TEXAS LAND & MINERAL OWNERS ASSOCIATION

OFFICIAL NEWSLETTER

Volume 16, Number 1 1st Quarter 2016

RAILROAD COMMISSION PRIMARY ELECTIONS HEAD TO RUNOFFS

The race continues as candidates vie to fill the seat of Railroad Commission Chairman David Porter, who is not seeking reelection. With no candidate taking more than 50% of the vote, primary runoff elections will be held May 24, with early voting from May 16 through May 20.

From a field of seven candidates jockeying for the Republican slot on November's ballot, two now find themselves in a runoff—former State Representative Wayne Christian and businessman Gary Gates. In the Democratic contest, Cody Garrett and Grady Yarbrough beat out former State Representative Lon Burnam, and now advance to the Democratic primary runoff.

Wayne Christian

Republican Candidates

Wayne Christian represented East Texas in the State House from 1997 to 2013. He served as a member of the Energy Resources Committee and as vice chairman of the Regulated Industries Committee. Christian ran unsuccessfully for the Texas Railroad Commission in 2014. He lost in the Republican primary runoff election to Ryan Sitton, who was ultimately elected to the Commission.

Gary Gates

Gary Gates is a real estate mogul who lives in Fort Bend County. He is the CEO and founder of real estate investment company Gatesco, Inc. Gates and his wife Melissa have 13 children, 11 of whom were adopted. This is not the first political race for Gates. He has mounted four failed bids for the Texas Legislature, most recently losing the race for Texas Senate District 18 in 2014.

Cody Garrett

Democratic Candidates

Cody Garrett is a journalist and former campaign director in the Austin area. Garrett served as a Democratic Party Precinct Chair and managed statewide Democratic political campaigns. Garrett has worked as a copy editor for syndicated columnist and former Ag Commissioner Jim Hightower since 2008.

Grady Yarbrough is a former schoolteacher. Originally from Smith County, Texas, Yarbrough retired from the San Antonio Independent School District. He ran unsuccessfully for U.S. Senate in 2012, losing in the Democratic primary runoff election.

Grady Yarbrough

IN THIS ISSUE

TLMA's mission is to create a business and legal environment that is accommodating to the continued exploration for and production of oil and natural gas by ensuring that the rights of both the mineral and surface owners are protected, reduce litigation and to protect our precious groundwater resources.

1005 Congress Ave., Suite 360
Austin, Texas 78701
(512) 479-5000 (phone)
(512) 479-5066 (fax)
info@tlma.org (email)
www.tlma.org

COURT HANDS DOWN FINAL DECISION IN *CHESAPEAKE V. HYDER*

The Supreme Court of Texas has reaffirmed a ruling in favor of royalty owners. As previously reported in the TLMA newsletter, the Court ruled in a five-to-four decision last summer that Chesapeake had been wrongfully deducting post-production costs from the Hyders' overriding royalty. Chesapeake filed a motion for rehearing after the verdict came down.

The TLMA and the National Association of Royalty Owners-Texas Inc. (NARO-TX) jointly filed amicus curiae briefs in the original Supreme Court case and again in opposition to Chesapeake's motion to rehear the case.

On January 29, 2016, the Court denied Chesapeake's motion for rehearing, falling along the same five-to-four split as in the original decision. Chief Justice Hecht penned a new opinion for the majority, which includes Justices Green, Johnson, Boyd, and Devine. Justice Brown, joined by Justices Willett, Guzman, and Lehrmann, also filed a new dissenting opinion.

You can find links to the opinions and briefs TLMA filed in this case by visiting the *News* page of our website.

SAVE THE DATE!

TLMA STATEWIDE MEMBERS MEETING
OCTOBER 20, 2016
SAN ANTONIO, TX

OTHER EVENTS AROUND THE STATE

April 8-10—Texas and Southwestern Cattle Raiser's Convention and Expo—Fort Worth Convention Center, Fort Worth, TX.

April 14-15—Texas A&M AgriLife Extension Service 3rd Annual Bennett Trust Resource Stewardship Conference—Inn of the Hills Resort and Conference Center, Kerrville, TX.

April 15, 2016—Texas Agricultural Land Trust Free Seminar, Impacts of Loss of Rural Land on Water, Wildlife, & Agriculture—Omni Hotel, Corpus Christi, TX.

May 6—Graves Dougherty Hearon & Moody 3rd Annual Land and Mineral Owner Seminar—Stephen F Austin Intercontinental Hotel, Austin, TX.

June 22-24, 2016—Independent Cattlemen's Association 42nd Annual Convention—Inn of the Hills, Kerrville, TX.

TLMA FILES AMICUS BRIEF IN DENBURY GREEN PIPELINE CASE

A long-running eminent-domain case, *Denbury Green Pipeline-Texas, LLC v. Texas Rice Land Partners, Ltd., et al*, has made its way back to the Supreme Court of Texas. Denbury filed a petition for review with the Court, and TLMA has again filed an amicus curiae brief in support of the landowners.

The dispute began in 2007 when the Hollands declined to give access to their Jefferson County property, which they operate as a rice farm and cattle ranch, for a survey to construct a carbon dioxide pipeline. Denbury wanted to extend its private pipeline in Louisiana to its newly-acquired oil fields in East Texas. Denbury boasted on its website that it had monopolized all sources of carbon dioxide in the Gulf Coast and would use its pipeline to carry its carbon dioxide to its own oil fields in Texas for enhanced-recovery operations.

Denbury filed for a pipeline permit with the Railroad Commission in 2008, checking the box on the T-4 form stating that it was a common carrier. The Hollands believed the pipeline was private, and Denbury had no eminent-domain authority, so they continued to refuse access to their property. Denbury filed for an injunction in Jefferson County District Court to allow it to begin surveying, and it initiated condemnation proceedings to take an easement across the Hollands' land. The court granted Denbury's use of eminent domain to build the pipeline. As the case slowly made its way through the appellate process, Denbury constructed the pipeline, and the Green Pipeline was in service delivering carbon dioxide to the Hastings Field by 2010.

In 2011, in a victory for landowners, the Texas Supreme Court ruled that Denbury had failed to show that its pipeline qualified for common-carrier status—simply checking a box on a Railroad Commission form does not prove you are a common carrier. The Court reaffirmed this when it denied Denbury's motion for rehearing in 2012. The Court set a new standard that, in order to qualify as a common carrier, "a reasonable probability must exist that the pipeline will at some point after construction serve the public by transporting gas for one or more customers who will either retain ownership of their gas or sell it to parties other than the carrier." It remanded the case to the trial court to determine if Denbury qualified as a common carrier when it began planning the pipeline.

Back in the Jefferson County court, Denbury offered evidence of new contracts to carry carbon dioxide, all signed after the Supreme Court issued its opinion. It argued that, despite its boasts at the time that it had monopolized the carbon dioxide supply, it had intended to make its pipeline available for hire, and these new contracts satisfy the "reasonable probability" test for common-carrier status. In February 2014, the district court judge granted summary judgment to Denbury, declaring it a common carrier.

In February 2015, the Beaumont Court of Appeals reversed the summary judgment. It focused on the test the Supreme Court articulated in the first case, and it examined evidence of Denbury's intent at the time it began planning the pipeline. The court concluded that a question-of-fact existed for a jury to decide, stating that "reasonable minds could differ regarding whether, at the time Denbury intended to build the Green Line, a reasonable probability existed that the Green Line would serve the public." Denbury has now appealed this decision to the Supreme Court of Texas.

TLMA filed an amicus brief asking the Court to deny Denbury's petition for review. TLMA believes that the Beaumont Court of Appeals properly applied the Supreme Court's test and found determination of Denbury's common-carrier status necessary for a jury to decide. As stated in TLMA's brief: "A jury should be allowed to consider the evidence to determine Denbury Green's intent at the time it sought to condemn land for its pipeline. Such evidence is the most relevant and direct evidence towards a resolution of this Court's 'reasonable probability' test. "

You can find a link to the brief TLMA filed by going to the *News* page on our website, or view all the pleadings filed in this case by visiting www.txcourts.gov/supreme. Enter case number No. 15-0225 in the box for "Find My Case."

TEXAS SUPREME COURT DECLINES TCEQ APPEAL IN TEXAS FARM BUREAU SURFACE WATER RIGHTS CASE

In February, the Supreme Court of Texas chose not to hear the appeal of a major water case. Last year the Corpus Christi Court of Appeals issued a major decision *TCEQ v. Texas Farm Bureau* regarding surface water rights in Texas. The ruling in favor of the Texas Farm Bureau stands.

The dispute began in 2012 when Dow Chemical Company notified the TCEQ that is was making a "priority call" on the Brazos River. Essentially, Dow requested TCEQ curtail water withdrawals by other users on the Brazos with water rights junior to Dow. Dow's water right was granted in 1942, and it was one of the most senior water rights holders.

Dow's request would obviously impact farmers on the Brazos River with junior water rights. When TCEQ issued the priority call, it suspended 845 water rights in total, and 716 of those were permits issued for irrigation. The controversy, however, surrounds the TCEQ making a controversial exception to water-rights suspension. The agency allowed municipalities and electric utilities to continue drawing water even where their water rights were obtained after 1942.

The Texas Farm Bureau, joined by individual water-rights holders subject to the curtailment, filed a lawsuit against the TCEQ. They argued that TCEQ violated prior appropriation law—the rule that first in time is first in right.

The lawsuit alleged that TCEQ did not comply with the Texas Water Code because it disregarded prior-appropriation law when it curtailed water draws by junior water-rights holder, but excepted cities and utilities. The Texas Farm Bureau argued that TCEQ abused its discretion by designating certain types of junior users to which the priority call did not apply. They agree that TCEQ has the authority to suspend water rights in times of drought; however, the TCEQ must still comply with the prior-appropriations doctrine if it suspends water rights.

TCEQ, on the other hand, argued that it had the authority to issue the order, including the special exceptions, because Texas law grants it the power to protect the public health, safety, and welfare. TCEQ claims that the exceptions for municipalities and utilities were in the interest of public health, safety, and welfare.

The trial court ruled in favor of the Texas Farm Bureau. It agreed that TCEQ did not have the authority to cherry-pick exceptions to the priority call and disregard the established doctrine of prior appropriation.

The Corpus Christi Court of Appeals affirmed the trial court ruling, finding that TCEQ violated its statutory authority by including the special exceptions to its curtailment order. In short, the Court of Appeals recognized TCEQ's authority to manage the state's drought-stricken water resources, but ruled that the agency must act within the rule of law set by the legislature, which requires compliance with the prior-appropriation doctrine.

The Texas Supreme Court declined to review the Court of Appeals decision.

WELL RECLASSIFICATIONS COULD AFFECT ROYALTY OWNERS' INTERESTS

It is no secret that petroleum companies in Texas are struggling in the current economic climate. With oil prices at a fraction of the price-per-barrel at the recent peak, operators look for new ways to save. They may scale back production, lay off employees, or look for more efficient and cost-effect methods of production. It seems, however, some have turned to another enticing option—reclassifying oil wells as gas wells.


Photo by Esteban Monclova

It is common for a producing well to free up both oil and gas. However, under Texas law, a well is classified at the Railroad Commission as either an oil well or a gas well, not both.

The Commission itself can look at new data from the well, realize that the well was misclassified in the first place, and reclassify the well on its own initiative. In the alternative, an operator can petition the Railroad Commission to reclassify an oil well as a gas well. The state has seen a surge in these requests.

In the Railroad Commission's 2015 budget year, it reclassified 844 oil wells as natural gas wells. This is more than three times the number in 2014, and almost six times the 2013 oil-to-gas well reclassifications. There has been an increase in gas-to-oil reclassifications in the last few years, as well; however that number only climbed from 68 up to 239. It is far more lucrative to move to gas-well status.

A pretty significant state tax credit provides a big benefit of classifying a well as a gas well. The state measure was originally intended to spur more drilling of "high-cost" natural gas wells. Good for 10 years or until the credits add up to half the cost of drilling and completing the well, the tax credit amounts to several percentage points off of Texas's 7.5% severance tax on natural gas production.

The surge in reclassifications to gas wells could significantly impact projected state tax revenue. From 2008 through 2014, the tax credit cut more than $8 billion from operators' tax bills. However, Comptroller Glenn Hegar estimates that, just looking at the Eagle Ford Shale where reclassifications are happening the most, reclassifications could cost the state up to $250 million in tax revenue this year. The matter of whether the state will retroactively apply the credit for the years the producing well as classified as an oil well could bring an even deeper hit to state coffers.

For royalty owners, though, the surge in reclassifications brings up a troublesome aspect. TLMA District Vice President and owner of Trinity Mineral Management in San Antonio, Trey Scott noted a critical concern. "The retained-acreage provisions of many oil and gas leases hinges on the Railroad Commission's oil or gas well classification. Often times, oil and gas leases allow for much more acreage to be retained by a gas well than an oil well. It is not uncommon to see leases that allow 640 acres for a gas well and only 40 for an oil well." The practical effect of reclassification from oil well to gas well is that an operator can retain acreage that would have been released back to the mineral owner under an oil well classification, and the operator does not have to drill as many wells to hold the entire lease.

TLMA is following two cases currently pending at the Railroad Commission. Devon Energy seeks to reclassify 200 oil wells as gas wells in the Eagle Ford, and at the same time to amend the field-wide rules to make it easier to classify a well as a gas well. In addition, Pioneer Natural Resources petitioned the Commission to reclassify 11 wells. The Commission already stated that two of Pioneer's wells do not fit the requirements for gas-well classification, and the administrative law judge recommended denying Pioneer's petition. The Commission has yet to rule on the matter. Pioneer asked to delay the decision until Devon's case concludes.

WATCH OUT FOR DECEPTIVE OR PREDATORY ROYALTY OFFERS

TLMA members have contacted the office reporting deceptive royalty offers, and a search through online mineral forums shows that other royalty owners around Texas have received such offers, too. Believing that they are signing a top lease or a new lease on as-yet unleased properties, royalty owners may unwittingly end up selling their royalty interests.

It is important to note that the companies making these offers call them leases or agreements, and they do not use the terms buyer or seller. The Texas Property Code §5.151 contains special requirements for offers to purchase mineral or royalty interests. The offer must conspicuously state in 14-point type or larger that by signing and returning the document, you are selling mineral or royalty interest.

The law, however, makes an exception for oil, gas, or mineral leases so that those documents are not considered a purchase of a mineral or royalty interest. By titling offers as leases, the company making the offer does not have to draw attention to the fact that you are effectively selling your royalty interest.

One member received a solicitation letter which referenced existing leases in Pecos County, noted that additional lands owned in the county were not leased, and then offered a 1/5th royalty. The company included a check and a "Term Royalty Agreement." By signing the agreement and cashing the check, the mineral owner ended up selling the royalties, not obtaining a new oil and gas lease with the possibility of new production.

What's worse, though the solicitation letter stated that the agreement was for a term of two years and the title of the agreement itself is "Term Royalty Agreement (Two Year)," buried in the language of the agreement it conveys the royalties for a primary term of two years and then continuing for as long as there is an oil and gas lease for the property.

Another TLMA member was sent a solicitation letter and "Oil and Gas Royalty Lease" for mineral interests in Loving County. The offer letter and lease provide the legal description of the properties "save and except, however," the name and permit number of the well on each tract. This creates the illusion that the offer is for property not held under lease by existing wells.

Careful inspection of the documents raised red flags for the royalty owner. For starters, the lease was not a standard Producers 88 oil and gas lease, which she was used to seeing. A binding arbitration clause in the proposed lease also appeared troublesome. In addition, she had a difficult time getting in touch with the offeror or getting straight answers when she did reach him.

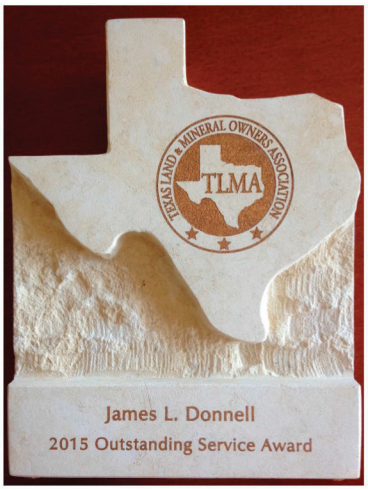
The lease was for a three-year term, and for as long thereafter as there is production in paying quantities. Again, this clause can be misleading in that it mirrors what is often in oil and gas leases, obscuring the fact that the agreement is actually to buy the royalty interest for the property. As the member told TLMA, "when you read [the proposed lease] carefully and look at the title, you see it is indeed about offering a one-time payment to acquire 75% of royalties in perpetuity. This is not about new exploration and production."

If you receive an offer for a "Royalty Lease," "Royalty Term Agreement," or any other similarly-named legal document, read all of the paperwork carefully so that you fully understand the terms of the agreement. If the offer comes with a short deadline for you to act and demands a quick decision from you, this should be a red flag, too. An offer should allow you a reasonable amount of time to consult an attorney as necessary.

The Association of Professional Landmen (AAPL) has a code of ethics and standards of practice that the AAPL strives to uphold. If you receive an offer from a landman that you feel is questionable, you can check with AAPL and see if the landman is a member in good standing. AAPL is located in Fort Worth, and can be reached by phone at (817)847-770. Please note that membership in AAPL is voluntary, and the organization is self-regulating, not subject to state law requirements for certifications.

TLMA OUTSTANDING SERVICE AWARD GOES TO JAMES DONNELL

The recipient of TLMA's 2015 Outstanding Service Award is Mr. James L. Donnell, Sr. of La Salle County, who has been a member of TLMA since its first year.



The Outstanding Service award honors a TLMA member who is dedicated to reinstating a sense of fairness in the relationship between those that use the land and those who live on it, and who has made an outstanding contribution toward that end.

Fellow TLMA member James McAllen nominated Mr. Donnell for the award in recognition of Mr. Donnell's commitment to ensuring fair treatment of landowners in pipeline condemnation proceedings.

Mr. Donnell fought a long battle with LaSalle Pipeline to ensure more just consideration for landowners faced with condemnations of pipeline easements.

The result of the case was the affirmation that a pipeline can affect the value of the entire property, not just the area of the easements taken, and the landowner is entitled compensation for the diminution in value of the whole. In addition, the court rejected the pipeline company's attempt to set unreasonably-high evidentiary burdens for a landowner to prove the change in market value.

Regarding Mr. Donnell's challenge of LaSalle's condemnation, Mr. McAllen stated: "It is my opinion that what Mr. Donnell was able to accomplish was a fair and equitable solution to a pipeline through your ranching operations." The TLMA Board of Directors agreed, and voted to present Mr. Donnell with the 2015 Outstanding Service Award.

TLMA MEMBERSHIP RECRUITMENT AWARD GOES TO TUCKER BRIDWELL

The TLMA is pleased to present the 2015 Membership Recruitment Award to Mr. Tucker Bridwell of Abilene, who became a TLMA member last year.

This annual award was created to honor a member who has taken an active role in introducing other land and mineral owners to TLMA and helping to bring new members to the association.

TLMA Board Chairman Carolyn Frost Keenan expressed her appreciation for Mr. Bridwell's advocacy on behalf of TLMA. "Tucker discovered and joined TLMA during the last legislative session. Boy, are we glad he found us! Since then, he has worked diligently to spread the word about TLMA's mission, which has led him to recruit many new members. Our thanks to Tucker Bridwell for his effort and enthusiasm," said Mrs. Keenan.

A long-time Abilenean, Mr. Bridwell graduated from Abilene's Cooper High School. He earned both his bachelor's and master's degrees in business at SMU, and eventually returned to his hometown. Mr. Bridwell has served as the president of both the Dian Graves Owen Foundation and the Mansefeldt Investment Corp. in Abilene since 1997.

Mr. Bridwell has been involved with the oil and gas business in Texas for nearly thirty years. The TLMA benefits from Mr. Bridwell's knowledge in this area as well as his willingness to engage with other land and mineral owners on the merits of TLMA membership.

Texas Land & Mineral Owners Association
1005 Congress Avenue, Suite 360
Austin, TX 78701

PRSRT STD
U.S. POSTAGE
PAID
PERMIT NO. 1425
AUSTIN, TX

TLMA Membership Information Form

☐ **I would like to join TLMA** ☐ **I am a member, please update my contact info**

Please return to: TLMA, 1005 Congress Ave., Suite 360, Austin, TX 78701

Name _____

Organization/Ranch Name _____

Address _____

City _____ **State** _____ **Zip** _____

Telephone Number _____

Email Address _____

Referred by _____

Don't forget!

If your contact information changes, be sure to update TLMA and avoid delays in receiving your newsletters, renewal notices, and other membership correspondence.

To change your address or any other membership information, contact Robbie Querner at (512) 479-5000, mail in this form, or email us at membership@tlma.org.

Find more information, join TLMA, or renew your membership online at www.tlma.org