

SWKROA

SOUTHWEST KANSAS ROYALTY OWNERS ASSOCIATION

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Testimony before the Senate Utilities Committee House Bill 2673 February 13, 2006

Chairman Emler and Members of the Committee:

My name is Erick Nordling, of Hugoton, Kansas. I am an attorney and have spent my legal career representing landowners. I am also the Executive Secretary of the Southwest Kansas Royalty Owners Association, a voluntary association with over 2,600 members who own mineral and royalty interests in the Hugoton Gas Field area. I am a royalty owner too. I am appearing on behalf of the members of SWKROA and on behalf of other Kansas royalty owners to urge your support for the passage of House Bill 2673.

Intro and Background.

K.S.A. 55-1620 regulates basic information to be reported to a royalty owner on the 'check stub' which accompanies a payment for proceeds attributable to oil or gas production. K.S.A. 55-1622 provides that a royalty owner may write to the payor and request additional information.

The oil and gas industry is an extremely complex and dynamic industry. There are literally hundreds of companies paying royalties on oil and gas production. Often, a lessee of the oil and gas lease may have contracted with a third party to pay the royalty owners. The accounting methodology and format of information reported on a check stub can vary significantly from payor to payor.

Royalty owners have requested revisions to these statutes to address a number of issues relating to these payments for oil and gas production. They desire an easy to understand statement, which provides clear, transparent, and consistent information from one payor to another payor. They also desired expansion of the information required by statute to be available upon request, and for an enforcement provision for payors who failed to provide the required information.

The check stub task force created by House Resolution No. 6024 worked hard to try and address these concerns.

House Bill No. 2673

H.B. 2673 is the result of the efforts of the check stub task force. I would like to provide an overview of the key elements of the bill.

Information Reported on Check Stub. First, it is important to note that as part of the compromise with industry, H.B. 2673 does not change the current provisions of K.S.A. 55-1620. So the basic information reported on a royalty payment check stub remains unchanged.

Royalty owners acknowledge that producers have a strong reluctance to change the basic information to be reported on the check stub. Royalty owners still believe changes are needed to provide more transparent, uniform payment information on the face of a check stub. However, due to the complexities of the industry, continued dialogue with industry is needed to see if we are able to voluntarily reach an accord on how to address these concerns. As a result of the compromise for H.B. 2673, royalty owners have agreed that revisions for the check stub will be an issue reserved for some future legislative sessions.

Information upon request - Section 1 of H.B. 2673.

Section one of H.B. 2673 makes revisions to K.S.A. 55-1622. Section one maintains the provision for a royalty owner to send a written request, by certified mail, for additional information regarding royalty payments. Sub-sections(a)(1, 2, and 3) provide the royalty owner with additional information to identify the land and formation from which the oil and gas was produced, and to be able to use identification numbers used by state agencies and industry groups to relate the payments to specific wells or units. This could help a royalty owner to track production better, and to aid in 'verifying' production information with the information reported to state agencies.

Sub-section (a)(4) can help an owner to verify production volumes vs. sales volumes for a given sales period. The sales period was utilized in this sub-section (rather than a production period) to address concerns of industry that the timing of a sale may not strictly follow the date of production. This is especially true for oil production, since the oil is only picked up for sale when the on-site storage tanks become full.

Sub-section (a)(5) would help to reveal any deductions or adjustments not detailed on the check stub.

Sub-section (a)(6) defines split stream sales. Discussions during task force meetings revealed that some companies which utilize the practice of a split stream sale, account to their royalty owners on different bases. A split stream sale is where there may be two or more companies which share in the production from a given well or unit, but they independently market their share of the production, and independently account to royalty owners. The proposed bill would make it much easier to discover the accounting methods used by each payor to determine if the royalty owner has been paid for their share of all of the production for a given period.

Sub-section (a)(7) helps to reveal if a sale is made to an affiliate of the payor. Then an owner could make further inquiry to determine if the sale to the affiliate is an 'arms length' transaction.

Sub-section (b) maintains a provision for a payor to provide a written response within 60 days from receipt of a request for information. It also contains several exceptions when a payor could decline to respond in certain instances.

Sub-section (c) is a new provision which helps to link the royalty owner with their lessee of the oil and gas lease or operator of the production unit. Many third party payors may not have some information about the leasehold interest. If the payor doesn't have the information, then they would need to provide the royalty owner with contact information for the seller of production. This tie to the seller of production continues in the enforcement provision under new Section 3.

Annual Notice Provision - New Section 2.

The annual notice provision, loosely patterned after the Texas provision, alerts royalty owners that they have the right to request additional information regarding their royalty payments. The section essentially outlines the provisions under Section 1 of the bill. The section also reaffirms the royalty owner's right to contact the payor by other means, such as telephone or email.

Many royalty owners have inherited their interests and they may not be familiar with oil and gas royalties. This provision is a positive step to notify an owner how to obtain more information. Education and communication are essential to foster a spirit of cooperativeness and openness with industry.

Enforcement Provisions - New Section 3.

The enforcement provision helps to level the playing field for payors who refuse to provide the requested information upon a written request, as well as for payors who fail to provide required information on the check stub.

The bill allows either party to request mediation. The process for mediation is a voluntary process.

The royalty owner can also bring an action in a district court of Kansas, where the oil and gas was produced, to enforce the provisions of the bill.

Summary.

Royalty owners are entitled to receive clear, transparent and accurate information for their royalty payments. H.B. 2673 is a step in the right direction, and we urge your adoption of House Bill 2673.

Respectfully submitted,

/s/ Erick E. Nordling

Erick E. Nordling
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