

BOARD FOR LEASE OF UNIVERSITY LANDS

RULES

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**BOARD FOR LEASE OF UNIVERSITY LANDS
RULES
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Chapter 1 General Administrative Provisions

Subchapter 1.1 Definitions

- 1.11 Defined Terms. As used in these Rules, the following terms shall have the meaning assigned in this subchapter.
- (a) "Affiliate" means a person or entity (i) that directly or indirectly controls, is controlled by, or is under common ownership or control with the Lessee or operator, specifically including parents and subsidiaries; (ii) that owns or controls at least a ten percent interest in the lessee or operator; or (iii) in which the Lessee or operator owns at least a ten percent interest.
 - (b) "Board" means the Board for Lease of University Lands.
 - (c) "Board of Regents" means the Board of Regents of The University of Texas System or its delegate.
 - (d) "BS&W" means basic sediment and water that contaminate crude oil and are separated by gravity or centrifugal force.
 - (e) "Commingling" means the combining of production from one or more reservoirs from two or more university Leases, two or more reservoirs from a single university Lease, or two or more reservoirs through the same production string. Unitized production shall not constitute commingling.
 - (f) "Completion" when used in these Rules or in oil and gas Leases with respect to continuous drilling obligations, means the "date of test" of initial potential as reported on Railroad Commission forms, or upon plugging of a well deemed incapable of production, if applicable.
 - (g) "Day" or "days" means calendar days.
 - (h) "Director" means the Executive Director or other person primarily responsible for University Lands, The University of Texas System, or his delegate.
 - (i) "Drilling operations" means the actual operation of drilling in the ground. Activities undertaken in preparation for the actual operation of drilling in the ground, such as surveying, building roads, and location preparation, shall not constitute drilling operations.
 - (j) "LACT system" means a lease automatic custody transfer system.
 - (k) "Lease" means a lease issued by the Board covering PUF Lands.
 - (l) "Lessee" means any person, other than the Board, the Board of Regents, or the State of Texas, with a working interest in any oil and gas Lease granted by the Board. Each reference to the "Lessee" in these Rules is a reference collectively to all of the Lessees under a particular Lease, whether one or more, and any persons acting on a Lessee's behalf or pursuant to rights granted under a university Lease.
 - (m) "Permanent University Fund" (or "PUF") means the fund described in Chapter 66, *Texas Education Code* and governed by Article VII, §§ 10, 11, 11a, 15, and 18 of the Texas Constitution.
 - (n) "Production in paying quantities" when used in these Rules or in oil and gas Leases, shall mean production in quantities sufficient to yield a return in excess of operating costs. Failure to sell oil or gas for a

- continuous one-hundred eighty (180) day period will create a rebuttable presumption that the production is not in paying quantities.
- (o) "PUF Lands" means lands dedicated to the Permanent University Fund.
 - (p) "RRC" shall mean and refer to the Railroad Commission of Texas.
 - (q) "RRC Lease" shall mean the well or grouping of wells assigned to a proration unit by the RRC and used for reporting purposes.
 - (r) "Special fee" means the fee payable pursuant to §66.66(g), *Texas Education Code*.
 - (s) "Reworking" means operations on an existing well to restore or reestablish production, or to enhance production. The term does not include normal maintenance of the well. In the context of the reworking provisions of an oil and gas Lease and §66.72, *Texas Education Code*, the operations must be related to the cause of cessation of production and must result in restored production.
 - (t) "Split-Out" means a subdivision of an original base Lease. For purposes of these Rules, a split-out Lease will be considered a separate Lease.
 - (u) "Staff" means personnel employed and compensated or assigned by the Board of Regents to assist the Board.
 - (v) "University Lands" means the office within The University of Texas System charged with management of PUF Lands.

Subchapter 1.2 Applicability

- 1.21 All Oil and Gas Operations on PUF Lands Covered. These Rules shall govern the activities of each and every person engaging in operations or other activities relating to exploration, drilling, or production of oil and gas on PUF Lands, including without limitation an operator under a farm-out agreement, joint operating agreement, or any other contract or agreement with the Lessee.
- 1.22 Responsible Lessee. The Lessee of record in the records of the Board of Regents at the time of the required payment, submission, notification, installation, or other activity is responsible, and liable to the Board and the Board of Regents, for assuring compliance with these Rules, relevant law, and Lease provisions. §66.76 *Texas Education Code* requires Lessees to promptly file assignments to assure that the records of the Board of Regents reflect current working interests in the Lease. The Board and the Board of Regents shall be bound by an assignment only after the date of filing of the assignment document in the records of the Board of Regents. The assignor shall be responsible and liable to the Board and the Board of Regents for performance of all of Lessee's obligations under the Lease or contract for development, including payment of all amounts due, that accrue on or before the date the assignment is properly filed in the records of the Board of Regents.

Subchapter 1.3 Organization of the Board for Lease of University Lands

- 1.31 Officers of the Board.
 - (a) Chair. The chairman of the Board shall preside over meetings of the Board and perform special administrative duties as a majority of the Board may delegate to him. In the absence of the commissioner, the

chief clerk may act as chairman of the Board pursuant to §31.015, *Texas Natural Resources Code*.

- (b) Vice Chair. At the first Board meeting following the appointment of new, Senate-confirmed regent member(s) to the Board or at the first meeting following the death, resignation, or removal of the standing vice chair of the Board, the Board shall elect a regent member to serve as vice chair for the remainder of such regent member's current term. The vice chair shall discharge the duties of the chairman in the absence of the chairman and the chief clerk of the General Land Office.
- (c) Secretary. At the first Board meeting following the appointment of new regent member(s) to the Board and at the first meeting following the death, resignation, or removal of the standing Secretary of the Board, the Board shall appoint an employee of The University of Texas System as Secretary. The Secretary serves at the will of the Board. The Secretary shall perform customary duties of a Secretary and other duties as may be expressly set out in these Rules or otherwise assigned by the Board. The Secretary may appoint an employee of The University of Texas System as Assistant Secretary. The Assistant Secretary will assist the Secretary with the Secretary's duties.

1.32 Meetings of the Board.

- (a) Time and Place. The Board shall hold regular meetings at times the Board finds necessary or appropriate. The chairman shall call a special meeting of the Board upon the request of two members of the Board or on his own motion. The date, time, and place of the meeting shall be stated in the notice or call issued for the meeting by the Secretary of the Board.
- (b) Agenda. All matters to be presented to the Board shall be referred to the Secretary. The agenda shall include all items recommended by one or more Board members, an executive officer of The University of Texas System, or the Director. The Secretary shall have charge of the agenda at all times and provide the members of the Board with a final and complete agenda at least one week prior to the meeting.
- (c) Quorum. Should a quorum of the Board not be present at the time designated for any meeting, those present may adjourn from day to day or time to time until a quorum is present.
- (d) Rules of Order. Robert's Rules of Order, when not in conflict with any of the rules and regulations of the Board, shall be the rule of parliamentary procedures when the Board is in session.
- (e) Minutes. The Secretary shall keep minutes of the meetings of the Board, which shall constitute the public record of the proceedings of the Board. The minutes may reflect only the action of the Board. The secretary shall keep and maintain documents, records, and other information pertaining to the business and proceedings of the Board in accordance with the practices and procedures, including records retention requirements, of the Board of Regents.
- (f) Certificates. The Secretary is authorized to certify actions and proceedings of the Board.

- 1.33 Rules. The Secretary shall maintain rules and policies promulgated by the Board.
- 1.34 Public Participation and Hearing. Members of the public may be recognized and heard by the Board at a meeting of the Board on an issue under the board's jurisdiction, or be heard with respect to a declaration of forfeiture, in accordance with these Rules. Persons wishing to be heard by the Board must register with the Secretary prior to the call to order of the meeting or during any recess with respect to agenda items not reached prior to such recess. The Chairman may limit the time allotted to any person to address the Board.

Subchapter 1.4 Adoption of Forms

- 1.41 Reporting Forms. The Board authorizes the Director to adopt reporting forms as may be necessary or desirable to assure the proper and efficient management of oil and gas interests in PUF Lands. However, forms for reporting and payment of royalties are authorized by the Board of Regents.
- 1.42 Lease Maintenance Forms. The Board authorizes the Director to adopt on behalf of the Board the following forms provided that any new or revised form is submitted to the Board at its next regularly scheduled meeting:
- (a) Lease Extension Application.
 - (b) Lease Extension.
 - (c) Lease Amendment Application.
 - (d) Lease Amendment.
 - (e) Any other application or certification form required by law or these Rules to be adopted by the Board.
- 1.43 Additional Forms. The Director may adopt other forms not required to be approved or adopted by the Board by law or these Rules as may be necessary or desirable to assure the proper and efficient management of oil and gas interests in PUF Lands.

Chapter 2 Oil and Gas Leases

Subchapter 2.1 Lease Sales

- 2.101 Tract Nominations. Following an action of the Board authorizing a sale by public auction, sealed bid, or a combination of the two, the Board authorizes the Director to solicit nominations for and select tracts to be offered in accordance with the lease terms and provisions and schedule approved by the Board. The solicitation shall include the latest time and date for receipt of nominations.
- 2.102 Tract Selection.
- (a) Basis for Selection. The Board, the Director, or persons interested in leasing a specific tract may nominate a tract for lease. Tract selection shall be made on the basis of tract nominations, as well as geological and other technical information relating to oil and gas exploration and development on PUF Lands.
 - (b) Tract Size. The size of tracts selected shall be in accordance with direction given by the Board. Generally, tracts shall be quarter, half, or full sections. Smaller, larger, or odd-configuration tracts may be selected when advisable and consistent with direction provided by the Board.

- (c) Multiple Leases for a Single Tract. A single Lease covering the entirety of an advertised tract will be issued unless otherwise designated by the Director and specified in the sale advertisement. The bonus paid for a tract on which two or more Leases are issued will be allocated to each Lease in the proportion that the surface acreage covered by the Lease bears to the total tract acreage.
 - (d) Oil and Gas Rights Offered Together. The oil and gas rights in each tract shall be offered together.
- 2.103 Establishing Minimum Bids and Stipulated Royalty Rates.
- (a) Minimum Bids. The minimum bid for each tract or contract for development will be set by the Director in accordance with the lease terms and conditions approved by the Board. Minimum bids shall be publicly announced prior to each sale except as provided in §2.191(c).
 - (b) Stipulated Royalty Rates. The Board authorizes the Director to stipulate the royalty rate for each tract in the notice of sale. The stipulated royalty rates must be within the parameters of acceptable royalty rates approved by the Board. The Director shall stipulate the royalty rate for each tract based on historical and current leasing activity in the area of the tract, industry interest in such area, oil and gas well drilling and completion activity in such area, historic oil and gas production from wells in such area, and general economic conditions, including oil and gas pricing data or trends.
- 2.104 Notice of Sale. The Director shall, on behalf and at the direction of the Board, cause to be published notice that the Board will receive bids for oil and gas Leases or contracts for development of oil and gas in accordance with §66.66, *Texas Education Code* and other directions, if any, provided by the Board. The Director shall also cause the notice of sale to be mailed to interested parties providing information regarding the sale including the latest time and date for submission of bids.
- 2.105 Withdrawal of Tracts. The Board authorizes the Director to withdraw any lands advertised for lease or development before the latest time set for receiving bids.
- 2.106 Bidder Qualifications. The Board may from time to time adopt a policy setting out objective criteria establishing the qualifications that a bidder must meet before a Lease will be issued to that bidder. Any policy establishing bidder qualifications shall be applicable to the next lease sale that is at least sixty (60) days after the adoption of the policy and shall remain in effect until rescinded or replaced by action of the Board.
- 2.107 Sealed Bid Procedures.
- (a) Bid Form. Each bid must be submitted on the form specified in the notice of sale. The bid form must be completed accurately and must be signed by the bidder, if the bidder is an individual, otherwise by an authorized representative or agent of the bidder.
 - (b) Payments. Each bidder must submit three (3) separate remittances for: (1) the bonus, (2) the special fee, and (3) pre-paid delay rental payment with the bid form as directed in the notice of sale. All remittances must be in good funds in United States dollars by check or money order. The Director shall ensure that proper procedures are

employed for the return of the Bonus, Pre-Paid Delay Rental Payment and Special Fee submitted by each unsuccessful bidder.

- (c) Delivery of Bids. Bids for tracts should be delivered in an envelope clearly marked "Sealed Bid – DO NOT OPEN" or other words to that effect. The date of the sale should also be clearly marked on the outside of the envelope. All bids must be delivered to the address shown in the notice of sale at or before the time and date specified in the notice of sale. The bid envelopes will be kept secure until the time and day the bids are to be opened.
- (d) Opening of Bids. The Board will determine the time and place for opening of sealed bids and staff will open sealed bids in accordance with the instructions of the Board applicable to that specific lease sale.

2.108 Public Auction Procedures.

- (a) Auctioneer. Following an action of the Board authorizing a sale by public auction, and unless the Board specifies otherwise in authorizing the sale, the Board authorizes the Director to select an auctioneer and enter into a contract for the auctioneer's services in accordance with requirements applicable to procurement of auctioning services under the law and the Regents' Rules and Regulations. The auctioneer shall be authorized to receive oral bids equal to or in excess of the minimum bid and to close the bids on each tract.
- (b) Bidding Increments. Bids will be accepted in increments of no less than \$100.
- (c) Additional Bidding Requirements and Procedures. The Board may set any additional requirements and procedures the Board finds necessary or appropriate with respect to a public auction. Additional procedures or requirements may include bidder qualification requirements, entry fees, payment requirements, and any other requirements or procedures the Board may wish to adopt.
- (d) Selection of Tracts for Oral Auction. The tracts selected for oral auction may be designated as such in the Notice of Sale, or the Director may include tracts that were offered for sale by sealed bids but were not sold due to no bids being received, or the bids received being otherwise rejected in accordance with these Rules.
- (e) Payment of Bonus, Pre-Paid Delay Rentals and Special Fee. The highest bidder shall remit to the Board of Regents immediately upon conclusion of the public auction, the full amount of the: (1) bonus, (2) special fee and (3) the pre-paid delay rental payment as specified in the notice of sale.

2.109 Acceptance of Bids.

- (a) Waiver of Irregularities. The Board may, but is not required to, waive any bidding irregularity provided that the irregularity is promptly corrected to the Board's satisfaction. *De minimus* discrepancies related to rounding errors on bonus, prepaid delay rental, and special fee checks, will not be considered irregularities.
- (b) Award of Leases and Contracts for Development. The Board shall award oil and gas Leases and contracts for development offered by sealed bid or oral auction at a meeting of the Board held within five (5) working days following the opening of bids. Unless the Board rejects

bids under §2.110, the Board will award each Lease to the qualified bidder offering the highest bid equal to or in excess of the minimum bid and on the terms adopted by the Board. Staff will thereafter prepare appropriate lease documents for execution by the chairman of the Board.

2.110 Rejection of Bids.

- (a) Generally. The Board may reject any and all bids for one or more tracts.
- (b) Minimum Bid. Any bid that does not meet the minimum royalty or bonus specified in the notice of sale will be deemed rejected.
- (c) Multiple High Bids. If the highest bid for a tract made at a sealed bid sale is made by more than one bidder, the Director may accept the withdrawal of all but one of the high bids, may reject all bids and include the tract in an oral auction at the same sale, or may withdraw the tract from the sale. If the tract is included in an oral auction at the same lease sale, the minimum bid at the auction will be the tie bid from the sealed bid sale, but in no case will the minimum bid at the auction be less than the minimum bid set in the notice of sale.

2.111 Withdrawal of Bids. Except as provided in §2.110(c), no bid may be withdrawn once submitted.

2.112 Good Funds. Any Lease awarded or issued to a bidder who has not remitted the bonus, the pre-paid delay rental payment, and special fee in good funds at the time and in the manner required by this Chapter shall, at the option of the Board, be void from its inception and of no force and effect. Alternatively, the Board may take actions, including legal action, necessary to collect the bonus, the pre-paid delay rental payment, and special fee amounts and may further elect to forfeit the Lease for failure of the bidder to make payment of amounts due thereunder.

Subchapter 2.2 Oil and Gas Leases

2.21 Form of Lease. Prior to each sale of oil and gas Leases, the Board shall approve a form of Lease, including the terms, conditions and provisions as the Board may specify, in compliance with Subchapter D, Chapter 66, *Texas Education Code* or its successor statute.

2.22 Additional Lease Terms and Provisions. Each oil and gas Lease issued by the Board shall include any additional terms and conditions adopted or approved by the Board that are not inconsistent with the law. Additional lease terms may include terms, conditions, and provisions to protect the surface of PUF Lands, to prevent damage to or waste of the surface, to restrict use of the surface to maximize the value of PUF Lands to the Permanent University Fund, and to assure that the Permanent University Fund will be protected against liabilities, losses, damages, costs and expenses that may be incurred as a result of oil and gas exploration, drilling and development on PUF Lands.

2.23 Subject to Board Rules. Each oil and gas Lease issued by the Board shall be subject to, and performance of the Lessee's obligations under the Lease shall be in conformance with, rules as adopted from time to time by the Board and Board of Regents.

2.24 Lease Amendment. On submission by the Lessee of an application in the specified form, and the payment of any applicable fee, the Director is

authorized to prepare a lease amendment, in the form adopted by the Board or on behalf of the Board, amending the oil and gas Lease as allowed by law. The lease amendment shall be executed by the chairman of the Board.

Chapter 3 Payments and Related Documents and Reports

Subchapter 3.1 Payments and Reports

- 3.101 Royalty Payments. The Lessee shall make or cause to be made royalty payments as stipulated in the oil and gas Lease. Except as specified in Subchapter 3.2, royalty payments are due on the fifth day of the second month succeeding the month of production of oil and on the fifteenth day of the second month succeeding the month of production of gas.
- 3.102 Other Payments. The Lessee shall make or cause to be made all payments other than royalty at the time and place stipulated in the oil and gas Lease.
- 3.103 Delivery Address for Royalty Payments and Other Amounts Payable to the Board of Regents. The Lessee shall deliver or cause to be delivered all royalty payments, delay rentals, deferred drilling fees, payments of annual rental, minimum payments, minimum royalty, and all other sums payable to the Board of Regents, except bonus, prepaid delay rentals, and special fee payments, to the address shown in this Section.
- (a) If delivered by United States mail, addressed to University Lands, P.O. Box 553, Midland, TX 79702-0553.
 - (b) If delivered by means other than United States mail or electronic funds transfer, addressed to University Lands, 704 W. Dengar Avenue, Midland, Texas 79705.
 - (c) If delivered by electronic funds transfer, transferred to the proper account with the Comptroller of the State of Texas.
 - (d) Notwithstanding the above, if another address is authorized in writing by the Director or is specified in rules or other written document approved by the Board of Regents, paid to that address.
- 3.104 Form of Payment. All payments shall be made in the form and manner determined by the Board of Regents and in compliance with applicable rules and regulations of the Board of Regents, if any. The purpose of the payment should be identified. The payment should be directed to a particular person only if requested by the Director. All checks and other instruments shall be made payable to the Board of Regents of The University of Texas System.
- 3.105 Due Dates for Production Documents. Unless otherwise specified in these Rules, the Lessee or Lessees of record in the records of the Board of Regents shall submit or cause to be submitted to the Board of Regents documents described in §66.77, *Texas Education Code* and true and correct copies of all documents and forms filed with the Railroad Commission on the fifth day of the second month succeeding the month of production of oil and on the fifteenth day of the second month succeeding the month of production of gas. A document that is materially incorrect will not be considered to be timely delivered.
- 3.106 Submissions to the Director. The Lessee shall deliver, or cause to be delivered, documents, contracts, applications, correspondence, and other

records as required by these Rules or the Lease to be submitted to the Director at the address specified in §3.103.

3.107 Submission of Documents, Applications, and Correspondence to University Lands. The Lessee shall deliver, or cause to be delivered, documents, contracts, applications, correspondence and other records as required by these Rules or the Lease to be submitted to University Lands at the address specified in §3.103.

3.108 Timely Receipt of Payments and Documents.

(a) Payments. A payment that is not submitted electronically shall be considered timely paid if delivered to the Director on or before the applicable due date or if deposited in a postpaid, properly addressed wrapper with a post office or official depository under the care and custody of, and postmarked by, the United States Postal Service before the applicable due date. A payment that is submitted electronically shall be considered to be timely paid if such payment is successfully transmitted to the proper account with the Comptroller on or before the due date.

(b) Documents, Reports, Notices or other Correspondence. A document, report, notice, or other correspondence that is not submitted electronically, shall be considered timely submitted or made if delivered to the Director on or before the applicable due date or if deposited in a postpaid, properly addressed wrapper with a post office or official depository under the care and custody of, and postmarked by, the United States Postal Service before the applicable due date. A document, report, notice or other correspondence that is submitted electronically shall be considered to be timely submitted or made if successfully transmitted on or before the applicable due date. Documents that are not materially correct may be returned and such documents will not be considered submitted until a materially correct version is submitted as provided herein.

3.109 Processing of Payments in the Ordinary Course of Business. All payments received by the Board of Regents on behalf of the Board shall be deposited in the ordinary course of business. No deposit of any payment shall ever be deemed to constitute acceptance of the money for the particular purpose for which it is tendered, and any money received for purposes that are not acceptable to the Board (i.e., shut-in royalty payments that are not submitted timely or are otherwise inapplicable) shall be refunded to the remitter, subject to §3.110 of these Rules.

3.110 No Refunds if Amounts Owing. The Director may withhold all refunds and/or credits due to any person owing amounts to the Board of Regents for interest, penalties, royalties, damages, or any other reason until the amounts owed are settled by payment or otherwise. The Director may also send notice to the Comptroller in accordance with §403.055, *Texas Government Code*.

3.111 Additional Information. For each production month, the Lessee shall provide information to the Director regarding whether the purchaser is an affiliate of the Lessee or operator.

3.112 Basis for Computing and Reporting Natural Gas Royalties. In keeping with the past policy of the Board and within the legal confines set out in the various Lease agreements and court settlements, the Director is authorized to

continue using the arm's length gas purchase contracts between non-affiliated parties as a basis for pricing the royalties on natural gas. Lessee shall compute and pay gas royalties due under each Lease on the basis of gross proceeds received by the seller. If the Lessee's gross proceeds reflect a deduction for production or severance taxes, or the cost of producing, gathering, storing, separating, treating, dehydrating, transporting, and otherwise making the natural gas and other products produced from the premises ready for sale or use, these deductions must be added back to gross proceeds before computing royalty due. Nothing in this subsection shall limit or waive the right of the Board of Regents to receive its royalties based on market value of the oil and gas produced, if authorized by the Lease, unit agreement, judgment, or other contract authorized by law.

- 3.113 Reporting Manual. The Lessee should consult the Reporting Manual maintained by University Lands for guidance in reporting production, payment of royalties, and submission of required documents.

Subchapter 3.2 In Kind Royalty Payments and Reports

- 3.21 Acceptance of Royalty In Kind. If oil and gas royalties due under the Lease are paid in kind at the election or request of the Board, then the delivery of the royalty oil and gas at the location determined by the Board in accordance with §66.79(e), *Texas Education Code* shall satisfy the Lessee's obligation for payment of the royalty due under the Lease.
- 3.22 Documents Required for Royalty Paid In Kind. For oil and gas royalties paid in kind at the election or request of the Board, the Lessee must submit to the Board of Regents documents required under §66.77(d)(1) and (d)(4), *Texas Education Code* on the fifth day of the second month succeeding the month of production of oil and on the fifteenth day of the second month succeeding the month of production of gas.
- 3.23 In Kind Properties. The Director shall regularly review the Take-In-Kind (TIK) program and add or delete properties as appropriate. If properties are selected to be included in the TIK program or dropped from the TIK program, the Director is authorized to give written notice to the Lessee and other interested parties on behalf of the Board. A report of the status of the TIK program will be made to the Board as warranted by changed conditions or upon request by any member of the Board.
- 3.24 In Kind Contracts. The Board authorizes the Director to take all actions reasonably necessary to contract for the sale of royalty oil and gas paid in kind in a manner that is most beneficial to the Permanent University Fund and protects the interests of the Permanent University Fund, provided that the Commissioner of the General Land Office must execute each contract for the sale of royalty paid in kind. The Board authorizes the Director to advertise the sale of royalty oil and gas paid in kind, accept bids, prepare and approve contracts on behalf of the Board, negotiate prices as necessary or appropriate, give notice of contract termination, and take other actions reasonably necessary to manage and carry out the royalty in kind program.
- 3.25 Delivery Point Election. The Board authorizes the Director to elect that delivery of royalty paid in kind be delivered at the wellhead, at the oil and gas separator, into a pipeline connected at the well, or at another location as may

be specified in the Lease or other agreement, and to give the Lessee notice of such election.

Subchapter 3.3 Penalties, Fees, and Other Amounts Payable

- 3.31 Lease Amendment Fee. The Board requires a fee in the amount of \$500 for the amendment of any Lease that does not contain the provisions mandated by §66.72, *Texas Education Code*.
- 3.32 Lease Extension Fee. If a Lease is eligible for extension, and the Lessee wishes to extend the Lease for a period of thirty days in accordance with §66.74, *Texas Education Code*, the Lessee must submit an application in the form approved by or on behalf of the Board of Regents and pay a fee in the amount of \$20.00 for each acre in the Lease for each such thirty-day extension period. The application and fee must be received by University Lands on or before the end of the primary term or the then current extension term. For purposes of these Rules, the primary term ends at midnight on the last day of the primary term of the Lease, but the application and extension fee must be received by the close of business (5:00 p.m.) on the last business day prior to the end of the primary term.
- 3.33 Assignment Filing Fee. The Director shall receive for filing in the records of the Board of Regents an assignment submitted in accordance with §66.76, *Texas Education Code* only if the document is accompanied by payment of an assignment filing fee in the amount of \$30 for each Lease or contract for development or part thereof assigned, an assignment summary in form adopted by the Board of Regents, and any applicable late filing penalty. An assignment document must be filed for recording in the county records before submission to the Director for filing. If the assignment document is not received by University Lands on or before the ninetieth day after the document is filed for record in the county records, a late filing penalty equal to the filing fee is due and payable.
- 3.34 Relinquishment. A Lessee may submit to the Director for filing in the records of the Board of Regents a relinquishment of the Lessee's interest in any Lease or contract for development, in whole or in part, at any time without payment of a fee.
- 3.35 Shut-in Royalty. The amount of the annual shut-in royalty payable in accordance with the terms of oil and gas Leases issued or amended by the Board from and after January 1, 1998, shall be an amount equal to \$1,200 per Lease.
- 3.36 Penalty for Failure to Timely File Required Documents
- (a) Penalties that Accrue Without Notice.
- (i) Forms and Documents related to royalty. A penalty in the amount of \$25 accrues and is payable immediately by the Lessee for each document not timely filed as required by §§66.77 and 66.80, *Texas Education Code*. In order to be considered filed, a document must be materially correct and in conformance with law and these Rules. Commencing on the thirty-first day after the document was required to be filed, an additional penalty of \$25 accrues and is immediately payable by the Lessee for each thirty-day period or part thereof the document remains unfiled. For purposes of this §3.36(a), a UT-3 Report relating to payments made by a single check, electronic funds

transfer, or other payment mechanism shall be considered a single document for the initial thirty-day period following the due date. Thereafter, for each thirty-day period or part thereof the UT-3 remains unfiled, a penalty shall accrue and be immediately payable in an amount equal to \$25 multiplied by the number of line items reported on the UT-3.

(ii) Penalty for Failure to File Required Forms, Reports and Logs. A penalty will be assessed in the greater of the amount provided in the governing Lease or \$25 for each form, report, supporting document, log or other required filing not timely filed as required by these Rules (other than those addressed in subparagraph (i) above), the governing Lease agreement or other official manual; or after receipt of a written request from the University Lands office requesting submission of an item of information. Commencing on the thirty-first day after the specified date an additional penalty of \$50 accrues and is immediately payable for each thirty-day period or part thereof the subject item is not filed.

(b) Unpaid Penalties After Notice. The Director may, but shall not be required to, provide notice to a Lessee that its records reflect that one or more documents required to be filed with the Board of Regents under §§66.77 and 66.80, *Texas Education Code* have not been timely filed or are materially in error. If notice is given pursuant to this §3.36(b), a penalty of one percent of the unpaid penalty amount or \$25, whichever is greater, shall accrue and be immediately payable by the Lessee if the penalty remains unpaid after the date specified in the notice for receipt of the documents. An additional penalty of one percent of the unpaid penalty amount or \$25, whichever is greater, accrues and is immediately payable by the Lessee for each thirty-day period or part thereof thereafter that the penalty remains unpaid. The penalties accruing under this §3.36(b) are in addition to penalties that accrue under §3.36(a). The date specified in the notice for receipt of the documents shall be at least fifteen days after the date the notice is deposited in the United States mail or otherwise delivered to the Lessee.

3.37 Penalty for Failure to Timely Pay. Penalties in an amount calculated in accordance with §66.78, *Texas Education Code* shall accrue and be payable with respect to any payment of royalty, annual rental, minimum payment, or minimum royalty not made on or before the applicable due date.

3.38 Penalties for Operational Violations. The Lessee shall be subject to a penalty in the amount of the greater of \$750 or \$25 for each day a violation of Chapters 4, 5, or 6 of these Rules continues after written notice to Lessee provided that the Lessee shall be given a period of thirty (30) days to correct the violation before penalties begin to accrue. Notwithstanding the foregoing, in emergency situations or where a substantial and imminent risk of harm exists, the Director may specify a shorter period within which violations must be corrected before penalties begin to accrue. In case of failure to give University Lands timely notification of the commencement of a well, no notice of violation shall be required and the penalty shall be applied immediately.

- 3.39 Reduction or Waiver of Amounts Owed. The Board, under Chapter 66, *Texas Education Code*, authorizes the Vice Chancellor and General Counsel of the University of Texas System to reduce or to waive amounts due for penalties and interest on delinquent royalties or reports when such delinquency is shown to have been clearly attributable to an Act of God, and the Lessee diligently meets its royalty and reporting requirements when able to do so. The Board further authorizes the Vice Chancellor and General Counsel of the University of Texas System to reduce or to waive amounts due for penalties and interest not to exceed \$5,000.00 if the Vice Chancellor and General Counsel (i) deems the amounts uncollectible or not cost-effective to collect or (ii) determines that the reduction, compromise, or waiver is in the best interests of the PUF. The Director shall apprise the Board of any such reduction or waiver at its next meeting.

Chapter 4 Lease Operations

Subchapter 4.1 Lease Administration

- 4.11 Suspension of Leases. If at any time the Board determines that there is a legitimate dispute regarding the validity of a Lease, the Board may elect to suspend the Lease and all of the conditions and covenants contained in the Lease in accordance with §66.74(e), *Texas Education Code*. In that event, a letter shall be sent in the name of the Board, signed by the secretary, notifying the Lessee(s) of record in the records of the Board of Regents of such suspension. The Board may rescind the suspension at any time the Board finds appropriate. Written notice of Board action to rescind the suspension of a Lease shall be sent within ten days after the action is taken by the Board.
- 4.12 Forfeiture and Reinstatement of Leases.
- (a) Forfeiture by Board Action. The Board may, at a meeting of the Board and following 21 days prior written notice to the Lessee as provided in §66.64(b), *Texas Education Code*, declare a Lease or any interest therein forfeited as allowed by law. The Board may forfeit a Lease in accordance with §66.82, *Texas Education Code* or applicable Lease provisions whether or not the party or parties currently claiming an interest in the Lease were responsible for the failure of performance or if an appropriate assignment has not been filed in the records of the Board of Regents, whether or not the party or parties currently claiming an interest in the Lease receive notice of forfeiture.
 - (b) Grounds for Forfeiture. The Board may forfeit a Lease for any failure or refusal of a Lessee to perform a material requirement of these Rules, the Lease, or Subchapter D of Chapter 66, *Texas Education Code*, as provided in §66.82(a) of such Chapter. The filing of a false or fraudulent report will constitute a failure to perform a material requirement of these Rules.
 - (c) Reinstatement. On proper showing by the affected Lessee or Lessees at the time of forfeiture, the Board may, at its discretion, authorize the reinstatement of the Lease on such terms as the Board may require.

- 4.13 Other Remedies. In case of violation by the Lessee of the Lease agreement, forfeiture is not the exclusive remedy, but the Board may, through the Attorney General, sue for damages or specific performance, or both.
- 4.14 Full Development. Lessee shall reasonably consider unitization as a means to fully develop the premises in order to enhance the production of oil and gas from a common reservoir that would not otherwise be produced by primary recovery operations only.

Subchapter 4.2 Required Approvals

4.201 Approval of Pooling and Unitization Agreements.

- (a) Application. A person seeking to pool or unitize PUF Lands must submit an application in the form specified and pay a non-refundable application fee as established under the criteria of item (c) below.
- (b) Forms. Pooling and unit agreements shall be approved by the Board. The Board may require additional provisions to be included in a pooling or unitization agreement as the Board may deem necessary for the protection of the interest of the state or the Permanent University Fund.
- (c) Authority to Approve. The Board may establish criteria for application fees and approval of pooling and unitization agreements by the Director. The Board authorizes the Director to approve on behalf of the Board pooling and unitization agreements that meet the criteria established by the Board.
- (d) Execution. Pooling and unitization agreements shall be submitted by the Director to the Commissioner of the General Land Office for his findings, approval, and execution, as required by Subchapter E, Chapter 52 and §101.051, *Texas Natural Resources Code*.

4.202 Approval of Surface Commingling. Prior to commingling oil and/or gas, installing a LACT system, or installing off-lease storage facilities for production from a university Lease, the Lessee must apply for and obtain the written approval of the Director. Lessee shall submit all information necessary for evaluation of the application, including the schematic diagrams identifying all lines, meters, equipment and the routing of the production stream. The Board authorizes the Director to approve on its behalf those applications, determined to be in the best interest of the PUF. No approval is valid or effective unless and until the applicant has received written notice of approval. Lessee must apply for and receive advance written approval of the Director for any modification or alteration of existing or previously approved facilities.

4.203 Withdrawal of Approval. An approval under this subchapter may be withdrawn by the Director or the Board at any time should a determination be made that:

(a) the Lessee has not installed or maintained the system in compliance with the approved application;

(b) the Lessee has discontinued or ceased to use an approved system or operation;

(c) a field inspection identifies inadequacies in the system;

(d) the Lessee has not otherwise complied with the requirements and provisions of these Rules; or

- (e) continuation of the approval is not in the best interest of the Permanent University Fund.
- 4.204 Expiration of Approval. If an activity approved under this subchapter has not commenced within six months after the date of the approval of the Director the approval shall terminate and be of no further force and effect.
- 4.205 Cessation of Operation of an Approved System. The Lessee shall notify the Director within thirty days after the discontinuance of any activity approved under this subchapter.
- 4.206 Off-Lease Storage. The Lessee may make application for approval of off-lease storage if storage of production on the Lease is uneconomic or impractical due to adverse terrain or other unusual adverse conditions. As a condition of approval of off-lease storage, the Director requires that all such off-lease storage facilities be subject to field inspections in accordance with Subchapter 6.1, including the right to require witnessed tests on wells connected to such off-lease facility. A surface lease and/or appropriate easements will be required. Unless authority to commingle is also granted by University Lands as provided in these Rules, separate meters or other approved measuring methods must be employed if wells from different Leases are included in the same facility.
- 4.207 Facilities and Lines. Installations shall be permanent, durable, and stable. Lessee must have identifying information including operator name, the Lease name, and well number stenciled or otherwise permanently marked on all installations. The flow lines, manifolds, vessels, meters and associated equipment must be marked so that the fluid flow can be properly identified.
- 4.208 Produced Water. Lessee shall obtain written approval from the Director to inject or dispose of produced water from any university Leases into subsurface formations, except unitized intervals within unitized Leases.
- 4.209 Inactive or Temporarily Abandoned Wells. Wells which are not actively being used to produce the Lease will be considered surplus. Wells which are not being produced will be subject to a production test at the request of the Director. Additionally, all equipment which is not actively being used to produce the Lease must be removed from PUF Lands. Inactive wells must be plugged as provided by applicable law. For purposes of these Rules, "inactive well" shall have the meaning given by §89.002(a)(11), *Texas Natural Resources Code*.
- 4.210 Surface Commingle Rules.
- (a) The Board authorizes the Director to approve on its behalf applications for commingling. Commingling must be approved before any commingling of production occurs. Commingling prior to approval by the Director, including adding new Leases to an approved commingling permission without prior approval, will be considered a violation of all Leases involved in the commingle and subject all of the Leases involved to forfeiture by the Board. Notwithstanding the granting of approval by the RRC, University Lands approval is independently required.
- (b) Applications shall include the following:
1. University Lease numbers
 2. RRC lease numbers (if available)
 3. Lease names and well numbers
 4. County, Block, Section, and part held by production in each Lease

5. Royalty rate of each Lease. Ordinarily, all commingled Leases should bear the same royalty rate.
6. Name of fields in which production is currently being reported
7. Name of field in which commingled production will be reported
8. Proposed method of testing
9. An initial plat or schematic of all facilities (flow lines, tankage, separation, headers, compression, and metering with latitude and longitude for each commingled battery.)
10. Copies of all RRC required documentation.

(c) Construction of Facilities.

1. All facilities must be constructed to industry standard.
2. Facilities shall be constructed with separate flow lines in a manner that provides the ability to test each well on each University Lease included in the commingle battery.
3. Production from each well shall enter by way of a header in which each Lease is clearly identified at the entry valve.
4. Header shall be constructed in such a manner that will allow each Lease to be isolated for testing purposes.
5. Satellite batteries are permitted.
6. Lessee must provide an as-built plat, including flow lines, tankage, separation, headers, compression, and metering with latitude and longitude for each commingled battery
7. Final approval of Director must be obtained before commingling may proceed.

(d) Testing Requirements.

1. Well tests will be performed on each well within an approved commingled Lease on at least an annual basis.
2. University Lands reserves the right to require well tests upon written notification.
3. Results of well tests shall be filed with University Lands within fifteen (15) days after testing or as approved in writing by the Director.

Subchapter 4.3 Required Reporting.

- 4.31 Well Location. Prior to commencement of drilling on PUF Lands, Lessee shall provide written notice to Lessor of Lessee's intent to drill a well, together with a plat of the premises showing the location of each well to be drilled. Prior to commencement of any surface preparation in connection with a drill site or the construction of a road to a drill site, Lessee shall obtain any necessary easements, pay amounts required under the then current Rate and Damage Schedule, and give notice to University Lands and the surface occupant.
- 4.32 Railroad Commission Forms. Copies of all forms and other information filed with the Railroad Commission pertaining to operations under a Lease shall be filed simultaneously by Lessee with University Lands. Lessee shall submit copies of correspondence and other information received by Lessee from the Railroad Commission to University Lands within ten (10) days after receipt by Lessee, the operator, or other contractor or agent of Lessee.
- 4.33 Logs. Lessee shall have an electric or radioactivity survey made of the bore-hole section, from the total depth of the well to the surface of the ground, as

required in the applicable Lease of all wells drilled on the Premises and shall provide a copy of each and every log of each required survey, along with copies of logs of all other bore-hole surveys completed with respect to the well, to University Lands within fifteen (15) days after the making of the survey.

- 4.34 Daily Gauge Reports. Lessee shall ensure that daily gauge reports relating to production of oil from PUF Lands accurately reflect actual stock on hand at the opening of business on the first day of the calendar month, actual stock on hand at the close of business on the last day of the calendar month, and actual gross production during the calendar month. All gauge reports shall show actual measurements in accordance with standard industry practice and the University Lands Operations Manual. Daily gauge reports must be in agreement with production reported for royalty compliance. Lessee shall maintain reports showing the monthly volume of injected gas-lift gas and power oil delivered to each Lease and producing reservoir.

Chapter 5 Measurement of Production

Subchapter 5.1 Measurement of Production

- 5.11 Oil Measurement. All measurements of oil production shall represent one hundred percent volume, consisting of United States barrels of forty-two gallons each, the quantity and gravity of which will be adjusted to sixty degrees Fahrenheit temperature. Procedures for measuring and testing shall be computed in accordance with applicable industry-standard methods for the meter in use. All hydrocarbons lost by spillage shall be reported to the University and shall be considered royalty bearing. Deduction shall be made for BS&W content according to the ASTM Standard Method then in effect. Upon request, buyer will provide advance notice to the Director and allow his representative to be present during any measuring and testing.

- 5.12 Gas Measurement.
- (a) Metering Required. Except as otherwise specifically provided in these Rules, all gas produced from wells on PUF Lands must be measured by regularly calibrated orifice metering equipment. Gas wells must be metered on an individual basis prior to the gas leaving the University Lease. Casinghead gas from oil wells on the same Lease may be combined into a production facility prior to being metered.
 - (b) Metering Equipment Installation and Calibration. Lessee shall take all actions reasonably necessary to assure that all metering devices and meter tubes shall be designed to measure and calculate gas volumes according to the current standards prescribed in the American Gas Association (AGA) Report No. 3, Orifice Metering of Natural Gas and Other Hydrocarbon Fluids, Parts 1-4 and 1992 AGA 8 (as amended from time to time). Meters will be calibrated not less often than every six (6) months and immediately following any maintenance. The measurement and tests for quantity and quality of gas will be made at the delivery point(s).
 - (c) Notifications of Calibration Events. Lessee will provide advance notice to the Director and allow a representative to be present during any measuring or testing. The Lessee shall have a witness at each

calibration event. The Lessee shall ensure that the most recent meter calibration and sampling results are posted at the meter location including, at a minimum, the following information:

1. calibration date;
2. name of person performing calibration;
3. name of person witnessing calibration;
4. orifice size;
5. date of orifice change; and
6. gas analysis date.

Failure to post this information may result in penalties under these Rules.

- (d) Gas Processing Contracts. Contracts governing residue and liquids processed at a gas processing plant must contain specific language allowing the audit of the gas stream including the residue meter and liquids meter at the tailgate of the gas processing plant and the related allocation schedules.
 - (e) Gas Sampling. Lessee shall take all actions reasonably necessary to assure that gas sampling is done in accordance with Gas Processors Association (G.P.A.) 2166, or its successor, to ensure gas collected in the sample container is representative of the gas flowing in the pipeline. Sampling should be completed at least once in any six-month period and immediately following any maintenance that may affect the heating value and liquid hydrocarbon content of the natural gas. Locations where gas heating value fluctuates should be sampled more frequently. In no case shall the sampling interval exceed that provided for in the gas purchasing agreement for that well. The Director may require that gas reporting be by volume or energy content, in his discretion.
- 5.13 Verification. The Lessee shall develop and perform systematic procedures to verify the accuracy of all oil and gas sales volumes which are determined by the purchaser. Upon request, the Lessee shall be required to demonstrate the procedures which are used to verify that all sales volumes reported are accurate. Failure to develop and demonstrate the required procedures may result in forfeiture of the Lease or other penalties as described in §3.38.
- 5.14 Records. Records documenting measurement activities shall be retained and made available upon request including, but not limited to, the following:
- (a) Oil Measurement Records
 1. Tank Gauge Records
 2. LACT Meter Calibration Records
 3. Oil Sales Run Ticket Records
 4. Monthly Purchase Statement Records
 - (b) Gas Measurement Records
 1. Gas Meter Calibration Records
 2. Gas Analysis Records
 3. Monthly Volume Statement Records
 - (a) Unedited
 - (b) Edited
 4. Monthly Purchase Statement Records

- 5. Electronic Flow Meter Data
- 6. Event Logs
- 5.15 Gross Production. Lessee shall take all reasonable actions necessary to prevent waste in any manner of oil or gas and pay to the Board of Regents a royalty at the rate specified in the Lease on any wasted oil or gas. All gas lost, vented, flared or used on the Lease shall be reported to University Lands and shall be considered royalty bearing unless otherwise specified in the Lease.
- 5.16 Gas-Lift Gas and Power Oil. Lessee shall measure accurately any injected gas-lift gas and power oil delivered to each Lease and producing reservoir and install all reasonably necessary meters and accessory equipment for that purpose.
- 5.17 Bypass Connections Prohibited. Lessee shall not install, maintain, or use bypass connections around meters and accessory equipment installed in accordance with these Rules.
- 5.18 Lease Automatic Custody Transfer (LACT) Systems.
 - (a) Applicable Standards. LACT systems shall conform to the A.P.I. Manual of Petroleum Measurement Standards, Chapters 4, 5 and 8, A.P.I. Bulletin 11 N, and other standards generally accepted in the industry.
 - (b) Meter Calibration. Lessee shall test-calibrate each meter as necessary to assure reliability and at least once in any ninety-day period, and at any other time requested by the Director. Records documenting measurement activities shall be retained and made available upon request including, but not limited to, the following:
 - 1. the date the meter was calibrated;
 - 2. the totalizer reading obtained at the time the meter was calibrated;
 - 3. the serial number of the meter being calibrated (when a LACT meter is replaced, the serial number of the meter being replaced and the serial number of the new meter must both be shown on the calibration report. For example, Meter Serial No. 188039 replaces Meter Serial No. 243496); and
 - 4. the University Lease number(s) and RRC lease number(s) associated with the meter.

Chapter 6 Operational Compliance

Subchapter 6.1 Field Inspections

- 6.11 Generally. Any system facility, activity or operation on PUF Lands is subject to field inspection at any reasonable time.
- 6.12 Installations. Prior to commencement of construction of a proposed facility or system, Lessee shall obtain the approval of the Director for such installation. A field inspection may include a review of any and all systems and accessory equipment to assure that:
 - (a) the system conforms to the approved application;
 - (b) the system is properly installed;
 - (c) the arrangement of lines, separator, and other equipment is appropriate;

- (d) all parts of the system are permanent and not temporary in nature; and
 - (e) all parts of the system are properly identified and marked.
- 6.13 Correction of Deficiencies. Lessee will immediately correct any deficiencies identified in the course of a field inspection. If deficiencies are not timely corrected, any applicable approval is subject to withdrawal. Deficiencies may be reported to the appropriate governmental agencies with jurisdiction.
- 6.14 Witnessed Tests. Demand may be made that the Lessee or operator, at the Lessee or operator's expense, conduct a witnessed test of any well, Lease, or equipment on PUF Lands at any reasonable time.

Subchapter 6.2 Environmental Compliance

- 6.21 Applicability. All Lessees having operations on PUF Lands shall comply with the environmental regulations of the state and federal government or as required by University Lands.
- 6.22 Notification. Lessees shall provide documented notification of any activity impacting the environment, including but not limited to: surface, subsurface, and atmospheric releases of hydrocarbon liquids, produced water, natural gas, or any material transported on the land which is associated with the exploration and production of minerals from the land.
- 6.23 Remediation. All environmental impacts which adversely affect the surface, subsurface or atmosphere of PUF Lands shall be reported to University Lands and remediated as prescribed by the Texas Railroad Commission and/or the Texas Commission on Environmental Quality. The Director shall receive copies of all correspondence between the Lessee and these agencies or their successor agency, and may require remedial efforts in addition to those prescribed by the Texas Railroad Commission and/or the Texas Commission on Environmental Quality.
- 6.24 Due Diligence. Upon request, Lessee shall perform tests to demonstrate and document environmental compliance on the Lessee's oil and gas Lease. Confirmation of non-compliant environmental conditions will require remediation by the Lessee.

Subchapter 6.3 Operations Manual.

The Lessee shall consult the *Field Manual of Required Operating Procedures for Oil and Gas Leases* maintained by University Lands for guidance in compliance with these Rules. This manual is available from the University Lands office or available on the internet at:

<http://www.utlands.utsystem.edu/forms/pdfs/FieldManual.pdf>

Subchapter 6.4 Water Wells & Water Usage

- 6.41 Permission. Lessees must obtain permission from University Lands before drilling a water well or using an existing water well for any purpose. Consideration for water used for drilling and completion activities is described in the University Lands Rate & Damage Schedule published at: http://www.utlands.utsystem.edu/forms/pdfs/Rate_Damage_Schedule.pdf
- 6.42 Removal of Facilities. Upon request by University Lands, the Lessee will plug water wells located on the oil and gas Lease that the Lessee has utilized regardless of the origin of such well. Temporary pipelines used to transport water from the well shall be removed when no longer required for on-going operations. All drilling and plugging activity will be performed by a water well driller licensed by the Texas Department of Licensing and Regulation (TDLR).

- 6.43 Logs. The Driller's Log or Plugging Report shall be provided to University Lands within fifteen (15) days of water well installation.
- 6.44 Identification of Facilities. No later than fifteen (15) days after installation of a water well, an identification plate constructed of a non-ferrous material shall be permanently posted on a component of the water well's surface infrastructure. The identification plate will be permanently marked, i.e. stamped or engraved, to show:
1. name of company or individual that caused the water well to be installed
 2. name and TDLR license number of company that installed the water well
 3. installation date
 4. total depth
 5. well capacity (gallons per minute)
 6. latitude and longitude of the well