Let the RRC Do Their Work

The earthquake scare needs careful study. One bad memory looms large as the oil and gas industry copes with emerging studies, including one from Southern Methodist University last week, showing its activities are the likely cause of induced seismicity in either Texas or Oklahoma.

Range Resources filed a case against Steven Lipsky, a North Texas man, who lit gas fumes from his water hose on fire and accused the company of contaminating his water well. Lipsky sued Range and Range countersued. As of Friday, the Range defamation case against Lipsky is heading back to a trial court. The Texas Supreme Court dismissed Lipsky’s wife and consultant from the defamation action, but not Lipsky himself.

“The industry certainly wishes to find a solution to all of this,” said Alex Mills, president of the Texas Alliance of Energy Producers, who raised questions about the SMU study but welcomed scientific research into seismicity’s relationship to production and injection wells. “We just want to make certain that we don’t get in the same situation we got into with the Range Resources case in Parker County where there were allegations made proved to be erroneous. Lawsuits filed, legal action was taken by EPA, and the (Texas) Railroad Commission got involved in it. The Railroad Commission vindicated Range Resources and the EPA backed down, but Lipsky continued with his complaints”. “There are a lot of uncertainties involved in these cases and a rush to judgment is not in the best interest of everybody.”

To date Mills has no knowledge of any lawsuit seeking damages for seismic activity related to oil and gas operations. Mills points to statements made in legislative hearings and at the Railroad Commission from the Azle-Reno area asking who would pay for damages to homes and property if the state allows oil and gas activities that cause harm. The Railroad Commission subsequently adopted rules allowing it to stop or modify injection well activities if they are causing earthquakes.

The SMU inquiry found that saltwater extraction and injection near two faults likely caused a rash of small earthquakes in Azle and Reno from late 2013 to spring 2014. That study will be the subject of a hearing next Monday of the House Energy Resources Committee, chaired by Rep. Drew Darby, R-San Angelo. The Railroad Commission has also scheduled hearings in June at which operators of two disposal wells in the Azle hearings should show cause for why injection permits for the wells should not be cancelled and the wells shut in. The wells were identified in the SMU study, which showed an “alleged connection” between their ongoing operations and seismic activity in the area.

“In light of SMU’s study linking disposal well activity to earthquakes in 2013, it is important to assess this new information in relation to the continued operational safety of the wells,” Commission Chairman Christie Craddick said last week. The Environmental Defense Fund praised the commission’s decision to hold the hearings. “The commission is taking a proactive approach to the important but complicated problem of earthquakes linked to oil and gas development,” said Scott Anderson, EDF’s senior policy director. “We couldn’t agree more with Commissioner Christie Craddick’s statement that it is incumbent on the commission to apply its rules where and when appropriate to protect public health and the environment.”

Anderson also cautioned that it could be difficult to determine whether a particular earthquake is caused by oil and gas activities. It raises questions about why Irving has been experiencing earthquakes, and it underlines why each quake must be viewed individually. He noted that Darby and other House leaders support budgeting $2.5 million for deploying mobile seismometers, and suggested an additional $1 million per year would be ideal for ongoing research and maintenance.

Mills released detailed statements raising several questions about SMU’s study and noting that seismic activity has occurred in specific sites with certain geologic characteristics. “Even though the study pointed a finger at water extraction and re-injection, it did not recommend any solutions,” the statement said. “Further, the study admits that there were six key areas where they had to make estimates, because important scientific facts were not known to researchers. The uncertainties listed in the report are brine production, bottom-hole pressure, regional structural geology, stress magnitude and orientation, permeability and modeling.”

Let the RRC do their work before jumping to conclusions and rushing to the courthouse.

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FROM THE WELLHEAD

By the time you are reading this, the Texas legislative season will be coming to an end (no way there is an extension, right?). Hopefully the bills affecting our industry have brought no new heartaches!

The dramatic decline in oil & gas prices has slowed down, but there is no consensus on whether we will see continued declines in prices, or when we might see a price recovery. The drilling rig count in the Texas panhandle is about one third where it was one year ago. I bet we all agree that this down cycle has to reverse at some point.

While the impact of a down energy market definitely has a negative impact on our region, our local economies are diversified enough to survive and even thrive. However, several OPEC and non-OPEC producers rely heavily on oil revenue to finance their national budgets. If crude oil prices fall further or are sustained at current levels, these oil-dependent producing countries will face tough decisions; decisions that could spark civil unrest or worse. Global geo-political risk could have a very significant impact on our industry.

Many analysts believe that lifting the U.S. crude export ban could help mitigate the impact of any extreme decisions by other oil producing nations. Lifting the ban could possibly bring about a greater balancing of world-wide crude supplies. Countries heavily dependent on OPEC for their energy would have an alternative for at least some of their energy needs. The resulting stabilization of world-wide energy prices would actually help the U.S. The resulting reduction in extreme high and low prices would allow U.S. producers to have greater confidence in their exploration budgets. This would then actually help the U.S. come closer to energy independence. Definitely food for thought.

On a lighter note, we are having a “first ever” summer networking event on Saturday, June 13th at the Piehl Ranch in Bushland. PPROA will be serving up some FUN FOOD & FESTIVITIES! Feel free to bring your friends and family for a barn dance along with prizes for horse shoe pitching, prairie golf and best dressed cowboy and cowgirl contests! I believe it will be a great time to enjoy time with old friends and make new ones. I hope to see you there. (P.S. cowboy attire is not required.)

Plans are well in motion for the 2015 PPROA Annual Meeting. Please mark your calendars for September 22 thru 24, because Judy and Cynthia are working hard and planning to “shake things up a bit”.

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EVP NOTES

The legislative session is beginning to “heat up” so to speak. Bills are being amended and moving to committee assignments and on to formal readings in the house and senate.

The hottest topics for are industry thus far are still (1) HB40 and SB1165 having to do with consistent language throughout the State of Texas regarding hydraulic fracturing by municipalities. There has been an agreement signed between the Texas Municipal League and Texas Oil & Gas Association witnessed by Drew Darby, the author of the bill, stating that both groups support or will remain neutral on the committee substitute to HB 40 provided no amendments are supported by either party unless mutually agreed. On Monday April 20th HB 40 passed its third reading 125-20. The margin was much higher than expected so that is good news moving forward. (2) HB 1552 and SB 919 Allocation Bill have been sent to committee with amendments expected before it proceeds to calendar and hearings (3) Question pertaining to the Texas Railroad Commission Name Change HJR 76 and HB 1106. There has been a lot of discussion regarding the pros and cons to the name change. At this point PPROA has remained neutral.

I continue to participate with peer associations regarding bills that are critical for that week. If you have a particular interest in any bill, please call and I will give you the latest update. The newsletter will provide you with a list of bills that are pertinent to our industry along with the latest updates at the time of publishing; however, if you need further information – please call!

**Summer Event** - June 13th at the Piehl Ranch in Bushland! Bring your co-workers, friends and family to the PPROA first annual Cowgirls & Cocktails Summer Party. We will provide the food, fun, drinks and dance – we just need YOU! Beer, wine and set ups will be provided. We will have a prairie golf chipping, cow calling, cow chip throwing contests along with best dressed cowboy and cowgirl. Each contest will have a prize. Be careful because the sheriff will be arresting outlaws and you must make bail.

**Events Committee** - Most volunteered committee! If you are interested in being a part of planning PPROA events, please call our office. Change only happens if you voice your interests!

**Quarterly Combined Meetings** – Our next quarterly joint meeting will be held in July. Our last meeting had about 60 attendees. Thanks to all our peer industry groups for supporting this joint venture.

**Annual Meeting** – September 22-24, 2015. Plans are already in motion for our Annual Meeting! We are currently approaching what we hope will be a significant panel of speakers.

**PPROA Administrative Improvements** - PPROA recently converted our newsletter to a digital version. Please be patient as we try to work out the “kinks”. By converting to all digital that allows us to track how many actually open the newsletter and what page(s) receive the most “clicks” or is the most viewed. This helps us know what members enjoy seeing most! You can still request a printed version of the Pipeline by dropping us an email or call the office.

Until next time……. 
XH, LLC v. Cabot Oil & Gas Corp., No. 12-12-00338-CV, 2014 WL 2505541 (Tex. App.—Tyler May 30, 2014, no pet.) (mem. op.), held that the parties’ express provision governing priority of interpretation would be given effect to resolve conflicting area of mutual interest (“AMI”) provisions in a Purchase Agreement (“PSA”) and its attached joint operating agreement (“JOA”). Under the PSA, Seller conveyed to Purchaser 80% of Seller’s interest in certain leases, reserving an overriding royalty interest (“ORI”) to Seller on the assigned leases. Seller subsequently conveyed the ORI to Cabot. Purchaser contended Cabot was subject to the AMI agreement and obligated to offer to Purchaser the opportunity to purchase Purchaser’s proportionate share of the ORI that Cabot acquired from Seller.

The PSA included an AMI provision (“PSA AMI”) and an attached JOA. The JOA also included an AMI provision (“JOA AMI”). The PSA AMI provision provided that “[a]ll leases subsequently acquired by either party . . . will be subject to the Area of Mutual Interest provision provided in the Joint Operating Agreement . . . .” The JOA AMI provision, in Article XVI, provided that “[i]n the event that any party or parties acquire any oil and/or gas interest (which shall be deemed to include royalties, mineral interests, and other payments out of production) or oil and gas leases or other contract rights which allow the Participation for oil and/or gas, within the AMIs as herein above defined, then the non-acquiring party or parties shall have the right to acquire their proportionate interest . . . .” In the definitions section of the JOA, “Lease” is defined as “oil and gas leases or interests therein, . . .” but the defined term is limited to its use in the JOA. Article XVI of the JOA also provided that “[i]n the event of any conflict between the provisions of the [JOA] and the [PSA], the provisions of the [PSA] shall prevail and control.”

Because the PSA and JOA were executed at the same time, for the same purpose, and in the course of the same transaction, the court held that they should be read and construed together. However, this principle is simply a device for ascertaining and giving effect to the intention of the parties and cannot be applied arbitrarily and without regard to the realities of the situation. The court held that the two AMI provisions were unambiguous. The PSA AMI was limited to subsequently acquired leases, and the JOA AMI was broader and included subsequently acquired oil and gas interests. There was no language in the JOA indicating that the JOA AMI provision was intended to supplement the PSA AMI provision, and the expanded definition of “lease” found in the JOA was expressly limited to its use in the JOA. “Similarly, the language of the [PSA] fails to indicate that the acquisitions covered by its AMI provision may be supplemented by the AMI provision in the JOA or that its references to ‘leases’ is merely an example.” The court concluded that the two provisions were in conflict, that they could not be harmonized, and that the court must follow the parties’ determination that the PSA would control. Therefore, the ORI acquired by Cabot was not subject to the AMI agreement as expressed in the two documents.

The court then held that its decision would be the same even if the two provisions could be harmonized. This part of the opinion is based upon another provision in the JOA that provides the JOA AMI is not applicable to any acquisition of an interest that, prior to or at the time of its acquisition, was subject to the JOA. Because the ORI was created after the JOA had taken effect, and was therefor subject to the JOA, the court held that the AMI did not apply to the ORI.

The terms and provisions of the assignments to Purchaser and to Cabot were not discussed in the opinion, and there was apparently no issue as to whether or not Cabot acquired its ORI subject to the PSA and/or the JOA.

PSAs and JOAs are frequently executed together as part of a single transaction. There are often many other documents attached and included in the PSA, such as the form of assignment. The parties generally do think of them as part of a single agreement, and there is clear precedent that the courts will harmonize the documents in a single transaction. When the parties include a provision prioritizing the documents for interpretation in the event of an irreconcilable conflict, the PSA is often listed first, because it is often perceived as the most “important.” This case illustrates that this choice may be a mistake. There is not likely to be an irreconcilable conflict about who is buying what for how much, but the ancillary documents often provide more detailed provisions governing the rights of the parties after closing and as to the particular matters covered by the ancillary documents. Of course another way to avoid conflicting provisions is to expressly prioritize those specific provisions, or perhaps even better, to avoid having two provisions on the same subject. If the parties in this case did not include any provision resolving conflicts, would the court have been more likely to harmonize the two AMI provisions and reach the opposite result? Would the result have been different if the provision referred to “any irreconcilable conflict” instead of “any conflict”?

Jeff McCarn may be contacted at (806) 345-6340 or jmccarn@bf-law.com
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March 17th we held a ribbon cutting with the Amarillo Chamber of Commerce. Several members attended, as well as current board president Greg Graham, past board president Brady Brown and past president/Living Legend Tom Cambridge. It may look like Judy is giving Greg an elbow, but we assure you no presidents were hurt!
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PRIORITY LEGISLATION

A FEW NOTES:
35 Days. As of Monday, April 27th we have 35 days in the Texas legislature. The sounds you will begin to hear are of bills dying. The calendars for the House and Senate will get longer with less time for committee hearings. Most of the House Committee hearings now through the mid May will be “mercy hearings”. Some, but few, will make it.

Big Issues Left. We now have House and Senate Budget Conferees. So that work is underway. The House will take up HB 31 and HB The vote on HB 31 was 141-0. The vote on HB 32 was 116-29. They are the franchise tax cut and the sales tax cut. They should move to the Senate by May 1st. Leadership has to begin reaching agreement on the big issues.

The more interesting vote was on the Smithie Amendment to raise the business exemption from $1 million to $4 million. The vote was 120 to 16 to table the amendment with the Speaker (who rarely votes) voting to table.

HB 40. It has been referred to Senate Natural Resources. The TXOGA, TML and Darby agreement on no amendments does not apply to the Senate. That said, Atmos is the only one we are aware of that wants an amendment. The 125 vote in favor of the bill in the House sure has some Senators wondering what there is to discuss.

Keffer Congestion Bill. HB 3288. It appears the bill now has legs...if we can get it out of House State Affairs. The Texas Industrial Electric Consumers have made some changes and is now in support of the bill. Anything to help on West Texas and South Texas congestion is welcomed.

Earthquakes and the RRC. As previously reported, on Friday the Railroad Commission issued Show Cause Orders to XTO and EnerVest on their Azle disposal wells. The hearings will be in June. Craddick and Porter supported the orders. Sitton continues to pursue his effort for a public hearing.

On Monday, May 4, House Energy has invited SMU and the Railroad Commission to testify on the SMU Study that was released last Wednesday.

HB 30 Larson, Lyle (R) Relating to the development of brackish groundwater. Remarks: Requires regional water planning groups to include in their regional water plan submitted to the development board: opportunities for developing large-scale desalination facilities for brackish groundwater or seawater to serve local or regional brackish groundwater production zones.

HB 31 Bonnen, Dennis (R) Relating to decreasing the state sales and use tax rate. Remarks: Sales Tax Decrease from 6.25% to 5.95%

HB 32 Bonnen, Dennis (R) Relating to decreasing the rates of the franchise tax. Companions: HB 1316 Bohac, Dwayne (Identical) Remarks: 25% Franchise Tax Decrease

HB 40 Darby, Drew (R) Relating to the express preemption of regulation of oil and gas operations and the exclusive jurisdiction of those operations by the state. Companions: SB 1165 Fraser, Troy (Identical) 4-15-15 S First placement on Senate Intent Calendar Remarks: TXOGA Preemption Bill. Local Ordinance. The authority of a municipality or other political subdivision to regulate an oil and gas operation is expressly preempted, except that a municipality is authorized to enact, amend, or enforce an ordinance or other measure that regulates only surface activity that is incident to an oil and gas operation, is commercially reasonable, does not effectively prohibit an oil and gas operation, and is not otherwise preempted by state or federal law.

HB 200 Keffer, Jim (R) Relating to the regulation of groundwater. Remarks: 8 page bill that sets out the process to contest the adoption of a desired future condition.

HB 1331 King, Phil (R) Relating to the treatment and recycling for beneficial use of certain waste arising out of or incidental to the drilling for or production of oil or gas. Remarks: Defines "drill cuttings" as subsurface rock and soil that is lifted to the surface by means of the circulation of drilling mud in a drilling operation and gives ownership to the person taking possession of the waste for subsequent beneficial use; limits the tort liability of the operator who transfers ownership of the drill cuttings to another person under a contract stating the operator will not be liable in tort for subsequent use of the drill cuttings.

HB 1946 Bonnen, Dennis (R) Relating to the appraisal for ad valorem tax purposes of a real property interest in oil or gas in place. Companions: SB 1985 Uresti, Carlos (Identical) Remarks: Ties the specific method for tax appraisal of the future income from the sale of oil or gas to be produced from an interest to the spot per-barrel price of West Texas Intermediate crude or the spot price of natural gas at the Henry Hub in nominal dollars per million British thermal units on specific dates as published in specific reports.

HB 2117 King, Tracy (D) Relating to the definition of "heavy equipment" for purposes of the ad valorem taxation of certain dealer's heavy equipment inventory. Remarks: Expands the definition of "heavy Equipment" for purposes of dealer's property tax to include a natural gas compressor that is leased or rented to a person at less than the prevailing market value.

HB 2207 Keffer, Jim (R) Relating to the foreclosure sale of property subject to oil or gas lease. Companions: SB 1384 Eltife, Kevin (Identical) Remarks: Chesapeake Foreclose Bill

(Legislation cont'd p. 9)
HB 2230 Larson, Lyle (R) Relating to the authority of the Texas Commission on Environmental Quality to authorize an injection well used for oil and gas waste disposal to be used for the disposal of nonhazardous brine. Remarks: TCEQ may authorize by individual permit, by general permit, or by rule a Class V injection well for the injection of nonhazardous brine from a desalination operation or nonhazardous drinking water treatment residuals into a Class II injection well that is also permitted by the railroad commission under Subchapter C.

HB 2691 King, Tracy (D) Relating to a sales and use tax exemption and an oil and gas severance tax credit for the use of alternative base fluids in energized fracturing operations. Remarks: Exempts from sale and use taxes: alternative base fluids used in fracking and tangible personal property used to process, reuse, or recycle the fluids; creates a tax credit for the use of fluids used as a substitution for water; establishes process for applying for the tax credit and penalties for false applications.

HB 2991 Paddie, Chris (R) Relating to provision of waivers from municipal regulation of mineral exploration and development activities within its boundaries. Remarks: Creates process where if there is a local setback and then development inside the setback, then there is a waiver process and that is filed in the county records to provide notice.

HB 2993 Paddie, Chris (R) Relating to the authority of a municipality to regulate location of mineral exploration and development activities within its boundaries. Remarks: Local Ordinance: If a local government establishes setbacks and then grants a waiver of the setback distance, then the distance of the waiver becomes the new uniform set back.

HB 3291 Raymond, Richard (D) Relating to the creation of the offense of theft of pipeline equipment, oil and gas equipment, oil, gas, or condensate and the unauthorized purchase or sale of oil, gas, or condensate. Remarks: Creates 2nd Degree felony if you steal these items and the value is $10,000 to $200,000. Goes to 1st degree felony if done by an employee or contractor. Creates 2nd Degree Felony if purchase or sell oil, gas or condensate without RRC registration or permits.

HB 3554 Dale, Tony (R) Relating to incentives for enhanced recovery of oil and gas. Remarks: Creates a $200,000 tax credit applied against severance taxes for the utilization of enhanced recovery techniques to increase production at a well; requires the RRC to encourage enhanced recovery, offer training, and certify qualification for the tax credit; application for the credit is made to the comptroller.
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It is a bad time to be in the renewable energy industry

2015 may go down in the books as the year support for renewable energy died. Policy adjustments—whether for electricity generation or transportation fuels—are in the works on both the state and federal levels.

About a decade ago, more than half of the states enacted strict Renewable Portfolio Standards (RPS). A few other states, agreed to voluntary targets. Now, nearly one-third of those states are reconsidering the legislation that sounded so good in a different energy era. Back then, it was widely believed that there was an energy shortage and “dealing with global warming” was a higher public priority.

“Roughly 30 bills relating to the Oklahoma wind industry have been filed in the state legislature in the 2015 session, including at least one targeting the tax breaks and others attempting to alter regulatory policies,” reports Fox News. On April 16, the Oklahoma House voted, 78-3, to eliminate the wind energy tax credit. The measure now moves to the Senate, where it is expected to pass, and will likely be headed to Governor Mary Fallin soon.

Oklahoma is just one state in what has become a new trend, but it isn’t the first state to reconsider its renewable energy policies. That distinction goes to Ohio, which in May 2014, passed legislation that paused the state’s RPS for two years. Governor John Kasich signed it in June.

Earlier this year, West Virginia became the first state to repeal its RPS.

Last month the Texas Senate voted to end its RPS and another program that, according to the Star Telegram, “helped fuel the state’s years-long surge in wind energy production.” The bill now moves to the House State Affairs Committee. It is expected to pass the House and be signed by Governor Greg Abbott.

Coming up, Kansas, North Carolina, and Michigan have legislation that revisits the states’ favorable renewable energy policies. New Mexico and Colorado had bills to repeal or revise the RPS that passed in one chamber, but not in the other.

While Louisiana doesn’t have an RPS, it does have generous tax credits for solar panel installations that have exploded the cost to the state’s taxpayers. Repealing or revising the policy is a key priority in the current legislative session.

“Taxpayer support for wind energy is also losing momentum in Congress,” says Fox News. It points out: “Capitol Hill lawmakers at the end of last year did not extend the Federal Production Tax Credit (PTC).

It is not just wind energy that has lost favor in Congress. The Ethanol mandates—known as the Renewable Fuel Standard (RFS)—are being re-examined, too.

On January 16, 2015, Senators Dianne Feinstein (D-CA) and Pat Toomey (R-PA) introduced the “Corn Ethanol Mandate Elimination Act of 2015.”

More recently, a “former Obama economic adviser” issued a report calling for changes to the 10-year-old RFS. Harvard University Professor Jim Stock served on the Council of Economic Advisers in 2013 and 2014. The Hill states: “His report comes at a time of growing angst among lawmakers, regulators and the industry over the future of the RFS, which mandates fuel refiners blend a certain volume of ethanol and biodiesel into their traditional gasoline and diesel supplies.”

Addressing growing skepticism and dwindling investment in biofuels, The Economist, on April 18, states: “Some companies, indeed, are starting to give up.”

Looking at all the policy reviews, the trend is clear. As Watchdog.org, in a report titled: “Why repealing the renewable energy mandates is good for the economy,” concludes: “The best policy for the states is to leave energy consumption decisions to consumers in the market rather than legislate them.”

The author of Energy Freedom, Marita Noon serves as the executive director for Energy Makes America Great Inc. and the companion educational organization, the Citizens’ Alliance for Responsible Energy (CARE). She hosts a weekly radio program: America’s Voice for Energy—which expands on the content of her weekly column.
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Connor McMillon Mitchell & Shennum
Certified Public Accountants & Consultants

Where more than numbers Count!

Janie Arnold
Mike Connor
Lani Hall
Gary Mitchell
Steve Shennum

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- Tax Preparation
- Tax Consulting/Planning
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- Oil & Gas Taxation

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806-373-6661
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J.D. Hand - Regional Operations Manager
Oscar Chaparro, Coy Maddox - Drilling Superintendents
Joe Hermosillo - Safety Manager

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Judy Stark - Executive V.P.
Cynthia Johnson - Office Manager

RRC District 10 Production Data
March 2014 - February 2015

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source: http://webapps.rrc.state.tx.U.S./PDQ

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