing with the quarter ending on March 31, 2003. Distributions will generally be made 98% to the common and subordinated unit-holders and 2% to the general partner, subject to the payment of incentive distributions as described below to the extent that certain target levels of cash distributions are achieved. Under the quarterly incentive distribution provisions, generally its general partner is entitled to 13% of amounts the Partnership distributes in excess of $0.50 per unit, 23% of the amounts the Partnership distributes in excess of $0.625 per unit and 48% of amounts the Partnership distributes in excess of $0.75 per unit. Incentive distributions totaling $954,000 were earned by the Company for the year ended December 31, 2003. To the extent there is sufficient available cash, the holders of common units are entitled to receive the minimum quarterly distribution of $0.50 per unit, plus arrearages, prior to any distribution of available cash to the holders of subordinated units. Subordinated units will not accrue any arrearages with respect to distributions for any quarter.

The Partnership increased its fourth quarter distribution on its common and subordinated units to $0.75 per unit which was paid on February 13, 2004.

(4) Significant Asset Purchases and Acquisitions

On April 3, 2001, CES entered into a purchase and sale agreement with Tejas Energy NS, LLC to acquire all of the assets and operations of Tejas Texas Pipeline GP, LLC, a Delaware limited liability company, and Tejas C Pipeline LP, LLC, a Delaware limited liability company, for a total purchase price of $30,003,120, after closing adjustments. The Company recorded the net assets acquired based on relative fair values, and the Company's results of operations include the results of the acquired assets as of May 1, 2001.

The purchase price consisted of the following (in thousands):

Gas plant	$	11,837
Gathering systems		10,192
Transmission assets		7,158
Other property, plant, and equipment		816
	$	30,003

On October 11, 2001, CES entered into a purchase and sale agreement with various individuals to acquire the common stock of Millennium Gas Services, Inc. ("Millennium") for a total of $2,124,000 after closing adjustments, which was allocated entirely to treating plants. The Company recorded goodwill and deferred tax liability in the amount of $862,000 due to the difference in book and tax basis of the assets. The Company's results of operations include the results of Millennium as of October 1, 2001.

On June 6, 2002, CES acquired 70 miles of then-inactive pipeline from Florida Gas Transmission Company for $1,500,000 in cash and a $800,000 note payable. On June 7, 2002, CES acquired the Pandale gathering system which is connected to two treating plants, one of which (the Will-O-Mills Plant) was half-owned by CES, from Star Field Services for $2,156,000 in cash. CES purchased the other one-half interest in the Will-O-Mills Plant on December 30, 2002 for $2,200,000 in cash.

On December 19, 2002, the Partnership acquired the Vanderbilt system, consisting of approximately 200 miles of gathering pipeline located near our Gulf Coast System from an indirect subsidiary of Devon Energy Corporation, for $12,000,000 cash.

On June 30, 2003, the Partnership completed the acquisition of certain assets from Duke Energy Field Services, L.P. for $68.1 million, including the effect of certain purchase price adjustments. The assets acquired included: the Mississippi pipeline system, a 12.4% interest in the Seminole gas processing plant, the Conroe gas plant and gathering system, the Alabama pipeline system and two small gathering systems in Louisiana. The Company has accounted for this acquisition as a business combination in accordance with SFAS No. 141, Business Combinations. The Company has utilized the purchase method of accounting for this acquisition with an acquisition date of June 30, 2003. The purchase price and allocation thereof is as follows (in thousands):

Purchase price to DEFS	$	66,356
Direct acquisition costs		1,768
Total purchase price	$	68,124
Current assets acquired	$	426
Liabilities assumed		(813)
Property, plant and equipment		67,589
Intangible assets		922
Total purchase price	$	68,124

Intangible assets relate to customer relationships and will be amortized over seven years. The purchase price allocation is preliminary and may be adjusted for post-closing adjustments. Unaudited pro forma results of operations as if the acquisition from DEFS had been acquired on January 1, 2002 are as follows (in thousands, except per share amounts):

	Year Ended December 31,	
	2003	2002
Revenue	$ 1,119,985	$ 589,748
Net income	$ 13,889	$ 6,866
Net income (loss) per common share—		
Basic	$ 2.96	$ 1.02
Diluted	$ 1.13	$ 0.61

(5) Investment in Limited Partnerships

The Partnership owns a 7.86% weighted average interest as the general partner in the five gathering systems of Crosstex Pipeline Company (CPC), a 20.31% interest as a limited partner in CPC, 50% interest in the J.O.B. J.V. and a 50% interest in Crosstex Denton County Gathering, J.V. (CDC). The Company accounts for its investments under the equity method, as it exercises significant influence in operating decisions as a general partner in CPC and as a 50% owner in the joint ventures. Under this method, the Company records its equity in net earnings of the affiliated partnerships as income in other income (expense) in the consolidated statement of operations, and distributions received from them are recorded as a reduction in the Company's investment in the affiliated partnership.

CDC was formed to build, own and operate a natural gas gathering system in Denton County, Texas. The Partnership manages the business affairs of CDC. The other 50% joint venture partner (the CDC Partner) is an unrelated third party and owns and operates natural gas wells connected to the CDC gathering systems.

In connection with the formation of CDC, the Partnership agreed to loan the CDC Partner up to $1.5 million for their initial capital contribution. The loan bears interest at an annual rate of prime plus 2%. CDC makes payments directly to the Partnership attributable to CDC Partner's 50% share of distributable cash flow to repay the loan. Any balance remaining on the note is due in August 2007. The current portion of loan receivable of $535,000 from the CDC Partner is included in current notes receivable. The remaining balance of $1,027,000 is included in other non-current assets.

The Company's investment in CDC is $2.3 million as of December 31, 2003. The Company also has $635,000 in receivables from affiliates for cash advances to CDC for current disbursements that are generally repaid on a month-to-month basis in the normal course of business. The Company's investment at risk of CDC at December 31, 2003, is approximately $4.5 million, including cash advances and the note receivable from the CDC Partner.

Summarized financial information for 100% of CDC for the year ended December 31, 2003 is as follows (in thousands):

Revenues	$ 203
Costs and expenses	(248)
Net loss	$ (45)
Current assets	$ 322
Non-current assets	4,513
Current liabilities	809
Non-current liabilities	—
Partners' equity	4,026

(6) Long-Term Debt

At December 31, 2002, the Partnership had amended the secured credit facility with Union Bank of California, N.A. ("UBOC") to provide a $67.5 million credit facility consisting of a senior secured revolving acquisition facility in the aggregate principal amount of $47.5 million and a senior secured revolving working capital facility in the aggregate principal amount of $20 million.

In June 2003, CES entered into a $100 million senior secured credit facility with UBOC (as a lender and administrative agent) and four other banks, which was increased to $120 million in October 2003, consisting of the following two facilities:

- a $70.0 million senior revolving acquisition facility; and
- a $50.0 million senior secured revolving working capital and letter of credit facility.

The acquisition facility will be used to finance the acquisition and development of gas gathering, treating, and processing facilities, as well as general partnership purposes. At December 31, 2003, $20.0 million was outstanding under the acquisition facility, leaving approximately $50.0 available for future borrowings. The acquisition facility will mature in June 2006, at which time it will terminate and all outstanding amounts shall be due and payable. Amounts borrowed and repaid under the acquisition credit facility may be re-borrowed.

The working capital and letter of credit facility will be used for ongoing working capital needs, letters of credit, distributions and general partnership purposes, including future acquisitions and expansions. At December 31, 2003, $30.3 million of letters of credit were issued under the working capital facility, leaving approximately $19.7 million available for future issuances of letters of credit, or up to $19.7 million of cash borrowings. The aggregate amount of borrowings under the working capital and letter of credit facility is subject to a borrowing base requirement relating to the amount of our cash and eligible receivables (as defined in the credit agreement), and there is a $25.0 million sub-limit for cash borrowings. This facility will mature in June 2006, at which time it will terminate and all outstanding amounts shall be due and payable. Amounts borrowed and repaid under the

working capital facility may be re-borrowed. We are required to reduce all working capital borrowings to zero for a period of at least 15 consecutive days once a year.

Our obligations under the credit facility are secured by first priority liens on all of our material pipeline, gas gathering and processing assets, all material working capital assets and a pledge of all of our equity interests in certain of our subsidiaries, and ranks *pari passu* in right of payment with the senior secured notes. The credit agreement is guaranteed by certain of our subsidiaries. We may prepay all loans under the credit facility at any time without premium or penalty (other than customary LIBOR breakage costs), subject to certain notice requirements.

Indebtedness under the acquisition facility and the working capital facility bear interest at our option at the administrative agent's reference rate plus 0.25% to 1.5% or LIBOR plus 1.75% to 3.00%. The applicable margin varies quarterly based on our leverage ratio. The fees charged for letters of credit range from 1.50% to 2.00% per annum, plus a fronting fee of 0.125% per annum. We incur quarterly commitment fees based on the unused amount of the credit facilities.

The credit agreement prohibits the Partnership from declaring distributions to unit-holders if any event of default, as defined in the credit agreement, exists or would result from the declaration of distributions. In addition, the bank credit facility contains various covenants that, among other restrictions, limit our operating partnership's ability to:

- incur indebtedness;
- grant or assume liens;
- make certain investments;
- sell, transfer, assign or convey assets, or engage in certain mergers or acquisitions;
- make distributions;
- change the nature of its business;
- enter into certain commodity contracts;
- make certain amendments to our operating partnership's agreement; and
- engage in transactions with affiliates.

The credit facility contains the following covenants requiring the Partnership to maintain:

- a maximum ratio of funded debt to consolidated EBITDA (each as defined in the bank credit facility), measured quarterly on a rolling four quarter basis, of 3.75 to 1 through March 31, 2004, declining to 3.5 to 1 beginning June 30, 2004, pro forma for any asset acquisitions;
- a minimum interest coverage ratio (as defined in the bank credit facility), measured quarterly on a rolling four quarter basis equal to 3.50 to 1;
- a minimum current ratio (as defined in the credit agreement), measured quarterly of 1 to l; and

- a minimum tangible net worth (as defined in the credit agreement) of $60 million, plus one-half of certain equity contributions.

Each of the following will be an event of default under the bank credit facility:

- failure to pay any principal, interest, fees, expenses or other amounts when due;
-

failure to observe any agreement, obligation, or covenant in the credit agreement, subject to cure periods for certain failures;

- certain judgments against us or any of our subsidiaries, in excess of certain allowances;
- certain ERISA events involving us or our subsidiaries;
- a change in control (as defined in the credit agreement); and
- the failure of any representation or warranty to be materially true and correct when made.

Senior Secured Notes. In June 2003, the Partnership's operating partnership entered into a master shelf agreement with an institutional lender pursuant to which it issued $30.0 million aggregate principal amount of senior secured notes with an interest rate of 6.95% and a maturity of seven years. In July 2003, our operating partnership issued $10.0 million aggregate principal amount of senior secured notes pursuant to the master shelf agreement with an interest rate of 6.88% and a maturity of seven years.

The following is a summary of the material terms of the senior secured notes.

The notes represent senior secured obligations of our operating partnership and will rank at least *pari passu* in right of payment with the bank credit facility. The notes are secured, on an equal and ratable basis with obligations of the operating partnership under the credit facility, by first priority liens on all of our material pipeline, gas gathering and processing assets, all material working capital assets and a pledge of all our equity interests in certain of our subsidiaries. The senior secured notes are guaranteed by our operating partnership's subsidiaries and us.

The senior secured notes are redeemable, at our operating partnership's option and subject to certain notice requirements, at a purchase price equal to 100% of the principal amount together with accrued interest, plus a make-whole amount determined in accordance with the master shelf agreement.

The master shelf agreement relating to the notes contains substantially the same covenants and events of default as the bank credit facility.

If an event of default resulting from bankruptcy or other insolvency events occurs, the senior secured notes will become immediately due and payable. If any other event of default occurs and is continuing, holders of at least 50.1% in principal amount of the outstanding notes may at any time declare all the notes then outstanding to be immediately due and payable. If an event of default relating to the nonpayment of principal, make-whole amounts or interest occurs, any holder of

outstanding notes affected by such event of default may declare all the notes held by such holder to be immediately due and payable.

The Partnership was in compliance with all debt covenants at December 31, 2003 and expects to be in compliance with debt covenants for the next twelve months.

Intercreditor and Collateral Agency Agreement. In connection with the execution of the master shelf agreement in June 2003, the lenders under the bank credit facility and the initial purchasers of the senior secured notes entered into an Intercreditor and Collateral Agency Agreement, which was acknowledged and agreed to by our operating partnership and its subsidiaries. This agreement appointed Union Bank of California, N.A. to act as collateral agent and authorized Union Bank to execute various security documents on behalf of the lenders under the bank credit facility and the initial purchasers of the senior secured notes. This agreement specifies various rights and obligations of lenders under the bank credit facility, holders of senior secured notes and the other parties thereto in respect of the collateral securing Crosstex Energy Services, L.P.'s obligations under the bank credit facility and the master shelf agreement.

Other Note Payable. In June 2002, as part of the purchase price of Florida Gas Transmission Company (FGTC), the Partnership issued a note payable for $800,000 to FGTC that is payable in $50,000 annual increments starting June 2003 through June 2006 with a final payment of $600,000 due in June 2007. The note bears interest payable annually at LIBOR plus 1%.

As of December 31, 2003 and 2002, long-term debt consisted of the following (in thousands):

	2003	2002
Acquisition credit facility, interest based at prime plus an applicable margin, interest rate at December 31, 2002 was 4.88%	$ —	$ 1,750
Acquisition credit facility, interest based on LIBOR plus an applicable margin, interest rates at December 31, 2003 and 2002 were 2.92% and 3.95%, respectively	20,000	20,000
Senior secured notes, weighted average interest rate of 6.93%	40,000	—
Note payable to Florida Gas Transmission Company	750	800
	60,750	22,550
Less current portion	(50)	(50)
Debt classified as long-term	$ 60,700	$ 22,500

Maturities for the long-term debt as of December 31, 2003 are as follows (in thousands):

2004	$ 50
2005	50
2006	28,874
2007	10,012
2008	9,412
Thereafter	12,352

In October 2002, the Partnership entered into an interest rate swap covering a principal amount of $20 million for a period of two years. The Partnership is subject to interest rate risk on its acquisition credit facility. The interest rate swap reduces this risk by fixing the LIBOR rate, prior to credit margin, at 2.29%, on $20 million of related debt outstanding over the term of the swap agreement which expires on November 1, 2004. The Company has accounted for this swap as a cash flow hedge of the variable interest payments related to the $20 million of the acquisition credit facility outstanding. Accordingly, unrealized gains or losses relating to the swap which are recorded in other comprehensive income will be reclassified from other comprehensive income to interest expense over the period hedged. The fair value of the interest rate swap at December 31, 2003 was a $209,000 liability and is included in fair value of derivative liabilities.

(7) Income Taxes

The Company provides for income taxes using the liability method. Accordingly, deferred taxes are recorded for the differences between the tax and book basis that will reverse in future periods (in thousands).

	2003	2002	2001
Current tax provision (benefit)	$ 54	$ —	$ (300)
Deferred tax provision (benefit)	10,103	7,451	(994)
	$ 10,157	$ 7,451	$ (1,294)

A reconciliation of the provision for income taxes is as follows (in thousands):

	2003	2002	2001
Federal income tax (benefit) at statutory rate	$ 8,262	$ 4,562	$ (1,409)
Tax basis adjustment in Partnership related to issuance of common units	1,895	2,873	—
Non-deductible expenses (primarily goodwill amortization)	—	16	162
Other	—	—	(47)
Tax provision (benefit)	$ 10,157	$ 7,451	$ (1,294)

The principal components of the Company's net deferred tax liability are as follows (in thousands):

	2003	2002
Deferred income tax assets:		
Net operating loss carryforward	$ 3,162	$ 3,224
Enron reserve	2,386	1,981
Investment in the Partnership	4,433	2,593
Other comprehensive income	—	284
	9,981	8,082
Less: valuation allowance	(4,433)	(2,593)
	5,548	5,489
Deferred income tax liabilities:		
Property, plant, equipment, and intangible assets	(24,913)	(14,177)
Other comprehensive income	(273)	—
Other	(45)	(335)
	(25,231)	(14,512)
Net deferred tax liability	$ (19,683)	$ (9,023)

At December 31, 2003, the Company had a net operating loss carryforward of approximately $9.0 million. This carry-forward can be utilized to offset future taxable income and does not expire until 2023.

Deferred tax liabilities relating to property, plant, equipment and intangible assets represent, primarily, the Company's share of the book basis in excess of tax basis for assets inside of the Partnership. The Company has also recorded a deferred tax asset in the amount of $4.4 million relating to the difference between its book and tax basis of its investment in the Partnership. Because the Company can only realize this deferred tax asset upon the liquidation of the Partnership and to the extent of capital gains, the Company has provided a full valuation allowance against this deferred tax asset.

(8) Retirement Plans

The Company sponsors a single employer 401(k) plan for employees who become eligible upon the date of hire. The Company, as stated within the plan document, will make discretionary contributions at the end of the year. Contributions during 2003, 2002 and 2001 totaled $259,000, $198,000 and $116,000, respectively.

(9) Employee Incentive Plans

(a)

Long-Term Incentive Plan

In December 2002, the Partnership adopted a long-term incentive plan for its employees, directors, and affiliates who perform services for the Partnership. The plan currently permits the grant of awards covering an aggregate of 700,000 common units, 233,000 of which may be awarded in the form of restricted units and 467,000 of which may be awarded in the form of unit options. The plan is administered by the compensation committee of the board of directors of the Partnership's general partner.

(b)

Restricted Units

A restricted unit is a "phantom" unit that entitles the grantee to receive a common unit upon the vesting of the phantom unit, or in the discretion of the compensation committee, cash equivalent to the value of a common unit. In addition, the restricted units will become exercisable upon a change of control of the Partnership, it's general partner, or the Company.

The restricted units are intended to serve as a means of incentive compensation for performance and not primarily as an opportunity to participate in the equity appreciation of the common units. Therefore, plan participants will not pay any consideration for the common units they receive and the Partnership will receive no remuneration for the units.

In May 2003, 48,000 restricted units were issued to senior management under the long-term incentive plan with an intrinsic value of $1,247,000. In September 2003, 1,075 restricted units with an intrinsic value of $39,000 were issued to a director, at his election, for his 2003 annual director fee. These restricted units vest over a five-year period and the intrinsic value of the units is amortized into stock-based compensation expense over the vesting period. The Company recognized stock-based compensation expense of $197,000 related to the amortization of these restricted units in 2003.

(c)

Partnership Unit Options

Unit options will have an exercise price that, in the discretion of the compensation committee, may be less than, equal to or more than the fair market value of the units on the date of grant. In general, unit options granted will become exercisable over a period determined by the compensation committee. In addition, unit options will become exercisable upon a change in control of the Partnership, or its general partner, or the Company.

A summary of the unit option activity for the year ended December 31, 2003 and for the period December 17, 2002 through December 31, 2002 is provided below:

	December 31, 2003		December 31, 2002	
	Number of units	Weighted average exercise price	Number of units	Weighted average exercise price
Outstanding, beginning of period	175,000	$ 20.00	—	—
Granted	147,386	$ 21.22	175,000	$ 20.00
Exercised	—	—	—	—
Forfeited	(750)	$ (20.00)	—	—
Outstanding, end of period	321,636	$ 20.56	175,000	$ 20.00
Options exercisable at end of period	71,667	$ 20.00	—	
Weighted average fair value of options granted		$ 2.56		$ 1.15

Outstanding options have exercise prices ranging from $20 to $36.29 per unit and have a remaining contractual lives of 9 to 10 years at December 31, 2003.

The Company accounts for option grants in accordance with APB No. 25, *Accounting for Stock issued to Employees* and follows the disclosure only provision of SFAS No. 123, *Accounting for Stock-based Compensation*. In September 2003, two directors elected to receive options to purchase 5,376 common units (in aggregate) in the Partnership for their 2003 annual director fees. The options vest over a three-year period with an exercise price of $23.25 per common unit. Since the exercise price was below the market price on the grant date, the Company recorded stock-based compensation of $27,000 in 2003 to recognize the vesting of a portion of such options during 2003.

(d)

Crosstex Energy, Inc.'s Option Plan

The Company has one stock-based compensation plan, the 2000 Stock Option Plan. The Company applies the provisions of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB No. 25), and the related interpretations in accounting for the plan. In accordance with APB No. 25 for fixed rate options, compensation is recorded to the extent the fair value of the stock exceeds the exercise price of the option at the measurement date. In addition, compensation expense is recorded for variable options based on the difference between fair value of the stock or unit and exercise price of the options at period end. Compensation expense of $5,041,000, $41,000, and $0 was recognized in 2003, 2002, and 2001, respectively, related to the Company's stock options.

A summary of the status of the 2000 Stock Option Plan as of December 31, 2003 and 2002, is presented in the table below (all amounts have been adjusted to reflect the two-for-one stock split made by the Company in conjunction with its January 2004 initial public offering):

	December 31, 2003		December 31, 2002	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of period	1,040,500	$ 5.39	681,000	$ 5.16
Granted	—	—	372,500	5.95
Cancelled	(176,110)	—	—	—
Forfeited	(2,000)	6.00	(13,000)	6.00
Outstanding, end of period	862,390	5.42	1,040,500	5.39
Options, exercisable at period end	711,213	5.29	577,006	5.18
Fair value of $5 options granted		N/A		1.59
Fair value of $6 options granted		N/A		0.70
Fair value of $7 options granted		N/A		0.46

All options outstanding have an exercise price ranging from $5 to $7 at December 31, 2003.

CEI modified certain outstanding options attributable to its common shares in the first quarter of 2003, which allowed the option holders to elect to be paid in cash for the modified options based on the fair value of the options. The total number of CEI options which have been modified is approximately 364,000. These modified options have been accounted for using variable accounting as of the option modification date. The Company accounted for the modified options as variable options until the holders elect to cash out the options or the election to cash out the options lapsed. CEI is responsible for paying the intrinsic value of the options for the holders who elect to cash out their options. December 31, 2003 was the last valuation date that a holder of modified options could elect the cash-out alternative. Accordingly, effective January 1, 2004, the remaining modified options will be accounted for as fixed options. Beginning in the first quarter of 2003, the Company recognized stock compensation expense based on the estimated fair value at period end of the options modified. The Company recognized stock-based compensation expense of approximately $5.0 million related to the variable options for the year ended December 31, 2003. As of December 31, 2003, the Company had cashed out $1,378,000 related to the modified options. The final cash out of the modified options totaling $49,000 was paid in February 2004 and is reflected in other current liabilities as of December 31, 2003. The remainder of $3,621,000 has been recorded in paid-in capital.

(e)

Earnings per share and anti-dilutive computations

Basic earnings per common share was computed by dividing net income less preferred dividends, by the weighted-average number of common shares outstanding for the periods presented.

The computation of diluted earnings per common share further assumes the dilutive effect of common share options and the conversion of preferred shares to common shares.

The following are the share amounts used to compute the basic and diluted earnings per common share (in thousands):

	Years Ended December 31,		
	2003	2002	2001
Basic earnings:			
Weighted-average common shares outstanding	3,486	3,766	3,766
Dilutive earnings per unit:			
Weighted-average common shares outstanding	3,486	3,766	3,766

Dilutive effect of exercise of options outstanding	573	235	—
Dilutive effect of preferred stock conversion to common shares	8,212	7,360	—
Dilutive common shares	12.271	11,361	3,766

All outstanding common shares were included in the computation of diluted earnings per common share. Preferred stock was anti-dilutive in the year ended December 31, 2001. Preferred stock was anti-dilutive for periods where the preferred stock dividends exceeded net income.

(10) Fair Value of Financial Instruments

The estimated fair value of the Company's financial instruments has been determined by the Company using available market information and valuation methodologies. Considerable judgment is required to develop the estimates of fair value; thus, the estimates provided below are not necessarily indicative of the amount the Company could realize upon the sale or refinancing of such financial instruments (in thousands).

	December 31, 2003		December 31, 2002	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	$ 1,479	$ 1,479	$ 3,808	$ 3,808
Trade accounts receivable and accrued revenues	134,008	134,008	104,802	104,802
Fair value of derivative assets	4,080	4,080	3,102	3,102
Account receivable from Enron	1,312	1,312	2,467	2,467
Accounts payable, drafts payable and accrued gas purchases	134,266	134,266	110,793	110,793
Long-term debt	60,750	60,750	22,500	22,500
Fair value of derivative liabilities	2,278	2,278	4,458	4,458

The carrying amounts of the Company's cash and cash equivalents, accounts receivable, and accounts payable approximate fair value due to the short-term maturities of these assets and

liabilities. The carrying value of trade accounts receivable includes the reserve for certain Enron receivables (see Note 11).

The Company's long-term debt was comprised of borrowings under a revolving credit facility totaling $20.0 million and $21.75 million as of December 31, 2003 and 2002, respectively, which accrues interest under a floating interest rate structure. Accordingly, the carrying value of such indebtedness approximates fair value for the amounts outstanding under the credit facility. As of December 31, 2003, the Company also had borrowings totaling $40 million under senior secured notes with a weighted average interest rate of 6.93%. The carrying amount of these borrowings approximates the fair value based on market conditions as of December 31, 2003.

The fair value of derivative contracts included in assets or liabilities represents the amount at which the instruments could be exchanged in a current arms-length transaction.

(11) Derivatives

The Company manages its exposure to fluctuations in commodity prices by hedging the impact of market fluctuations. Swaps are used to manage and hedge prices and location risk related to these market exposures. Swaps are also used to manage margins on offsetting fixed-price purchase or sale commitments for physical quantities of natural gas and NGLs.

The fair value of derivative assets and liabilities, excluding the interest rate swap, are as follows (in thousands):

	December 31	
	2003	2002
Fair value of derivative assets—current	$ 4,080	$ 2,947
Fair value of derivative assets—long term	—	155
Fair value of derivative liabilities—current	(2,278)	(4,006)
Fair value of derivative liabilities—long term	—	(271)
Net fair value of derivatives	$ 1,802	$ (1,175)

Set forth below is the summarized notional amount and terms of all instruments held for price risk management purposes at December 31, 2003 (all quantities are expressed in British Thermal Units). The remaining term of the contracts extend no later than December 2004, with no single contract longer than 6 months. The Company's counterparties to hedging contracts include Williams Energy Services Company, Sempra Energy Trading Corp., Morgan Stanley Capital Group, BP Corporation, Duke Field Services, and Duke Energy Trading and Marketing. As discussed in note 2, changes in the fair value of the Company's derivatives related to Producer Services gas marketing activities are recorded in earnings. The effective portion of changes in the fair value of cash flow hedges is recorded in accumulated other comprehensive income until the related anticipated future cash flow is recognized in earnings.

December 31, 2003

Transaction type	**Total volume**	**Pricing terms**	**Remaining term of contracts**	**Fair value (in thousands)**
Cash Flow Hedge:				
Natural gas swaps Cash flow hedge	(2,630,000)	Fixed prices ranging from $4.01 to $6.545 settling against the various Inside FERC Index prices	January-December 2004	$ (563)
Natural gas swaps Cash flow hedge	8,314,000		January-December 2004	2,391
Total natural gas swaps Cash flow hedge				$ 1,828
Producer Services:				
Marketing trading financial swaps	910,000	Fixed prices ranging from $3.14 to $6.24 settling against the various Inside FERC Index prices	January-December 2004	$ 284
Marketing trading financial swaps	(723,000)		January-December 2004	(522)
Total marketing trading financial swaps				$ (238)
Physical offset to marketing trading transactions	(910,000)	Fixed prices ranging from $3.59 to $6.155 settling against the various Inside FERC Index prices	January-December 2004	$ (282)
Physical offset to marketing trading transactions	723,000		January-December 2004	494
Total physical offset to marketing trading transactions swaps				$ 212

On all transactions where the Company is exposed to counterparty risk, the Company analyzes the counterparty's financial condition prior to entering into an agreement, establishes limits, and monitors the appropriateness of these limits on an ongoing basis.

Assets and liabilities related to Producer Services that are accounted for as energy trading contracts are included in the fair value of derivative assets and liabilities. The Company estimates the fair value of all of its energy trading contracts using prices actively quoted. The estimated fair value of energy trading contracts by maturity date was as follows (in thousands):

	Maturity periods			
	Less than one year	**One to two years**	**Two to three years**	**Total fair value**
December 31, 2003	$ (26)	—	—	(26)
December 31, 2002	$ (99)	(81)	—	(180)

Termination of Enron Positions

On December 2, 2001, Enron Corp. and certain subsidiaries, including Enron North America Corp. ("Enron"), each filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Bankruptcy Code. Enron failed to make timely payment of approximately $3.9 million for physical delivery of gas in 2001. This amount remained outstanding as of December 31, 2002. Additionally, the Company had entered into natural gas hedging and physical delivery contracts with Enron. According to the terms of the contract, Enron is liable to the Company for the mark-to-market value of all contracts outstanding on the date the Company exercised its termination right under the contracts, which totaled approximately $4.6 million. The Company has accounted for these contracts as energy trading contracts whereby changes in fair value of the fixed price purchase commitments are recognized in earnings.

The Company had offsets to the above amounts totaling approximately $0.3 million, resulting in a net amount of $8.2 million receivable from Enron at December 31, 2001. Due to the uncertainty of future collections, a charge and related allowance for 70% of the net receivable, or $5.8 million was recorded at December 31, 2001. The 30% recovery factor was management's best estimate based on current market transactions. The ultimate recovery of the Enron receivable is uncertain and may be impacted by many factors including approval of Enron's reorganization plan, litigation against Enron advisors and other third parties and the market which exists for monetizing Enron claims. Based on the reorganization plan filed by Enron in September 2003 and current negotiations with Enron, the Company expects to recover approximately $1.3 million of its receivable from Enron through the bankruptcy process. Therefore, the Company has written the receivable down to $1.3 million as of December 31, 2003. Due to the uncertainty of the timing of recovery of this receivable due to Enron's bankruptcy, the Company has classified this receivable as long-term. Further adjustments to the Enron receivable will be recognized in earnings when management believes recovery of the asset is assured or additional reserves warranted.

For the year ended December 31, 2001, the Company recorded a loss on energy trading contracts related to natural gas marketing of $5.8 million, substantially all of which relates to estimated losses on claims from Enron. This loss was partially offset by gains of $1.9 million on energy trading contracts which physically settled during 2001.

(12) Transactions with Related Parties

Camden Resources, Inc.

The Partnership treats gas for, and purchases gas from, Camden Resources, Inc. (Camden). Camden is an affiliate of the Partnership by way of equity investments made by Yorktown in Camden. During the years ended December 31, 2003, 2002 and 2001, the Partnership purchased natural gas from Camden in the amount of approximately $8,416,000, $10,076,000, and $17,300,000, respectively, and received approximately $190,000, $399,000, and $737,000 in treating fees from Camden.

Crosstex Pipeline Partners, L.P.

The Partnership had related-party transactions with Crosstex Pipeline Partners, L.P. (CPP), as summarized below:

- During the years ended December 31, 2003, 2002 and 2001, the Partnership bought natural gas from CPP in the amount of approximately $8.2 million, $3.4 million and $6.5 million and paid for transportation of approximately $41,000, $27,500 and $31,000, respectively, to CPP.

- During the years ended December 31, 2003, 2002 and 2001, the Partnership received a management fee from CPP in the amount of approximately $125,000 for each year.

- During the years ended December 31, 2003, 2002 and 2001, the Partnership received distributions from CPP in the amount of approximately $104,000, $90,000 and $152,000, respectively.

Crosstex Denton County Gathering J.V.

- During the year ended December 1, 2003, the Company received a management fee from Crosstex Denton County Gathering J.V. (CDC) of $110,000. Also, see Note (5) for a discussion of loans related to CDC.

(13) Commitments and Contingencies

(a)

Leases

Leased office space and equipment have remaining non-cancelable lease terms in excess of one year. The following table summarizes our remaining non-cancelable future payments under operating leases as of December 31, 2003 (in thousands):

2004	$ 1,228
2005	1,091
2006	960
2007	811
2008	684
Thereafter	852
	$ 5,626

Operating lease rental expense for the years ended December 31, 2003, 2002, and 2001 was approximately $1,812,000, $951,000 and $1,200,000, respectively.

(b)

Employment Agreements

Each member of senior management of the Company is a party to an employment contact with the general partner. The employment agreements provide each member of senior management with severance payments in certain circumstances and prohibit each such person from competing with the

general partner or its affiliates for a certain period of time following the termination of such person's employment.

(c)

Environmental Issues

The Partnership acquired two assets from DEFS in June 2003 that have environmental contamination, including a gas plant in Montgomery County near Conroe, Texas and a compressor station near Cadeville, Louisiana. At both of these sites, contamination from historical operations has been identified at levels that exceed the applicable state action levels. Consequently, site investigation and/or remediation are underway to address those impacts. The estimated remediation cost for the Conroe plant site is currently estimated to be approximately $3.2 million, and the remediation cost for the Cadeville site is currently estimated to be approximately $1.2 million. Under the purchase agreement, DEFS has retained liability for cleanup of both the Conroe and Cadeville sites. Moreover, the remediation costs associated with the Conroe site will be covered by agreements with TRC Companies and AIG. Therefore, the Company does not expect to incur any material environmental liability associated with the Conroe or Cadeville sites.

(d)

Other

The Company is involved in various litigation and administrative proceedings arising in the normal course of business. In the opinion of management, any liabilities that may result from these claims would not individually or in the aggregate have a material adverse effect on its financial position or results of operations.

The Partnership receives notices from pipeline companies from time to time of gas volume allocation corrections related to gas deliveries on their pipeline systems. These allocation corrections normally have little impact on the Partnership's gross margin because the Partnership balances its purchases and sales in the pipelines and both the purchase and sale on the pipeline system require corrections. At December 31, 2003, a subsidiary of the Partnership was involved in a dispute related to one such allocation correction with a pipeline company and a customer on that pipeline. In reallocating previous settled deliveries, the pipeline company billed the Partnership's subsidiary for approximately $1.2 million of gas deliveries, that occurred in the period from December, 2000 through February, 2001. The Partnership's subsidiary, in turn, billed its customer who was overpaid due to the allocation error. The customer is disputing its liability for such amount, asserting that the corrected billing was untimely.. The allocation error occurred prior to the Partnership's acquisition of the subsidiary involved in the dispute. The Company has an indemnity from the seller of the subsidiary for liabilities arising prior to the acquisition date. As of December 31, 2003, the Company has recorded a receivable of $1.2 million in other current receivables and a liability of $1.2 million in other current liabilities related to this allocation correction. The Partnership believes the customer's dispute of the receivable is without merit, and further believes that it is protected against loss by its right to indemnification.

(14) Capital Stock

(a)

Convertible Preferred Stock

The Company has authorized 3,500,000 shares of Convertible Preferred Stock—A, 1,000,000 shares of Convertible Preferred Stock—B and 3,000,000 shares of Convertible Preferred Stock—C, all shares with $.01 par values. At December 31, 2003 and 2002 the Company had 2,579,743 shares of Convertible Preferred Stock—A issued and outstanding. The Company issued 491,663 Convertible Preferred Stock—B shares for cash in 2001 and issued 10,000 shares for $12,000 in cash and $108,000 in shareholder notes receivable in August 2003. At December 31, 2003 and 2002 the Company had 523,899 and 513,899 shares, respectively, of Convertible Preferred Stock—B issued and outstanding. The Company issued 1,000,000 Convertible Preferred Stock—C shares for cash in 2002 and issued 20,000 shares for $28,000 in cash and $252,000 in shareholder notes receivable in August 2003. At December 31, 2003 and 2002 the Company had 1,020,000 and 1,000,000 shares of Convertible Preferred Stock—C Shares issued and outstanding for the respective periods. All preferred shares accrue dividends at a rate of 7.5% per year. The dividends can either be paid in cash or additional shares of preferred stock at the Company's election. The Company paid the 2000 and 2001 dividends in preferred stock. The Company paid the 2002 dividends in cash in June and September 2003 and paid the 2003 dividends in cash in January 2004.

In January 2004, the Company converted all its preferred stock to common stock in conjunction with its initial public offering discussed in Note 1(b).

(b)

Common Stock

The Company has authorized 7,000,000 shares of common stock at $.01 par value. At December 31, 2003 and 2002 the Company had 1,882,772 and 1,743,032 shares, respectively, issued and outstanding. In January 2003, certain members of management redeemed 139,740 common shares for $2.5 million ($17.89 per common share) representing management's estimate of the fair value of the stock at redemption.

In January 2004, the Company made a two-for-one stock split in conjunction with its initial public offering discussed in Note 1(b) and increased the number of authorized common shares to shares.

(c)

Notes Receivable

Shares of common stock and preferred stock have been sold to certain members of management in return for notes receivable. The notes receivable are guaranteed by the related stock and bear interest. The common stock and preferred stock sold to management were sold at fair value as evidenced by the price paid by third parties. Accordingly, no compensation expense has been recorded on the stock sold to management. The stockholder notes receivable have been reflected as a reduction to stockholders' equity.

In January 2004, $4.9 million in stockholder notes receivable were repaid in conjunction with the Company's initial public offering discussed in Note 1(b).

(15) Segment Information

Identification of operating segments is based principally upon differences in the types and distribution channel of products. The Company's reportable segments consist of Midstream and Treating. The Midstream division consists of the Company's natural gas gathering and transmission operations and includes the Mississippi System, the Conroe System, the Gulf Coast System, the Corpus Christi System, the Gregory gathering system located around the Corpus Christi area, the Arkoma System in Oklahoma, the Vanderbilt System and various other small systems. Also included in the Midstream division are the Company's

Producer Services operations (note 2(i)). The Treating division generates fees from its plants either through volume-based treating contracts or though fixed monthly payments. Included in the Treating division are four gathering systems that are connected to the treating plants.

The accounting policies of the operating segments are the same as those described in note 2 of the Notes to Consolidated Financial Statements. The Company evaluates the performance of its operating segments based on earnings before gain or issuance of units by CELP, income taxes, interest of non-controlling partners in CELP's net income and accounting changes, and after an allocation of corporate expenses. Corporate expenses are allocated to the segments on a pro rata basis based on assets. Intersegment sales are at cost.

Summarized financial information concerning the Company's reportable segments is shown in the following table. There are no other significant non-cash items.

	Midstream	Treating	Totals
		(In thousands)	
Year ended December 31, 2003:			
Sales to external customers	$ 993,140	$ 20,523	$ 1,013,663
Intersegment sales	6,893	(6,893)	—
Interest expense	3,040	63	3,103
Stock based compensation	4,276	1,069	5,345
Depreciation and amortization	10,600	2,942	13,542
Segment profit	8,900	1,526	10,426
Segment assets	326,439	43,299	369,738
Capital expenditures	28,728	10,275	39,003
Year ended December 31, 2002:			
Sales to external customers	$ 437,676	$ 14,817	$ 452,493
Intersegment sales	4,073	(4,073)	—
Interest expense	2,039	342	2,381
Impairments	—	4,175	4,175
Depreciation and amortization	5,738	2,007	7,745
Segment profit (loss)	3,133	(1,055)	2,078
Segment assets	205,645	35,031	240,676
Capital expenditures	11,154	3,391	14,545
Year ended December 31, 2001:			
Sales to external customers	$ 362,673	$ 24,353	$ 387,026
Intersegment sales	10,633	(10,633)	—
Interest expense	1,840	413	2,253
Impairments	2,873	—	2,873
Depreciation and amortization	4,611	1,597	6,208
Segment profit (loss)	(4,714)	689	(4,025)
Segment assets	139,129	32,240	171,369
Capital expenditures	6,484	16,201	22,685

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(16) Quarterly Financial Data (Unaudited)

Summarized unaudited quarterly financial data is presented below.

	First	Second	Third	Fourth	Total
			(In thousands)		
2003:					
Revenues	$ 250,570	$ 229,252	$ 283,198	$ 250,643	$ 1,013,663
Operating income(1)	605	3,631	4,047	5,067	13,350
Net income (loss)	30	1,091	11,376(2)	951	13,448
Basic earnings per common share	(0.25)	0.05	3.01	0.02	2.83
Diluted earnings per common share	(0.25)	0.05	0.92	0.02	1.10
2002:					
Revenues	$ 80,993	$ 126,480	$ 114,611	$ 130,409	$ 452,493
Operating income(1)	4,681	5,468	6,182	5,934	22,265
Net income (loss)	(119)(3)	189	1,028	4,484(4)	5,582
Basic earnings per common share	(0.19)	(0.13)	0.04	0.96	0.68
Diluted earnings per common share	(0.19)	(0.13)	0.04	0.37	0.49

(1)

Operating income is defined as revenues less purchased gas less operating expenses.

(2) Included in the 2003 third quarter results is a $18.4 million (before taxes) gain related to the issuance of additional common units in the Partnership's September 2003 follow-on offering.

(3) Included in the 2002 first quarter results is an impairment charge of $3.2 million related to the impairment of certain intangibles related to gas plants.

(4) Included in the 2002 fourth quarter results is an impairment of $1.0 million related to the impairment of certain intangibles related to gas plants and an $11.1 million (before taxes) gain related to the issuance of additional common units in the Partnership's 2002 offering of common units.

SCHEDULE I

CROSSTEX ENERGY, INC. (PARENT COMPANY)

CONDENSED BALANCE SHEETS

(In thousands)

	December 31, 2003	December 31, 2002
Assets		
Current assets:		
Cash and cash equivalents	$ 1,313	$ 2,500
Federal income tax refund receivable	—	400
Prepaid expenses and other	75	—
Total current assets	1,388	2,900
Investment in the Partnership	89,680	63,244
Investment in subsidiary	7,459	8,488
Other non-current assets	465	—
Total assets	$ 98,992	$ 74,632
Liabilities and Stockholders' Equity		
Current liabilities:		
Accrued taxes payable	$ —	$ —
Preferred dividend payable	3,471	3,021
Payable to the Partnership	886	104
Other accrued liabilities	49	—
Total current liabilities	4,406	3,125
Deferred tax liability	19,683	9,023
Stockholders' equity:		
Convertible preferred stock	42	42
Common stock	19	19
Additional paid-in capital	68,934	64,913
Retained earnings	7,902	(1,962)
Treasury stock, at cost	(2,500)	—
Accumulated other comprehensive income	506	(528)
Total stockholders' equity	74,903	62,484
Total liabilities and stockholders' equity	$ 98,992	$ 74,632

See "Notes to Consolidated Financial Statements" of Crosstex Energy, Inc. included in this report.

Schedule I (continued)

CROSSTEX ENERGY, INC. (PARENT COMPANY)

CONDENSED STATEMENTS OF OPERATIONS

(In thousands except share data)

	Years Ended December 31,		
	2003	2002	2001
Operating income and expenses:			
Income (loss) from investment in the Partnership	$ 10,045	$ 1,903	$ (4,025)
(Loss) from investment in subsidiary	(1,252)	(11)	—
General and administrative	(3,542)	(150)	—
Operating income (loss)	5,251	1,742	(4,025)
Other income (expense):			
Interest income	(6)	337	—
Other expense	—	(100)	—
Gain on issuance of units in the Partnership	18,360	11,054	—
Income tax provision benefit (expense)	(10,157)	(7,451)	1,294
Total other income and expense	8,197	3,840	1,294
Net income (loss)	$ 13,448	$ 5,582	$ (2,731)
Earnings (loss) per share:			
Basic	$ 2.83	$ 0.68	$ (1.25)
Diluted	$ 1.10	$ 0.49	$ (1.25)

See "Notes to Consolidated Financial Statements" of Crosstex Energy, Inc. included in this report.

Schedule I (continued)

CROSSTEX ENERGY, INC. (PARENT COMPANY)

CONDENSED STATEMENTS OF CASH FLOW

(In thousands)

	Years Ended December 31,		
	2003	2002	2001
Cash flows from operating activities:			
Net income (loss)	$ 13,448	$ 5,582	$ (2,731)
Adjustments to reconcile net income (loss) to net cash flow provided by (used in) operating activities:			
(Income) loss from investment in the Partnership	(10,045)	(1,903)	4,025
(Income) loss from investment in subsidiary	1,252	11	—
Deferred taxes	10,103	7,451	(994)
Stock-based compensation	—	41	—
Gain on issuance of units in the Partnership	(18,360)	(11,054)	—
Changes in assets and liabilities:			
Accounts receivable	400	—	(400)

Prepaid expenses and other	(539)	299	(198)
Accounts payable and other accrued liabilities	780	46	(200)
Net cash provided by (used in) operating activities	(2,961)	473	(498)
Cash flows from investing activities:			
Investment in the Partnership	(1,263)	(14,000)	(4,964)
Distributons from the Partnership	9,872	2,500	442
Investment in subsidiary	137	—	—
Net cash provided by (used in) investing activities	8,746	(11,500)	(4,522)
Cash flows from financing activities:			
Issuance of preferred stock	40	14,000	5,020
Increase in shareholder note receivables	—	(473)	—
Dividends due to shareholders	(3,134)	—	—
Redemptions of stock options for cash	(1,378)	—	—
Purchase of treasury stock	(2,500)	—	—
Net cash provided by (used in) financing activities	(6,972)	13,527	5,020
Net increase (decrease) in cash	(1,187)	2,500	—
Cash, beginning of year	2,500	—	—
Cash, end of year	$ 1,313	$ 2,500	$ —

See "Notes to Consolidated Financial Statements" of Crosstex Energy, Inc. included in this report.

SCHEDULE II

CROSSTEX ENERGY, INC.

VALUATION AND QUALIFYING ACCOUNTS

(in thousands)

	Balance at Beginning of Period	Additions: Charged to Costs and Expenses	Additions: Charged to Other Accounts	Deductions	Balance at End of Period
Year Ended December 31, 2003:					
For doubtful receivables classified as non-current assets	$ 5,776	1,155	—	—	$ 6,931
Year Ended December 31, 2002:					
For doubtful receivables classified as non-current assets	$ 5,776	—	—	—	$ 5,776
Year Ended December 31, 2001:					
For doubtful receivables classified as non-current assets	$ —	5,776(a)	—	—	$ 5,776

(a) Allowance for doubtful receivables on energy trading contracts related to natural gas marketing, substantially all of which relates to estimated losses from Enron claims. See Note 11 to Consolidated Financial Statements.

Item 16. Exhibits.

(a)

The following documents are filed as exhibits to this registration statement:

Exhibit		
3.1*	—	Restated Certificate of Incorporation of Crosstex Energy, Inc.
3.2*	—	Restated Bylaws of Crosstex Energy, Inc.
3.3	—	Certificate of Limited Partnership of Crosstex Energy, L.P (incorporated by reference from Exhibit 3.1 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.4	—	Amended and Restated Agreement of Limited Partnership of Crosstex Energy, L.P., dated as of December 17, 2002 (incorporated by reference from Exhibit 3.2 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
3.5	—	Certificate of Limited Partnership of Crosstex Energy Services, L.P. (incorporated by reference from Exhibit 3.3 to Amendment No. 2 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed November 4, 2002)
3.6	—	Amended and Restated Agreement of Limited Partnership of Crosstex Energy Services, L.P., dated as of December 17, 2002 (incorporated by reference from Exhibit 3.4 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
3.7	—	Certificate of Limited Partnership of Crosstex Energy GP, L.P. (incorporated by reference from Exhibit 3.5 to Crosstex Energy, L.P.'s Registration Statement, file No. 333-97779, filed August 7, 2002)
3.8	—	Agreement of Limited Partnership of Crosstex Energy GP, L.P., dated as of July 12, 2002 (incorporated by reference from Exhibit 3.6 to Crosstex Energy L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.9	—	Certificate of Formation of Crosstex Energy GP, LLC (incorporated by reference from Exhibit 3.7 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-97779, filed August 7, 2002)
3.10	—	Amended and Restated Limited Liability Company Agreement of Crosstex Energy GP, LLC, dated as of December 17, 2002 (incorporated by reference from Exhibit 3.8 from Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
3.11	—	Amended and Restated Certificate of Formation of Crosstex Holdings GP, LLC (incorporated by reference from Exhibit 3.11 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.12	—	Limited Liability Company Agreement of Crosstex Holdings GP, LLC, dated as of October 27, 2003 (incorporated by reference from Exhibit 3.12 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.13	—	Certificate of Formation of Crosstex Holdings LP, LLC (incorporated by reference from Exhibit 3.13 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.14	—	Limited Liability Company Agreement of Crosstex Holdings LP, LLC, dated as of November 4, 2003 (incorporated by reference from Exhibit 3.14 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.15	—	Amended and Restated Certificate of Limited Partnership of Crosstex Holdings, L.P. (incorporated by reference from Exhibit 3.15 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
3.16	—	Agreement of Limited Partnership of Crosstex Holdings, L.P., dated as of November 4, 2003 (incorporated by reference from Exhibit 3.16 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
4.1	—	Specimen Certificate representing shares of common stock (incorporated by reference from Exhibit 4.1 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
10.1	—	Omnibus Agreement, dated December 17, 2002, among Crosstex Energy, Inc. and certain other parties (incorporated by reference from Exhibit 10.5 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.2*	—	Form of Indemnity Agreement, entered into with directors and/or officers on December 31, 2003
10.3+	—	Crosstex Energy GP, LLC Long-Term Incentive Plan dated July 12, 2002 (incorporated by reference from Exhibit 10.4 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.4*	—	Agreement Regarding 2003 Registration Rights Agreement and Termination of Stockholders' Agreement, dated October 27, 2003
10.5*+	—	Crosstex Energy, Inc. Long-Term Incentive Plan, dated December 31, 2003
10.6*	—	Registration Rights Agreement, dated December 31, 2003
10.7	—	Second Amended and Restated Credit Agreement, dated November 26, 2002, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated reference from Exhibit 10.1 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.8	—	First Amendment to Second Amended and Restated Credit Agreement dated as of June 3, 2003, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated by reference from Exhibit 10.2 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
10.9	—	Second Amendment to Second Amended and Restated Credit Agreement, dated as of June 3, 2003, among Crosstex Energy Services, L.P., Union Bank of California, N.A. and certain other parties (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 10, 2004)
10.10	—	$50,000,000 Senior Secured Notes Master Shelf Agreement as of June 3, 2003 (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Registration Statement on Form S-1, file No. 333-106927, filed July 10, 2003)
10.11	—	First Contribution, Conveyance and Assumption Agreement dated November 27, 2002, among Crosstex Energy, L.P. and certain other parties (incorporated by reference from Exhibit 10.2 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.12	—	Closing Contribution, Conveyance and Assumption Agreement dated December 11, 2002, among Crosstex Energy, L.P. and certain other parties (incorporated by reference from Exhibit 10.3 to Crosstex Energy, L.P.'s Annual Report on Form 10-K, file No. 000-50067, filed March 25, 2003)
10.13	—	Crosstex Energy Holdings Inc. 2000 Stock Option Plan (incorporated by reference from Exhibit 10.14 to Amendment No. 2 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed December 30, 2003)
21.1	—	List of Subsidiaries (incorporated by reference from Exhibit 21.1 to Crosstex Energy, Inc.'s Registration Statement on Form S-1, file No. 333-110095, filed October 30, 2003)
31.1*	—	Certification of the principal executive officer
31.2*	—	Certification of the principal financial officer
32.1*	—	Certification of the principal executive officer and the principal financial officer of the Company pursuant to 18 U.S.C. Section 1350

* Filed herewith.

+ Compensatory benefit plan or arrangement in which directors and executive officers are eligible to participate.

Exhibit 3.1

RESTATED CERTIFICATE OF INCORPORATION

OF

CROSSTEX ENERGY, INC.

Crosstex Energy, Inc., a corporation organized and existing under the laws of the State of Delaware (the "Corporation"), does hereby certify:

1. The name of the corporation is Crosstex Energy, Inc.

2. The original Certificate of Incorporation was filed with the Secretary of State of the State of Delaware on April 28, 2000 under the corporation's original name Crosstex Energy Holdings Inc.

3. This Restated Certificate of Incorporation restates, integrates and amends the Certificate of Incorporation of the Corporation, and has been duly adopted and approved by the Board of Directors of the Corporation and its stockholders in accordance with Sections 242 and 245 of the Delaware General Corporation Law.

4. The Restated Certificate of Incorporation shall not become effective until 10:58 a.m., Eastern Time, on January 16, 2004.

5. The Restated Certificate of Incorporation so adopted reads as follows.

FIRST: The name of the corporation is Crosstex Energy, Inc.

SECOND: The address of its registered office in the State of Delaware is Corporation Trust Center, 1209 Orange Street, Wilmington, County of New Castle, Delaware 19801. The name of its registered agent at such address is The Corporation Trust Company.

THIRD: The nature of the business or purpose to be conducted or promoted is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of the State of Delaware.

FOURTH: The total number of shares of all classes of stock which the Corporation shall have authority to issue is 20,000,000 shares, consisting solely of (i) 19,000,000 shares of Common Stock, par value $0.01 per share (the "Common Stock"), and (ii) 1,000,000 shares of Preferred Stock, par value $0.01 per share (the "Preferred Stock").

The following is a statement of the designations and the powers, preferences and rights, and the qualifications, limitations or restrictions thereof, of the classes of stock of the Corporation:

(a) *Common Stock*.

(i) *Dividends*. After the requirements with respect to preferential dividends on Preferred Stock, if any, shall have been met and after the Corporation shall have complied with all the requirements, if any, with respect to the setting aside of sums as sinking funds or redemption or purchase accounts and subject further to any other conditions which may be fixed in accordance with the provisions of this Certificate of Incorporation, then, but not otherwise, the holders of the Common Stock shall be entitled to receive such dividends, if any, as may be declared from time to time by the Board of Directors on the Common Stock, which dividends shall be paid out of assets legally available for the payment of dividends and shall be distributed among the holders of shares of the Common Stock pro rata in accordance with the number of shares of such stock held by each such holder.

(ii) *Liquidation*. After distribution in full of the preferential amount, if any, to be distributed to the holders of Preferred Stock in the event of voluntary or involuntary liquidation, distribution or sale of assets, dissolution or winding-up of the Corporation, the holders of the Common Stock shall be entitled to receive all the remaining assets of the Corporation, tangible and intangible, of whatever kind available for distribution to stockholders, which assets shall be distributed pro rata in accordance with the number of shares of such stock held by each such holder.

(iii) *Voting*. Except as may otherwise be required by law or the provisions of the resolution or resolutions as may be adopted by the Board of Directors pursuant to subsection (b) of this Article FOURTH, each holder of Common Stock shall have one vote in respect of each share of Common Stock held by such holder on each matter voted upon by the stockholders.

(b)

Preferred Stock.

Shares of Preferred Stock may be issued from time to time in one or more series as from time to time may be determined by the Board of Directors of the Corporation. Each series shall be distinctly designated. The Board of Directors of the Corporation is hereby expressly granted authority to fix, by resolution or resolutions adopted prior to the issuance of any shares of each particular series of Preferred Stock, the designation, powers, preferences and relative, participating, optional or other special rights, and the qualifications, limitations or restrictions thereof, if any, of such series, including, but without limiting the generality of the foregoing, the following:

(i) the designation of, and the number of shares of Preferred Stock which shall constitute, the series, which number may be increased (except as otherwise fixed by the Board of Directors, and in any event not above the total number of authorized shares of the class) or decreased (but not below the number of shares thereof then outstanding) from time to time by action of the Board of Directors;

(ii) the rate and times at which (or the method of determination thereof), and the terms and conditions upon which, dividends, if any, on shares of the series shall be paid, the nature of any preferences or the relative rights of priority of such dividends to the dividends payable on any other class or classes of stock of the Corporation or on any other series of Preferred Stock, and a statement whether such dividends shall be cumulative;

(iii) whether shares of the series shall be convertible into or exchangeable for shares of capital stock or other securities or property of the Corporation or of any other corporation or entity, and, if so, the terms and conditions of such conversion or exchange, including any provisions for the adjustment of the conversion or exchange rate in such events as the Board of Directors shall determine;

(iv) whether shares of the series shall be redeemable, and, if so, the terms and conditions of such redemption, including the date or dates upon or after which they shall be redeemable, and the amount and type of consideration payable in case of redemption, which amount may vary under different conditions and at different redemption dates;

(v) the rights, if any, of the holders of shares of the series upon voluntary or involuntary liquidation, merger, consolidation, distribution or sale of assets, dissolution or winding-up of the Corporation;

(vi) whether shares of the series shall have a sinking fund or purchase account for the redemption or purchase of shares of the series, and, if so, the terms, conditions and amount of such sinking fund or purchase account;

(vii) whether shares of the series shall have voting rights in addition to the voting rights provided by law, which may, without limiting the generality of the foregoing, include (A) the right to more or less than one vote per share on any or all matters voted upon by the Corporation's stockholders and (B) the right to vote, as a series by itself or together with other series of Preferred Stock or together with all series of Preferred Stock as a class or with the Common Stock as a class, upon such matters, under such circumstances and upon such conditions as the Board of Directors may fix, including, without limitation, the right, voting as a series by itself or together with other series of Preferred Stock or together with all series of Preferred Stock as a class, to elect one or more directors of the Corporation in the event there shall have been a default in the payment of dividends on any one or more series of Preferred Stock or under such other circumstances and upon such conditions as the Board of Directors may determine; and

(viii) any other powers, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions, of shares of that series.

The relative powers, preferences and rights of each series of Preferred Stock in relation to the powers, preferences and rights of each other series of Preferred Stock shall, in each case, be as fixed from time to time by the Board of Directors in the resolution or resolutions adopted pursuant to the authority granted in this subsection (b), and the consent, by class or series vote or otherwise, of the holders of Preferred Stock or such of the series of the Preferred Stock as are from time to time outstanding shall not be required for the issuance by the Corporation of any other series of Preferred Stock, whether the powers, preferences and rights of such other series shall be fixed by the Board of Directors as senior to, or on a parity with, the powers, preferences and rights of such outstanding series, or any of them; provided, however, that the Board of Directors may provide in such resolution or resolutions adopted with respect to any series of Preferred Stock that the consent of the holders of a majority (or such greater proportion as shall be therein fixed) of the outstanding shares of such series voting thereon shall be required for the issuance of any or all other series of Preferred Stock.

FIFTH: The following provisions are inserted for the management of the business and for the conduct of the affairs of the Corporation, and for further definition, limitation and regulation of the powers of the Corporation and of its directors and stockholders:

(a) *Management*. The business and affairs of the Corporation shall be managed by or under the direction of the Board of Directors.

(b) *Number of Directors*. Subject to the rights of the holders of any series of Preferred Stock to elect additional directors under specified circumstances, the directors shall be divided into three classes (I, II, and III), as nearly equal in number as possible, and no class shall include less than one director. The initial term of office for members of Class I shall expire at the annual meeting of stockholders in 2005; the initial term of office for members of Class II shall expire at the annual meeting of stockholders in 2006; and the initial term of office for members of Class III shall expire at the annual meeting of stockholders in 2007. At each annual meeting of stockholders beginning in 2005, directors elected to succeed those directors whose terms expire shall be elected for a term of office to expire at the third succeeding annual meeting of stockholders after their election. The number of directors of the Corporation, having initially been established at three, may be changed to any number not less than three nor more than nine as fixed from time to time by or pursuant to the Bylaws of the Corporation. Each director, other than a director who may be elected by the holders of any series of Preferred Stock under specified circumstances, shall hold office until his successor is elected and qualified or until his earlier resignation or removal. Election of directors need not be by written ballot unless the Bylaws of the Corporation so provide. No action shall be taken by the directors (whether through amendment to the Bylaws or otherwise) to increase the number of directors unless at least 67% of the directors then in office shall concur in said action.

(c) *Stockholder Nomination of Directors and Introduction of Business*. Advance notice of stockholder nominations for the election of directors and of business to be brought by stockholders before any meeting of the stockholders of the Corporation shall be given in the manner and to the extent provided in the Bylaws of the Corporation.

(d) *Bylaws*. In furtherance and not in limitation of the powers conferred by law, the Board of Directors is expressly authorized to adopt, alter, amend and repeal the Bylaws of the Corporation, subject to the power of the stockholders of the Corporation to adopt, alter, amend and repeal the Bylaws. Notwithstanding the foregoing and anything contained herein to the contrary, Sections 2, 7 and 8 of Article II and Article VI of the Bylaws shall not be altered, amended or repealed and no provision inconsistent therewith shall be adopted without the affirmative vote of the holders of at least 67% of the shares of the capital stock of the Corporation entitled to vote, voting together as a single class.

(e) *Powers of Directors*. In addition to the powers and authority hereinbefore or by statute expressly conferred upon them, the directors are hereby empowered to exercise all such powers and do all such acts and things as may be exercised or done by the Corporation, subject, nevertheless, to the provisions of the statutes of Delaware, this Certificate of Incorporation and any Bylaws adopted by the stockholders; provided, however, that no Bylaws thereafter adopted by the stockholders shall invalidate any prior act of the directors which would have been valid if such Bylaws had not been adopted.

SIXTH: Whenever a compromise or arrangement is proposed between the Corporation and its creditors or any class of them and/or between the Corporation and its stockholders or any class of them, any court of equitable jurisdiction within the State of Delaware may, on the application in a summary way of the Corporation or of any creditor or stockholder thereof or on the application of any receiver or receivers appointed for the Corporation under the provisions of Section 291 of Title 8 of the Delaware Code or on the application of trustees in dissolution or of any receiver or receivers appointed for the Corporation under the provisions of Section 279 of Title 8 of the Delaware Code order a meeting of the creditors or class of creditors, and/or of the stockholders or class of stockholders of the Corporation, as the case may be, to be summoned in such manner as the said court directs. If a majority in number representing three fourths in value of the creditors or class of creditors, and/or of the stockholders or class of stockholders of the Corporation, as the case may be, agree to any compromise or arrangement and to any reorganization of the Corporation as a consequence of such compromise or arrangement, the said compromise arrangement and the said reorganization shall, if sanctioned by the court to which the said application has been made, be binding on all the creditors or class of creditors and/or on all the stockholders or class of stockholders, of the Corporation, as the case may be, and also on the Corporation.

SEVENTH: (a) *Elimination of Certain Liability of Directors*. To the fullest extent permitted by the Delaware General Corporation Law as the same exists or may hereafter be amended, a director of the Corporation shall not be personally liable to the Corporation or its stockholders for monetary damages for breach of duty as a director. Without limiting the foregoing in any respect, a director of the Corporation shall not be personally liable to the Corporation or its stockholders for monetary damages for breach of duty as a director, except for liability (i) for any breach of the director's duty of loyalty to the Corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived an improper personal benefit. If the Delaware General Corporation Law is amended to authorize corporate action further eliminating or limiting the personal liability of directors, then the liability of a director of the Corporation shall be eliminated or limited to the fullest extent permitted by the Delaware General Corporation Law, as so amended. Any repeal or modification of this provision shall not adversely affect any right or protection of a director of the Corporation existing at the time of such repeal or modification.

(b)

Indemnification and Insurance.

(i) *Right to Indemnification*. Each person who was or is made a party or is threatened to be made a party to or is involved in any action, suit or proceeding, whether civil, criminal, administrative or investigative (hereinafter a "proceeding"), by reason of the fact that he or she, or a person of whom he or she is the legal representative, is or was a director or officer of the Corporation, or serves, in any capacity, any corporation, partnership or other entity in which the Corporation has a partnership or other interest, including service with respect to employee benefit plans, whether the basis of such proceeding is alleged action in an official capacity as a director, officer, employee or agent or in any other capacity while serving as a director, officer, employee or agent, shall be indemnified and held harmless by the Corporation to the fullest extent authorized by the Delaware General Corporation Law, as the same exists or may hereafter be amended (but, in case of any such amendment, only to the extent that such amendment permits the Corporation to provide broader indemnification rights than said law permitted the Corporation to provide prior to such amendment), against all expense, liability and loss reasonably incurred or suffered by such person in connection therewith and such indemnification shall continue as to a person who has ceased to be a director, officer, employee or agent and shall inure to the benefit of his or her heirs, executors and administrators; provided, however, the Corporation shall indemnify any such person seeking indemnification pursuant to this subsection in connection with a proceeding (or part thereof) initiated by such person only if such proceeding (or part thereof) was authorized by the Board of Directors of the Corporation. The Corporation may, by action of its Board of Directors, provide indemnification to employees or agents of the Corporation with the same scope and effect as the foregoing indemnification of directors and officers.

(ii) *Nonexclusivity of Rights*. The right to indemnification and the payment of expenses incurred in defending a proceeding in advance of its final disposition conferred in this Article SEVENTH shall not be exclusive of any right which any person may have or hereafter acquire under any statute, provision of the Certificate of Incorporation, by-law, agreement, vote of stockholders or disinterested directors or otherwise.

(iii) *Insurance*. The Corporation may maintain insurance, at its expense, to protect itself and any director officer, employee or agent of the Corporation or another corporation, partnership, joint venture, trust or other enterprise against any such expense, liability or loss, whether or not the corporation would have the power to indemnify such person against such expense, liability or loss under the Delaware General Corporation Law.

(iv) *Severability*. If any subsection of this Section (b) of this Article SEVENTH shall be deemed to be invalid or ineffective in any proceedings, the remaining subsections hereof shall not be affected and shall remain in full force and effect.

EIGHTH: The Corporation shall not, without first obtaining the affirmative vote of the holders of at least 67% of the shares of capital stock of the Corporation issued and outstanding and entitled to vote, voting together as a single class, sell all or substantially all of its assets, or merge into or consolidate with any other entity, or effect any transaction or series of related transactions in which the Corporation's stockholders as constituted immediately prior to such transaction or series of related transactions own immediately after such transaction or series of related transactions less than a majority of the voting power of the surviving or acquiring entity.

NINTH: The stockholders of the Corporation shall not be permitted to take any action without a meeting and only the Board of Directors of the Corporation shall be permitted to call a meeting of stockholders.

TENTH: (a) *Higher Vote Required for Certain Related Party Business Combinations*

(i) In addition to any affirmative vote required by law or under this Restated Certificate of Incorporation, and except as otherwise expressly provided in subsection (b) of this Article TENTH, any Related Party Business Combination (as hereinafter defined) shall require the affirmative vote of the holders of at least 67% of the Voting Stock (as hereinafter defined), voting together as a single class. For purposes of this Article TENTH, each share of Voting Stock shall have the number of votes granted to it pursuant to this Restated Certificate of Incorporation.

(ii) Such affirmative votes shall be required notwithstanding the fact that no vote may be required, or that a lesser percentage or separate class vote may be specified, by law or in any agreement with any national securities exchange or otherwise.

(b)

When Higher Vote Not Required

The provisions of subsection (b) of this Article TENTH shall not be applicable to any particular Related Party Business Combination, and such Related Party Business Combination shall require only such affirmative vote as is required by law or any other provision of this Restated Certificate of Incorporation or the Bylaws of the Corporation, or any agreement with any national securities exchange, if all of the conditions specified in either of the following subsections (i) or (ii) of this Article TENTH are met:

(i) *Approval of Disinterested Directors*. The Related Party Business Combination shall have been expressly approved by a majority (whether such approval is made prior to or subsequent to the acquisition of beneficial ownership of the Voting Stock that caused the Related party, as hereinafter defined, to become a Related Party) of the Disinterested Directors (as hereinafter defined); or

(ii) *Fair Price, Form of Consideration and Procedural Requirements*. All of the following conditions shall have been met:

(A) The aggregate amount of the cash and the Fair Market Value (as hereinafter defined) as of the date of the consummation of the Related Party Business Combination (the "Consummation Date") of consideration other than cash to be received per share by holders of shares of any class or series of Capital Stock (as hereinafter defined) in such Related Party Business Combination shall be at least equal to the highest of the following (it being intended that the requirements of subsection (ii)(A) of this Article TENTH shall be required to be met with respect to every class or series of outstanding Capital Stock, whether or not the Related Party has previously acquired beneficial ownership of any shares of a particular class or series of Capital Stock):

(i) (if applicable) the highest per share price (including any brokerage commissions, transfer taxes and soliciting dealers' fees) paid by or on behalf of the Related Party for any shares of such class or series of Capital Stock acquired by or on behalf of the Related Party (a) within the two-year period immediately prior to the first public announcement of the proposal of the Related Party Business Combination (the "Announcement Date") or (b) in the transaction in which it became a Related Party, whichever is higher;

(ii) the Fair Market Value per share of such class or series of Capital Stock on the Announcement Date or on the date on which the Related Party became a Related Party (the "Determination Date"), whichever is higher;

(iii) (if applicable) the price per share equal to the Fair Market Value per share of such class or series of Capital Stock determined pursuant to the immediately preceding clause (ii), multiplied by the ratio calculated by dividing (a) the highest per share price (including any brokerage commissions, transfer taxes and soliciting dealers' fees) paid by or on behalf of the Related Party for any share of such class or series of Capital Stock in connection with the acquisition by the Related party of beneficial ownership of shares of such class or series of Capital Stock within the two-year period immediately prior to the Announcement Date by (b) the Fair Market Value per share of such class or series of

Capital Stock on the first day in such two-year period on which the Related Party acquired beneficial ownership of any share of such class or series of Capital Stock;

(iv) in the case of Common Stock, the Corporation's net income per share of Common Stock for the four full consecutive fiscal quarters immediately preceding the Announcement Date, multiplied by the higher of the then price/earnings multiple (if any) of such Related Party or the highest price/earnings multiple of the corporation within the two-year period immediately preceding the Announcement Date (such price/earnings multiples being determined as customarily computed and reported in the financial community); or

(v) in the case of any class or series of Capital Stock other than Common Stock, the highest preferential amount per share to which the holders of shares of such class or series of Capital Stock are entitled in the event of any voluntary or involuntary liquidation, dissolution or winding up of the Corporation.

All per share prices shall be adjusted for any intervening stock splits, stock dividends and reverse stock splits.

(B) The consideration to be received by holders of a particular class or series of Capital Stock shall be in cash or in the same form as the Related Party has previously paid for shares of such particular stock. If the Related Party has paid for shares of any class or series of Capital Stock with varying forms of consideration, the form of consideration for such particular stock shall be either cash or the form used to acquire the largest number of shares of such particular stock previously acquired by it.

(C) After such Related Party has become a Related Party and prior to the Consummation Date:

(i) there shall have been (a) no reduction in the annual rate of dividends paid on the Common Stock (except as necessary to reflect any subdivision of Common Stock), except as approved by a majority of the Disinterested Directors, and (b) an increase in such annual rate of dividends as necessary to reflect any reclassification (including any reverse stock split), recapitalization, reorganization or any similar transaction which has the effect of reducing the number of outstanding shares of the Common Stock, unless the failure so to increase such annual rate is approved by a majority of the Disinterested Directors;

(ii) there shall have been no failure to declare and pay at the regular date therefor any full quarterly dividends (whether or not cumulative) payable in accordance with the terms of any other outstanding class or series of Capital Stock, except as approved by a majority of the Disinterested Directors; and

(iii) such Related Party shall have not become the beneficial owner of any additional shares of Capital Stock, except as part of the transaction which results in such Related Party becoming a Related Party.

(D) After such Related Party has become a Related Party, such Related Party shall not have received the benefit, directly or indirectly (except proportionately as a stockholder), of any loans, advances, guaranties, pledges or other financial assistance or any tax credits or other tax advantages provided by the Corporation, whether in anticipation of or in connection with such Related Party Business Combination, or otherwise.

(E) A proxy or information statement describing the proposed Related Party Business Combination and complying with the requirements of the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder (or any subsequent provisions replacing such Act, rules or regulations) shall be mailed to public stockholders of the Corporation at least 30 calendar days prior to the consummation of such Related Party Business Combination (whether or not such proxy or information statement is required to be mailed pursuant to such Act or subsequent provisions). The proxy or information statement shall contain on the first page thereof, in a prominent place, any statement as to the advisability (or inadvisability) of the Related Party Business Combination that the Disinterested Directors, or any of them, may choose to make and, if deemed advisable by a majority of the Disinterested Directors, the opinion of an investment banking firm selected by a majority of the disinterested Directors as to the fairness (or not) of the terms of the Related Party Business Combination from a financial point of view to the holders of the shares of any class or series of Capital Stock other than the Related party and its Affiliates or Associates (as hereinafter defined), such investment banking firm to be paid a reasonable fee for its services by this Corporation.

(F) Such Related Party shall not have made any major change in the Corporation's business or equity capital structure without the approval of a majority of the Disinterested Directors.

(c)

Definitions for Article TENTH

For the purposes of this Article TENTH:

(i) The term "Related Party Business Combination" shall mean any transaction referred to in one or more of the following:

(A) any merger or consolidation of the Corporation or any Subsidiary (as hereinafter defined) with (1) any Related Party or (2) any other corporation (whether or not itself a Related Party) which is, or after such merger or consolidation would be, an Affiliate or Associate (as hereinafter defined) of any Related Party; or

(B) any sale, lease, exchange, mortgage, pledge, transfer or other disposition (in one transaction or a series of transactions) to or with any Related Party or any Affiliate or Associate of any Related Party of any assets of the Corporation or any subsidiary having an aggregate Fair Market Value of Two Million Dollars ($2,000,000) or more; or

(C) the issuance or transfer by the Corporation or any Subsidiary (in one transaction or a series of transactions) of any securities having an aggregate Fair Market Value of Two Million Dollars ($2,000,000) or more of the Corporation or any subsidiary to any Related Party or any Affiliate or Associate of any Related Party in exchange for cash, securities or other property (or combination thereof); or

(D) the adoption of any plan or proposal for the liquidation or dissolution of the Corporation proposed by or on behalf of any Related Party or any Affiliate or Associate of any Related Party; or

(E) any reclassification of securities (including any reverse stock split), or recapitalization of the Corporation, or any merger or consolidation of the Corporation with any of its Subsidiaries or any other transaction (whether or not with or into or otherwise involving a Related Party or any Affiliate or Associate of any Related Party) which has the effect, directly or indirectly, of increasing the proportionate share of the outstanding shares of any class of equity or convertible securities of the Corporation or any Subsidiary which is directly or indirectly owned by any Related Party or any Affiliate or Associate of any Related Party; or

(F) any agreement, contract or other arrangement providing for any one or more of the actions specified in the foregoing clauses (A) through (E).

(ii) The term "Related Party" shall mean any person (other than the Corporation or any Subsidiary, and other than any profit-sharing, employee stock ownership or other employee benefit plan of the Corporation or any Subsidiary or any trustee of or fiduciary with respect to any such plan when acting in such capacity) who or which:

(A) is the beneficial owner (as hereinafter defined) of more than ten percent (10%) of the voting power of the outstanding Voting Stock; or

(B) is an Affiliate or Associate of the Corporation and at any time within the two-year period immediately prior to the date in question was the beneficial owner, directly or indirectly, of ten percent (10%) or more of the voting power of the then outstanding Voting Stock; or

(C) is an assignee of or has otherwise succeeded to any shares of Voting Stock which were at any time within the two-year period immediately prior to the date in question beneficially owned by any Related Party, if such assignment or succession shall have occurred in the course of a transaction or series of transactions not involving a public offering within the meaning of the Securities Act of 1933, as amended.

For purposes of determining whether a person is a Related Party, the number of shares of Voting Stock deemed to be outstanding shall include shares deemed owned through application of subsection (C)(iv) of this Article TENTH, hereof, but shall not include any other shares of Voting Stock which may be issuable pursuant to any agreement, arrangement or understanding, or upon exercise of conversion rights, warrants or options, or otherwise.

(iii) The term "person" shall mean any individual, firm, partnership, trust, corporation or other entity and shall include any group comprised of any person and any other person with whom such person or any Affiliate or Associate of such person has any agreement, arrangement or understanding, directly or indirectly, for the purpose of acquiring, holding, voting or disposing of Voting Stock.

(iv) A person shall be a "beneficial owner" of any Voting Stock:

(A) which such person or any of its Affiliates or Associates beneficially owns, directly or indirectly; or

(B) which such person or any of its Affiliates or Associates has (1) the right to acquire (whether such right is exercisable immediately or only after the passage of time) pursuant to any agreement, arrangement, understanding or relationship or upon the exercise of conversion rights, exchange rights, warrants or options, or otherwise; or (2) the right to vote pursuant to any agreement, arrangement, understanding or relationship; or (3) the right to invest, including the power to dispose or to direct the disposition of, pursuant to any agreement, arrangement, understanding or relationship; or

(C) which is beneficially owned, directly or indirectly, by any other person with which such person or any of its Affiliates or Associates has any agreement, arrangement, understanding or relationship for the purpose of acquiring, holding, voting or disposing of any shares of Voting Stock.

(v) The term "Affiliate," used to indicate a relationship with a specified person, shall mean a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.

(vi) The term "Associate," used to indicate a relationship with a specified person, shall mean:

(A) any corporation or organization (other than the Corporation or a Subsidiary) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of ten percent (10%) or more of any class of equity securities; or

(B) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity; or

(C) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person; or

(D) any person who is a director or officer of such specified person or any of its parents or subsidiaries (other than the Corporation or a Subsidiary).

(vii) The term "Subsidiary" shall mean any corporation of which a majority of any class of equity security is owned, directly or indirectly, by the Corporation; provided, however, that for the purposes of the definition of Related Party set forth in subsection (c)(ii) of this Article TENTH, the term "Subsidiary" shall mean only a corporation of which a majority of each class of equity security is owned, directly or indirectly, by the Corporation.

(viii) The term "Disinterested Director" shall mean:

(A) any member of the Board of Directors of the Corporation who is unaffiliated with the Related Party and was a member of the Board of Directors prior to the time that the Related Party became a Related Party, except with respect to a Related Party Business Combination involving a person who is a Related Party on the effective date hereof, any member of the Board of Directors of the Corporation who is unaffiliated with the Related Party and was a member of the Board of Directors prior to or upon election at the first annual meeting of stockholders of the Corporation after the effective date hereof; or

(B) any successor of a Disinterested Director who is unaffiliated with the Related Party and is recommended to succeed a Disinterested Director by a majority of Disinterested Directors then on the Board of Directors.

(ix) The term "Fair Market Value" shall mean:

(A) in the case of stock, the highest closing sale price during the 30-calendar-day period immediately preceding the date in question of a share of such stock on the Composite Tape for New York Stock Exchange-Listed Stocks, or, if such stock is not quoted on the Composite Tape, on the New York Stock Exchange, Inc., or, if such stock is not listed on such Exchange, on the principal United States securities exchange registered under the Securities Exchange Act of 1934, as amended, on which such stock is listed or, if such stock is not listed on any such exchange, the highest closing bid quotation with respect to a share of such stock during the 30-calendar-day period preceding the date in question on the National Association of Securities Dealers, Inc., Automated Quotations System or any system then in use, or if no such quotation is available, the Fair Market Value on the date in question of a share of such stock as determined by a majority of the disinterested Directors in good faith; and

(B) in the case of property other than cash or stock, the Fair Market Value of such property on the date in question as determined by a majority of the Disinterested Directors in good faith.

(x) The term "Capital Stock" shall mean all Capital Stock of the Corporation authorized to be issued from time to time under Article FOURTH of this Restated Certificate of Incorporation, and the term "Voting Stock" shall mean the then outstanding shares of Capital Stock of the Corporation entitled to vote generally in the election of directors.

(xi) In the event of any Related Party Business Combination in which the Corporation survives, the phrase "other consideration to be received" as used in subsections (b)(ii)(A) and (b)(ii)(B) of this Article TENTH shall include the shares of Common Stock and/or the shares of any other class or series of Capital Stock retained by the holders of such shares.

(d)

Determination by the Disinterested Directors

A majority of the Disinterested Directors or, if there should be no Disinterested Directors, a majority of the directors, shall have the power and duty to determine for the purposes of this Article TENTH, on the basis of information known to them after reasonable inquiry:

(i) Whether a person is a Related Party;

(ii) The number of shares of Voting Stock beneficially owned by any person;

(iii) Whether a person is an Affiliate or Associate of another;

(iv) Whether the assets which are the subject of any Related Party Business Combination have, or the consideration to be received for the issuance or transfer of securities by the Corporation or any Subsidiary in any Related Party Business Combination has, an aggregate Fair Market Value of Two Million Dollars ($2,000,000) or more; and

(v) Such other matters with respect to which a determination is required under this Article TENTH.

A majority of the Disinterested Directors or, if there should be no Disinterested Directors, a majority of the directors shall have the further power to interpret all of the terms and provisions of this Article TENTH.

(e)

Effect on Fiduciary Obligations

(i) Nothing contained in this Article TENTH shall be construed to relieve any Related Party from any fiduciary obligation imposed by law.

(ii) The fact that any Related Party Business Combination complies with the provisions of subsection (b) of this Article TENTH shall not be construed to impose any fiduciary duty, obligation or responsibility on the Board of Directors, or any member thereof, to approve such Related Party Business Combination or recommend its adoption or approval to the stockholders of the Corporation, nor shall such compliance limit, prohibit or otherwise restrict in any manner the Board of Directors, or any member thereof, with respect to evaluations of or actions and responses taken with respect to such Related Party Business Combination.

ELEVENTH: The Corporation reserves the right to amend, alter, change or repeal any provision contained in this Certificate of Incorporation, in the manner now or hereafter prescribed by statute, and all rights conferred upon stockholders herein are granted subject to this reservation; provided, however, that the affirmative vote of the holders of at least 67% of the shares of capital stock of the Corporation issued and outstanding and entitled to vote, voting together as a single class, shall be required to alter, amend or repeal Articles FIFTH, EIGHTH, NINTH and TENTH of this Restated Certificate of Incorporation; provided however that this Article ELEVENTH shall not apply to, and such 67% vote shall not be required for, any amendment, repeal or adoption unanimously recommended by the Board of Directors if all such directors are persons who would be eligible to serve as Disinterested Directors within the meaning of Article TENTH.

TWELFTH: The Corporation renounces any interest or expectancy of it in, or being offered an opportunity to participate in, any business opportunities, including any business opportunities within those classes of opportunity currently pursued by the Corporation through its subsidiaries, presented (a) to persons who are officers or directors of the Corporation or who, on October 1, 2003, were, and at the time of presentation are, stockholders of the Corporation (or to persons who are affiliates or associates of such officers, directors or stockholders), if the Corporation is prohibited from participating in such opportunities by the Omnibus Agreement dated December 17, 2002 or (b) to Yorktown Energy Partners IV, L.P., Yorktown Energy Partners V, L.P. or any other investment fund sponsored or managed by Yorktown Partners, LLC, including any fund still to be formed, or to any director of the

Corporation who is an affiliate or designate of such an entity, so long as such entity was a stockholder of the Corporation at the time of presentation of the opportunity.

IN WITNESS WHEREOF, the Corporation has caused this Restated Certificate of Incorporation to be signed by its duly authorized officer on this 14th day of January, 2004.

CROSSTEX ENERGY, INC.

By:	/s/ LESLIE J. WYLIE
Name:	Leslie J. Wylie
Title:	Vice President and Secretary

QuickLinks

Exhibit 3.1
RESTATED CERTIFICATE OF INCORPORATION OF CROSSTEX ENERGY, INC.

Exhibit 3.2

RESTATED BYLAWS

OF

CROSSTEX ENERGY INC.

ARTICLE I

OFFICES

Section 1. *Name*. The name of the corporation is Crosstex Energy Inc. (hereinafter called the "Corporation").

Section 2. *Offices*. The Corporation shall have such offices, and keep the books and records of the Corporation as may be required by law, and at such other place or places as the Board of Directors may from time to time determine or the business of the Corporation require.

ARTICLE II

MEETINGS OF STOCKHOLDERS

Section 1. *Annual Meetings*. The annual meetings of stockholders for the election of directors and for the transaction of such other business as may properly come before the meeting shall be held in [May] of each year, beginning in [2004], at such place as designated by the Board of Directors in the notice of such meeting.

Section 2. *Special Meetings*. Special meetings of the stockholders for any purpose or purposes may be called by a majority of the entire Board of Directors. Only such business as is specified in the notice of any special meeting of the stockholders shall come before such meeting.

Section 3. *Notice of Meetings*. Except as otherwise provided by law, written notice of each meeting of the stockholders, whether annual or special, shall be given, either by personal delivery or by mail, not less than 10 nor more than 60 days before the date of the meeting to each stockholder of record entitled to notice of the meeting. If mailed, such notice shall be deemed given when deposited in the United States mail, postage prepaid, directed to the stockholder at such stockholder's address as it appears on the records of the Corporation. Each such notice shall state the place, date and hour of the meeting, and the purpose or purposes for which the meeting is called. Notice of any meeting of stockholders shall not be required to be given to any stockholder who shall attend such meeting in person or by proxy without protesting, prior to or at the commencement of the meeting, the lack of proper notice to such stockholder. Notice of adjournment of a meeting of stockholders need not be given if the time and place to which it is adjourned are announced at such meeting, unless the adjournment is for more than 30 days or, after adjournment, a new record date is fixed for the adjourned meeting.

Section 4. *Quorum*.

(a) The holders of a majority of the shares of stock entitled to be voted, present in person or represented by proxy, shall constitute a quorum at any meeting of the stockholders. In the absence of a quorum, the holders of a majority of the shares of stock entitled to be voted at the meeting may adjourn the meeting from time to time. At any such adjourned meeting at which a quorum is present, any business may be transacted which might have been transacted at the meeting as originally called.

(b) For purposes of voting a particular class of stock (when class votes are necessary), the holders of a majority of the shares of each class of stock entitled to be voted, present in person or represented by proxy, shall constitute a quorum at any meeting of the class of stockholders. In the absence of a quorum, the holders of a majority of the shares of each class of stock entitled to be voted at such meeting may adjourn the meeting from time to time. At any such adjourned meeting at which a quorum is present, any business may be transacted which might have been transacted at the meeting as originally called.

Section 5. *Voting*. At each meeting of the stockholders, all corporate actions, other than the election of directors, to be taken by vote of the stockholders (except as otherwise provided in the Certificate of Incorporation) shall be authorized by a majority of the votes cast by the stockholders entitled to vote thereon, present in person or represented by proxy. There shall be no separate votes of classes of capital stock, except as specifically required by law, the Certificate of Incorporation, or the Bylaws. Directors shall be elected by a plurality of the votes of the shares present in person or represented by proxy at the meeting and entitled to vote on the election of the directors. Each stockholder entitled to vote at any meeting of stockholders may authorize any person or persons to act for such stockholder by a proxy signed by such stockholder or such stockholder's attorney-in-fact.

The vote on any matter, including the election of directors, need not be by written ballot. In the case of a vote by written ballot, each ballot shall be signed by the stockholder voting, or by such stockholder's proxy, and shall state the number of shares voted.

Section 6. *Participation in Meeting by Means of Communication Equipment*. Any stockholder may participate in any meeting of the stockholders by means of conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other, and such participation shall constitute presence in person at such meeting.

Section 7. *Notice of Stockholder Business*. At an annual or special meeting of the stockholders, only such business shall be conducted as shall have been property brought before the meeting. To be properly brought before a meeting of stockholders, business must be (i) specified in the notice of meeting (or any supplement thereto) given at the direction of the Board of Directors, (ii) properly brought before the meeting by or at the direction of the Board of Directors, or

(iii) properly brought before a meeting by a stockholder who is a stockholder of record on the date of the giving of the notice provided for in this Section 7 and on the record date for the determination of stockholders entitled to vote at such annual meeting and who complies with the notice provisions set forth in this Section 7. For business to be properly brought before a meeting by a stockholder, it must be a proper matter for stockholder action under the Delaware General Corporation Law, and the stockholder must have given timely notice thereof in proper written form to the Secretary of the Corporation.

To be timely, notice by a stockholder must be delivered to or mailed and received at the principal executive offices of the Corporation, not less than 120 calendar days prior to the one year anniversary of the date of the Corporation's proxy statement issued in connection with the prior year's annual meeting in the case of an annual meeting, and not less than 60 days prior to the meeting the case of a special meeting; provided however, that if a public announcement of the date of the special meeting is not given at least 70 days before the scheduled date for such special meeting, then a stockholder's notice shall be timely if it is received at the principal executive offices of the Corporation within 10 days following the date public notice of the meeting date is first given, whether by press release or other public filing.

To be in proper written form, notice by a stockholder to the Secretary of the Corporation shall set forth as to each matter the stockholder proposes to bring before the annual or special meeting (i) a description of the business desired to be brought before the meeting, (ii) the name and address of the stockholder proposing such business and of the beneficial owner, if any, on whose behalf the business is being brought, (iii) the class, series and number of shares of the Corporation which are beneficially owned by the stockholder and such other beneficial owner, (iv) any material interest of the stockholder and such other beneficial owner in such business and (v) a representation that such stockholder intends to appear in person or by proxy at the annual or special meeting to bring such business before such meeting. In no event shall an announcement of an adjournment or postponement of a meeting of stockholders commence a new time period (or extend any time period) for the giving of a stockholder's notice as described above.

Section 8. *Nomination of Director Candidates*. Subject to any provision of the Restated Certificate of Incorporation or any Certificate of Designations establishing the rights of holders of any class or series of capital stock then outstanding, nominations for the election or re-election of directors at a meeting of the stockholders may be made by (i) the Board of Directors or a duly authorized committee thereof or (ii) any stockholder entitled to vote in the election of directors generally who complies with the procedures set forth in these Bylaws and who is a stockholder of record at the time notice is delivered to the Secretary of the Corporation and on the record date for the determination of stockholders entitled to vote at such annual meeting and who complies with the notice provisions set forth in this Section 8. Subject to any provision of the Restated Certificate of Incorporation or any Certificate of Designations establishing the rights of holders of any class or series of capital stock then outstanding, any stockholder entitled to vote in the election of directors generally may nominate one or more persons for election or re-election as directors at an annual meeting only if timely notice of such stockholder's intent to make such nominations has been given in writing to the Secretary of the Corporation.

To be timely, notice of a stockholder nomination for a director to be elected must be delivered to or mailed and received at the principal executive offices of the Corporation, not less than 120 calendar days prior to the one year anniversary of the date of the Corporation's proxy statement issued in connection with the prior year's annual meeting in the case of an annual meeting, and not less than 60 days prior to the meeting the case of a special meeting; provided however, that if a public announcement of the date of the special meeting is not given at least 70 days before the scheduled date for such special meeting, then a stockholder's notice shall be timely if it is received at the principal executive offices of the Corporation within 10 days following the date public notice of the meeting date is first given, whether by press release or other public filing.

To be in proper written form, notice by a stockholder to the Secretary of the Corporation shall set forth as to each matter the stockholder proposes to bring before the annual or special meeting (i) the name and address of the stockholder who intends to make the nomination, of the beneficial owner, if any on whose behalf the nomination is being made and of each person to be nominated, (ii) a representation that the stockholder is the holder of record of stock of the Corporation entitled to vote for the election of directors on the date of such notice and intends to appear in person or by proxy at the meeting to nominate each person specified in the notice, (iii) a description of all the arrangements or understandings between the stockholder or such beneficial owner and each nominee and any other person (naming such person) pursuant to which the nomination is to be made by the stockholder, (iv) such other information regarding each nominee proposed by such stockholder as would be required to be included in solicitations of proxies for the election of directors in an election contest or is otherwise required pursuant to the federal securities laws and regulations, had the nominee been nominated, or intended to be nominated, by the Board of Directors, and (v) the consent of each nominee to serve as a director of the Corporation if so elected.

Notwithstanding the foregoing, in the event that the number of directors to be elected at an annual meeting is increased and there is no public announcement by the Corporation naming the nominees for the additional directorships at least 130 days prior to such meeting, a stockholder's notice required by this Section 8 shall also be considered timely, but only with respect to nominees for the additional directorships, if it shall be delivered to the Secretary of the Corporation no later than the close of business on the 10th day following the day on which such public announcement is first made by the Corporation. In no event shall an announcement of an adjournment or postponement of a meeting of stockholders commence a new time period (or extend any time period) for the giving of a stockholder's notice as described above.

ARTICLE III

BOARD OF DIRECTORS

Section 1. *Number*. The Board of Directors shall consist of not less than three (3) and not more than nine (9) directors, and the exact number of directors which shall constitute the Board of Directors shall be fixed from time to time by resolution of the Board; provided, however, that no decrease in the number of directors constituting the Board shall have the effect of shortening the term of any incumbent director. None of the directors need be stockholders of the Corporation or residents of the State of Delaware.

Section 2. *Vacancies*. Any vacancies in the Board of Directors for any reason, and any newly created directorships resulting from any increase in the authorized number of directors, may be filled only by a majority of the directors then in office, though less than a quorum, or by a sole remaining director, and the directors so chosen shall hold office for a term expiring at the next annual meeting of stockholders and until their successors are duly elected and qualified or until their earlier resignation or removal. If there are no directors in office, then an election of directors may be held in the manner provided by statute.

Section 3. *Quorum and Manner of Acting*. A majority of the entire Board of Directors shall constitute a quorum for the transaction of business at any meeting of the Board, and the vote of a majority of the directors present at any meeting at which there is a quorum shall be the act of the Board. In the absence of a quorum, a majority of the directors present may adjourn the meeting to another time and place. At any adjourned meeting at which a quorum is present, any business that might have been transacted at the meeting as originally called may be transacted.

Section 4. *Regular and Special Meetings*. Regular meetings of the Board of Directors shall be held at such times and places as the Board shall from time to time by resolution determine. Special meetings of the Board of Directors shall be held whenever called by the Chairman of the Board, the President, or by at least two of the directors.

Section 5. *Participation in Meeting by Means of Communication Equipment*. Any one or more members of the Board of Directors or any committee thereof may participate in any meeting of the Board or of any such committee by means of conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other, and such participation shall constitute presence in person at such meeting.

Section 6. *Committees*. The Board of Directors may, by unanimous resolution, designate one or more committees, each committee to consist of two or more of the directors of the Corporation. The Board of Directors may designate one or more directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of the committee. Any such committee, to the extent provided in the resolution, shall have and may exercise the powers of the Board of Directors in the management of the business and affairs of the Corporation, and may authorize the seal of the Corporation to be affixed to all papers which may require it; provided, however, that in the absence or disqualification of any member of such committee or committees the member or members thereof present at any meeting and not disqualified from voting, whether or not he or they constitute a quorum, may unanimously appoint another member of the Board of Directors to act at the meeting in the place of any such absent or disqualified member. Such committee or committees shall have such name or names as may be determined from time to time by resolution adopted by the Board of Directors. Each committee shall keep regular minutes of its meetings and report the same to the Board of Directors when required.

Section 7. *Compensation*. The directors may be paid their expenses, if any, of attendance at each meeting of the Board of Directors and may be paid a fixed sum for attendance at each meeting of the Board of Directors or a stated salary as a director. No such payment shall preclude any director from serving the corporation in any other capacity and receiving compensation therefor. Members of special or standing committees may be allowed like compensation for attending committee meetings.

Section 8. *Resignations*. Any director of the Corporation may at any time resign by giving written notice to the Board of Directors, the Chairman of the Board, the President or the Secretary of the Corporation. Such resignation shall take effect at the time specified therein or, if the time be not specified, upon receipt thereof; and unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

ARTICLE IV

NOTICES

Section 1. Whenever, under the provisions of the statutes or of the certificate of incorporation or of these bylaws, notice is required to be given to any director or stockholder, it shall not be construed to mean personal notice, but such notice may be given in writing, by mail, addressed to such director or stockholder, at his address as it appears on the records of the Corporation, with postage thereon prepaid, and such notice shall be deemed to be given at the time when the same shall be deposited in the United States mail. Notice to directors may also be given by prepaid telegram, facsimile, or reputable courier service.

Section 2. Whenever any notice is required to be given under the provisions of the statutes or of the certificate of incorporation or of these Bylaws, a waiver thereof in writing, signed by the person or persons entitled to said notice, whether before or after the time stated therein, shall be deemed equivalent thereto.

ARTICLE V

OFFICERS

Section 1. *Number, Term of Office*. The officers of the Corporation shall be a Chairman of the Board, a President, one or more Vice Presidents, a Treasurer, a Secretary and such other officers or agents with such titles and such duties as the Board of Directors may from time to time determine, each to have such authority, functions or duties as in these Bylaws provided or as the Board may from time to time determine, and each to hold office for such term as may be prescribed by the Board and until such person's successor shall have been chosen and shall qualify, or until such person's death or resignation, or until such person's removal in the manner hereinafter provided. The Chairman of the Board shall be elected from among the directors. One person may hold the offices and perform the duties of any two or more of said officers; provided, however, that no officer shall execute, acknowledge or verify any instrument in more than one capacity if such instrument is required by law, the Certificate of Incorporation of the Corporation or these Bylaws to be executed, acknowledged or verified by two or more officers. The Board may from time to time authorize any officer to appoint and remove any such other officers and agents and to prescribe their powers and duties. The Board may require any officer or agent to give security for the faithful performance of such person's duties.

Section 2. *Removal*. Any officer may be removed, either with or without cause, by the Board of Directors at any meeting thereof called for that purpose, or, except in the case of any officer elected by the Board, by any committee or superior officer upon whom such power may be conferred by the Board.

Section 3. *Resignation*. Any officer may at any time resign by giving written notice to the Board of Directors, the President or the Secretary of the Corporation. Any such resignation shall take effect at the date of receipt of such notice or at any later date specified therein, and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 4. *Vacancies*. A vacancy in any office because of death, resignation, removal or any other cause may be filled for the unexpired portion of the term by the Board of Directors in the manner prescribed in these Bylaws for election to such office.

Section 5. *President*. The President shall be the chief executive officer of the Corporation and as such shall have general supervision and direction of the business and affairs of the Corporation, subject to the control of the Board of Directors. The President shall, if present and in the absence of the Chairman of the Board, preside at meetings of the stockholders, meetings of the Board. The President shall perform such other duties as the Board may from time to time determine. The President may sign and execute in the name of the Corporation deeds, mortgages, bonds, contracts or other instruments authorized by the Board or any committee thereof empowered to authorize the same.

Section 6. *Chairman of the Board*. The Chairman of the Board shall, if present, preside at meetings of the stockholders and meetings of the Board. The Chairman of the Board shall counsel with and advise the President and perform such other duties as the President or the Board may from time to time determine. The President may sign and execute in the name of the Corporation deeds, mortgages, bonds, contracts or other instruments authorized by the Board or any committee thereof empowered to authorize the same.

Section 7. *Vice Presidents*. Each Vice President shall have such powers and duties as shall be prescribed by the President, the Chairman of the Board or the Board of Directors. Any Vice President may sign and execute in the name of the Corporation deeds, mortgages, bonds, contracts or other instruments authorized by the Board or any committee thereof empowered to authorize the same.

Section 8. *Treasurer*. The Treasurer shall perform all duties incident to the office of Treasurer and such other duties as from time to time may be assigned to the Treasurer by the President, the Chairman of the Board or the Board of Directors.

Section 9. *Secretary*. It shall be the duty of the Secretary to act as secretary at all meetings of the Board of Directors and of the stockholders and to record the proceedings of such meetings in a book or books to be kept for that purpose; the Secretary shall see that all notices required to be given by the Corporation are duly given and served; the Secretary shall be custodian of the seal of the Corporation and shall affix the seal or cause it to be affixed to all certificates of stock of the Corporation (unless the seal of the Corporation on such certificates shall be a facsimile, as hereinafter provided) and to all documents, the execution of which on behalf of the Corporation under its seal is duly authorized in accordance with the provisions of these Bylaws. The Secretary shall have charge of the stock ledger and also of the other books, records and papers of the Corporation and shall see that the reports, statements and other documents required by law are properly kept and filed; and the Secretary shall in general perform all the duties incident to the office of Secretary and such other duties as from time to time may be assigned to such person by the President, the Chairman of the Board or the Board of Directors.

Section 10. *Assistant Treasurers and Secretaries*. The Assistant Treasurers and the Assistant Secretaries shall perform such duties as shall be assigned to them by the Treasurer or Secretary, respectively, or by the President, the Chairman of the Board or the Board of Directors.

ARTICLE VI

INDEMNIFICATION OF DIRECTORS, OFFICERS, EMPLOYEES AND AGENTS

Section 1. *Power to Indemnify in Actions, Suits or Proceedings*. Subject to Section 2 of this Article VI, the Corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (including an action by or in the right of the Corporation) by reason of the fact that he is or was a director or officer of the Corporation, or is or was serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding. Such indemnification shall be made pursuant to the terms of the form of Indemnity Agreement attached hereto as Exhibit A. The Board of Directors of the Corporation expressly has the power and authority to change, revise or amend the terms of the form of Indemnity Agreement without further notice to or approval from the stockholders of the Corporation, whether or not either the Corporation or the party to be indemnified has signed the Indemnity Agreement.

Section 2. *Indemnification by a Court*. Notwithstanding anything to the contrary contained herein, any director or officer may apply to any court of competent jurisdiction in the State of Delaware for indemnification. The basis of such indemnification by a court shall be a determination by such court that indemnification of the director or officer is proper in the circumstances because he has met the applicable standards of conduct set forth in the Delaware General Corporation Law. Notice of any application for indemnification pursuant to this Section 2 shall be given to the Corporation promptly upon the filing of such application. If successful, in whole or in part, the director or officer seeking indemnification shall also be entitled to be paid the expense of prosecuting such application.

Section 3. *Expenses Payable in Advance*. Expenses incurred by a director or officer in defending or investigating a threatened or pending action, suit or proceeding shall be paid by the Corporation in advance of the final disposition of such action, suit or proceeding upon receipt of an undertaking by or on behalf of such director or officer to repay such amount if it shall ultimately be determined that he is not entitled to be indemnified by the Corporation as authorized this Article VI.

Section 4. *Nonexclusivity of Indemnification and Advancement of Expenses*. The indemnification and advancement of expenses provided by or granted pursuant to this Article VI shall not be deemed exclusive of any other rights to which those seeking indemnification or advancement of expenses may be entitled under any Bylaw, agreement, contract, vote of stockholders or disinterested directors or pursuant to the direction (howsoever embodied) of any court of competent jurisdiction or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, it being the policy of the Corporation that indemnification of the persons specified in this Article VI shall be made to the fullest extent permitted by law. The provisions of this Article VI shall not be deemed to preclude the indemnification of any person who is not specified in Sections 1 or 2 of this Article VI but whom the Corporation has the power or obligation to indemnify under the provisions of the General Corporation Law of the State of Delaware, or otherwise.

Section 5. *Insurance*. The Corporation may purchase and maintain insurance on behalf of any person who is or was a director or officer of the Corporation, or is or was a director or officer of the Corporation serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise against any liability asserted against him and incurred by him in any such capacity, or arising out of his status as such, whether or not the Corporation would have the power or the obligation to indemnify him against such liability under the provisions of this Article VI.

Section 6. *Certain Definitions*. For purposes of this Article VI, references to "the Corporation" shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors, officers, and employees or agents, so that any person who is or was a director, officer, employee or agent of such constituent corporation, or is or was serving at the request of such constituent corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, shall stand in the same position under the provisions of this section with respect to the resulting or surviving corporation as he would have with respect to such constituent corporation if its separate existence had continued. For purposes of this Article VI, references to "fines" shall include any excise taxes assessed on a person with respect to an employee benefit plan; and references to "serving at the request of the Corporation" shall include any service as a director, officer, employee or agent of the Corporation which imposes duties on, or involves services by, such director or officer with respect to an employee benefit plan, its participants or beneficiaries; and a person who acted in good faith and in a manner he reasonably believed to be in the interest of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the Corporation" as referred to in this Article VI.

Section 7. *Survival of Indemnification and Advancement of Expenses*. The indemnification and advancement of expenses provided by, or granted pursuant to, this Article VI shall, unless otherwise provided when authorized or ratified, continue as to a person who has ceased to be a director or officer and shall inure to the benefit of the heirs, executors and administrators of such a person.

Section 8. *Limitation on Indemnification*. Notwithstanding anything contained in this Article VI to the contrary, except for proceedings to enforce rights to indemnification (which shall be governed by Section 2 hereof), the Corporation shall not be obligated to indemnify any director or officer in connection with a proceeding (or part thereof) initiated by such person unless such proceeding (or part thereof) was authorized or consented to by the Board of Directors of the Corporation.

Section 9. *Indemnification of Employees and Agents*. The Corporation may, to the extent authorized from time to time by the Board of Directors, provide rights to indemnification and the advancement of expenses to employees and agents of the Corporation similar to those conferred in this Article VI to directors and officers of the Corporation.

ARTICLE VII

SEAL

The corporate seal shall have inscribed thereon the name of the corporation and shall be in such form as may be approved from time to time by the Board of Directors. The seal may be used by causing it or a facsimile thereof to be impressed, affixed, imprinted or in any manner reproduced.

ARTICLE VIII

CONSENTS

Any action which may be taken at a meeting of the Board of Directors or any committee thereof may be taken without a meeting in compliance with Delaware General Corporation Law.

ARTICLE IX

AMENDMENTS

These bylaws may be altered, amended or repealed or new bylaws may be adopted by the stockholders or by the Board of Directors at any regular meeting of the stockholders or of the Board of Directors or at any special meeting of the stockholders or of the Board of Directors if notice of such alteration, amendment, repeal or adoption of new bylaws be contained in the notice of such special meeting. Pursuant to subsection (d) of Article FIFTH of the Restated Certificate of Incorporation, Sections 2, 7 and 8 of Article II and Article VI shall not be altered, amended or repealed and no provision inconsistent therewith shall be adopted without the affirmative vote of the holders of at least [67%] of the shares of the capital stock of the Corporation entitled to vote, voting together as a single class. Notwithstanding anything contained herein to the contrary, the affirmative vote of the holders of [67%] of the shares of the capital stock of the Corporation entitled to vote, voting together as a single class, shall be required to adopt, alter or amend any provision inconsistent with or to repeal this Article IX.

ADOPTED, as of the 31st day of December, 2003.

QuickLinks

Exhibit 3.2
RESTATED BYLAWS OF CROSSTEX ENERGY INC.

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 10.2

INDEMNITY AGREEMENT

This Agreement made and entered into as of this 31 day of December, 2003, by and between Crosstex Energy Holdings Inc., a Delaware corporation (the "Company"), and ("Indemnitee"), who is currently serving the Company in the capacity of a director and/or officer thereof;

W I T N E S S E T H:

WHEREAS, the Company and Indemnitee recognize that the interpretation of ambiguous statutes, regulations and court opinions and of the Certificate of Incorporation and Bylaws of the Company, and the vagaries of public policy, are too uncertain to provide the directors and officers of the Company with adequate or reliable advance knowledge or guidance with respect to the legal risks and potential liabilities to which they become personally exposed as a result of performing their duties in good faith for the Company; and

WHEREAS, the Company and the Indemnitee are aware that highly experienced and capable persons are often reluctant to serve as directors or officers of a corporation unless they are protected to the fullest extent permitted by law by comprehensive insurance or indemnification, especially since the legal risks and potential liabilities, and the very threat thereof, associated with lawsuits filed against the officers and directors of a corporation, and the resultant substantial time, expense, harassment, ridicule, abuse and anxiety spent and endured in defending against such lawsuits, whether or not meritorious, bear no reasonable or logical relationship to the amount of compensation received by the directors or officers from the corporation; and

WHEREAS, Section 145 of the General Corporation Law of the State of Delaware and the Certificate of Incorporation of the Company, which set forth certain provisions relating to the mandatory and permissive indemnification of, and advancement of expenses to, officers and directors (among others) of a Delaware corporation by such corporation, is specifically not exclusive of other rights to which those indemnified thereunder may be entitled under any bylaw, agreement, vote of stockholders or disinterested directors or otherwise, and, thus, does not by itself limit the extent to which the Company may indemnify persons serving as its officers and directors (among others); and

WHEREAS, after due consideration and investigation of the terms and provisions of this Agreement and the various other options available to the Company and the Indemnitee in lieu thereof, the board of directors of the Company has determined that the following Agreement is not only reasonable and prudent but necessary to promote and ensure the best interests of the Company and its stockholders; and

WHEREAS, the Company desires to have Indemnitee serve or continue to serve as an officer and/or director of the Company, free from undue concern for unpredictable, inappropriate or unreasonable legal risks and personal liabilities by reason of his acting in good faith in the performance of his duty to the Company; and Indemnitee desires to serve, or to continue to serve (provided that he is furnished the indemnity provided for hereinafter), in either or both of such capacities;

NOW, THEREFORE, in consideration of the premises and the mutual agreements herein set forth and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company and Indemnitee, intending to be legally bound, do hereby agree as follows:

1. Agreement to Serve. Indemnitee agrees to serve or continue to serve as director and/or officer of the Company and as Indemnitee and the Company may agree, as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise, for so long as he is duly elected or appointed and qualified in accordance with the provisions of the General Corporation Law of the State of Delaware and the Certificate of Incorporation and Bylaws of the Company or until such time as he tenders his resignation. The Company acknowledges that the Indemnitee is relying on this Agreement in so serving.

2. Definitions. As used in this Agreement:

(a) The term "Proceeding" shall mean any threatened, pending or completed action, suit, or proceeding, whether civil, criminal, administrative, arbitrative or investigative, any appeal in such an action, suit, or proceeding, and any inquiry or investigation that could lead to such an action, suit or proceeding irrespective of the initiator thereof. The final disposition of a Proceeding shall be as determined by a settlement or the judgment of a court or other investigative or administrative body. The Board of Directors shall not make a determination as to the final disposition of a Proceeding.

(b) "Change in Control" means a change in control of the Company of a nature that would be required to be reported in response to Item 6(e) of Schedule 14A of Regulation 14A (or in response to any similar item on any similar schedule or form) promulgated under the Securities Exchange Act of 1934 (the "Act"), whether or not the Company is then subject to such reporting requirement; provided, however, that, without limitation, such a Change in Control shall be deemed to have occurred if (i) any "person" (as such term is used in Sections 13(d) and 14(d) of the Act) other than a trustee or other fiduciary holding securities under an employee benefit plan of the Company or a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Act), directly or indirectly, of securities of the Company representing 15% or more of the combined voting power of the Company's then outstanding securities (other than Yorktown Energy Partners IV, L.P. or Yorktown Energy Partners V, L.P. and/or any of their "affiliates" or "associates" (as both terms are defined in Rule 12b-2 under the Act)) without the prior approval of at least two-thirds of the members of the board of directors of the Company in office immediately prior to such person attaining such percentage interest; (ii) there occurs a proxy contest, or the Company is a party to a merger, consolidation, sale of assets, plan of liquidation or other reorganization not approved by at least two-thirds of the members of the board of directors of the Company then in office, as a consequence of which members of the board of directors in office immediately prior to such transaction or event constitute less than a majority of the board of directors thereafter; or (iii) during any period of two consecutive years, other than as a result of an event described in clause (ii) of this subsection (c), individuals who at the beginning of such period constituted the board of directors of the Company (including for this purpose any new director whose election or nomination for election by the Company's stockholders was approved by a vote of at least two-thirds of the directors then still in office who were directors at the beginning of such period) cease for any reason to constitute at least a majority of the board of directors.

(c) "Disinterested Director" means a director of the Company who is not and was not a party to the Proceeding in respect of which indemnification is sought by Indemnitee.

(d) The term "Expenses" includes, without limitation, all reasonable attorneys' fees, retainers, court costs, transcript costs, fees of experts, witness fees, travel expenses, duplicating costs, printing and binding costs, telephone charges, postage, delivery service fees and all other disbursements or expenses of the types customarily incurred in connection with prosecuting, defending, preparing to prosecute or defend, investigating, or being or preparing to be a witness in, or otherwise involved in, a Proceeding. Should any payments by the Company under this Agreement be determined to be subject to any federal, state or local income or excise tax, "Expenses" will also include such amounts as are necessary to place Indemnitee in the same after-tax position, after giving effect to all applicable taxes, Indemnitee would have been in had such tax not have been determined to apply to those payments. Expenses also shall include Expenses incurred in connection with any appeal resulting from any Proceeding, including, without limitation, the premium, security for, and other costs relating to any cost bond, supersedeas bond, or other appeal bond or its equivalent.

(e) "Independent Counsel" means a law firm, or a member of a law firm, that is experienced in matters of corporation law and neither presently is, nor in the past five years has been, retained to represent: (i) the Company or Indemnitee in any matter material to either such party (other than with respect to matters concerning the Indemnitee under this Agreement, or of other indemnitees under similar indemnification agreements), or (ii) any other party to the Proceeding giving rise to a claim for indemnification hereunder. Notwithstanding the foregoing, the term "Independent Counsel" shall not include any person who, under the applicable standards of professional conduct then prevailing, would have a conflict of interest in representing either the Company or Indemnitee in an action to determine Indemnitee's rights under this Agreement. The Company agrees to pay the reasonable fees and expenses of the Independent Counsel referred to above and to fully indemnify such counsel against any and all Expenses, claims, liabilities and damages arising out of or relating to this Agreement or its engagement pursuant hereto.

(f) References to "other enterprise" shall include employee benefit plans; references to "fines" shall include any (i) excise taxes assessed with respect to any employee benefit plan and (ii) penalties; references to "serving at the request of the Company" shall include any service as a director, officer, employee or agent of the Company which imposes duties on, or involves services by, such director, officer, employee or agent with respect to an employee benefit plan, its participants or beneficiaries; and a person who acts in good faith and in a manner he reasonably believed to be in the interest of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the Company" as referred to in this Agreement.

3. Indemnity in Third Party Proceedings. The Company shall indemnify Indemnitee in accordance with the provisions of this Section 3 if Indemnitee is a party to or is threatened to be made a party to or is otherwise involved in any Proceeding (other than a Proceeding by or in the right of the Company to procure a judgment in its favor) by reason of the fact that Indemnitee is or was a director and/or officer of the Company, or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise, against all Expenses, judgments, fines and amounts paid in settlement actually and reasonably incurred by Indemnitee (or on his behalf) in connection with such Proceeding or any claim, issue or matter therein, provided it is determined pursuant to Section 8 of this Agreement or by the court having jurisdiction in the matter, that Indemnitee acted in good faith and in a manner that he reasonably believed to be in or not opposed to the best interests of the Company, and, with respect to any criminal Proceeding, had no reasonable cause to believe his conduct was unlawful. The termination of any Proceeding or of any claim, issue or matter therein, by judgment, order, settlement or conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, adversely affect the right of Indemnitee to indemnification or create a presumption that Indemnitee did not act in good faith and in a manner that he reasonably believed to be in or not opposed to the best interests of the Company, or, with respect to any criminal Proceeding, had reasonable cause to believe that his conduct was unlawful. Indemnitee shall have the right to employ Indemnitee's own legal counsel in any Proceeding for which indemnification is available under this Section 3.

4. Indemnity in Proceedings By or In the Right of the Company. The Company shall indemnify Indemnitee in accordance with the provisions of this Section 4 if Indemnitee is a party to or is threatened to be made a party to or otherwise involved in any Proceeding by or in the right of the Company to procure a judgment in its favor by reason of the fact that Indemnitee is or was a director and/or officer of the Company, or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise, against all Expenses actually and reasonably incurred by Indemnitee (or on his behalf) in connection with such Proceeding but only if he acted in good faith and in a manner that he reasonably believed to be in or not opposed to the best interests of the Company, except that no indemnification shall be made under this Section 4 in respect of any claim, issue or matter as to which Indemnitee shall have been adjudged to be liable to the Company unless and only to the extent that the Delaware Court of Chancery or the court in which such Proceeding was brought or is pending, shall determine upon application that, despite the adjudication of liability but in view of all the circumstances of the case, Indemnitee is fairly and reasonably entitled to indemnity for such Expenses as the Delaware Court of Chancery or such other court shall deem proper. Indemnitee shall have the right to employ Indemnitee's own legal counsel in any Proceeding for which indemnification is available under this Section 4.

5. Indemnification for Expenses of a Witness. Notwithstanding any other provision of this Agreement, to the extent that Indemnitee is, by reason of the fact that Indemnitee is or was a director and/or officer of the Company, or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise, a witness in any Proceeding to which Indemnitee is not a party, he shall be indemnified against all Expenses actually and reasonably incurred by Indemnitee (or on his behalf) in connection therewith.

6. Indemnification for Expenses of Successful Party. Notwithstanding any other provision of this Agreement to the contrary, to the extent that Indemnitee has been successful on the merits or otherwise in defense of any Proceeding referred to in Sections 3 and/or 4 of this Agreement, or in defense of any claim, issue or matter therein, including dismissal without prejudice, Indemnitee shall be indemnified against all Expenses actually and reasonably incurred by Indemnitee (or on his behalf) in connection therewith. If Indemnitee is not wholly successful in any Proceeding referred to in Sections 3 and/or 4 of this Agreement, but is successful on the merits or otherwise (including dismissal without prejudice) as to one or more, but less than all claims, issues or matters therein, including dismissal without prejudice, Indemnitee shall be indemnified against all Expenses actually and reasonably incurred by Indemnitee (or on his behalf) in connection with each successfully resolved claim, issue or matter. For purposes of this Section 6, and without limitation, the termination of any claim, issue or matter in any Proceeding referred to in Sections 3 and/or 4 of this Agreement by dismissal, with or without prejudice, shall be deemed to be a successful result as to such claim, issue or matter.

7. Advances of Expenses. To the fullest extent permitted by applicable law, the Expenses incurred by Indemnitee pursuant to Sections 3 and/or 4 of this Agreement in connection with any Proceeding or any claim, issue or matter therein shall be paid by the Company in advance of the final disposition of such Proceeding or any claim, issue or matter therein no later than 10 days after receipt by the Company of an undertaking by or on behalf of Indemnitee ("Indemnitee Undertaking") to repay such amount to the extent that it is ultimately determined that Indemnitee is not entitled to be indemnified by the Company. The Indemnitee Undertaking, which shall not be secured and shall be interest free, shall be substantially on the form of Exhibit A to this Agreement.

8. Procedure for Determination of Entitlement to Indemnification.

(a) To obtain indemnification under this Agreement, Indemnitee shall submit to the Company a written request.

(b) Upon written request by Indemnitee for indemnification pursuant to Section 8(a) hereof, a determination, if required by applicable law, with respect to Indemnitee's entitlement thereto shall be made in the specific case: (i) if a Change in Control shall have occurred, by Independent Counsel in a written opinion to the board of directors of the Company, a copy of which shall be delivered to Indemnitee; or (ii) if a Change in Control shall not have occurred, (A) by a majority vote of the Disinterested Directors, even though less than a quorum of the board of directors of the Company, or (B) by a committee of the Disinterested Directors designated by a majority vote of Disinterested Directors, even though less than a quorum, or (C) if there are no Disinterested Directors or, if the Disinterested Directors so direct, by Independent Counsel in a written opinion to the board of directors of the Company, a copy of which shall be delivered to Indemnitee; and, if it is so determined that Indemnitee is entitled to indemnification, payment to Indemnitee shall be made within 10 days after such determination. Any costs or expenses (including attorneys' fees and disbursements) incurred by Indemnitee in cooperating with the person, persons or entity making the determination discussed in this Section 8(b) with respect to Indemnitee's entitlement to indemnification, shall be borne by the Company (irrespective of the determination as to Indemnitee's entitlement to indemnification) and the Company hereby indemnifies and agrees to hold Indemnitee harmless therefrom.

(c) In the event the determination of entitlement to indemnification is to be made by Independent Counsel pursuant to Section 8(b) hereof, the Independent Counsel shall be selected as provided in this Section 8(c). If a Change in Control shall not have occurred, the Independent Counsel shall be selected by the board of directors of the Company, and the Company shall give written notice to Indemnitee advising him of the identity of the Independent Counsel so selected. If a Change in Control shall have occurred, the Independent Counsel shall be selected by Indemnitee (unless Indemnitee shall request that such selection be made by the board of directors of the Company, in which event the preceding sentence shall apply), and Indemnitee shall give written notice to the Company advising it of the identity of the Independent Counsel so selected. In either event, Indemnitee or the Company, as the case may be, may, within 10 days after such written notice of selection shall have been given, deliver to the Company or to Indemnitee, as the case may be, a written objection to such selection; provided, however, that such objection may be asserted only on the ground that the Independent Counsel so selected does not meet the requirements of "Independent Counsel" as defined in this Agreement, and the objection shall set forth with particularity the factual basis of such assertion. Absent a proper and timely objection, the person so selected shall act as Independent Counsel. If such written objection is so made and substantiated, the Independent Counsel so selected may not serve as Independent Counsel unless and until such objection is withdrawn or a court has determined that such objection is without merit. If, within 20 days after submission by Indemnitee of a written request for indemnification pursuant to Section 8(b) hereof, no Independent Counsel shall have been selected and not objected to, either the Company or Indemnitee may petition the Delaware Court of Chancery or other court of competent jurisdiction for resolution of any objection which shall have been made by the Company or Indemnitee to the other's selection of Independent Counsel and/or for the appointment as Independent Counsel of a person selected by the Court or by such other person as the Court shall designate, and the person with respect to whom all objections are so resolved or the person so appointed shall act as Independent Counsel under Section 8(a) hereof.

(d) Indemnitee will be deemed a party to a Proceeding for all purposes hereof if Indemnitee is named as a defendant or respondent in a complaint or petition for relief in that Proceeding, regardless of whether Indemnitee is ever served with process or makes an appearance in that Proceeding.

9. Presumptions and Effect of Certain Provisions. (a) In making a determination with respect to entitlement to indemnification hereunder, the person or persons or entity making such determination shall presume that Indemnitee is entitled to indemnification under this Agreement if Indemnitee has submitted a request for indemnification in accordance with Section 8(a) of this Agreement, and the Company shall have the burden of proof in overcoming such presumption by clear and convincing evidence. Neither the failure of the Company (including its board of directors or independent legal counsel) to have made a determination prior to the commencement of such action pursuant to this Agreement that indemnification is proper in the circumstances because Indemnitee has met the applicable standard of conduct, nor an actual determination by the Company (including its board of directors or independent legal counsel) that Indemnitee has not met such applicable standard of conduct, shall be a defense to the action or create a presumption that Indemnitee has not met the applicable standard of conduct.

(b) If the person, persons or entity empowered or selected under Section 8 of this Agreement to determine whether Indemnitee is entitled to indemnification shall not have made a determination within 30 days after receipt by the Company therefor, the requisite determination of entitlement to indemnification shall be deemed to have been made and Indemnitee shall be entitled to such indemnification, absent (i) a misstatement by Indemnitee of a material fact, or an omission of a material fact necessary to make Indemnitee's statement not materially misleading, in connection with the request for indemnification, or (ii) a prohibition of such indemnification under applicable law; provided, however, that such 30-day period may be extended for a reasonable time, not to exceed an additional 15 days, if the person, persons or entity making the determination with respect to entitlement to indemnification in good faith requires such additional time for the obtaining or evaluating of documentation and/or information relating thereto.

(c) For purposes of any determination of whether Indemnitee acted in good faith and in a manner reasonably believed to be in or not opposed to the best interests of the Company, and, with respect to any criminal Proceeding, Indemnitee had no reasonable cause to believe his conduct was unlawful (collectively, "Good Faith"), Indemnitee shall be deemed to have acted in Good Faith if Indemnitee's action is based on the records or books of account of the Company and any other corporation, partnership, joint venture, trust, employee benefit plan or other enterprise of which Indemnitee is or was serving at the request of the Company as a director, officer, employee or agent ("Enterprise"), information, opinions, reports or statements, including financial statements and other financial information, concerning the Enterprise or any other Person which were prepared or supplied to Indemnitee by: (i) one or more officers or employees of the Enterprise; (ii) appraisers, engineers, investment bankers, legal counsel or other Persons as to matters Indemnitee reasonably believed were within the professional or expert competence of those Persons; and (iii) any committee of the Board of Directors or equivalent managing body of the Enterprise of which Indemnitee is or was, at the relevant time, not a member. The provisions of this Section 9(c) shall not be deemed to be exclusive or to limit in any way the other circumstances in which the Indemnitee may be deemed to have met the applicable standard of conduct set forth in this Agreement.

(d) The knowledge and/or actions, or failure to act, of any director, officer, agent or employee of the Enterprise shall not be imputed to Indemnitee for purposes of determining the right to indemnification under this Agreement.

10. Remedies of Indemnitee.

(a) n the event that (i) a determination is made pursuant to Section 8(b) of this Agreement that Indemnitee is not entitled to indemnification under this Agreement, (ii) advancement of Expenses is not timely made pursuant to Section 7 of this Agreement, (iii) no determination of entitlement to indemnification shall have been made pursuant to Section 8(b) of this Agreement within the time period provided in Section 9(b) after receipt by the Company of the request for indemnification, (iv) payment of indemnification is not made pursuant to Section 5, Section 6, the last sentence of Section 8(b), or the last sentence of Section 2(d) of this Agreement within 10 days after receipt by the Company of a written request therefor, or (v) payment of indemnification pursuant to Section 3 or Section 4 of this Agreement is not made within 10 days after a determination has been made that Indemnitee is entitled to indemnification, Indemnitee shall be entitled to an adjudication by the Delaware Court of Chancery of his entitlement to such indemnification or advancement of Expenses and appeals therefrom, concluding in a final and unappealable judgment by the Delaware Supreme Court. The Board of Directors shall not make a determination as to the final disposition of such adjudication. The Company shall not oppose Indemnitee's right to seek any such adjudication.

(b) In the event that a determination shall have been made pursuant to Section 8(b) of this Agreement that Indemnitee is not entitled to indemnification, any judicial proceeding commenced pursuant to this Section 10 shall be conducted in all respects as a de novo trial on the merits and Indemnitee shall not be prejudiced by reason of that adverse determination.

(c) If a determination shall have been made pursuant to Section 8(a) of this Agreement that Indemnitee is entitled to indemnification, the Company shall be bound by such determination in any judicial proceeding commenced pursuant to this Section 10, absent (i) a misstatement by Indemnitee of a material fact, or an omission of a material fact necessary to make Indemnitee's statement not materially misleading, in connection with the request for indemnification, or (ii) a prohibition of such indemnification under applicable law.

(d) In the event that Indemnitee, pursuant to this Section 10, seeks a judicial adjudication of his rights under, or to recover damages for breach of, this Agreement, Indemnitee shall be entitled to recover from the Company, and shall be indemnified by the Company against, any and all expenses (of the types described in the definition of Expenses in Section 2(d) of this Agreement) actually and reasonably incurred by him in such judicial adjudication, but only if (and only to the extent) he prevails therein. If it shall be determined in said judicial adjudication that Indemnitee is entitled to receive part but not all of the indemnification or advancement of Expenses sought, the expenses incurred by Indemnitee in connection with such judicial adjudication shall be appropriately prorated.

(e) The Company shall be precluded from asserting in any judicial proceeding commenced pursuant to this Section 10 that the procedures and presumptions of this Agreement are not valid, binding and enforceable and shall stipulate in any such court that the Company is bound by all the provisions of this Agreement.

11. Indemnification and Advancement of Expenses Under this Agreement Not Exclusive; Survival of Rights. The rights of indemnification and to receive advancement of Expenses as provided by this Agreement shall not be deemed exclusive of any other rights to which Indemnitee may be entitled under the Certificate of Incorporation or Bylaws of the Company, any other agreement, any vote of stockholders or disinterested directors, the General Corporation Law of the State of Delaware, or otherwise. No amendment, alteration or repeal of this Agreement or of any provision hereof shall limit or restrict any right of Indemnitee under this Agreement in respect of any action taken or omitted by such Indemnitee prior to such amendment, alteration or repeal. To the extent that a change in the General Corporation Law of the State of Delaware, whether by statute or judicial decision, permits greater indemnification or advancement of Expenses than would be afforded currently under the Certificate of Incorporation of the Company and this Agreement, it is the intent of the parties hereto that Indemnitee shall enjoy by this Agreement the greater benefits so afforded by such change. No right or remedy herein conferred is intended to be exclusive of any other right or remedy, and every other right and remedy shall be cumulative and in addition to every other right and remedy given hereunder or now or hereafter existing at law or in equity or otherwise. The assertion or employment of any right or remedy hereunder, or otherwise, shall not prevent the concurrent assertion or employment of any other right or remedy.

12. Partial Indemnification. If Indemnitee is entitled under any provision of this Agreement to indemnification or to receive advancement by the Company for a portion of the Expenses, judgments, fines, penalties or amounts paid in settlement actually and reasonably incurred by Indemnitee (or on his behalf) in connection with such Proceeding, or any claim, issue or matter therein, but not, however, for the total amount thereof, the Company shall nevertheless indemnify Indemnitee for the portion thereof to which Indemnitee is entitled.

13. Rights Continued. The rights of indemnification and to receive advancement of Expenses as provided by this Agreement shall continue as to Indemnitee even though Indemnitee may have ceased to be a director or officer of the Company and shall inure to the benefit of Indemnitee's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees and legatees.

14. No Construction as an Employment Agreement or Any Other Commitment. Nothing contained in this Agreement shall be construed as giving Indemnitee any right to be retained in the employ or as an officer of the Company or any of its subsidiaries, if Indemnitee currently serves as an officer of the Company, or to be renominated or reelected as a director of the Company, if Indemnitee currently serves as a director of the Company.

15. Liability Insurance. To the extent the Company maintains an insurance policy or policies providing liability insurance for directors, officers, employees or agents of the Company or of any other corporation, partnership, joint venture, trust, employee benefit plan or other enterprise which such person serves at the request of the Company, Indemnitee shall be covered by such policy or policies in accordance with its or their terms, to the maximum extent of the coverage available for any director, officer, employee or agent under such policy or policies.

16. No Duplication of Payments. The Company shall not be liable under this Agreement to make any payment of amounts otherwise indemnifiable under this Agreement if, and to the extent that, Indemnitee has otherwise actually received such payment under any contract, agreement or insurance policy, the Certificate of Incorporation or Bylaws of the Company, or otherwise.

17. Subrogation. In the event of payment under this Agreement, the Company shall be subrogated to the extent of such payment to all the rights of recovery of Indemnitee, who shall execute all papers required and shall do everything that may be necessary to secure such rights, including without limitation the execution of such documents as may be necessary to enable the Company effectively to bring suit to enforce such rights.

18. Exceptions. Notwithstanding any other provision in this Agreement, but except as provided in Section 10(d), the Company shall not be obligated pursuant to the terms of this Agreement, to indemnify or advance Expenses to Indemnitee with respect to any Proceeding, or any claim, issue or matter therein, (i) brought or made by Indemnitee, unless the bringing of such Proceeding or the making of such claim, issue or matter shall have been approved by the Board of Directors of the Company, or (ii) in which final judgment is rendered against Indemnitee for an accounting of profits made from the purchase and sale or the sale and purchase by Indemnitee of securities of the Company pursuant to the provisions of Section 16(b) of the Securities Exchange Act of 1934, as amended, or similar provisions of any federal, state or local statute.

19. Notices. Any notice or other communication required or permitted to be given or made to the Company or Indemnitee pursuant to this Agreement shall be given if made in writing and deposited in the United States mail, with postage thereon prepaid, addressed to the person to whom such notice or communication is directed at the address of such person on the records of the Company, and such notice or communication shall be deemed given or made at the time when the same shall be so deposited in the United States mail. Any such notice or communication to the Company shall be addressed to the Secretary of the Company.

20. Contractual Rights. The right to be indemnified or to receive advancement of Expenses under this Agreement (i) is a contract right based upon good and valuable consideration, pursuant to which Indemnitee may sue, (ii) is and is intended to be retroactive and shall be available as to events occurring prior to the date of this Agreement and (iii) shall continue after any rescission or restrictive modification of this Agreement as to events occurring prior thereto.

21. Severability. If any provision or provisions of this Agreement shall be held to be invalid, illegal or unenforceable for any reason whatsoever, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby; to the fullest extent possible, the provisions of this Agreement shall be construed so as to give effect to the intent manifested by the provisions held invalid, illegal or unenforceable; and those provision or provisions held to be invalid, illegal or unenforceable for any reason whatsoever shall be deemed reformed to the extent necessary to conform to applicable law and to give the maximum effect to the intent of the parties hereto.

22. Successors; Binding Agreement. The Company shall require and cause any successor (whether direct or indirect) by purchase, merger, consolidation or otherwise) to all or substantially all of the business or assets of the Company, by written agreement in form and substance reasonably satisfactory to Indemnitee, to expressly assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform if no such succession had taken place. As used in this Agreement, "Company" shall mean the Company as hereinbefore defined and any successor to its business and/or assets as aforesaid that executes and delivers the agreement provided for in this Section 22 or that otherwise becomes bound by the terms and provisions of this Agreement by operation of law. This Agreement shall be binding upon the Company and its successors and assigns (including, without limitation, any direct or indirect successor by purchase, merger, consolidation or otherwise to all or substantially all of the business or assets of the Company) and will inure to the benefit of Indemnitee (and Indemnitee's spouse, if Indemnitee resides in Texas or another community property state), heirs, executors and administrators.

23. Counterparts, Modification, Headings, Gender.

(a) This Agreement may be executed in counterparts, each of which shall constitute one and the same instrument, and either party hereto may execute this Agreement by signing any such counterpart.

(b) No provisions of this Agreement may be modified, waived or discharged unless such waiver, modification or discharge is agreed to in writing and signed by Indemnitee and an appropriate officer of the Company. No waiver by any party at any time of any breach by any other party of, or compliance with, any condition or provision of this Agreement to be performed by any other party shall be deemed a waiver of similar or dissimilar provisions or conditions at the same time or at any prior or subsequent time.

(c) Section headings are not to be considered part of this Agreement, are solely for convenience of reference, and shall not affect the meaning or interpretation of this Agreement or any provision set forth herein.

(d) Pronouns in masculine, feminine and neuter genders shall be construed to include any other gender, and words in the singular form shall be construed to include the plural and vice versa, unless the context otherwise requires.

24. Exclusive Jurisdiction; Governing Law. The Company and Indemnitee agree that all disputes in any way relating to or arising under this Agreement, including, without limitation, any action for advancement of Expenses or indemnification, shall be litigated, if at all, exclusively in the Delaware Court of Chancery, and if necessary, the corresponding appellate courts. This Agreement shall be governed by and construed and enforced in accordance with the laws of the State of Delaware applicable to contracts made and to be performed in such state without giving effect to the principles of conflicts of laws. The Company and Indemnitee (i) expressly submit themselves to the personal jurisdiction of the Delaware Court of Chancery for purposes of any action or proceeding arising out of or in connection with this Agreement, (ii) irrevocably appoint, to the extent such party is not a resident of the State of Delaware, The Corporation Trust Company, 1209 Orange Street, Wilmington, Delaware 19801 as its agent in the State of Delaware as such party's agent for acceptance of legal process in connection with any such action or proceeding against such party with the same legal force and validity as if served upon such party personally within the State of Delaware, (iii) waive any objection to the laying of venue of any such action or proceeding in the Delaware Court of Chancery, and (iv) waive, and agree not to plead or to make, any claim that any such action or proceeding brought in the Delaware Court of Chancery has been brought in an improper or otherwise inconvenient forum.

25. Duration of Agreement. This Agreement shall continue until and terminate upon the later of: (a) 10 years after the date that Indemnitee shall have ceased to serve as a director and/or officer of the Company or director, officer, employee or agent of any other corporation, partnership, joint venture, trust, employee benefit plan or other enterprise which Indemnitee served at the request of the Company; or (b) one year after the final, nonappealable termination of any Proceeding then pending in respect of which Indemnitee is granted rights of indemnification or advancement of Expenses hereunder and of any proceeding commenced by Indemnitee pursuant to Section 10 of this Agreement relating thereto.

26. Contribution. If it is established, under Section 8 or otherwise, that Indemnitee has the right to be indemnified under this Agreement in respect of any claim, but that right is unenforceable by reason of applicable law or public policy, then, to the fullest extent applicable law permits, the Company, in lieu of indemnifying or causing the indemnification of Indemnitee under this Agreement, will contribute to the amount Indemnitee has incurred, whether for judgments, fines, penalties, excise taxes, amounts paid or to be paid in settlement or for Expenses reasonably incurred, in connection with that Proceeding, in such proportion as is deemed fair and reasonable in light of all the circumstances of that Proceeding in order to reflect:

(a) the relative benefits Indemnitee and the Company have received as a result of the event(s) or transactions(s) giving rise to that Proceeding; or

(b) the relative fault of Indemnitee and of the Company and its other functionaries in connection with those event(s) or transaction(s).

IN WITNESS WHEREOF, the Company and Indemnitee have executed this Agreement as of the date and year first above written.

CROSSTEX ENERGY HOLDINGS INC.

By: ______________________

Name: ______________________

Title: ______________________

INDEMNITEE

____

EXHIBIT A

INDEMNITEE'S UNDERTAKING

, 2003

Crosstex Energy Holdings Inc.
410 Park Avenue
New York, NY 10022

Re:

Indemnity Agreement

Ladies and Gentlemen:

Reference is made to the Indemnity Agreement dated as of , 2003 by and between Crosstex Energy Holdings Inc. and the undersigned Indemnitee, and particularly to Section 7 thereof relating to advance payment by the Company of certain Expenses incurred by the undersigned Indemnitee. Capitalized terms used and not otherwise defined in this Indemnitee's Undertaking shall have the respective meanings given to such terms in the Agreement.

The types and amounts of Expenses incurred by or on behalf of the undersigned Indemnitee are itemized on Attachment I to this Indemnitee's Undertaking. The undersigned Indemnitee hereby requests that the total amount of these Expenses (the "Advanced Amount") be paid by the Company in advance of the final disposition of such Proceeding in accordance with the Agreement.

The undersigned Indemnitee hereby agrees to repay the Advanced Amount to the Company to the extent that it is ultimately determined pursuant to Section 8, or, in the event the Indemnitee elects to pursue other remedies pursuant to Section 10, that the undersigned Indemnitee is not entitled to be indemnified therefor by the Company. This agreement of Indemnitee to repay shall be unsecured and shall be interest free.

Very truly yours,

Signature

Name of Indemnitee (Type or Print)

ATTACHMENT I TO
INDEMNITEE'S UNDERTAKING

ITEMIZATION OF
TYPES AND AMOUNTS OF EXPENSES

Attached hereto are receipts, statements or invoices for the following qualifying Expenses which Indemnitee represents have been incurred by Indemnitee in connection with a Proceeding:

	Type	Amount
1.		

Total Advanced Amount

QuickLinks

Exhibit 10.2
INDEMNITY AGREEMENT

EXHIBIT A
INDEMNITEE'S UNDERTAKING
ATTACHMENT I TO INDEMNITEE'S UNDERTAKING ITEMIZATION OF TYPES AND AMOUNTS OF EXPENSES

Exhibit 10.4

AGREEMENT REGARDING 2003 REGISTRATION STATEMENT
AND WAIVER AND TERMINATION OF STOCKHOLDERS' AGREEMENT

THIS AGREEMENT REGARDING 2003 REGISTRATION STATEMENT AND WAIVER AND TERMINATION OF STOCKHOLDERS' AGREEMENT, dated October 27, 2003, is by and among Yorktown Energy Partners IV, L.P., a Delaware limited partnership, Yorktown Energy Partners V, L.P., a Delaware limited partnership, Lubar Nominees, a general partnership, Barry E. Davis, A. Chris Aulds, James R. Wales, William W. Davis, Jack M. Lafield, Michael P. Scott, Lisa M. Brecht, John W. Daugherty, Mike Hopkins, Mark E. Huff, Marc Lyons, Rodney A. Madden, Stewart McCorkle and Dale Wilson (collectively, the "Stockholders"), and Crosstex Energy Holdings Inc., a Delaware corporation (the "Company").

W I T N E S E T H:

WHEREAS, the Stockholders and the Company are parties to a Stockholders' Agreement dated May 5, 2000 and amended May 2, 2001 (the "Stockholders' Agreement);

WHEREAS, the Company intends to register under the Securities Act of 1933, as amended, Registrable Shares (as defined in the Stockholders' Agreement) of the Stockholders in the numbers set forth opposite their signatures hereto (the "Offering");

WHEREAS, the Stockholders will use the proceeds from the sale of the Registrable Shares to pay off promissory notes held by the Company;

WHEREAS, in connection with the Offering, the parties hereto desire to define the obligations of the Company and the Stockholders with respect to the Offering and waive and terminate certain provisions of the Stockholders' Agreement, upon the terms and conditions contained herein;

NOW, THEREFORE, in consideration such good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

1. *Registration*. The Company shall include in a registration statement the number of Registrable Shares of the Stockholders set forth opposite their signatures hereto and the provisions of Article V of the Stockholders' Agreement are adopted by all the parties hereto with respect to the Offering and agreed to in all respects.

2. *Waiver and Termination*. The parties agree to, and do hereby, waive the terms of any and all options and rights to purchase, voting agreements, registration rights, and all other rights and requirements under the Stockholders' Agreement and terminate the Stockholders' Agreement effective concurrent with the closing of the Offering, except for the provisions of Section 5.8, which shall survive such termination. Upon termination, no party shall have any further liability or obligations to any other party under the Stockholders' Agreement except as otherwise expressly provided for herein.

3. *Title*. Each Stockholder represents and warrants that (a) he has not sold, transferred, assigned, pledged or otherwise conveyed to any other party any interest in the Stockholders' Agreement and (b) he has the full right, power and authority to enter into this Termination Agreement and to terminate the Stockholders' Agreement.

4. *Joinder of Spouses*. The spouses of each Stockholder hereby join in the execution and delivery of this Agreement for the purpose of binding their respective community property interests, if any, in the Stockholders' Agreement to the terms and conditions hereof in all respects.

5. *Entire Agreement*. This Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter hereof and supersedes all prior agreements and understandings, both written and oral, between the parties with respect to the subject matter hereof.

6. *Binding Effect*. This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors, assigns, heirs and legal representatives.

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7. *Amendment and Waiver*. This Agreement may be amended, superseded, cancelled, renewed or extended, and the terms hereof may be waived, only by a written instrument signed by the parties or, in the case of a waiver, by the party waiving compliance.

8. *Governing Law*. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware.

9. *Counterparts*. This Agreement may be executed in any number of counterparts, each of which shall be deemed an original, but all of which shall constitute one and the same agreement.

10. *Gender*. Pronouns in masculine, feminine and neuter genders shall be construed to include any other gender, and words in the singular form shall be construed to include the plural and vice versa, unless the context otherwise requires.

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

1,371,000
Number of Registrable Shares

YORKTOWN ENERGY PARTNERS IV, L.P.

By: Yorktown IV Company LLC,

its General Partner

By: /s/ PETER A. LEIDEL

Name: Peter A. Leidel

Title: Member

343,000
Number of Registrable Shares

YORKTOWN ENERGY PARTNERS V, L.P.

By: Yorktown V Company LLC,
its General Partner

By: /s/ PETER A. LEIDEL

Name: Peter A. Leidel

Title: Member

-0-
Number of Registrable Shares

LUBAR NOMINEES

By: /s/ SHELDON B. LUBAR

Name: Sheldon B. Lubar

Title: General Partner

190,000
Number of Registrable Shares

/s/ BARRY E. DAVIS

Barry E. Davis

/s/ ANTOINETTE DAVIS

Spouse of Barry E. Davis

150,000
Number of Registrable Shares

/s/ A. CHRIS AULDS

A. Chris Aulds

/s/ TERESA P. AULDS

Spouse of A. Chris Aulds

85,000
Number of Registrable Shares

/s/ JAMES R. WALES

James R. Wales

/s/ LORI M. WALES

Spouse of James R. Wales

26,000
Number of Registrable Shares

/s/ WILLIAM W. DAVIS

William W. Davis

/s/ CATHY C. DAVIS

Spouse of William W. Davis

25,000
Number of Registrable Shares

/s/ JACK M. LAFIELD

Jack M. Lafield

/s/ MICHELE LAFIELD

Spouse of Jack M. Lafield

18,500
Number of Registrable Shares

/s/ MICHAEL P. SCOTT

Michael P. Scott

/s/ DONNA SCOTT

Spouse of Michael P. Scott

20,000
Number of Registrable Shares

/s/ LISA M. BRECHT

Lisa M. Brecht

25,500
Number of Registrable Shares

/s/ JOHN W. DAUGHERTY

John W. Daugherty

/s/ JO ANN R. DAUGHERTY

Spouse of John W. Daugherty

21,000
Number of Registrable Shares

/s/ MIKE HOPKINS

Mike Hopkins

/s/ MARY H. HOPKINS

Spouse of Mike Hopkins

22,000
Number of Registrable Shares

/s/ MARK E. HUFF

Mark E. Huff

/s/ LISA Y. HUFF

Spouse of Mark E. Huff

9,000
Number of Registrable Shares

/s/ RODNEY A. MADDEN

Rodney A. Madden

/s/ KIM MADDEN

Spouse of Rodney A. Madden

-0-

Number of Registrable Shares	/s/ MARC LYONS Marc Lyons /s/ GEORGIA O. LYONS Spouse of Marc Lyons
-0- Number of Registrable Shares	/s/ STEWART MCCORKLE Stewart McCorkle
-0- Number of Registrable Shares	/s/ DALE WILSON Dale Wilson
-0- Number of Registrable Shares	MK Holdings, L.P. By: MK Holdings GP, L.L.C. By: /s/ BARRY E. DAVIS Name: Barry E. Davis Title: Manager CROSSTEX ENERGY HOLDINGS INC. By: /s/ BRYAN H. LAWRENCE Name: Bryan H. Lawrence Title: Chairman

QuickLinks

Exhibit 10.4
AGREEMENT REGARDING 2003 REGISTRATION STATEMENT AND WAIVER AND TERMINATION OF STOCKHOLDERS' AGREEMENT

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 10.5

CROSSTEX ENERGY, INC.
LONG-TERM INCENTIVE PLAN
(Amended and Restated Effective as of December 31, 2003)

ARTICLE I. ESTABLISHMENT AND PURPOSE

1.1 Establishment. The Crosstex Energy Holdings, Inc. 2000 Stock Option Plan was originally approved by the Board of Directors of Crosstex Energy, Inc., a Delaware corporation, on May 5, 2000. In furtherance of the purposes of said plan and in order to amend said plan in certain respects, the plan is hereby amended and restated in its entirety and renamed the Crosstex Energy, Inc. Long-Term Incentive Plan (the "Plan"), as set forth in this document.

1.2 Purpose. The purposes of the Plan are to attract able persons to enter the employ of the Company, to encourage Employees to remain in the employ of the Company and to provide motivation to Employees to put forth maximum efforts toward the continued growth, profitability and success of the Company, by providing incentives to such persons through the ownership and/or performance of the Common Stock of Crosstex. A further purpose of the Plan is to provide a means through which the Company may attract able persons to become directors of the Company and to provide such individuals with incentive and reward opportunities. Toward these objectives, Awards may be granted under the Plan to Employees and Outside Directors on the terms and subject to the conditions set forth in the Plan.

1.3 Effectiveness. This amended and restated Plan shall become effective as of December 31, 2003, the date of its adoption by the Board, provided it is duly approved by the holders of at least a majority of the shares of Common Stock present or represented and entitled to vote at a meeting of the stockholders of Crosstex duly held in accordance with applicable law within twelve months after the date of adoption of the Plan by the Board. If the amended and restated Plan is not so approved, the amended and restated Plan shall not be effective, any Award granted under the amended and restated Plan shall be null and void, and the Superseded Plan (and option grants made under said plan) shall remain in full force and effect.

ARTICLE II. DEFINITIONS

2.1 Affiliate. "Affiliate" means, with respect to any Person, any other Person that directly or indirectly through one or more intermediaries controls, is controlled by or is under common control with, the Person in question. As used herein, the term "control" means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a Person, whether through ownership of voting securities, by contract or otherwise. With respect to an Incentive Stock Option, "Affiliate" means a "parent corporation" or a "subsidiary corporation" of Crosstex, as those terms are defined in Section 424(e) and (f) of the Code.

2.2 Award. "Award" means an award granted to a Participant in the form of an Option, Phantom Option, Restricted Stock, SAR, or Other Incentive Award, whether granted singly, in combination or in tandem. All Awards shall be granted by, confirmed by, and subject to the terms of, an Award Agreement.

2.3 Award Agreement. "Award Agreement" means a written agreement between Crosstex and a Participant that sets forth the terms, conditions, restrictions and/or limitations applicable to an Award.

2.4 Board. "Board" means the Board of Directors of Crosstex.

2.5 Cause. "Cause" means the termination of a Participant's employment or service by reason of fraud, dishonesty, any unauthorized use or disclosure by the Participant of any confidential information or trade secrets of Crosstex, or the performance of other acts detrimental to Crosstex or an Affiliate, as determined by the Committee in its absolute discretion.

2.6 Change of Control. "Change of Control" shall have the meaning set forth in Section 12.1.

2.7 Code. "Code" means the Internal Revenue Code of 1986, as amended from time to time, including regulations thereunder and successor provisions and regulations thereto.

2.8 Committee. "Committee" means (i) with respect to the application of this Plan to Employees, the Compensation Committee of the Board or such other committee of the Board as may be designated by the Board to administer the Plan, which committee shall consist of two or more non-employee directors, each of whom is both a "non-employee director" under Rule 16b-3 of the Exchange Act and an "outside director" under Section 162(m) of the Code, and (ii) with respect to the application of this Plan to an Outside Director, the Board. To the extent that no Committee exists that has the authority to administer the Plan, the functions of the Committee shall be exercised by the Board. If for any reason the appointed Committee does not meet the requirements of Rule 16b-3 or Section 162(m) of the Code, such noncompliance with such requirements shall not affect the validity of Awards, grants, interpretations or other actions of the Committee.

2.9 Common Stock. "Common Stock" means the common stock, $.01 par value per share, of Crosstex, or any stock or other securities of Crosstex hereafter issued or issuable in substitution or exchange for the Common Stock.

2.10 Company. "Company" means Crosstex and its Affiliates.

2.11 Crosstex. "Crosstex" means Crosstex Energy, Inc., a Delaware corporation, or any successor thereto.

2.12 Effective Date. "Effective Date" means the date this Plan becomes effective as provided in Section 1.3.

2.13 Employee. "Employee" means an employee of Crosstex or an Affiliate of Crosstex; provided, however, that the term "Employee" does not include an Outside Director or an individual performing services for Crosstex or an Affiliate who is treated for tax purposes as an independent contractor at the time of performance of the services.

2.14 Exchange Act. "Exchange Act" means the Securities Exchange Act of 1934, as amended.

2.15 Fair Market Value. "Fair Market Value" means the closing sales price of a share of Common Stock on the applicable date (or if there is no trading in the Common Stock on such date, on the next preceding date on which there was trading) as reported in *The Wall Street Journal*(or other reporting service approved by the Committee). In the event the Common Stock is not publicly traded at the time a determination of fair market value is required to be made hereunder, the determination of fair market value shall be made in good faith by the Committee.

2.16 Grant Date. "Grant Date" means the date an Award is granted by the Committee.

2.17 Incentive Stock Option. "Incentive Stock Option" means an Option that is intended to meet the requirements of Section 422(b) of the Code.

2.18 Nonqualified Stock Option. "Nonqualified Stock Option" means an Option that is not an Incentive Stock Option.

2.19 Option. "Option" means an option to purchase shares of Common Stock granted to a Participant pursuant to Article VII. An Option may be either an Incentive Stock Option or a Nonqualified Stock Option, as determined by the Committee.

2.20 Other Incentive Award. "Other Incentive Award" means an incentive award granted to a Participant pursuant to Article XI.

2.21 Outside Director. "Outside Director" means a "non-employee director" of the Company, as defined in Rule 16b-3.

2.22 Participant. "Participant" means an Employee or Outside Director to whom an Award has been granted under the Plan.

2.23 Person. "Person" means an individual or a corporation, limited liability company, partnership, joint venture, trust, unincorporated organization, association, government agency or political subdivision thereof or other entity.

2.24 Phantom Option. "Phantom Option" means a fictional option granted to a Participant pursuant to Article VIII.

2.25 Plan. "Plan" means this Crosstex Energy, Inc. Long-Term Incentive Plan, as amended from time to time.

2.26 Restricted Stock. "Restricted Stock" means shares of Common Stock granted to a Participant pursuant to Article IX, which are subject to such restrictions as may be determined by the Committee. Restricted Stock shall constitute issued and outstanding shares of Common Stock for all corporate purposes.

2.27 Rule 16b-3. "Rule 16b-3" means Rule 16b-3 promulgated by the SEC under the Exchange Act, or any successor rule or regulation thereto as in effect from time to time.

2.28 SAR. "SAR" means a stock appreciation right granted to a Participant pursuant to Article X.

2.29 Superseded Plan. "Superseded Plan" means the Crosstex Energy Holdings, Inc. 2000 Stock Option Plan, as in effect prior to the Effective Date.

ARTICLE III. PLAN ADMINISTRATION

3.1 Plan Administrator. The Plan shall be administered by the Committee. The Committee may delegate some or all of its power to the Chief Executive Officer or other executive officer of the Company as the Committee deems appropriate; provided, that (i) the Committee may not delegate its power with regard to the grant of an Award to any person who is a "covered employee" within the meaning of Section 162(m) of the Code or who, in the Committee's judgment, is likely to be a covered employee at any time during the period an Award to such employee would be outstanding, and (ii) the Committee may not delegate its power with regard to the selection for participation in the Plan of an officer or other person subject to Section 16 of the Exchange Act or decisions concerning the timing, pricing or amount of an Award to such an officer or other person.

3.2 Authority of Administrator. The Committee shall have total and exclusive responsibility to control, operate, manage and administer the Plan in accordance with its terms. The Committee shall have all the authority that may be necessary or helpful to enable it to discharge its responsibilities with respect to the Plan. Without limiting the generality of the preceding sentence, the Committee shall have the exclusive right to: (i) interpret the Plan and the Award Agreements executed hereunder; (ii) determine eligibility for participation in the Plan; (iii) decide all questions concerning eligibility for, and the amount of, Awards granted under the Plan; (iv) construe any ambiguous provision of the Plan or any Award Agreement; (v) prescribe the form of the Award Agreements embodying Awards granted under the Plan; (vi) correct any defect, supply any omission or reconcile any inconsistency in the Plan or any Award Agreement; (vii) issue administrative guidelines as an aid to administering the Plan and make changes in such guidelines as the Committee from time to time deems proper; (viii) make regulations for carrying out the Plan and make changes in such regulations as the Committee from time to time deems proper; (ix) determine whether Awards should be granted singly, in combination or in tandem; (x) to the extent permitted under the Plan, grant waivers of Plan terms, conditions, restrictions and limitations; (xi) accelerate the exercise, vesting or payment of an Award when such action or actions would be in the best interests of the Company; (xii) grant Awards in replacement of Awards previously granted under the Plan or any other employee benefit plan of the Company; and (xiii) take any and all other actions the Committee deems necessary or advisable for the proper operation or administration of the Plan.

3.3 Discretionary Authority. The Committee shall have full discretionary authority in all matters related to the discharge of its responsibilities and the exercise of its authority under the Plan, including, without limitation, its construction of the terms of the Plan and its determination of eligibility for participation and Awards under the Plan. The decisions of the Committee and its actions with respect to the Plan shall be final, conclusive and binding on all persons having or claiming to have any right or interest in or under the Plan, including Participants and their respective estates, beneficiaries and legal representatives.

3.4 Liability; Indemnification. No member of the Committee nor any person to whom authority has been delegated, shall be personally liable for any action, interpretation or determination made in good faith with respect to the Plan or Awards granted hereunder, and each member of the Committee (or delegatee of the Committee) shall be fully indemnified and protected by Crosstex with respect to any liability he or she may incur with respect to any such action, interpretation or determination, to the extent permitted by applicable law.

ARTICLE IV. SHARES SUBJECT TO THE PLAN

4.1 Available Shares. The maximum number of shares of Common Stock that shall be available for grant of Awards under the Plan shall not exceed a total of 1,200,000, subject to adjustment as provided in Sections 4.2 and 4.3; provided, however, that from and after such time as Crosstex registers a class of equity securities under Section 12 of the Exchange Act, the maximum number of shares of Common Stock for which Options and SARs may be granted under the Plan to any one Participant during a calendar year is 100,000. Shares of Common Stock issued pursuant to the Plan may be shares of original issuance or treasury shares or a combination of the foregoing, as the Committee, in its absolute discretion, shall from time to time determine.

4.2 Adjustments for Recapitalizations and Reorganizations.

(a) The shares with respect to which Awards may be granted under the Plan are shares of Common Stock as presently constituted, but if, and whenever, prior to the expiration or satisfaction of an Award theretofore granted, Crosstex shall effect a subdivision or consolidation of shares of Common Stock or the payment of a stock dividend on Common Stock in the form of Crosstex Common Stock without receipt of consideration by Crosstex, the number of shares of Common Stock with respect to which such Award may thereafter be exercised or satisfied, as applicable, (i) in the event of an increase in the number of outstanding shares, shall be proportionately increased, and the exercise price per share shall be proportionately reduced, and (ii) in the event of a reduction in the number of outstanding shares, shall be proportionately reduced, and the exercise price per share shall be proportionately increased.

(b) If Crosstex recapitalizes or otherwise changes its capital structure, thereafter upon any exercise or satisfaction, as applicable, of an Award theretofore granted the Participant shall be entitled to (or entitled to purchase, if applicable) under such Award, in lieu of the number of shares of Common Stock then covered by such Award, the number and class of shares of stock or other securities to which the Participant would have been entitled pursuant to the terms of the recapitalization if, immediately prior to such recapitalization, the Participant had been the holder of record of the number of shares of Common Stock then covered by such Award.

(c) In the event of changes in the outstanding Common Stock by reason of a reorganization, merger, consolidation, combination, separation (including a spin-off or other distribution of stock or property), exchange, or other relevant change in capitalization occurring after the date of grant of any Award and not otherwise provided for by this Section 4.2, any outstanding Awards and any Award Agreements evidencing such Awards shall be subject to adjustment by the Committee in its absolute discretion as to the number, price and kind of shares or other consideration subject to, and other terms of, such Awards to reflect such changes in the outstanding Common Stock.

(d) In the event of any changes in the outstanding Common Stock provided for in this Section 4.2, the aggregate number of shares available for grant of Awards under the Plan may be equitably adjusted by the Committee, whose determination shall be conclusive. Any adjustment provided for in this Section 4.2 shall be subject to any required stockholder action.

4.3 Adjustments for Awards. The Committee shall have full discretion to determine the manner in which shares of Common Stock available for grant of Awards under the Plan are counted. Without limiting the discretion of the Committee under this Section 4.3, unless otherwise determined by the Committee, the following rules shall apply for the purpose of determining the number of shares of Common Stock available for grant of Awards under the Plan:

(a) **Options and Restricted Stock.** The grant of Options and Restricted Stock shall reduce the number of shares available for grant of Awards under the Plan by the number of shares subject to such Award.

(b) **SARs and Phantom Options.** The grant of SARs and Phantom Options shall not affect the number of shares available for grant of Awards under the Plan.

(c) **Other Incentive Awards.** The grant of an Other Incentive Award in the form of Common Stock or that may be paid or settled only in Common Stock shall reduce the number of shares available for grant of Awards under the Plan by the number of shares subject to such Award. The grant of an Other Incentive Award that may be paid or settled only for cash shall not affect the number of shares available for grant of Awards under the Plan. The grant of an Other Incentive Award that may be paid or settled in either Common Stock or cash shall reduce the number of shares available for grant of Awards under the Plan by the number of shares subject to such Award.

(d) **Termination.** If any Award referred to in paragraphs (a) and (c) above (other than an Other Incentive Award that may be paid or settled only for cash) is canceled or forfeited, or terminates, expires or lapses, for any reason (other than the termination of a Related Option (as defined in Section 10.1) upon exercise of its corresponding SARs), the shares then subject to such Award shall again be available for grant of Awards under the Plan.

(e) **Payment of Exercise Price and Withholding Taxes.** If previously acquired shares of Common Stock are used to pay the exercise price of an Award, the number of shares available for grant of Awards under the Plan shall not be increased by the number of shares delivered as payment of such exercise price. If previously acquired shares of Common Stock are used to pay withholding taxes payable upon exercise, vesting or payment of an Award, or shares of Common Stock that would be acquired upon exercise, vesting or payment of an Award are withheld to pay withholding taxes payable upon exercise, vesting or payment of such Award, the number of shares available for grant of Awards under the Plan shall not be increased by the number of shares delivered or withheld as payment of such withholding taxes.

(f) **Fractional Shares.** If any such adjustment would result in a fractional security being (i) available under the Plan, such fractional security shall be disregarded or (ii) subject to an Award, Crosstex shall pay the holder of such Award, in connection with the first vesting, exercise or settlement of such Award in whole or in part occurring after such adjustment, an amount in cash determined by multiplying (x) the fraction of such security (rounded to the nearest hundredth) by (y) the excess, if any, of the Fair Market Value on the vesting, exercise or settlement date over the exercise price, if any, of such Award.

ARTICLE V. ELIGIBILITY

All Employees and Outside Directors are eligible to participate in the Plan. The Committee shall recommend, from time to time, Participants from those Employees and Outside Directors who, in the opinion of the Committee, can further the Plan purposes. Once a Participant is recommended for an Award by the Committee, the Committee shall determine the type and size of Award to be granted to the Participant and shall establish in the related Award Agreement the terms, conditions, restrictions and/or limitations applicable to the Award, in addition to those set forth in the Plan and the administrative rules and regulations, if any, established by the Committee. Outside Directors shall be eligible to participate in the Plan and receive Awards in the discretion of the Committee.

ARTICLE VI. FORM OF AWARDS

Awards may, at the Committee's sole discretion, be granted under the Plan in the form of Options pursuant to Article VII, Phantom Options pursuant to Article VIII, Restricted Stock pursuant to Article IX, SARs pursuant to Article X, and Other Incentive Awards pursuant to Article XI, or a combination thereof. All Awards shall be subject to the terms, conditions, restrictions and limitations of the Plan. The Committee may, in its absolute discretion, subject any Award to such other terms, conditions, restrictions and/or limitations (including, but not limited to, the time and conditions of exercise, vesting or payment of an Award and restrictions on transferability of any shares of Common Stock issued or delivered pursuant to an Award), provided they are not inconsistent with the terms of the Plan. Awards under a particular Article of the Plan need not be uniform, and Awards under more than one Article of the Plan may be combined into a single Award Agreement. Any combination of Awards may be granted at one time and on more than one occasion to the same Participant.

ARTICLE VII. OPTIONS

7.1 General. Awards may be granted to Employees and Outside Directors in the form of Options. Options granted under the Plan may be Incentive Stock Options or Nonqualified Stock Options, or a combination of both; provided, however, that Incentive Stock Options may be granted only to Employees.

7.2 Terms and Conditions of Options. An Option shall be exercisable in whole or in such installments and at such times as may be determined by the Committee. The price at which a share of Common Stock may be purchased upon exercise of a Nonqualified Stock Option shall be determined by the Committee, but such exercise price shall not be less than 50% of the Fair Market Value per share of Common Stock on the Grant Date. Except as otherwise provided in Section 7.3, the term of each Option shall be as specified by the Committee; provided, however, that, no Options shall be exercisable later than ten years from the Grant Date. Options may be granted with respect to Restricted Stock or shares of Common Stock that are not Restricted Stock, as determined by the Committee in its absolute discretion.

7.3 Restrictions Relating to Incentive Stock Options. Options granted in the form of Incentive Stock Options shall, in addition to being subject to the terms and conditions of Section 7.2, comply with Section 422(b) of the Code. Accordingly, no Incentive Stock Options shall be granted later than ten years from the date of adoption of the Plan by the Board. In addition, no Incentive Stock Option shall be exercisable after the expiration of ten years from the Grant Date. To the extent that the aggregate Fair Market Value (determined at the time the respective Incentive Stock Option is granted) of Common Stock with respect to which Incentive Stock Options are exercisable for the first time by an individual during any calendar year under all incentive stock option plans of Crosstex and its Affiliates exceeds $100,000, such excess Incentive Stock Options shall be treated as options which do not constitute Incentive Stock Options. The Committee shall determine, in accordance with the applicable provisions of the Code, which of a Participant's Incentive Stock Options will not constitute Incentive Stock Options because of such limitation and shall notify the Participant of such determination as soon as practicable after such determination. The price at which a share of Common Stock may be purchased upon exercise of an Incentive Stock Option shall be determined by the Committee, but such exercise price shall not be less than 100% of the Fair Market Value of a share of Common Stock on the Grant Date. No Incentive Stock Option shall be granted to an Employee under the Plan if, at the time such Option is granted, such Employee owns stock possessing more than 10% of the total combined voting power of all classes of stock of Crosstex or an Affiliate, within the meaning of Section 422(b)(6) of the Code, unless (i) on the Grant Date of such Option, the exercise price of such Option is at least 110% of the Fair Market Value of the Common Stock subject to the Option and (ii) such Option by its terms is not exercisable after the expiration of five years from the Grant Date of the Option.

7.4 Additional Terms and Conditions. The Committee may subject any Award of an Option to such other terms, conditions, restrictions and/or limitations as it determines are necessary or appropriate, provided they are not inconsistent with the Plan.

7.5 Exercise of Options. Subject to the terms and conditions of the Plan, Options shall be exercised by the delivery of a written notice of exercise to Crosstex, setting forth the number of shares of Common Stock with respect to which the Option is to be exercised, accompanied by full payment for such shares.

Upon exercise of an Option, the exercise price of the Option shall be payable to Crosstex in full either: (i) in cash or an equivalent acceptable to the Committee, or (ii) in the absolute discretion of the Committee and in accordance with any applicable administrative guidelines established by the Committee, by tendering one or more previously acquired nonforfeitable, unrestricted shares of Common Stock that have been held by the Participant for at least six months having an aggregate Fair Market Value at the time of exercise equal to the total exercise price (including an actual or deemed multiple series of exchanges of such shares), or (iii) in a combination of the forms of payment specified in clauses (i) and (ii) above.

From and after such time as Crosstex registers the Common Stock under Section 12 of the Exchange Act, payment of the exercise price of an Option may also be made, in the absolute discretion of the Committee, by delivery to Crosstex or its designated agent of an executed irrevocable option exercise form together with irrevocable instructions to a broker-dealer to sell or margin a sufficient portion of the shares with respect to which the Option is exercised and deliver the sale or margin loan proceeds directly to Crosstex to pay the exercise price and any required withholding taxes.

As soon as reasonably practicable after receipt of written notification of exercise of an Option and full payment of the exercise price and any required withholding taxes, Crosstex shall deliver to the Participant, in the Participant's name, a stock certificate or certificates in an appropriate amount based upon the number of shares of Common Stock purchased under the Option.

7.6 Termination of Employment or Service. Each Award Agreement embodying the Award of an Option shall set forth the extent to which the Participant shall have the right to exercise the Option following termination of the Participant's employment or service with the Company. Such provisions shall be determined by the Committee in its absolute discretion, need not be uniform among all Options granted under the Plan and may reflect distinctions based on the reasons for termination of employment or service. In the event a Participant's Award Agreement embodying the award of an

Option does not set forth such termination provisions, the following termination provisions shall apply with respect to such Award:

(a) **Death or Disability.** If the employment or service of a Participant shall terminate by reason of death or permanent and total disability (within the meaning of Section 22(e)(3) of the Code), each outstanding Option held by the Participant may be exercised, to the extent then vested, until the earlier of (i) the expiration of one year from the date of such termination of employment or service, or (ii) the expiration of the term of such Option.

(b) **Other Termination.** If the employment or service of a Participant shall terminate for any reason other than a reason set forth in paragraph (a) above or paragraph (c) below, whether on a voluntary or involuntary basis, each outstanding Option held by the Participant may be exercised, to the extent then vested, until the earlier of (i) the expiration of three months from the date of such termination of employment or service, or (ii) the expiration of the term of such Option.

(c) **Termination for Cause.** Notwithstanding paragraphs (a) and (b) above, if the employment or service of a Participant is terminated for Cause, all outstanding Options held by the Participant shall immediately be forfeited to the Company and no additional exercise period shall be allowed, regardless of the vested status of the Option.

ARTICLE VIII. PHANTOM OPTIONS

8.1 General. Awards may be granted to Employees and Outside Directors in the form of Phantom Options. Phantom Options shall be awarded in such numbers and at such times as the Committee shall determine. All Phantom Options shall be evidenced by an Award Agreement as described in Section 8.2 below and any payment or settlement made upon exercise of a Phantom Option shall be made to the Participant in accordance with the terms and conditions set forth in the Award Agreement.

8.2 Award of Phantom Options. Each Award Agreement embodying a Phantom Option granted pursuant to the Plan shall specify the strike price for each fictional share of Common Stock subject to the Phantom Option, the number of fictional shares subject to the Phantom Option being awarded, the manner and timing of the vesting of the Phantom Option and of payments or transfer of shares to the Participant under such Award and such other terms and conditions not inconsistent with the provisions of the Plan as may be approved by the Committee in its absolute discretion. The strike price of a Phantom Option shall be determined by the Committee, but such strike price shall not be less than 100% of the Fair Market Value per share of Common Stock on the Grant Date of the Phantom Option. The term of each Phantom Option shall be as specified by the Committee; provided, however, that unless otherwise designated by the Committee, no Phantom Option shall be exercisable later than ten years after the Grant Date of the Phantom Option. Except as otherwise provided in an applicable Award Agreement, Participants holding Phantom Options shall not be entitled to any dividends, rights upon liquidation or other rights of a holder of shares of Common Stock.

8.3 Exercise. Subject to the terms and conditions of the Plan, Phantom Options shall be exercised by the delivery of a written notice of exercise to Crosstex, setting forth the number of fictional shares with respect to which the Phantom Option is to be exercised. Subject to the terms and conditions of this Plan and the applicable Award Agreement, upon exercise each fictional share subject to a Phantom Option entitles the Participant holding such Phantom Option to receive the amount, if any, by which the Fair Market Value as of the date of exercise exceeds the strike price, payable in one or a combination of the following forms, as determined by the Committee in its absolute discretion: (i) a cash payment or (ii) a whole number of shares of Common Stock (with cash payable in lieu of fractional shares).

8.4 Termination of Employment or Service. Upon a Participant's termination of employment or service with the Company for any reason other than for Cause, the vested portion of such Participant's

Phantom Option shall be deemed to be exercised pursuant to Section 8.3 above and the unvested portion of such Phantom Option shall immediately be forfeited to Crosstex. If the employment or service of a Participant shall be terminated for Cause, all outstanding Phantom Options held by the Participant shall immediately be forfeited to Crosstex, regardless of the vested status of such Phantom Options.

ARTICLE IX. RESTRICTED STOCK

9.1 General. Awards may be granted to Employees and Outside Directors in the form of Restricted Stock. Restricted Stock shall be awarded in such numbers and at such times as the Committee shall determine.

9.2 Restriction Period. At the time an Award of Restricted Stock is granted, the Committee shall establish a period of time (the "Restriction Period") applicable to such Restricted Stock. Each Award of Restricted Stock may have a different Restriction Period, in the discretion of the Committee. The Restriction Period applicable to a particular Award of Restricted Stock shall not be changed except as permitted by Article IV or Section 9.3 of this Article.

9.3 Other Terms and Conditions. Restricted Stock awarded to a Participant under the Plan shall be represented by a stock certificate registered in the name of the Participant or, at the option of Crosstex, in the name of a nominee of Crosstex. Subject to the terms and conditions of the Award Agreement, a Participant to whom Restricted Stock has been awarded shall have the right to receive dividends thereon during the Restriction Period, to vote the Restricted Stock and to enjoy all other stockholder rights with respect thereto, except that (i) the Participant shall not be entitled to possession of the stock certificate representing the Restricted Stock until the Restriction Period shall have expired, (ii) Crosstex shall retain custody of the Restricted Stock during the Restriction Period, (iii) the Participant may not sell, transfer, pledge, exchange, hypothecate or otherwise dispose of the Restricted Stock during the Restriction Period, and (iv) a breach of the terms and conditions established by the Committee pursuant to the Award of the Restricted Stock shall cause a forfeiture of the Restricted Stock. At the time of an Award of Restricted Stock, the Committee may, in its absolute discretion, prescribe additional terms, conditions, restrictions and/or limitations applicable to the Restricted Stock, including, but not limited to, rules pertaining to the termination of employment or service (by reason of death, permanent and total disability, or otherwise) of a Participant prior to expiration of the Restriction Period.

9.4 Payment for Restricted Stock. A Participant shall not be required to make any payment for Restricted Stock awarded to the Participant, except to the extent otherwise required by the Committee or by applicable law.

9.5 Miscellaneous. Nothing in this Article shall prohibit the exchange of shares of Restricted Stock issued under the Plan pursuant to a plan of reorganization for stock or securities of Crosstex or another corporation that is a party to the reorganization, but the stock or securities so received for shares of Restricted Stock shall, except as provided in Article IV or XII, become subject to the restrictions applicable to the Award of such Restricted Stock. Any shares of stock received as a result of a stock split or stock dividend with respect to shares of Restricted Stock shall also become subject to the restrictions applicable to the Award of such Restricted Stock.

ARTICLE X. SARs

10.1 General. The Committee may from time to time grant SARs in conjunction with all or any portion of any Option (the "Related Option") either (i) at the time of the initial Option grant (not including any subsequent modification that may be treated as a new grant of an Incentive Stock Option for purposes of Section 424(h) of the Code) or (ii) with respect to Nonqualified Stock Options, at any time after the initial Option grant while the Nonqualified Stock Option is still outstanding. SARs shall not be granted other than in conjunction with an Option granted hereunder.

10.2 Terms and Conditions. SARs granted hereunder shall comply with the following conditions and also with the terms of the Award Agreement governing the Related Option:

(a) The SAR shall expire no later than the expiration of the Related Option.

(b) Upon the exercise of an SAR, the Participant shall be entitled to receive from Crosstex or the appropriate Affiliate an amount in cash equal to the excess of the aggregate Fair Market Value of the shares of Common Stock with respect to which the SAR is then being exercised (determined as of the date of such exercise) over the aggregate purchase price of such shares as provided in the Related Option.

(c) SARs shall be exercisable (i) only at such time or times and only to the extent that the Related Option shall be exercisable, (ii) only when the Fair Market Value of the shares subject to the Related Option exceeds the purchase price of the shares as provided in the Related Option, and (iii) only upon surrender of the Related Option or any portion thereof with respect to the shares for which the SARs are then being exercised.

(d) Upon the exercise of an SAR, the Related Option shall be deemed to have been terminated to the extent of the number of shares of Common Stock with respect to which such SARs are exercised. Upon the exercise or termination of the Related Option, the SARs with respect to such Related Option shall be deemed to have been terminated to the extent of the number of shares of Common Stock with respect to which the Related Option was so exercised or terminated.

10.3 Exercise of SARs. Each exercise of SARs, or a portion thereof, shall be evidenced by a notice in writing to Crosstex.

ARTICLE XI. OTHER INCENTIVE AWARDS

Subject to the terms and provisions of the Plan, Other Incentive Awards may be granted to Employees and Outside Directors in such amounts, upon such terms and at any time and from time to time as shall be determined by the Committee in its absolute discretion. Other Incentive Awards may be granted based upon, payable in or otherwise related to, in whole or in part, shares of Common Stock if the Committee, in its absolute discretion, determines that such Other Incentive Awards are consistent with the purposes of the Plan. Each grant of an Other Incentive Award shall be evidenced by an Award Agreement that shall specify the amount of the Other Incentive Award and the terms, conditions, restrictions and/or limitations applicable to such Award. Payment of Other Incentive Awards shall be made at such times and in such form, which may be cash, shares of Common Stock or other property (or a combination thereof), as established by the Committee, subject to the terms of the Plan.

ARTICLE XII. CHANGE OF CONTROL

12.1 Definition of Change of Control. A "Change of Control" shall be deemed to have occurred if (i) Yorktown Partners LLC, a Delaware limited liability company, or its Affiliates including any funds under its management ("Yorktown") no longer directly or indirectly owns a controlling interest in Crosstex, other than as a result of a firm commitment underwritten public offering, (ii) any sale, lease, exchange or other transfer (in one or a series of related transactions) of all or substantially all of the assets of Crosstex to any Person or its Affiliates, other than an Affiliates, or (iii) any merger, reorganization, consolidation or other transaction pursuant to which more than 50% of the combined voting power of the equity interests in Crosstex ceases to be owned by Persons who own such interests as of the initial public offering date of the Common Stock. The phrase "Immediately prior to a Change of Control" shall be understood to mean sufficiently in advance of a Change of Control to permit

Participants to take all steps reasonably necessary to exercise an Award, if applicable, and to deal with the Common Stock underlying all Awards so that all Awards and Common Stock issuable with respect thereto may be treated in the same manner as the shares of stock of other stockholders in connection with the Change of Control.

12.2 Effect on Outstanding Awards. Immediately prior to a Change or Control, all Awards (other than Options granted under the Superseded Plan) shall automatically vest and become payable or exercisable, as the case may be, in full. In this regard, all restriction periods shall terminate and all performance criteria, if any, shall be deemed to have been achieved at the maximum level. To the extent that an Option or SAR is not exercised upon a Change of Control, the Committee may, in its discretion, cancel such Award without payment or provide for a replacement Award with respect to such property and on such terms as it deems appropriate.

ARTICLE XIII. AMENDMENT AND TERMINATION

13.1 Plan Amendment and Termination. The Board may at any time suspend, terminate, amend or modify the Plan, in whole or in part; provided, however, that no amendment or modification of the Plan shall become effective without the approval of such amendment or modification by the stockholders of Crosstex (i) if such amendment or modification increases the maximum number of shares subject to the Plan (except as provided in Article IV) or changes the designation or class of persons eligible to receive Awards under the Plan, or (ii) if counsel for Crosstex determines that such approval is otherwise required by or necessary to comply with applicable law. The Plan shall terminate upon the earlier of (i) the termination of the Plan by the Board, or (ii) the expiration of ten years from the Effective Date. Upon termination of the Plan, the terms and provisions of the Plan shall, notwithstanding such termination, continue to apply to Awards granted prior to such termination. No suspension, termination, amendment or modification of the Plan shall adversely affect in any material way any Award previously granted under the Plan, without the consent of the Participant (or the permitted transferee) holding such Award.

13.2 Award Amendment and Cancellation. The Board may amend the terms of any outstanding Award granted pursuant to this Plan, but no such amendment shall adversely affect in any material way the Participant's (or a permitted transferee's) rights under an outstanding Award without the consent of the Participant (or the permitted transferee) holding such Award. The Board may, with a Participant's (or a permitted transferee's) written consent, cancel any outstanding Award held by such Participant (or permitted transferee) in exchange for a new Award.

ARTICLE XIV. MISCELLANEOUS

14.1 Award Agreements. After the Committee grants an Award under the Plan to a Participant, Crosstex and the Participant shall enter into an Award Agreement setting forth the terms, conditions, restrictions and/or limitations applicable to the Award and such other matters as the Committee may determine to be appropriate. The terms and provisions of the respective Award Agreements need not be identical. All Award Agreements shall be subject to the provisions of the Plan, and in the event of any conflict between an Award Agreement and the Plan, the terms of the Plan shall govern. Any provision of this Plan to the contrary notwithstanding, all Options granted under the Superseded Plan shall be subject to the provisions of the Superseded Plan, and in the event of any conflict between the terms of an Award Agreement granted under the Superseded Plan and the Superseded Plan, the terms of the Superseded Plan shall govern.

14.2 Listing Conditions.

(a) As long as the Common Stock is listed on a national securities exchange or system sponsored by a national securities association, the issuance of any shares of Common Stock pursuant to an Award shall be conditioned upon such shares being listed on such exchange or system. Crosstex shall have no obligation to issue such shares unless and until such shares are so listed, and the right to exercise any Option or other Award with respect to such shares shall be suspended until such listing has been effected.

(b) If at any time counsel to Crosstex or its Affiliates shall be of the opinion that any sale or delivery of shares of Common Stock pursuant to an Award is or may in the circumstances be unlawful or result in the imposition of excise taxes on Crosstex or its Affiliates under the statutes, rules or regulations of any applicable jurisdiction, Crosstex or its Affiliates shall have no obligation to make such sale or delivery, or to make any application or to effect or to maintain any qualification or registration under the Securities Act of 1933, as amended, or otherwise, with respect to shares of Common Stock or Awards, and the right to exercise any Option or other Award shall be suspended until, in the opinion of said counsel, such sale or delivery shall be lawful or will not result in the imposition of excise taxes on Crosstex or its Affiliates.

(c) Upon termination of any period of suspension under this Section 14.2, any Award affected by such suspension which shall not then have expired or terminated shall be reinstated as to all shares available before such suspension and as to shares which would otherwise have become available during the period of such suspension, but no such suspension shall extend the term of any Award.

14.3 Additional Conditions. Notwithstanding anything in the Plan to the contrary: (i) Crosstex may, if it shall determine it necessary or desirable for any reason, at the time of grant of any Award or the issuance of any shares of Common Stock pursuant to any Award, require the recipient of the Award or such shares of Common Stock, as a condition to the receipt thereof, to deliver to Crosstex a written representation of present intention to acquire the Award or such shares of Common Stock for his or her own account for investment and not for distribution; (ii) the certificate for shares of Common Stock issued to a Participant may include any legend which the Committee deems appropriate to reflect any restrictions on transfer, and (iii) all certificates for shares of Common Stock delivered under the Plan shall be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations and other requirements of the SEC, any stock exchange upon which the Common Stock is then quoted, any applicable federal or state securities law, and any applicable corporate law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

14.4 Nonassignability. No Award granted under the Plan may be sold, transferred, pledged, exchanged, hypothecated or otherwise disposed of, other than by will or pursuant to the applicable laws of descent and distribution. Further, no such Award shall be subject to execution, attachment or similar process. Any attempted sale, transfer, pledge, exchange, hypothecation or other disposition of an Award not specifically permitted by the Plan or the Award Agreement shall be null and void and without effect. All Awards granted to a Participant under the Plan shall be exercisable during his or her lifetime only by such Participant or, in the event of the Participant's legal incapacity, by his or her guardian or legal representative.

14.5 Withholding Taxes. The Company shall be entitled to deduct from any payment made under the Plan, regardless of the form of such payment, the amount of all applicable income and employment taxes required by law to be withheld with respect to such payment, may require the Participant to pay to the Company such withholding taxes prior to and as a condition of the making of any payment or the issuance or delivery of any shares of Common Stock under the Plan, and shall be entitled to deduct from any other compensation payable to the Participant any withholding obligations with respect to Awards under the Plan. In accordance with any applicable administrative guidelines it establishes, the Committee may allow a Participant to pay the amount of taxes required by law to be withheld from or with respect to an Award by (i) withholding shares of Common Stock from any payment of Common Stock due as a result of such Award, or (ii) permitting the Participant to deliver to the Company previously acquired shares of Common Stock, in each case having a Fair Market Value equal to the amount of such required withholding taxes. No payment shall be made and no shares of Common Stock shall be issued pursuant to any Award unless and until the applicable tax withholding obligations have been satisfied.

14.6 No Fractional Shares. No fractional shares of Common Stock shall be issued or delivered pursuant to the Plan or any Award granted hereunder, and except as otherwise provided herein, no payment or other adjustment shall be made in respect of any such fractional share.

14.7 Notices. All notices required or permitted to be given or made under the Plan or any Award Agreement shall be in writing and shall be deemed to have been duly given or made if (i) delivered personally, (ii) transmitted by first class registered or certified United States mail, postage prepaid, return receipt requested, (iii) sent by prepaid overnight courier service, or (iv) sent by telecopy or facsimile transmission, answer back requested, to the person who is to receive it at the address that such person has theretofore specified by written notice delivered in accordance herewith. Such notices shall be effective (i) if delivered personally or sent by courier service, upon actual receipt by the intended recipient, (ii) if mailed, upon the earlier of five days after deposit in the mail or the date of delivery as shown by the return receipt therefor, or (iii) if sent by telecopy or facsimile transmission, when the answer back is received. Crosstex or a Participant may change, at any time and from time to time, by written notice to the other, the address that it or such Participant had theretofore specified for receiving notices. Until such address is changed in accordance herewith, notices hereunder or under an Award Agreement shall be delivered or sent (i) to a Participant at his or her address as set forth in the records of the Company or (ii) to Crosstex at the principal executive offices of Crosstex clearly marked "Attention: LTIP Administrator."

14.8 Binding Effect. The obligations of Crosstex under the Plan shall be binding upon any successor corporation or organization resulting from the merger, consolidation or other reorganization of Crosstex, or upon any successor corporation or organization succeeding to all or substantially all of the assets and business of Crosstex. The terms and conditions of the Plan shall be binding upon each Participant and his or her heirs, legatees, distributees and legal representatives.

14.9 Severability. If any provision of the Plan or any Award Agreement is held to be illegal or invalid for any reason, the illegality or invalidity shall not affect the remaining provisions of the Plan or such agreement, as the case may be, but such provision shall be fully severable and the Plan or such agreement, as the case may be, shall be construed and enforced as if the illegal or invalid provision had never been included herein or therein.

14.10 No Restriction of Corporate Action. Nothing contained in the Plan shall be construed to prevent Crosstex or any Affiliate from taking any corporate action (including any corporate action to suspend, terminate, amend or modify the Plan) that is deemed by Crosstex or such Affiliate to be appropriate or in its best interest, whether or not such action would have an adverse effect on the Plan or any Awards made or to be made under the Plan. No Participant or other person shall have any claim against Crosstex or any Affiliate as a result of such action.

14.11 Governing Law. The Plan shall be governed by and construed in accordance with the internal laws (and not the principles relating to conflicts of laws) of the State of Delaware except as superseded by applicable federal law.

14.12 No Right, Title or Interest in Company Assets. No Participant shall have any rights as a stockholder of Crosstex as a result of participation in the Plan until the date of issuance of a stock certificate in his or her name and, in the case of Restricted Stock, unless and until such rights are granted to the Participant pursuant to the Plan. To the extent any person acquires a right to receive payments from the Company under the Plan, such rights shall be no greater than the rights of an unsecured general creditor of the Company, and such person shall not have any rights in or against any specific assets of the Company. All of the Awards granted under the Plan shall be unfunded.

14.13 Risk of Participation. Nothing contained in the Plan shall be construed either as a guarantee by Crosstex or its Affiliates, or their respective stockholders, directors, officers or employees, of the value of any assets of the Plan or as an agreement by Crosstex or its Affiliates, or their respective stockholders, directors, officers or employees, to indemnify anyone for any losses, damages, costs or expenses resulting from participation in the Plan.

14.14 No Guarantee of Tax Consequences. No person connected with the Plan in any capacity, including, but not limited to, Crosstex and the Affiliates and their respective directors, officers, agents and employees, makes any representation, commitment or guarantee that any tax treatment, including, but not limited to, federal, state and local income, estate and gift tax treatment, will be applicable with respect to any Awards or payments thereunder made to or for the benefit of a Participant under the Plan or that such tax treatment will apply to or be available to a Participant on account of participation in the Plan.

14.15 Continued Employment or Service. Nothing contained in the Plan or in any Award Agreement shall confer upon any Participant the right to continue in the employ or service of the Company, or interfere in any way with the rights of the Company to terminate a Participant's employment or service at any time, with or without cause.

14.16 Miscellaneous. Headings are given to the articles and sections of the Plan solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction of the Plan or any provisions hereof. The use of the masculine gender shall also include within its meaning the feminine. Wherever the context of the Plan dictates, the use of the singular shall also include within its meaning the plural, and vice versa.

IN WITNESS WHEREOF, this Plan has been executed as of this 31st day of December 2003.

CROSSTEX ENERGY, INC.

By: ____________________

William W. Davis
Senior Vice President and Chief Financial Officer

QuickLinks

Exhibit 10.5
CROSSTEX ENERGY, INC. LONG-TERM INCENTIVE PLAN (Amended and Restated Effective as of December 31, 2003)

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 10.6

REGISTRATION RIGHTS AGREEMENT

THIS REGISTRATION RIGHTS AGREEMENT (this "Agreement") is entered into as of December 31, 2003, by and among Crosstex Energy Holdings Inc., a Delaware corporation (the "Company"); Yorktown Energy Partners IV, L.P., a Delaware limited partnership, Yorktown Energy Partners V, L.P., a Delaware limited partnership and Lubar Nominees, a general partnership (the "Investor Stockholders"); Barry E. Davis, A. Chris Aulds, James R. Wales, William W. Davis, Jack M. Lafield, Michael P. Scott, Lisa M. Brecht, John W. Daugherty, Mike Hopkins, Mark E. Huff, Marc Lyons, Rodney A. Madden, Stewart McCorkle and Dale Wilson (the "Management Stockholders"). The Investor Stockholders and the Management Stockholders are herein sometimes called the "Stockholders".

RECITALS

WHEREAS, in connection with that certain Agreement Regarding 2003 Registration Statement and Waiver and Termination of Stockholders' Agreement dated as of October 27, 2003 between the Company, the Investor Stockholders and the Management Stockholders, the Company, the Investor Stockholders and the Management Stockholders desire to enter into this Agreement in order to grant the registration rights as set forth below.

AGREEMENT

1. **Definitions**

For purposes of this Agreement, the following terms have the following meanings:

(a) "Affiliate" means, when used with respect to a specified Person, any other Person which, directly or indirectly, owns or controls, is under common ownership or control with, or is owned or controlled by, such Person, and any directors, officers, partners or 5% or more owners of such Person, including without limitation, with respect to the Investor Stockholders, Yorktown IV Company LLC, a Delaware limited liability company, Yorktown Partners LLC, a Delaware limited liability company, or an entity managed or otherwise controlled (by contract or otherwise) by Yorktown IV Company LLC or Yorktown Partners LLC;

(b) "Common Stock" means shares of common stock, par value $.01 per share, of the Company;

(c) "Common Stock Equivalent" means (without duplication with any other Common Stock or Common Stock Equivalents) any rights, warrants, options, convertible securities or Indebtedness, exchangeable securities or Indebtedness, or other rights, exercisable for or convertible or exchangeable into, directly or indirectly, Common Stock of the Company and securities convertible or exchangeable into Common Stock (at the time of issuance or upon the passage of time or the occurrence of some future event), including the shares of Common Stock issuable upon conversion of the Series A and Series B Preferred Stock;

(d) "Disposition" means any sale, assignment, hypothecation, gift, inter vivos transfer, pledge, mortgage or other encumbrance, or any other disposition of capital stock of the Company whatsoever, whether voluntary or involuntary;

(e) "Equity Securities" means any capital stock of the Company, any securities directly or indirectly convertible into, or exercisable or exchangeable for, any capital stock of the Company, or any right, option, warrant or other security which, with the payment of additional consideration, the expiration of time or the occurrence of any event shall give the holder thereof the right to acquire any capital stock of the Company or any security convertible into or exercisable or exchangeable for, any capital stock of the Company;

(f) "Excluded Registration" means a registration under the Securities Act of (i) securities issuable under employee compensation or benefit programs or otherwise on Form S-8 or an equivalent form, or (ii) securities issuable under an exchange offer or an offering of securities solely to the existing stockholders or employees of the Company or to the existing stockholders of another company in connection with a merger or acquisition or otherwise on Form S-4 or an equivalent form;

(g) "Indebtedness" means (i) indebtedness for borrowed money or for the deferred purchase price of property or services or which is evidenced by a note, bond, debenture, or similar instrument, (ii) obligations under any financing lease, (iii) obligations in respect of letters of credit, acceptances, or similar obligations, (iv) guaranty obligations, and (v) liabilities secured by any lien on any property owned by the Person, whether or not the Person has assumed or otherwise become liable for the payment thereof;

(h) "Person(s)" means an individual, partnership, limited partnership, limited liability company, foreign limited liability company, trust, estate, corporation, custodian, trustee, executor, administrator, nominee or entity in a representative capacity;

(i) "register," "registered" and "registration" means a registration effected by preparing and filing a registration statement or similar document in compliance with the Securities Act, and the declaration or order of effectiveness of such registration statement or similar document;

(j) "Registrable Shares" means at any time the shares of Common Stock and any other Equity Securities issued or issuable with respect thereto by way of stock dividend or stock split or in connection with a combination of shares, recapitalization, merger, consolidation or other reorganization or otherwise; provided, however, that Registrable Shares shall not include any shares (i) the sale of which has been registered pursuant to the Securities Act and which shares have been sold pursuant to such registration, or (ii) which have been sold to the public pursuant to Rule 144 of the SEC under the Securities Act;

(k) "Registrable Shares then outstanding" means the number of shares of Common Stock and Equity Securities outstanding which are, and the number of shares of Common Stock and Equity Securities issuable pursuant to then exercisable or convertible securities which are, Registrable Securities;

(l) "SEC" means the Securities and Exchange Commission;

(m) "Securities" Act means the Securities Act of 1933, as amended; and

(n) "Stockholder" means any person owning or having the right to acquire Registrable Securities who is a party to this Agreement as of the date hereof.

2.

Request for Registration

(a) If the Company shall receive a written request from either at least 50% of the Registrable Securities held by (i) the Management Stockholders or (ii) the Investor Stockholders that the Company file a registration statement under the Securities Act covering the registration of the requesting Management or Investor Stockholders' Registrable Securities, then the Company shall use commercially reasonable efforts to effect as soon as practicable the registration under the Securities Act of all of the Registrable Securities; provided, however, that the Registrable Securities requested to be registered must have an anticipated aggregate offering price of $25,000,000 (prior to the deduction of underwriting discounts and commissions).

(b) The Company is obligated to effect two registrations for the Management Stockholders and four registrations for the Investor Stockholders pursuant to this Section 2; provided, however, that the Company shall not be required to effect more than [two] registrations in any 12-month period.

(c) Notwithstanding the foregoing, if the Company shall furnish, as applicable, to the Management Stockholders or the Investor Stockholders requesting a registration pursuant to Section 2 (a) within 30 days of receiving such request a certificate signed by the President of the Company stating that in the good faith judgment of the Board of Directors of the Company it would be seriously detrimental to the Company and its stockholders for such registration statement to be filed and it is therefore essential to defer the filing of such registration statement, the Company shall have the right to defer such filing for up to two periods of not more than 45 days each after receipt of the request of the Management Stockholders or Investor Stockholders, as applicable; provided, however, that the Company may not use this right more than once (for a total of up to 90 days) in any 12-month period; provided, however, that the Company shall promptly notify the Management Stockholders or Investor Stockholders, as applicable, requesting a registration pursuant to this Section 2 of any decision by the Company to abandon or indefinitely delay such public offering.

3.

Company Registration

(a) Piggyback Registration

Each time the Company proposes to register any of its Equity Securities (other than pursuant to an Excluded Registration) under the Securities Act for sale to the public (whether for the account of the Company or the account of any security holder of the Company) or proposes to make such an offering of equity securities pursuant to a previously filed registration statement pursuant to Rule 415 under the Securities Act (such as a "universal shelf" registration statement) and the form of registration statement to be used permits the registration of Registrable Shares, the Company shall give prompt written notice to each Stockholder, holding Registrable Shares (which notice shall be given not less than 30 days prior to the effective date of the Company's registration statement), which notice shall offer each such Stockholder the opportunity to include any or all of its or his Registrable Shares in such registration statement, subject to the limitations contained in Section 3(b) hereof. Each Stockholder who desires to have its or his Registrable Shares included in such registration statement shall so advise the Company in writing (stating the number of shares desired to be registered) within 20 days after the date of such notice from the Company. Any Stockholder shall have the right to withdraw such Stockholder's request for inclusion of such Stockholder's Registrable Shares in any registration statement pursuant to this Section 3(a) by giving written notice to the Company of such withdrawal. Subject to Section 3(b) below, the Company shall include in such registration statement all such Registrable Shares so requested to be included therein; provided, however, that the Company may at any time withdraw or cease proceeding with any such registration if it shall at the same time withdraw or cease proceeding with the registration of all other Equity Securities originally proposed to be registered.

(b) Priority on Registration

If (i) a registration pursuant to Section 3(a) involves an underwritten offering of the securities being registered to be distributed (on a firm commitment basis) by or through one or more underwriters of recognized standing under underwriting terms customary and appropriate for such a transaction and (ii) the lead managing underwriter of such underwritten offering shall inform the Company by letter of its belief that the amount of Registrable Shares requested to be included in such registration exceeds the amount which can be sold in (or during the time of) such offering within a price range acceptable to the Stockholders requesting registration pursuant to Section 3(a), then the Company will include in such registration such amount of securities which the Company is so advised can be sold in (or during the time of) such offering pro rata on the basis of the amount of such Registrable Shares so proposed to be sold and so requested to be included by the Stockholders; provided, however, that (A) if the underwritten registration is a primary offering on behalf of the Company, any shares requested to be included in the registration statement (or registration statements) for any Person other than the Stockholders shall be eliminated first prior to any such pro rata reduction, (B) if the underwritten registration is a secondary offering pursuant to Section 2, any shares requested to be included in the registration statement (or registration statements) for any Person other than the requesting Management Stockholders or Investor Stockholders, as applicable, shall be eliminated prior to any such pro rata reduction, (C) if the underwritten registration is a secondary offering on behalf of any holder(s) of Common Stock, other than pursuant to section 2, the shares requested to be included therein by the holders requesting such registration and the Registrable Shares requested to be included by the Stockholders shall be included pro rata on the basis of the number of shares held by each such holder and (D) no such reduction shall reduce the securities being offered by the Company for its own account.

4.

Obligations of Purchaser

A Stockholder shall not participate in any registration statement hereunder unless such Stockholder agrees to (i) sell its Registrable Shares on the basis provided in any customary underwriting arrangements approved by the Company and (ii) complete and execute all questionnaires, powers of attorney, indemnities, underwriting agreements, and other documents reasonably required under the terms of such underwriting arrangements; provided, however, that a Stockholder shall not be required to make any representations or warranties in connection with any such registration other than representations and warranties as to (A) the Stockholder's ownership of Registrable Shares to be sold or transferred free and clear of all liens, claims, and encumbrances, (B) the Stockholder's power and authority to effect such transfer, and (C) such matters pertaining to compliance with securities laws as may be reasonably requested.

5.

Holdback Agreement

Unless the managing underwriter otherwise agrees, each of the Company and the Stockholders agree, and the Company agrees, in connection with any underwritten registration, to use its reasonable efforts to cause its Affiliates to agree, not to effect any public sale or private offer or distribution of any Common Stock or Common Stock Equivalents during the ten business days prior to the effectiveness under the Securities Act of any underwritten registration and during such time period after the effectiveness under the Securities Act of any underwritten registration (not to exceed 120 days) (except, if applicable, as part of such underwritten registration) as the Company and the managing underwriter may agree.

6.

Registration Procedures

Whenever any Stockholder has requested that any Registrable Shares be registered pursuant to this Agreement, the Company will use its commercially reasonable efforts to effect the registration and the sale of such Registrable Shares in accordance with the intended method of Disposition thereof, and pursuant thereto the Company will as expeditiously as possible:

(a) prepare and file with the SEC a registration statement on any appropriate form under the Securities Act with respect to such Registrable Shares and use its commercially reasonable efforts to cause such registration statement to become effective;

(b) prepare and file with the SEC such amendments, post-effective amendments, and supplements to such registration statement and the prospectus used in connection therewith as may be necessary to keep such registration statement effective for a period of not less than 180 days (or such lesser period as is necessary for the underwriters in an underwritten offering to sell unsold allotments) and comply with the provisions of the Securities Act with respect to the Disposition of all securities covered by such registration statement during such period in accordance with the intended methods of Disposition by the sellers thereof set forth in such registration statement;

(c) furnish to each seller of Registrable Shares and the underwriters of the securities being registered such number of copies of such registration statement, each amendment and supplement thereto, the prospectus included in such registration statement (including each preliminary prospectus), any documents incorporated by reference therein and such other documents as such seller or underwriters may reasonably request in order to facilitate the Disposition of the Registrable Shares owned by such seller or the sale of such securities by such underwriters (it being understood that, subject to Section 9 and the requirements of the Securities Act and applicable state securities laws, the Company consents to the use of the prospectus and any amendment or supplement thereto by each seller and the underwriters in connection with the offering and sale of the Registrable Shares covered by the registration statement of which such prospectus, amendment or supplement is a part);

(d) use its commercially reasonable efforts to register or qualify such Registrable Shares under such other securities or blue sky laws of such jurisdictions as the managing underwriter reasonably requests; use its commercially reasonable efforts to keep each such registration or qualification (or exemption therefrom) effective during the period in which such registration statement is required to be kept effective; and do any and all other acts and things which may be reasonably necessary or advisable to enable each seller to consummate the Disposition of the Registrable Shares owned by such seller in such jurisdictions (provided, however, that the Company will not be required to (i) qualify generally to do business in any jurisdiction where it would not otherwise be required to qualify but for this subparagraph or (ii) consent to general service of process in any such jurisdiction);

(e) promptly notify each seller and each underwriter and (if requested by any such Person) confirm such notice in writing (i) when a prospectus or any prospectus supplement or post-effective amendment has been filed and, with respect to a registration statement or any post-effective amendment, when the same has become effective, (ii) of the issuance by any state securities or other regulatory authority of any order suspending the qualification or exemption from qualification of any of the Registrable Shares under state securities or "blue sky" laws or the initiation of any proceedings for that purpose, and (iii) of the happening of any event which makes any statement made in a registration statement or related prospectus untrue or which requires the making of any changes in such registration statement, prospectus or documents so that they will not contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary to make the statements therein not misleading, and, as promptly as practicable thereafter, prepare and file with the SEC and furnish a supplement or amendment to such prospectus so that, as thereafter deliverable to the purchasers of such Registrable Shares, such prospectus will not contain any untrue statement of a material fact or omit a material fact necessary to make the statements therein, in light of the circumstances under which they were made, not misleading;

(f) if requested by the managing underwriter or any seller promptly incorporate in a prospectus supplement or post-effective amendment such information as the managing underwriter or any seller reasonably requests to be included therein, including, without limitation, with respect to the Registrable Shares being sold by such seller, the purchase price being paid therefor by the underwriters and with respect to any other terms of the underwritten offering of the Registrable Shares to be sold in such offering, and promptly make all required filings of such prospectus supplement or post-effective amendment;

(g) as promptly as practicable after filing with the SEC of any document which is incorporated by reference into a registration statement (in the form in which it was incorporated), deliver a copy of each such document to each seller;

(h) cooperate with the sellers and the managing underwriter to facilitate the timely preparation and delivery of certificates (which shall not bear any restrictive legends unless required under applicable law) representing securities sold under any registration statement, and enable such securities to be in such denominations and registered in such names as the managing underwriter or such sellers may request and keep available and make available to the Company's transfer agent prior to the effectiveness of such registration statement a supply of such certificates;

(i) promptly make available for inspection by any seller, any underwriter participating in any Disposition pursuant to any registration statement, and any attorney, accountant or other agent or representative retained by any such seller or underwriter (collectively, the "Inspectors"), all financial and other records, pertinent corporate documents and properties of the Company (collectively, the "Records"), as shall be reasonably necessary to enable them to exercise their due diligence responsibility, and cause the Company's officers, directors and employees to supply all information requested by any such Inspector in connection with such registration statement; provided, that, unless the disclosure of such Records is necessary to avoid or correct a misstatement or omission in the registration statement or the release of such Records is ordered pursuant to a subpoena or other order from a court of competent jurisdiction, the Company shall not be required to provide any information under this subparagraph (i) if (A) the Company believes, after consultation with counsel for the Company, that to do so would cause the Company to forfeit an attorney-client privilege that was applicable to such information or (B) if either (1) the Company has requested and been granted from the SEC confidential treatment of such information contained in any filing with the SEC or documents provided supplementally or otherwise or (2) the Company reasonably determines in good faith that such Records are confidential and so notifies the Inspectors in writing unless prior to furnishing any such information with respect to (A) or (B) such Stockholder requesting such information agrees to enter into a confidentiality agreement in customary form and subject to customary exceptions; and provided, further that such Stockholder agrees that it will, upon learning that disclosure of such Records is sought in a court of competent jurisdiction, give notice to the Company and allow the Company at its expense, to undertake appropriate action and to prevent disclosure of the Records deemed confidential;

(j) furnish to each seller underwriter a signed counterpart of (i) an opinion or opinions of counsel to the Company, and (ii) a comfort letter or comfort letters from the Company's independent public accountants, each in customary form and covering such matters of the type customarily covered by opinions or comfort letters, as the case may be, as the sellers or managing underwriter reasonably requests;

(k) cause the Registrable Shares included in any registration statement to be (i) listed on each securities exchange, if any, on which similar securities issued by the Company are then listed, or (ii) authorized to be quoted and/or listed (to the extent applicable) on the National Association of Securities Dealers, Inc. Automated Quotation ("NASDAQ") or the NASDAQ National Market System if the Registrable Shares so qualify;

(l) provide a CUSIP number for the Registrable Shares included in any registration statement not later than the effective date of such registration statement;

(m) cooperate with each seller and each underwriter participating in the Disposition of such Registrable Shares and their respective counsel in connection with any filings required to be made with the National Association of Securities Dealers, Inc. ("NASD");

(n) during the period when the prospectus is required to be delivered under the Securities Act, promptly file all documents required to be filed with the SEC pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act;

(o) notify each seller of Registrable Shares promptly of any request by the SEC for the amending or supplementing of such registration statement or prospectus or for additional information;

(p) prepare and file with the SEC promptly any amendments or supplements to such registration statement or prospectus which, in the opinion of counsel for the Company or the managing underwriter, is required in connection with the distribution of the Registrable Shares;

(q) enter into such agreements (including underwriting agreements in the managing underwriter's customary form) as are customary in connection with an underwritten registration; and

(r) advise each seller of such Registrable Shares, promptly after it shall receive notice or obtain knowledge thereof, of the issuance of any stop order by the SEC suspending the effectiveness of such registration statement or the initiation or threatening of any proceeding for such purpose and promptly use its best efforts to prevent the issuance of any stop order or to obtain its withdrawal at the earliest possible moment if such stop order should be issued.

7.

Suspension of Dispositions

Each Stockholder agrees by acquisition of any Registrable Shares that, upon receipt of any notice (a "Suspension Notice") from the Company of the happening of any event of the kind described in Section 6(e)(iii) such Stockholder will forthwith discontinue Disposition of Registrable Shares until such Stockholder's receipt of the copies of the supplemented or amended prospectus, or until it is advised in writing (the "Advice") by the Company that the use of the prospectus may be resumed, and has received copies of any additional or supplemental filings which are incorporated by reference in the prospectus, and, if so directed by the Company, such Stockholder will deliver to the Company all copies, other than permanent file copies then in such Stockholder's possession, of the prospectus covering such Registrable Shares current at the time of receipt of such notice. In the event the Company shall give any such notice, the time period regarding the effectiveness of registration statements set forth in Section 6(b) hereof shall be extended by the number of days during the period from and including the date of the giving of the Suspension Notice to and including the date when each seller of Registrable Shares covered by such registration statement shall have received the copies of the supplemented or amended prospectus or the Advice. The Company shall use its commercially reasonable efforts and take such actions as are reasonably necessary to render the Advice as promptly as practicable.

8.

Registration Expenses

All expenses incident to the Company's performance of or compliance with this Agreement, including, without limitation, (i) all registration and filing fees, (ii) all fees and expenses associated with filings required to be made with the NASD (including, if applicable, the fees and expenses of any "qualified independent underwriter" as such term is defined in Schedule E of the By-Laws of the NASD, and of its counsel), as may be required by the rules and regulations of the NASD, (iii) fees and expenses of compliance with securities or "blue sky" laws (including reasonable fees and disbursements of counsel in connection with "blue sky" qualifications of the Registrable Shares), (iv) rating agency fees, (v) printing expenses (including expenses of printing certificates for the Registrable Shares in a form eligible for deposit with Depository Trust Company and of printing prospectuses if the printing of prospectuses is requested by a holder of Registrable Shares), (vi) messenger and delivery expenses, (vii) the Company's internal expenses (including without limitation all salaries and expenses of its officers and employees performing legal or accounting duties), (viii) the fees and expenses incurred in connection with any listing of the Registrable Shares, (ix) fees and expenses of counsel for the Company and fees and expenses of the Company's independent certified public accountants (including the expenses of any special audit or "cold comfort" letters required by or incident to such performance), (x) securities acts liability insurance (if the Company elects to obtain such insurance), (xi) the fees and expenses of any special experts retained by the Company in connection with such registration, (xii) the fees and expenses of other Persons retained by the Company and (xiii) reasonable fees and expenses of one firm of counsel for the sellers (which shall be selected by the holders of a majority of the Registrable Shares being included in any particular registration statement) (all such expenses being herein called "Registration Expenses"), will be borne by the Company whether or not any registration statement becomes effective; provided that, except as expressed otherwise provided above, in no event shall Registration Expenses include any underwriting discounts or commissions and transfer taxes.

9.

Indemnification

(a) The Company agrees to indemnify and reimburse, to the fullest extent permitted by law, each seller of Registrable Shares, and each of its employees, advisors, agents, representatives, partners, officers, and directors and each Person who controls such seller (within the meaning of the Securities Act or the Exchange Act) and any agent or investment advisor thereof (collectively, the "Seller Affiliates") (i) against any and all losses, claims, damages, liabilities, and expenses, joint or several (including, without limitation, attorneys' fees and disbursements except as limited by Section 9(c)) based upon, arising out of, related to or resulting from any untrue or alleged untrue statement of a material fact contained in any registration statement, prospectus, or preliminary prospectus relating to the offer and sale of Registrable Shares, or any amendment thereof or supplement thereto, or any omission or alleged omission of a material fact required to be stated therein or necessary to make the statements therein not misleading, (ii) against any and all loss, liability, claim, damage, and expense whatsoever, as incurred, to the extent of the aggregate amount paid in settlement of any litigation or investigation or proceeding by any governmental agency or body, commenced or threatened, or of any claim whatsoever based upon, arising out of, related to or resulting from any such untrue statement or omission or alleged untrue statement or omission, and (iii) against any and all costs and expenses (including reasonable fees and disbursements of counsel) as may be reasonably incurred in investigating, preparing, or defending against any litigation, or investigation or proceeding by any governmental agency or body, commenced or threatened, or any claim whatsoever based upon, arising out of, related to or resulting from any such untrue statement or omission or alleged untrue statement or omission, to the extent that any such expense or cost is not paid under subparagraph (i) or (ii) above; except insofar as the same are made in reliance upon and in strict conformity with information furnished in writing to the Company by such seller or any Seller Affiliate for use therein or arise from such seller's or any Seller Affiliate's failure to deliver a copy of the registration statement or prospectus or any amendments or supplements thereto after the Company has furnished such seller or Seller Affiliate with a sufficient number of copies of the same. The reimbursements required by this Section 9(a) will be made by periodic payments during the course of the investigation or defense, as and when bills are received or expenses incurred.

(b) In connection with any registration statement in which a seller of Registrable Shares is participating, each such seller will furnish to the Company in writing such information and affidavits as the Company reasonably requests for use in connection with any such registration statement or prospectus and, to the fullest extent permitted by law, each such seller will indemnify the Company and its directors and officers and each Person who controls the Company (within the meaning of the Securities Act or the Exchange Act) against any and all losses, claims, damages, liabilities, and expenses (including, without limitation, reasonable attorneys' fees and disbursements except as limited by Section 9(c)) resulting from any untrue statement or alleged untrue statement of a material fact contained in the registration statement, prospectus, or any preliminary prospectus or any amendment thereof or supplement thereto or any omission or alleged omission of a material fact required to be stated therein or necessary to make the statements therein not misleading, but only to the extent that such untrue statement or alleged untrue statement or omission or alleged omission is contained in any information or affidavit so furnished in writing by such seller or any of its Seller Affiliates specifically for inclusion in the registration statement; provided that the obligation to indemnify will be several, not joint and several, among such sellers of Registrable Shares, and the liability of each such seller of Registrable Shares will be in proportion to, and provided further that such liability will be limited to, the net amount received by such seller from the sale of Registrable Shares pursuant to such registration statement; provided, however, that such seller of Registrable Shares shall not be liable in any such case to the extent that prior to the filing of any such registration statement or prospectus or amendment thereof or supplement thereto, such seller has furnished in writing to the Company information expressly for use in such registration statement or prospectus or any amendment thereof or supplement thereto which corrected or made not misleading information previously furnished to the Company.

(c) Any Person entitled to indemnification hereunder will (i) give prompt written notice to the indemnifying party of any claim with respect to which it seeks indemnification (provided that the failure to give such notice shall not limit the rights of such Person) and (ii) unless in such indemnified party's reasonable judgment a conflict of interest between such indemnified and indemnifying parties may exist with respect to such claim, permit such indemnifying party to assume the defense of such claim with counsel reasonably satisfactory to the indemnified party; provided, however, that any Person entitled to indemnification hereunder shall have the right to employ separate counsel and to participate in the defense of such claim, but the fees and expenses of such counsel shall be at the expense of such Person unless (i) the indemnifying party has agreed to pay such fees or expenses, or (ii) the indemnifying party shall have failed to assume the defense of such claim and employ counsel reasonably satisfactory to such Person. If such defense is not assumed by the indemnifying party as permitted hereunder, the indemnifying party will not be subject to any liability for any settlement made by the indemnified party without its consent (but such consent will not be unreasonably withheld). If such defense is assumed by the indemnifying party pursuant to the provisions hereof, such indemnifying party shall not settle or otherwise compromise the applicable claim unless (i) such settlement or compromise contains a full and unconditional release of the indemnified party or (ii) the indemnified party otherwise consents in writing. An indemnifying party who is not entitled to, or elects not to, assume the defense of a claim will not be obligated to pay the fees and expenses of more than one counsel for all parties indemnified by such indemnifying party with respect to such claim.

(d) Each party hereto agrees that, if for any reason the indemnification provisions contemplated by Section 9(a) or Section 9(b) are unavailable to or insufficient to hold harmless an indemnified party in respect of any losses, claims, damages, liabilities, or expenses (or actions in respect thereof) referred to therein, then each indemnifying party shall contribute to the amount paid or payable by such indemnified party as a result of such losses, claims, liabilities, or expenses (or actions in respect thereof) in such proportion as is appropriate to reflect the relative fault of the indemnifying party and the indemnified party in connection with the actions which resulted in the losses, claims, damages, liabilities or expenses as well as any other relevant equitable considerations. The relative fault of such indemnifying party and indemnified party shall be determined by reference to, among other things, whether the untrue or alleged untrue statement of a material fact or omission or alleged omission to state a material fact relates to information supplied by such indemnifying party or indemnified party, and the parties, relative intent, knowledge, access to information and opportunity to correct or prevent such statement or omission. The parties hereto agree that it would not be just and equitable if contribution pursuant to this Section 9(d) were determined by pro rata allocation (even if the Stockholders or any underwriters or all of them were treated as one entity for such purpose) or by any other method of allocation which does not take account of the equitable considerations referred to in this Section 9(d). The amount paid or payable by an indemnified party as a result of the losses, claims, damages, liabilities, or expenses (or actions in respect thereof) referred to above shall be deemed to include any legal or other fees or expenses reasonably incurred by such indemnified party in connection with investigating or, except as provided in Section 9(c), defending any such action or claim. Notwithstanding the provisions of this Section 9(d), no Stockholder shall be required to contribute an amount greater than the dollar amount by which the proceeds received by such Stockholder with respect to the sale of any Registrable Shares exceeds the amount of damages which such Stockholder has otherwise been required to pay by reason of such statement or omission. No Person guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the Securities Act) shall be entitled to contribution from any Person who was not guilty of such fraudulent misrepresentation. The Stockholders' obligations in this Section 9(d) to contribute shall be several in proportion to the amount of Registrable Shares registered by them and not joint.

If indemnification is available under this Section 9, the indemnifying parties shall indemnify each indemnified party to the full extent provided in Section 9(a) and Section 9(b) without regard to the relative fault of said indemnifying party or indemnified party or any other equitable consideration provided for in this Section 9(d).

(e) The indemnification and contribution provided for under this Agreement will remain in full force and effect regardless of any investigation made by or on behalf of the indemnified party or any officer, director, or controlling Person of such indemnified party and will survive the transfer of securities.

10.

Termination of Registration Rights

The registration rights granted under Sections 2 and 3 of this Agreement shall terminate as to each Stockholder when the Registrable Securities cease to be Registrable Securities; provided, however, that the provisions of Section 9 shall survive the termination of this Agreement.

11.

Miscellaneous

(a) Notices

Any notice, demand or other communication which any party to this Agreement may be required, or may elect, to give to anyone interested hereunder shall be validly given if personally delivered or sent by facsimile, registered or certified mail, return receipt requested, or reputable overnight courier service (providing next business day service), addressed to the recipient as follows:

If to the Company:

Crosstex Energy Services, Inc.
2501 Cedar Springs, Suite 600
Dallas, Texas 75201
Attention: Barry E. Davis
Facsimile No.: (214) 953-9501

With additional copies to:

Bryan Lawrence
Yorktown Energy Partners IV, L.P.
410 Park Avenue
New York, New York 10022-4407
Facsimile No.: (212) 515-2105

Jeffrey A. Zlotky
Thompson & Knight L.L.P.
1700 Pacific Avenue, Suite 3300
Dallas, Texas 75201
Facsimile No.: (214) 969-1751

Joe A. Davis
Hunton & Williams
Energy Plaza, 30/F
1601 Bryan Street
Dallas, Texas 75201
Facsimile No.: (214) 880-0011

If to any Stockholder, to such Stockholder's address as set forth opposite such Stockholder's name on the counterpart signature page to this Agreement; or, in either case, to such other address as such party may designate by written notice to the other in accordance with the provisions of this Section 11(a). Notice shall be deemed to have been given when delivered personally or on the first business day following confirmation of the receipt of a facsimile, five (5) business days following the date of deposit with the U.S. Post Office or on the first business day following deposit with the office of such reputable courier service.

(b) Entire Agreement

This Agreement, together with the Exhibits and Annexes and other writings referred to herein or delivered pursuant hereto, constitute the entire agreement between the parties hereto with respect to the subject matter hereof and supersede all prior agreements and understandings, both written and oral, between the parties with respect to the subject matter hereof.

(c) Binding Effect; Assignment; No Third Party Benefit

This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, legal representatives, successors and permitted assigns. Except as otherwise expressly provided in this Agreement, neither this Agreement nor any of the rights, interests, or obligations hereunder shall be assigned by any of the parties hereto without the prior written consent of the other parties. Nothing in this Agreement, express or implied, is intended to or shall confer upon any person other than the parties hereto, and their respective heirs, legal representatives, successors, and permitted assigns, any rights, benefits, or remedies of any nature whatsoever under or by reason of this Agreement.

(d) Severability

If any provision of this Agreement is held to be unenforceable, this Agreement shall be considered divisible and such provision shall be deemed inoperative to the extent it is deemed unenforceable, and in all other respects this Agreement shall remain in full force and effect; provided, however, that if any such provision may be made enforceable by limitation thereof, then such provision shall be deemed to be so limited and shall be enforceable to the maximum extent permitted by applicable law.

(e) GOVERNING LAW

THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH THE LAWS OF THE STATE OF DELAWARE, WITHOUT REGARD TO THE PRINCIPLES OF CONFLICTS OF LAWS THEREOF.

(f) Descriptive Headings

The descriptive headings herein are inserted for convenience of reference only, do not constitute a part of this Agreement, and shall not affect in any manner the meaning or interpretation of this Agreement.

(g) Gender

Pronouns in masculine, feminine, and neuter genders shall be construed to include any other gender, and words in the singular form shall be construed to include the plural and vice versa, unless the context otherwise requires.

(h) References

All references in this Agreement to Sections and other subdivisions refer to the Sections and other subdivisions of this Agreement unless expressly provided otherwise. The words "this Agreement," "herein," "hereof," "hereby," "hereunder" and words of similar import refer to this Agreement as a whole and not to any particular subdivision unless expressly so limited. Whenever the words "include," "includes" and "including" are used in this Agreement, such words shall be deemed to be followed by the words "without limitation." Each reference herein to an Exhibit refers to the item identified separately in writing by the parties hereto as the described Exhibit or Annex to this Agreement. All Exhibits and Annexes are hereby incorporated in and made a part of this Agreement as if set forth in full herein.

(i) Injunctive Relief

The parties hereto acknowledge and agree that irreparable damage would occur in the event any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to an injunction or injunctions to prevent breaches of the provisions of this Agreement, and shall be entitled to enforce specifically the provisions of this Agreement, in any court of the United States or any state thereof having jurisdiction, in addition to any other remedy to which the parties may be entitled under this Agreement or at law or in equity.

(j) Consent to Jurisdiction

(i) The parties hereto hereby irrevocably submit to the exclusive jurisdiction of the courts of the State of Delaware and the federal courts of the United States of America located in Delaware, and appropriate appellate courts therefrom, over any dispute arising out of or relating to this Agreement or any of the transactions contemplated hereby, and each party hereby irrevocably agrees that all claims in respect of such dispute or proceeding may be heard and determined in such courts. The parties hereby irrevocably waive, to the fullest extent permitted by applicable law, any objection which they may now or hereafter have to the laying of venue of any dispute arising out of or relating to this Agreement or any of the transactions contemplated hereby brought in such court or any defense of inconvenient forum for the maintenance of such dispute. Each of the parties hereto agrees that a judgment in any such dispute may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law. This consent to jurisdiction is being given solely for purposes of this Agreement and is not intended to, and shall not, confer consent to jurisdiction with respect to any other dispute in which a party to this Agreement may become involved.

(ii) Each of the parties hereto hereby consents to process being served by any party to this Agreement in any suit, action, or proceeding of the nature specified in subsection (a) above by the mailing of a copy thereof in the manner specified by the provisions of Section 7.1.

(iii) EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM ARISING OUT OF OR RELATING TO THIS AGREEMENT.

(k) Amendment

The provisions of this Agreement may only be amended, waived or modified with a written instrument duly executed by a Super-Majority in Interest. Notwithstanding the immediately preceding sentence, with respect to any change, modification or amendment to this Agreement which is necessary to admit an additional Stockholder in the manner expressly permitted by this Agreement, such change, modification or amendment may be contained in a written instrument executed solely by the Company, provided that the Company notifies the Stockholders of such change, modification or amendment.

(l) Waiver

No failure or delay by a party hereto in exercising any right, power, or privilege hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power, or privilege.

(m) Counterparts

This Agreement may be executed by the parties hereto in any number of counterparts, each of which shall be deemed an original, but all of which shall constitute one and the same agreement. Each counterpart may consist of a number of copies hereof each signed by less than all, but together signed by all, the parties hereto.

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

YORKTOWN ENERGY PARTNERS IV, L.P.

By: Yorktown IV Company LLC, its General Partner

By: /s/ PETER A. LEIDEL

Name: Peter A. Leidel

Title: Member

YORKTOWN ENERGY PARTNERS V, L.P.

By: Yorktown V Company LLC, its General Partner

By: /s/ PETER A. LEIDEL

Name: Peter A. Leidel

Title: Member

LUBAR NOMINEES

By: /s/ SHELDON B. LUBAR

Name: Lubar Nominees

Title: General Partners

/s/ BARRY E. DAVIS

Barry E. Davis

/s/ A. CHRIS AULDS

A. Chris Aulds

/s/ JAMES R. WALES

James R. Wales

/s/ WILLIAM W. DAVIS

William W. Davis

/s/ JACK M. LAFIELD

Jack M. Lafield

/s/ MICHAEL P. SCOTT

Michael P. Scott

/s/ LISA M. BRECHT

Lisa M. Brecht

/s/ JOHN W. DAUGHERTY

John W. Daugherty

/s/ MIKE HOPKINS

Mike Hopkins

/s/ MARK E. HUFF

Mark E. Huff

/s/ MARC LYONS

Marc Lyons

/s/ RODNEY A. MADDEN

Rodney A. Madden

/s/ STEWART MCCORKLE

Stewart McCorkle

/s/ DALE WILSON

Dale Wilson

MK Holdings, L.P.
By: MK Holdings GP, L.L.C.

By:	/s/ BARRY E. DAVIS
Name:	Barry E. Davis
Title:	Manager

CROSSTEX ENERGY HOLDINGS INC.

By:	/s/ BRYAN H. LAWRENCE
Name:	Bryan H. Lawrence
Title:	Chairman

QuickLinks

Exhibit 10.6
REGISTRATION RIGHTS AGREEMENT

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 31.1

CERTIFICATION

I, Barry E. Davis, certify that:

1. I have reviewed this annual report on Form 10-K of Crosstex Energy, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 26, 2004

/s/ BARRY E. DAVIS

Barry E. Davis,
President and Chief Executive Officer
(principal executive officer)

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Exhibit 31.1

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 31.2

CERTIFICATIONS

I, William W. Davis, certify that:

1. I have reviewed this annual report on Form 10-K of Crosstex Energy, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 26, 2004

/s/ WILLIAM W. DAVIS

William W. Davis,
Executive Vice President and Chief Financial Officer
(principal financial and accounting officer)

QuickLinks

Exhibit 31.2

Exhibit 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Crosstex Energy, Inc. (the "Registrant") on Form 10-K for the fiscal year ending December 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned, Barry E. Davis and William W. Davis certifies, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Registrant.

/s/ BARRY E. DAVIS

Barry E. Davis
Chief Executive Officer

March 26, 2004

/s/ WILLIAM W. DAVIS

William W. Davis
Chief Financial Officer

March 26, 2004

A signed original of this written statement required by Section 906 has been provided to the Registrant and will be retained by the Registrant and furnished to the Securities and Exchange Commission or its staff upon request. The foregoing certification is being furnished to the Securities and Exchange Commission as an exhibit to the Report.

QuickLinks

Exhibit 32.1
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002