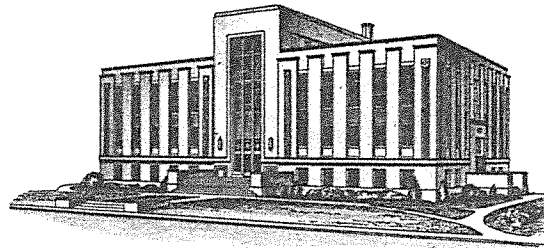
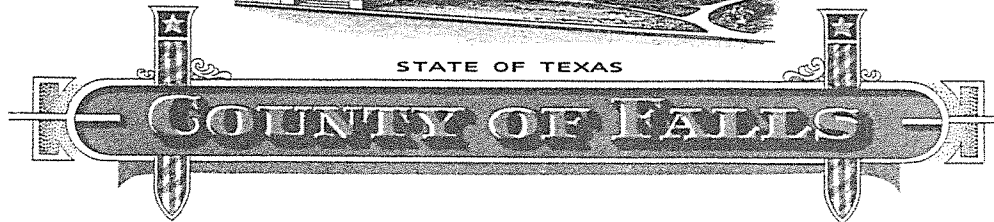


Jay T. Elliott
COUNTY JUDGE



FALLS COUNTY COURTHOUSE
P.O. BOX 458
(254) 883-1426
FAX (254) 883-1408



MARLIN, TEXAS
76661

Rosebud-Lott I.S.D.
P.O. 638
Rosebud, Texas 76570

FALLS COUNTY COURTHOUSE
P.O. BOX 458
(254) 883-1426
FAX (254) 883-1408

April 1, 2015

Re: Falls County School Lands

Dear Rosebud-Lott I.S.D.:

As you are aware, Falls County holds certain land in Archer County, Texas that was granted to Falls County for the benefit of school children living in Falls County. The County is currently considering a change to the current structure of the way that certain additional royalties with regard to oil and gas production from the property are handled.

Factual Background.

On April 19, 1994, Falls County, Texas, acting by and through its Commissioners Court and County Judge, as Lessor, executed a certain Oil & Gas Lease to Bob Craig, Robert Alan Craig and Carl L. Craig, as Lessees, covering Lessors undivided one-half (1/2) mineral interest in certain tracts of land in Archer County, Texas, described therein; said Oil and Gas Lease duly recorded in Volume 537, Page 879, of the Deed Records of Archer County, Texas, to which reference is made for purposes. ("The 1994 Oil and Gas Lease"). (Paragraph 4(a) of the 1994 Oil and Gas Lease provides for a royalty on oil and gas produced, saved and marketed from said lands equal to $1/8 \times 8/8$ ths of production proportionately reduced by any outstanding mineral interest not owned by Lessor. Paragraph 4(h) of the 1994 Oil and Gas Lease provides that should average posted price for sales of oil in District 9 of the Texas Railroad Commission exceed \$22.00 per barrel of oil, Lessor is entitled to an additional royalty from Lessees in the form of an annual payment due on or before March 1 of the next succeeding calendar year for sales of oil in the preceding year.

Paragraph 4(h)iii of the 1994 Oil and Gas Lease provides that should said average posted price for District 9 of the Texas Railroad Commission exceed \$30.00 per barrel of oil, the additional royalty to be paid on an annual basis would be equal to 7.50% of production in proportion to Lessors mineral ownership. Under this provision, Lessor is currently receiving an additional royalty of 3.75% of production annually from Craig, and was paid its additional royalty for the calendar year of 2012 on or before March 1, 2013.

By Assignment, Conveyance and Bill of Sale dated January 13, 2011, Carl L. Craig, Robert Alan Craig and Randy Turner, successors in interest to Bob Craig, assigned 100% of the working interest in the subject property to Banner Oil & Gas, LLC, but reserved an overriding royalty interest equal to 3.75% of production in satisfaction of the terms of said 1994 Oil and Gas Lease executed by Falls County, Texas. Carl L. Craig ("Craig") currently holds title to such overriding royalty interest as "Carl L. Craig, f/a/o Falls County, Texas," and receives payment monthly for this overriding royalty interest from Phillips 66 Company. Craig is legally obligated to pay to Falls County, Texas, annually for such additional royalty in satisfaction of Paragraph 4(h) of the said 1994 Oil and Gas Lease.

In the event the average posted price for sales of oil in District 9 of the Texas Railroad Commission should fall below \$30.00 per barrel, the additional payment of royalty to Falls County, Texas, would be reduced and would become payable to Craig under Paragraph 4(i), (ii) and (iii) of the said 1994 Oil and Gas Lease. That is, on the sliding scale, once the price averages below \$30.00 per barrel, Craig's share increases and the County's share decreases.

Proposed Change.

Entry into a Stipulation of Interest and Assignment of Overriding Royalty Interest with Carl Craig which gives Falls County a 3.5% ownership interest in the additional royalties, locks-in the parties' respective entitlement to additional royalties, and provides for additional royalties to be paid on the same basis as the Base Royalty (monthly) instead of in the succeeding year for the whole of the previous year.

Pros of Proposed Change.

- It makes the additional royalties payable concurrent with base royalty, on a monthly basis, instead of having to wait until the next year to be paid for additional royalties generated in the previous year. Furthermore, it simplifies administration.
- It creates more stability by solving concerns as to what complications might arise if Mr. Craig dies, becomes bankrupt, etc.
- It locks in the respective share of additional royalties. As it currently stands, if oil ever fell below a \$30.00 per barrel average, Mr. Craig's take would increase while the County's share would decrease. At this point it might be difficult to envision oil going below \$30.00 per barrel again; however, over the long-term it could.¹ For example, as alternative fuels are pushed and regulations to increase mileage and address environmental concerns come into play, the demand for oil (and domestic production) could decrease. Under the proposed arrangement, if any additional royalties are paid—the respective percentages are locked-in, regardless of the price.

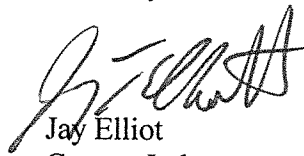
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¹ Oil posted prices in the applicable district have fluctuated and there is concern that prices could go below \$40.00 per barrel or lower in the near future. Of course, in the short-term the price may jump back up. Long-term fluctuation/trending is the risk factor that would be mitigated by the change.

- Giving up $\frac{1}{4}$ of a percent (going from 3.75% to 3.50%)

Looking from a long-range perspective I believe that this change is beneficial overall and intend to recommend its approval to the Commissioners Court. The purpose of this letter is to notify each of the school districts of the proposed change and to explain it. The proposed change will be considered at the Commissioners Court meeting to be held on April 27, 2015. If you have any objections to this proposed change I would appreciate being informed of them before that date. An objection will not necessarily prevent the proposed change from being approved, but it will be considered as part of the process of considering the proposed change.

Sincerely,



Jay Elliot
County Judge