

TEXAS PACIFIC LAND TRUST
Form 10-Q
November 07, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended September 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the transition period from _____ to _____

Commission File Number: 1-737

Texas Pacific Land Trust

(Exact Name of Registrant as Specified in Its Charter)

NOT APPLICABLE 75-0279735
(State or Other Jurisdiction of Incorporation (I.R.S. Employer
or Organization) Identification No.)

1700 Pacific Avenue, Suite 2770, Dallas, Texas 75201
(Address of Principal Executive Offices) (Zip Code)
(214) 969-5530
(Registrant's Telephone Number, Including Area Code)

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of October 31, 2018, the Registrant had 7,774,394 Sub-share Certificates outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

TEXAS PACIFIC LAND TRUST
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (in thousands, except acres, shares and per share amounts)

	September 30, 2018	December 31, 2017
	(Unaudited)	
ASSETS		
Cash and cash equivalents	\$ 110,617	\$ 79,580
Accrued receivables	39,615	17,773
Other assets	7,702	849
Prepaid income taxes	—	1,202
Property, plant and equipment, net of accumulated depreciation of \$1,952 and \$463 as of September 30, 2018 and December 31, 2017, respectively	57,989	19,516
Real estate acquired	3,778	1,115
Real estate and royalty interests assigned through the 1888 Declaration of Trust, no value assigned:		
Land (surface rights) situated in eighteen counties in Texas – 877,467 acres and 877,633 acres as of September 30, 2018 and December 31, 2017, respectively	—	—
1/16th nonparticipating perpetual royalty interest in 373,777 acres	—	—
1/128th nonparticipating perpetual royalty interest in 85,414 acres	—	—
Total assets	\$ 219,701	\$ 120,035
LIABILITIES AND CAPITAL		
Accounts payable and accrued expenses	\$ 8,884	\$ 5,608
Income taxes payable	3,059	851
Deferred taxes payable	114	114
Unearned revenue	12,604	8,364
Total liabilities	24,661	14,937
Commitments and contingencies	—	—
Capital:		
Certificates of Proprietary Interest, par value \$100 each; none outstanding	—	—
Sub-share Certificates in Certificates of Proprietary Interest, par value \$.03 1/3 each; outstanding 7,781,831 and 7,821,599 Sub-share Certificates as of September 30, 2018 and December 31, 2017, respectively	—	—
Accumulated other comprehensive loss	(765) (804
Net proceeds from all sources	195,805	105,902
Total capital	195,040	105,098
Total liabilities and capital	\$ 219,701	\$ 120,035

See accompanying notes to condensed consolidated financial statements.

TEXAS PACIFIC LAND TRUST

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND TOTAL COMPREHENSIVE INCOME

(in thousands, except shares and per share amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Income:				
Oil and gas royalties	\$31,253	\$ 20,481	\$88,078	\$ 43,252
Easements and sundry income	22,068	23,454	66,845	51,247
Water sales and royalties	18,178	7,917	47,428	19,584
Land sales	1,543	—	4,293	220
Other operating income	126	125	375	374
Total income	73,168	51,977	207,019	114,677
Expenses:				
Salaries and related employee benefits	3,703	671	9,548	1,637
Water service-related expenses	3,707	201	7,601	211
General and administrative expenses	1,405	511	3,390	1,122
Legal and professional fees	556	1,011	1,623	2,630
Depreciation and amortization	706	209	1,519	313
Taxes, other than income taxes	130	66	387	183
Trustees' compensation	2	2	6	6
Total expenses	10,209	2,671	24,074	6,102
Operating income	62,959	49,306	182,945	108,575
Other income	236	18	526	31
Income before income taxes	63,195	49,324	183,471	108,606
Income taxes	12,433	16,322	36,415	35,995
Net income	\$50,762	\$ 33,002	\$ 147,056	\$ 72,611
Other comprehensive income — periodic pension costs, net of income taxes of \$3, \$9, \$10, and \$28, respectively	13	17	39	52
Total comprehensive income	\$50,775	\$ 33,019	\$ 147,095	\$ 72,663
Weighted average number of Sub-share Certificates outstanding	7,786,697	7,851,916	7,797,262	7,872,554
Net income per Sub-share Certificate — basic and diluted	\$6.52	\$ 4.20	\$18.86	\$ 9.22
Cash dividends per Sub-share Certificate	\$—	\$—	\$4.05	\$ 1.35

See accompanying notes to condensed consolidated financial statements.

TEXAS PACIFIC LAND TRUST
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$147,056	\$72,611
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred taxes	—	(337)
Depreciation and amortization	1,519	313
Gain on disposal of fixed assets	(2)	(4)
Changes in operating assets and liabilities:		
Accrued receivables and other assets	(28,704)	(17,040)
Prepaid income taxes	1,202	—
Accounts payable, accrued expenses and other liabilities	7,555	5,067
Income taxes payable	2,208	5,249
Cash provided by operating activities	130,834	65,859
Cash flows from investing activities:		
Proceeds from sale of fixed assets	25	28
Acquisition of land	(2,663)	—
Purchase of fixed assets	(40,006)	(7,970)
Cash used in investing activities	(42,644)	(7,942)
Cash flows from financing activities:		
Purchase of Sub-share Certificates in Certificates of Proprietary Interest	(25,501)	(27,158)
Dividends paid	(31,652)	(10,681)
Cash used in financing activities	(57,153)	(37,839)
Net increase in cash and cash equivalents	31,037	20,078
Cash and cash equivalents, beginning of period	79,580	49,418
Cash and cash equivalents, end of period	\$110,617	\$69,496
Supplemental disclosure of cash flow information:		
Income taxes paid	\$34,251	\$31,102

See accompanying notes to condensed consolidated financial statements.

TEXAS PACIFIC LAND TRUST
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Organization and Description of Business Segments

Texas Pacific Land Trust (which, together with its subsidiaries as the context requires, may be referred to as “Texas Pacific”, the “Trust”, “our”, “we” or “us”) is one of the largest landowners in the State of Texas with approximately 890,000 acres of land in West Texas. Texas Pacific was organized under a Declaration of Trust, dated February 1, 1888, to receive and hold title to extensive tracts of land in the State of Texas, previously the property of the Texas and Pacific Railway Company, and to issue transferable Certificates of Proprietary Interest pro rata to the original holders of certain debt securities of the Texas and Pacific Railway Company.

The Trust is organized to manage land, including royalty interests, for the benefit of its owners. The Trust’s income is derived primarily from oil, gas and water service-related royalties, sales of water and land, easements and leases of the land.

We operate our business in two segments: Land and Resource Management and Water Service and Operations. Our segments provide management with a comprehensive financial view of our key businesses. The segments enable the alignment of strategies and objectives of the Trust and provide a framework for timely and rational allocation of resources within businesses. See Note 8, “Business Segment Reporting” for further information regarding our segments.

2. Summary of Significant Accounting Policies

Interim Unaudited Financial Information

The results for the interim periods shown in this report are not necessarily indicative of future financial results. The accompanying condensed consolidated financial statements include all adjustments necessary to present fairly the financial position of the Trust as of September 30, 2018 and the results of its operations for the three and nine months ended September 30, 2018 and 2017, respectively, and its cash flows for the nine months ended September 30, 2018 and 2017, respectively. Such adjustments are of a normal recurring nature.

Principles of Consolidation and Basis of Presentation

The accompanying condensed consolidated financial statements include our accounts and the accounts of our wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. The accompanying condensed consolidated financial statements should be read in conjunction with the annual financial statements and notes thereto included in the Trust’s Annual Report on Form 10-K for the year ended December 31, 2017, which was filed with the SEC on February 28, 2018. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted from this report.

Use of Estimates in the Preparation of Financial Statements

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent asset and liabilities at the date of the financial statements and reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Recently Adopted Accounting Guidance

Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, “Revenue Recognition (Topic 606): Revenue from Contracts with Customers.” The ASU provides a five-step revenue recognition model in which an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU allows for a practical expedient for companies to exclude sales or similar taxes collected from customers from the transaction

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price. Additionally, the ASU requires disclosures sufficient to enable users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers, including qualitative and quantitative disclosures about contracts with customers, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract.

The most significant impact of the new standard relates to our accounting for easement agreements and to a lesser extent oil and gas royalties. Specifically, we recognize revenue for term easements upon execution of the easement agreements, and as a result, we no longer defer revenue on our term easements. Historically, oil and gas royalties have been adjusted for production taxes paid by operators with a charge to taxes, other than income taxes and a corresponding increase to revenue. We elected the practical expedient allowed by the ASU and exclude production taxes from revenue. Revenue recognition related to our land sales and other sundry income remains substantially unchanged. Adoption of the standard resulted in (i) the acceleration of easement and sundry income as unearned revenue decreased, (ii) a reduction in oil and gas royalty revenue with a corresponding reduction in taxes, other than income taxes, and (iii) an increase in income tax expense for the three and nine months ended September 30, 2017. We adopted the new standard on January 1, 2018 applying the full retrospective method with optional practical expedients. Adoption of the standard using the full retrospective method required us to restate certain previously reported results as though the new standard had always been in effect.

Adoption of the standard related to revenue recognition impacted our previously reported results as follows (in thousands, except per share amounts):

	As reported in prior year	Retrospective Adjustment	As reported in current year
Condensed Consolidated Statements of Income:			
For the three months ended September 30, 2017			
Revenue	\$42,476	\$ 9,501	\$51,977
Taxes, other than income taxes	797	(731)	66