



TEXAS LAND & MINERAL OWNERS ASSOCIATION

OFFICIAL NEWSLETTER

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THE 87TH TEXAS LEGISLATURE ADJOURNS SINE DIE...FOR NOW.

On January 12, 2021 the 87th Texas Legislature convened in Austin for a session like no one had been through. The pandemic was expected to dominate the session in many ways—the number of bills that would move through the process, the topics of bills that would move through the process, and the day to day operations of the Legislature. Many anticipated a budget session similar to the 2011 session when the state was several billion in the red. Thankfully, that wasn't the case and near the end of session, Comptroller Glenn Hegar revised his biennial revenue estimate to include an additional \$1.7 billion.

As mentioned in the March newsletter, the House elected a new speaker, while the Lt. Governor presided over the Senate for the fourth legislative session.

On February 1, 2021, Governor Abbott gave the State of the State Address where he outlined his legislative priorities for the legislative session. At that time, his emergency items were as follows:

- Expanding broadband internet access
- Preventing cities from defunding police
- Bail reform—the Damon Allen Act
- Election Integrity
- Protection from civil liabilities for businesses that operated safely during the pandemic

Other legislative priorities included: protection of religious activities, protection of gun rights, pro-life bills, making relaxed regulations passed during the pandemic (such as alcohol to go and telemedicine) permanent, eliminating human trafficking and drug smuggling, funding public education at levels passed during the 86th legislative session, bolstering civic education, addressing and mental health issues.

After the winter freeze and near loss of the electric grid just days after the State of the State, Governor Abbott added winterizing Texas' power system and the necessary funding for winterization to the emergency items list. In addition to this, there was a strong desire to reform the Public Utility Commission and Electric Reliability Council of Texas.

The Lieutenant Governor also released a list of thirty priorities—most of which passed. The House had its own set of priorities and most of those passed, too.

As deadlines quickly approached at the end of session, many priority bills had yet to be sent to the Governor's office. Tensions began to run high, as they typically do. One of the bills remaining was election

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UPDATE FROM THE EXECUTIVE DIRECTOR

TLMA Members—

I hope that you all are enjoying this summer.

This legislative session proved to be its own kind of unique! This session was expected to present new challenges, but I don't think anyone could have anticipated a record breaking freeze to pivot the entire focus of the legislature.

All in all, TLMA had a very successful session. As always, there was a curveball we weren't expecting, but the government relations team was ready and stepped into action. We have a few items to work on during the interim, but as you read earlier, we have at least one, if not multiple, special sessions to get through first.

As TLMA has always said, the number of members we have and represent is critical to assisting us in our efforts. TLMA will be testing new methods of membership development, but need our members to continue to spread the word about us and what we do to your family and friends!

We are excited to begin hosting more membership and educational events. I am working on finalizing details for a fall membership event and look forward to announcing that information very soon!

I will be attending the NARO-TX Convention in Houston from July 15-17 and TLMA will have a booth at the Texas A&M Beef Cattle Short Course in August. If you will be at either event, please make sure to say hello!

I am very excited to see most conferences transition back to in-person events and hope to see you all in person very soon!



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TIPS FOR MANAGING MINERAL RIGHTS DURING VOLATILE TIMES

By Robert Turnbull, Argent Mineral Management

As the Covid-19 pandemic and one of the most severe declines in oil prices appears to be ending, the lesson for mineral owners was to not panic and trust that the economy and demand for commodities would rebound.

As of this writing the oil and gas market has stabilized, and we are seeing renewed interest in leasing and operators willing to drill new wells. Here are four important elements of a mineral management plan to keep in mind as activity resumes:

1. Consult a professional for lease negotiations and contracts

Negotiating a lease agreement – the most important document for a mineral owner – is a complex process. Mineral owners unfamiliar with lease forms and their clauses, such as Pugh, warranty, post-production costs, depth and gross vs. net – and how those terms affect how royalties are calculated and acreage is held – should engage an experienced mineral professional to handle these negotiations.

While lease negotiation and understanding are incredibly important, it isn't the only sensitive portion of the leasing process. Lease bonus terms are highly competitive and often secretive, making connections and experience key. Seasoned mineral professionals typically have access to valuable research tools and an abundant inventory of acreage under management to negotiate the best lease terms available.

2. Understand oil & gas revenue detail

While oil and gas producers are held to the “reasonably prudent operator” standard when performing their duties, there is no generally accepted standard for production and financial reporting provided to mineral rights owners.

For many landowners, making sense of these reports can be frustrating. Inexperienced rights owners may also find it incredibly challenging to understand how oil and gas accounting affects royalty payments.

Here are a few of the typical errors proper accounting may uncover:

Expenses: Deductions are taken from royalties that exceed what is allowed in the lease

Production volumes: Operators do not make payment for the full quantity of the product that was produced and sold

Pricing: Operators may pay the weighted average price of oil and gas instead of the actual price received

Nonpayment: Operators may fail to set up royalty owners on a producing well

Complex oil and gas accounting will likely require use of an accounting system to track royalty payments to ensure timely and accurate payments. Working with a professional advisor on royalty accounting can also allow owners insight into industry trends and better understand the status of their owned acreage.

3. Consider auditing the production company

For oil and gas rights owners, the audit is a friend. An audit can identify mistakes and ensure transparency so both parties are on the same page and payments are in compliance with the lease agreement. Mistakes can

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ANOTHER SUCCESSFUL LEGISLATIVE SESSION FOR MINERAL OWNERS

HB 3794—relating to oil & gas liens by Chairman Charlie Geren, sponsored by Senator Chuy Hinojosa

Signed by the Governor; effective 9/1/2021.

In 2020, TLMA was notified of the *SemCrude* decision out of the United States 5th Circuit Court of Appeals impacting royalty owners and producers.

In 1983, Representative Tom Craddick passed the first purchaser statute to protect royalty owners and producers in the event of a bankruptcy of their operator. The Texas First Purchaser statute provided that producers and royalty owners have a security interest in the oil and gas (as personal property) that is produced from their properties to secure the purchaser's obligation to pay for that oil and gas. This specific type of security interest is automatically perfected without the filing of a financing statement. Automatic perfection protects Texas producers and interest owners by making sure they are first in line to get paid if the purchaser goes bankrupt.

The *SemCrude* decision began in 2008 when First River Energy filed for Chapter 11 bankruptcy protection. At that time, the Court found that because Texas and Oklahoma have non-standard Uniform Commercial Code provisions, out-of-state courts, like Delaware where *SemCrude* is domiciled, will instead use the standard UCC provision to determine which law to apply to personal property. For example, when a purchaser is organized under the laws of a different state, like Delaware in the *SemCrude* decision, the UCC provides for that state's law to apply. Further, under the commercial codes of Delaware, Texas, and Oklahoma, in order to determine whether a security interest in collateral is properly perfected, the court must apply the law of the state where the debtor was organized. If the debtor is not located in Texas, the Texas first purchaser statute is not applied to the case, and a royalty owner's security interest was not automatically perfected. Therefore, Oklahoma and Texas royalty owners and producers were not protected.



Chairman Charlie Geren
(R-Fort Worth)

In 2010, Oklahoma amended their law. When the lawsuit was tried again, the Court found that Oklahoma interest owners were protected, but Texas' interest owners remained unprotected. In 2013, Texas attempted to change this law but was unsuccessful. The Delaware bankruptcy court affirmed this in *SemCrude*. The court held that the UCC provision that applies is from the jurisdiction where the debtor is located, rather than where the oil and gas (as collateral) is located. Therefore, Texas interest owners cannot use the state's non-standard provision of the Texas Business and Commerce Code (i.e. Texas' First Purchaser statute) if the debtor is organized outside of Texas. When a court holds that the debtor's state law governs, Texas producers no longer have a perfected interest because they did not file a financing statement – despite the fact that the Texas producer relied on the protection's automatic perfection from the First Purchaser Statute.

The United States 5th Circuit Court of Appeals further affirmed this position in February 2021 and specifically mentioned that the "Texas Legislature should take note".

To resolve this loophole, the First Purchaser Statute needed to be revised to ensure that Texas oil and gas

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ANOTHER SUCCESSFUL LEGISLATIVE SESSION FOR MINERAL OWNERS CONT

production is treated as real property which is governed by the state where the property is located (i.e. Texas law), rather than personal property subject to the UCC's choice-of-law rules.



Senator Juan "Chuy" Hinojosa
D-Edinburg

With the increase in bankruptcies due to the pandemic, TLMA knew that changing this law was timely and imperative to protect all interest owners—our members and even producers. Knowing the impact to producers, TLMA was hopeful that we could negotiate a bill that TLMA and industry could work on together for the third session in a row.

The as filed version of HB 3794 was modeled after the Oklahoma statute that Courts have ruled protect their royalty owners and producers. Industry identified areas of concern and the negotiations began.

In the end, the final bill contained all original protections for royalty owners and producers, while also providing the necessary protections for refiners and other downstream processors.

TLMA negotiated this bill with industry partners representing upstream, midstream and downstream entities and banks. We are immensely grateful for Chairman Charlie Geren's leadership in ensuring fair negotiations for all parties and seeing this bill through the entire legislative process and to Senator Chuy Hinojosa for navigating this bill through the Senate.

SB 1259—relating to causes of action for withholding payments of the proceeds from the sale of oil and gas production by Chairman Brian Birdwell; sponsored by Representative Reggie Smith

SB 1259 bill was introduced as a result of a Texas Supreme Court decision, *ConocoPhillips v. Koopmann*, which held that the division order statute, Chapter 91 of the Natural Resources Code, does not provide the sole remedy for royalty owners suing for their royalties. *ConocoPhillips* argued that Chapter 91 was intended to supersede a royalty owner's contractual right to sue for royalties due under their lease. SB 1259, signed by the Governor, provides that a royalty owner "does not have a common law cause of action for breach of contract against a payor for withholding payments under subsection b) unless, for a dispute concerning the title, the contract requiring payment specifies otherwise." Under the division order statute a payor may withhold payment without interest if there is a dispute concerning title to the royalty owner's interest. The intent of the bill is to protect payors from having to pay interest or attorneys' fees if the payor withholds payment because of a title dispute.

Note that the amendment provides that the royalty owner does have a cause of action for breach of contract for a dispute concerning title if "the contract requiring payment provides otherwise." So a lease can include provisions as to the lessee's obligations if there is a dispute concerning title. For example, the lease could provide that, in such event, the lessee must deposit the disputed royalties in an interest-bearing account pending the outcome of the title dispute. If the lessee fails to do so, the lessor could sue for breach of the lease. Presumably this provision in the lease would pre-empt the statutory provision denying the royalty owner the right to sue for breach of contract for failure to pay royalties in event of a title dispute. If a lease provides for specified interest on unpaid royalties, would that be a contract provision "specifying otherwise"? Not clear.

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ANOTHER SUCCESSFUL LEGISLATIVE SESSION FOR MINERAL OWNERS CONT.

SB 1259 was originally filed in the 2019 legislative session. TLMA was successful in defeating the bill then because the parties could not reach a consensus on the bill. This session, we negotiated language that TLMA does not believe irreparably harms mineral owners.

SB 367—relating to the requirements for an application for a permit to drill an oil or gas well at a site adjacent to a well blowout site by Senator Borris Miles; sponsored by Representative Ron Reynolds

SB 367 was not a bill the TLMA was working until the last week of session. However, in mid-May, the Travis County District Court released its judgement in the *Opiela v. RRC* case impacting allocation wells. The last week of session, Representative Tom Craddick amended this bill that would have given the RRC exclusive authority to issue allocation well permits, circumventing the legislative and judicial processes. This would have been detrimental to many mineral owners—especially the small owners and those with older leases that do not address new technologies like horizontal drilling. The bill finally died at the last minute possible—midnight on Monday, May 31, 2021. Thank you to all of our members who sent emails and made phone calls to their representatives!

RRC Budget

A portion of the Railroad Commission's budget is dedicated to plugging abandoned wells that become the state's responsibility after left unplugged by an operator. In years past, the RRC was given a large sum of funds from the Economic Stabilization Fund to contract with service providers to increase the number of wells plugged each year. As you are all likely aware, orphan wells are a problem in Texas that is growing exponentially. The Legislature saw the benefit of these funds and appropriated the same level of funding from the general revenue account.

This session was not any different at the start. Both chambers fully funded the well plugging program. However, the Senate removed nearly half of funding from the strategy. Since the House kept the full funding amount, the conference committee was able to choose which level they desired. Between the time the House and Senate selected conferees and when the final budget was approved, Comptroller Glenn Hegar revised his biennial revenue estimate to include an additional \$1.7 billion. The conference committee fully funded the well plugging strategy in for the biennium.

Eminent Domain

For the past three sessions, eminent domain has been a heavily negotiated issue. Each session has had at least one main bill with many reforms to the condemnation process, as well as smaller bills that contained a piece of reform. This session proved to be no different than the others with one exception—the “major” bill, HB 2730 by Chairman Joe Deshotel, passed! The bill is pared down significantly from the original version, but still adds additional protections for landowners. The bill includes the following provisions: additional information in the Landowner Bill of Rights (LBoR); adds continuing education requirements for right-of-way agents and creates a penalty if they low ball a landowner; adds the following requirements to a bona fide initial offer; contact information for the condemning entity; adds required provisions to easement terms; adds notice requirements for condemnation petitions; and, adds timelines for the special commissioners court process.

Additional bills relating to eminent domain that passed relate to disclosure of appraisal reports, determining actual progress, land change of use taxes due to condemnation, and notice of entry by common carrier pipelines.

You can learn more about each bill at the Texas Legislature Online website capitol.texas.gov or www.tlma.org.

TIPS FOR MANAGING MINERAL RIGHTS DURING VOLATILE TIMES CONT.

easily and inadvertently happen and often go unnoticed for years. In our work with clients, Argent Mineral Management typically finds underpayments in seven out of every 10 mineral rights audits we undertake.

The audit process can take a substantial amount of time, as it usually involves reviewing hundreds of pages of check detail and communicating with multiple operators, invariably requiring the involvement of a professional experienced in the process. When deciding whom to hire, considerations should include qualifications, familiarity with relevant operator(s) and geographic location, cost, what sort of software, if any, is used to increase efficiency and accuracy of the audit, and references.

4. Lastly, have discipline

A disciplined strategy for managing mineral assets can help owners make it through difficult times as well as good times. Proper management can help avoid poor decisions that could impact generations of family members, especially as owners receive low ball offers for mineral rights that may look attractive when production is down.

You can learn more about Argent Mineral Management at <https://argentsfinancial.com/subsidiary/argent-mineral-management/>.

THE 87TH TEXAS LEGISLATURE ADJOURNS SINE DIE...FOR NOW CONT.

integrity. When the bill came up for a vote, the House Democrats walked out, breaking quorum, and prevented the bill from passing.

At the conclusion of session when two of Governor Abbott's emergency items did not pass—bail reform and election integrity—Governor Abbott indicated there would be a special session for those items. Further, as a result of the walkout, he threatened, and eventually followed through on, vetoing Article X (the Legislature's budget). In addition to these three items, there will be a later special session on redistricting and appropriating federal funding.

In late June, Governor Abbott announced a special session that will begin on July 8. The legislative agenda has not yet been announced, but is expected to include at least the three above items.

TLMA worked on several bills throughout the legislative session that are presented in greater detail beginning on page 4. Additional bills included on the website.

Now that the regular legislative session is complete, campaign announcements are coming rapidly! Future newsletters will include information on relevant races.

UPCOMING DATES OF INTEREST

July 8, 2021—Graves Dougherty Hearon and Moody Land & Mineral Owner Webinar
July 15-17, 2021—NARO-TX Convention, Houston
July 23-25, 2021—Texas & Southwestern Cattle Raisers Convention
August 2-4, 2021—Texas A&M Beef Cattle Short Course, College Station
August 3, 2021—RRC Hearing, Livestream
August 17, 2021—RRC Hearing, Livestream
September 14, 2021—RRC Hearing, Livestream
September 28, 2021—RRC Hearing, Livestream



Be sure to watch for emails relating to deadlines to register for the TLMA Regional Meetings.



Texas Land & Mineral Owners Association
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TLMA Membership Information Form

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