

MESA ROYALTY TRUST/TX  
Form 10-Q  
August 14, 2014

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-Q**

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

For the Quarterly Period ended June 30, 2014

o **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: **1-7884**

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**MESA ROYALTY TRUST**

(Exact name of registrant as specified in its charter)

**Texas**  
(State or other jurisdiction of  
Incorporation or Organization)

**76-6284806**  
(I.R.S. Employer  
Identification No.)

**The Bank of New York Mellon Trust Company, N.A.,**

**Trustee**

**919 Congress Avenue**

**Austin, Texas**

(Address of Principal Executive Offices)

**78701**

(Zip Code)

**1-512-236-6545**

(Registrant's Telephone Number, Including Area Code)

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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 ý No o

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a  
smaller reporting company)

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 August 14, 2014 1,863,590 Units of Beneficial Interest were outstanding in Mesa Royalty Trust.

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## PART I FINANCIAL INFORMATION

## Item 1. Financial Statements.

## MESA ROYALTY TRUST

## STATEMENTS OF DISTRIBUTABLE INCOME

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Royalty income	\$ 2,487,660	\$ 690,404	\$ 3,732,244	\$ 1,729,479
Interest income		43	35	84
General and administrative expense	(46,395)	(37,148)	(89,843)	(90,133)
Distributable income	\$ 2,441,265	\$ 653,299	\$ 3,642,436	\$ 1,639,430
Distributable income per unit	\$ 1.3100	\$ 0.3505	\$ 1.9545	\$ 0.8797
Units outstanding	1,863,590	1,863,590	1,863,590	1,863,590

## STATEMENTS OF ASSETS, LIABILITIES AND TRUST CORPUS

	June 30, 2014	December 31, 2013
	(Unaudited)	
<b>ASSETS</b>		
Cash and short-term investments	\$ 3,441,265	\$ 1,939,254
Net overriding royalty interest in oil and gas properties	42,498,034	42,498,034
Accumulated amortization	(39,129,672)	(38,768,076)
Total assets	\$ 6,809,627	\$ 5,669,212
<b>LIABILITIES AND TRUST CORPUS</b>		
Distributions payable	\$ 2,441,265	\$ 939,254
Trust corpus (1,863,590 units of beneficial interest authorized, issued and outstanding)	4,368,362	4,729,958

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Total liabilities and trust corpus	\$	6,809,627	5,669,212
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(The accompanying notes are an integral part of these financial statements.)

**MESA ROYALTY TRUST**

**STATEMENTS OF CHANGES IN TRUST CORPUS**

**(Unaudited)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Trust corpus, beginning of period	\$ 4,556,768	\$ 5,251,869	\$ 4,729,958	\$ 5,484,813
Distributable income	2,441,265	653,299	3,642,436	1,639,430
Distributions to unitholders	(2,441,265)	(653,299)	(3,642,436)	(1,639,430)
Amortization of net overriding royalty interest	(188,406)	(154,693)	(361,596)	(387,637)
Trust corpus, end of period	\$ 4,368,362	\$ 5,097,176	\$ 4,368,362	\$ 5,097,176

(The accompanying notes are an integral part of these financial statements.)

**MESA ROYALTY TRUST**

**NOTES TO FINANCIAL STATEMENTS**

**(Unaudited)**

**Note 1 Trust Organization and Provisions**

The Mesa Royalty Trust (the "Trust") was created on November 1, 1979. On that date, Mesa Petroleum Co., predecessor to Mesa Limited Partnership ("MLP"), which was the predecessor to MESA Inc., conveyed to the Trust an overriding royalty interest (the "Royalty") equal to 90% of the Net Proceeds (as defined in the Conveyance and described below) attributable to the specified interests in properties conveyed by the assignor on that date (the "Subject Interests"). The Subject Interests consisted of interests in certain producing oil and gas properties located in the Hugoton field of Kansas, the San Juan Basin field of New Mexico and Colorado and the Yellow Creek field of Wyoming (the "Royalty Properties"). The Royalty is evidenced by counterparts of an Overriding Royalty Conveyance dated as of November 1, 1979 (the "Conveyance"). On April 30, 1991, MLP sold its interests in the Royalty Properties located in the San Juan Basin field to ConocoPhillips. ConocoPhillips sold the portion of its interests in the San Juan Basin Royalty Properties located in Colorado to MarkWest Energy Partners, Ltd. (effective January 1, 1993) and Red Willow Production Company (effective April 1, 1992). On October 26, 1994, MarkWest Energy Partners, Ltd. sold substantially all of its interest in the Colorado San Juan Basin Royalty Properties to BP Amoco Company ("BP"), a subsidiary of BP p.l.c. Until August 7, 1997, MESA Inc. operated the Hugoton Royalty Properties through Mesa Operating Co., a wholly owned subsidiary of MESA Inc. On August 7, 1997, MESA Inc. merged with and into Pioneer Natural Resources Company ("Pioneer"), formerly a wholly owned subsidiary of MESA Inc., and Parker & Parsley Petroleum Company merged with and into Pioneer Natural Resources USA, Inc. (successor to Mesa Operating Co.), a wholly owned subsidiary of Pioneer ("PNR") (collectively, the mergers are referred to herein as the "Merger"). Subsequent to the Merger, the Hugoton Royalty Properties have been operated by PNR. Substantially all of the San Juan Basin Royalty Properties located in New Mexico are operated by ConocoPhillips. Effective January 1, 2005, ConocoPhillips assigned its interest in an immaterial number of San Juan Basin Royalty Properties located in New Mexico to XTO Energy Inc. The San Juan Basin Royalty Properties located in Colorado are operated by BP. As used in this report, PNR refers to the operator of the Hugoton Royalty Properties, ConocoPhillips refers to the operator of the San Juan Basin Royalty Properties, other than the portion of such properties located in Colorado, and BP refers to the operator of the Colorado San Juan Basin Royalty Properties unless otherwise indicated.

Effective October 2, 2006, The Bank of New York Mellon Trust Company, N.A. (the "Trustee") succeeded JPMorgan Chase Bank, N.A. as Trustee of the Trust. JPMorgan Chase Bank, N.A. is the successor by mergers to the original name of the Trustee, Texas Commerce Bank National Association. The terms of the Mesa Royalty Trust Indenture (the "Trust Indenture") provide, among other things, that:

- (a) the Trust cannot engage in any business or investment activity or purchase any assets;
- (b) the Royalty can be sold in part or in total for cash upon approval by the unitholders;
- (c) the Trustee can establish cash reserves and borrow funds to pay liabilities of the Trust and can pledge assets of the Trust to secure payment of the borrowings;

**MESA ROYALTY TRUST**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**Note 1 Trust Organization and Provisions (Continued)**

(d) the Trustee will make cash distributions to the unitholders in January, April, July and October each year as discussed more fully in Note 2;

(e) the Trust will terminate upon the first to occur of the following events: (i) at such time as the Trust's royalty income for two successive years is less than \$250,000 per year or (ii) a vote by the unitholders in favor of termination. Upon termination of the Trust, the Trustee will sell for cash all the assets held in the Trust estate and make a final distribution to unitholders of any funds remaining after all Trust liabilities have been satisfied; and

(f) PNR, ConocoPhillips and BP (collectively the "Working Interest Owners") will reimburse the Trust for 59.34%, 27.45% and 1.77%, respectively, for general and administrative expenses of the Trust.

During 2011, the Trustee withheld \$1.0 million for future unknown contingent liabilities and expenses in accordance with the Trust Indenture. As of June 30, 2014, the \$1.0 million is included in cash and short term investments.

For the quarter ended June 30, 2014, the Trustee was paid fees totaling \$108,288 in connection with services performed in its capacity as Trustee. These fees have been reimbursed by the working interest owners in accordance with the Trust Indenture. These reimbursements totaled \$95,900. For year to date June 30, 2014 such fees were \$192,226. Reimbursements received for year to date June 30, 2014 were \$170,235. For the quarter ended June 30, 2013 and year to date June 30, 2013 trustee fees were \$83,938 and \$167,876 respectively. Reimbursements received for the quarter ended June 30, 2013 and year to date June 30, 2013 were \$74,335 and \$148,670 respectively.

The Trust's distributable income for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013.

**Note 2 Basis of Presentation**

The accompanying unaudited financial information has been prepared by the Trustee in accordance with the instructions to Form 10-Q. The preparation of the financial statements requires estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. The Trustee believes such information includes all the disclosures necessary to make the information presented not misleading. The information furnished reflects all adjustments which are, in the opinion of the Trustee, necessary for a fair presentation of the results for the interim periods presented. The financial information should be read in conjunction with the financial statements and notes thereto included in the Trust's Annual Report on Form 10-K for the year ended December 31, 2013. The Trust considers all highly liquid

**MESA ROYALTY TRUST**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**Note 2 Basis of Presentation (Continued)**

investments with a maturity of three months or less to be cash equivalents. Subsequent events were evaluated through the issuance date of the financial statements.

In accordance with the Conveyance, the Working Interest Owners are obligated to calculate and pay the Trust each month an amount equal to 90% of the Net Proceeds (as defined in the Conveyance) attributable to the month. In 1985, the Trust Indenture was amended and the Trust conveyed to an affiliate of Mesa Petroleum Co. 88.5571% of the original Royalty (such transfer, the "1985 Assignment"). The effect of the 1985 Assignment was an overall reduction of approximately 88.56% in the size of the Trust. As a result, the Trust is now entitled to receive 11.44% of 90% of the Net Proceeds attributable to each month.

The financial statements of the Trust are prepared on the following basis:

- (a) Royalty income recorded for a month is the amount computed and paid by the Working Interest Owners to the Trustee for such month rather than either the value of a portion of the oil and gas produced by the Working Interest Owners for such month or the amount subsequently determined to be the Trust's proportionate share of the net proceeds for such month;
- (b) Interest income, interest receivable and distributions payable to unitholders include interest to be earned on short-term investments from the financial statement date through the next date of distribution;
- (c) Trust general and administrative expenses, net of reimbursements, are recorded in the month they are included in the calculation of the monthly distribution amount;
- (d) Amortization of the Royalty is computed on a unit-of-production basis and is charged directly to trust corpus since such amount does not affect distributable income; and
- (e) Distributions payable are determined on a monthly basis and are payable to unitholders of record as of the last business day of each month or such later date as the Trustee determines is required to comply with applicable law or stock exchange requirements. However, cash distributions are made quarterly in January, April, July and October, and include interest earned from the monthly record dates to the date of distribution.

This basis for reporting distributable income is considered to be the most meaningful because distributions to the unitholders for a month are based on net cash receipts for such month. However, these statements differ from financial statements prepared in accordance with accounting principles generally accepted in the United States of America because, under such principles, royalty income for a month would be based on net proceeds from production for such month without regard to when calculated or received, general and administrative expenses would be recorded in the month they accrue, and interest income for a month would be calculated only through the end of such month.



**MESA ROYALTY TRUST**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**Note 3 Legal Proceedings**

There are no pending legal proceedings to which the Trust is a named party. The Trustee has been advised by PNR, ConocoPhillips and BP that it is subject to litigation in the ordinary course of business for certain matters that include the Royalty Properties. While each of the working interest owners has advised the Trustee that it does not currently believe any of the pending litigation will have a material adverse effect net to the Trust, in the event such matters were adjudicated or settled in a material amount and charges were made against Royalty income, such charges could have a material impact on future Royalty income.

**Note 4 Income Tax Matters**

In a technical advice memorandum dated February 26, 1982, the IRS advised the Dallas District Director that the Trust is classifiable as a grantor trust and not as an association taxable as a corporation. As a grantor trust, the Trust incurs no federal income tax liability and each unitholder is subject to tax on the unitholder's pro rata share of the income and expense of the Trust as if the unitholder were the direct owner of a pro rata share of the Trust's assets. In addition, there is no state tax liability for the period.

For taxable years beginning after December 31, 2012, individuals, estates, and trusts with income above certain thresholds are subject under Section 1411 of the Internal Revenue Code to an additional 3.8% tax also known as the "Medicare contribution tax" on their net investment income. Grantor trusts such as Mesa Royalty Trust are not subject to the 3.8% tax; however, the unitholders may be subject to the tax. For these purposes, investment income would generally include certain income derived from investments, such as the royalty income derived from the units and gain realized by a unitholder from a sale of units.

The Trustee assumes that some Trust Units are held by a middleman, as such term is broadly defined in U.S. Treasury Regulations (and includes custodians, nominees, certain joint owners, and brokers holding an interest for a custodian in street name). Therefore, the Trustee considers the Trust to be a non-mortgage widely held fixed investment trust ("WHFIT") for U.S. federal income tax purposes. The Bank of New York Mellon Trust Company, N.A., 919 Congress Avenue, Austin, Texas 78701, telephone number 512-236-6545, is the representative of the Trust that will provide tax information in accordance with applicable U.S. Treasury Regulations governing the information reporting requirements of the Trust as a WHFIT.

Notwithstanding the foregoing, the middlemen holding units on behalf of unitholders, and not the Trustee of the Trust, are solely responsible for complying with the information reporting requirements under the Treasury Regulations with respect to such units, including the issuance of IRS Forms 1099 and certain written tax statements. Unitholders whose units are held by middlemen should consult with such middlemen regarding the information that will be reported to them by the middlemen with respect to the units.

**MESA ROYALTY TRUST**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**(Unaudited)**

**Note 5 Excess Production Costs**

Excess production costs result when costs, charges, and expenses attributable to a Working Interest Property exceed the revenue received from the sale of oil, gas, and other hydrocarbons produced from such property. The excess production costs must be recovered by the working interest owners before any distribution of Royalty income from the properties will be made to the Trust. As of June 30, 2014 and December 31, 2013, there were \$478 and \$478, respectively, of excess production costs. Excess production costs in the amount of \$478 and \$478 as of June 30, 2014 and December 31, 2013, respectively, related to the San Juan Basin New Mexico properties operated by XTO Energy Inc. XTO Energy Inc. made distributions to the Trust during the first and second quarters of 2014 without recovering the \$478 excess production costs. The remainder of the excess production costs in the amount of \$35,152 as of March 31, 2014 related to the San Juan Basin Colorado properties operated by BP were recovered during the quarter ended June 30, 2014.

**Note 6 Subsequent Events**

On August 4, 2014, Pioneer announced that it has entered into a purchase and sale agreement to sell all of its assets in the Hugoton field in Kansas to Linn Energy, LLC. The transaction has an effective date of July 1, 2014, and is expected to close by the end of the third quarter of 2014. The assets being sold represent all of Pioneer's interests in the field, including all of its producing oil and gas wells, all of its interest in the Satanta gas processing plant and all other associated infrastructure. Accordingly, Linn Energy, LLC is expected to become the operator of the Hugoton Royalty Properties following the closing of this transaction.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

The following review of the Trust's financial condition and results of operations should be read in conjunction with the financial statements and notes thereto. The discussion of net production attributable to the Hugoton and San Juan properties represents production volumes that are to a large extent hypothetical as the Trust does not own and is not entitled to any specific production volumes. See Note 9 to the financial statements in the Trust's Annual Report on Form 10-K for the year ended December 31, 2013. Any discussion of "actual" production volumes represents the hydrocarbons that were produced from the properties in which the Trust has an overriding royalty interest.

The Trust is a passive entity whose purposes are limited to: (1) converting the Royalties to cash, either by retaining them and collecting the proceeds of production (until production has ceased or the Royalties are otherwise terminated) or by selling or otherwise disposing of the Royalties; and (2) distributing such cash, net of amounts for payments of liabilities to the Trust, to the unitholders. The Trust has no sources of liquidity or capital resources other than the revenues, if any, attributable to the Royalties and interest on cash held by the Trustee as a reserve for liabilities or for distribution.

On August 4, 2014, Pioneer announced that it has entered into a purchase and sale agreement to sell all of its assets in the Hugoton field in Kansas to Linn Energy, LLC. The transaction has an effective date of July 1, 2014, and is expected to close by the end of the third quarter of 2014. The assets being sold represent all of Pioneer's interests in the field, including all of its producing oil and gas wells, all of its interest in the Satanta gas processing plant and all other associated infrastructure. Accordingly, Linn Energy, LLC is expected to become the operator of the Hugoton Royalty Properties following the closing of this transaction.

**Note Regarding Forward-Looking Statements**

This Form 10-Q includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements other than statements of historical facts included in this Form 10-Q, including without limitation the statements under "Management's Discussion and Analysis of Financial Condition and Results of Operations," are forward-looking statements. Although the Working Interest Owners have advised the Trust that they believe that the expectations reflected in the forward-looking statements contained herein are reasonable, no assurance can be given that such expectations will prove to be correct. Important factors that could cause actual results to differ materially from expectations ("Cautionary Statements") are disclosed in this Form 10-Q and in the Trust's Annual Report on Form 10-K for the year ended December 31, 2013, including under "Item 1A. Risk Factors". All subsequent written and oral forward-looking statements attributable to the Trust or persons acting on its behalf are expressly qualified in their entirety by the Cautionary Statements.

**SUMMARY OF ROYALTY INCOME, PRODUCTION AND AVERAGE PRICES  
(Unaudited)**

Royalty income is computed after deducting the Trust's proportionate share of capital costs, operating costs and interest on any cost carryforward from the Trust's proportionate share of "Gross Proceeds," as defined in the Conveyance. The following summary illustrates the net effect of the components of the actual Royalty computation for the periods indicated.

	Three Months Ended June 30,			
	2014		2013	
	Natural Gas	Oil, Condensate and Natural Gas Liquids	Natural Gas	Oil, Condensate and Natural Gas Liquids
The Trust's proportionate share of Gross Proceeds(1)	\$ 1,591,566	\$ 855,702	\$ 1,031,168	\$ 741,319
Less the Trust's proportionate share of:				
Capital costs recovered	(43,824)	(28,440)	(179,816)	(182,518)
Operating costs	(485,663)	(248,124)	(407,539)	(312,210)
<b>Net proceeds(2)</b>	<b>\$ 1,062,079</b>	<b>\$ 579,138</b>	<b>\$ 443,813</b>	<b>\$ 246,591</b>
Royalty income(2)	\$ 1,026,927	\$ 579,138	\$ 443,813	\$ 246,591
Average sales price	\$ 4.47	\$ 29.99	\$ 2.98	\$ 28.91
Average production costs(3)	\$ 2.31	\$ 14.32	\$ 3.94	\$ 58.00
	(Mcf)	(Bbls)	(Mcf)	(Bbls)
Net production volumes attributable to the Royalty paid(4)	229,537	19,313	148,941	8,529

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	Six Months Ended June 30,			
	2014		2013	
	Natural Gas	Oil, Condensate and Natural Gas Liquids	Natural Gas	Oil, Condensate and Natural Gas Liquids
The Trust's proportionate share of Gross Proceeds(1)	\$ 2,771,030	\$ 1,701,276	\$ 2,005,747	\$ 1,522,427
Less the Trust's proportionate share of:				
Capital costs recovered	(78,443)	(57,484)	(220,586)	(229,264)
Operating costs	(946,668)	(539,062)	(761,670)	(587,175)
<b>Net proceeds(2)</b>	<b>1,745,919</b>	<b>1,104,730</b>	<b>1,023,491</b>	<b>705,988</b>
Royalty income(2)	1,745,919	1,104,730	1,023,491	705,988
Average sales price	\$ 3.94	\$ 29.85	\$ 2.95	\$ 27.98
Average production costs(3)	\$ 2.32	\$ 16.12	\$ 2.84	\$ 32.36
	(Mcf)	(Bbls)	(Mcf)	(Bbls)
Net production volumes attributable to the Royalty paid(4)	442,705	37,011	346,377	25,227

(1) Gross Proceeds from natural gas liquids attributable to the Hugoton and San Juan Basin Properties are net of a volumetric in-kind processing fee retained by PNR and ConocoPhillips, respectively. The Trust's gross proceeds for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013.

(2) As a result of excess production costs incurred in one monthly operating period and then recovered in a subsequent monthly operating period(s), the Royalty income paid to the Trust may not agree to the Trust's royalty interest in the Net Proceeds. Excess production costs related to the San Juan Basin New Mexico properties operated by XTO Energy Inc. were approximately \$478 as of June 30, 2014 and December 31, 2013. Excess production costs of \$35,152 related to the San Juan Basin Colorado properties operated by BP were recovered during the quarter ended June 30, 2014 and are \$0 as of June 30, 2014. The excess production costs must be recovered by

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the working interest owners before any distribution of Royalty income will be made to the Trust.

- (3) Average production costs attributable to the Royalty are calculated as stated capital costs plus operating costs, divided by stated net production volumes attributable to the Royalty paid. As noted above in footnote (2), production costs may be incurred in one operating period and then recovered in a subsequent operating period, which may cause Royalty income paid to the Trust not to agree to the Trust's Royalty interest in the Net Proceeds.
- (4) Net production volumes attributable to the Royalty are determined by dividing Royalty income by the average sales price received.

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Three Months Ended June 30, 2014 and 2013

*Financial Review*

	Three Months Ended June 30,	
	2014	2013
Royalty income	\$ 2,487,660	\$ 690,404
Interest income		43
General and administrative expense	(46,395)	(37,148)
Distributable income	\$ 2,441,265	\$ 653,299
Distributable income per unit	\$ 1.3100	\$ 0.3505
Units outstanding	1,863,590	1,863,590

The Trust's Royalty income was \$2,487,660 in the second quarter of 2014, an increase of approximately 260% as compared to \$690,404 in the second quarter of 2013, primarily as a result of higher natural gas and natural gas liquids prices, decreased capital expenditures and increased natural gas and natural gas liquids volumes in the second quarter of 2014 as compared to the second quarter of 2013, offset in part by higher operating costs in the second quarter of 2014 compared to the second quarter of 2013. In addition, the Trust income distribution for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013.

The distributable income of the Trust for each period includes the Royalty income received from the working interest owners during such period, plus interest income earned to the date of distribution (if any). Trust administration expenses are deducted in the computation of distributable income. Distributable income for the quarter ended June 30, 2014 was \$2,441,265, representing \$1.3100 per unit, compared to \$653,299, representing \$0.3505 per unit, for the quarter ended June 30, 2013. Based on 1,863,590 units outstanding for the quarters ended June 30, 2014 and 2013, respectively, the per unit distributions were as follows:

	2014	2013
April	\$ .7513	\$ .1801
May	.2836	.0565
June	.2751	.1139

\$ 1.3100    \$ 0.3505

During 2011, the Trustee withheld \$1.0 million for future unknown contingent liabilities and expenses in accordance with the Trust Indenture. As of June 30, 2014, the \$1.0 million is included in cash and short term investments.





*Operational Review*

*Hugoton Field*

Natural gas and natural gas liquids production attributable to the Royalty from the Hugoton field accounted for approximately 38% of the Royalty income of the Trust during the second quarter of 2014.

PNR has advised the Trust that since June 1, 1995 natural gas produced from the Hugoton field has generally been sold under short-term and multi-month contracts at market clearing prices to multiple purchasers. During 2013 the primary purchaser was Oneok Gas Marketing, Inc. PNR has advised the Trust that it expects to continue to market gas production from the Hugoton field under short-term and multi-month contracts. As discussed below, overall market prices received for natural gas from the Hugoton Royalty Properties were higher in the second quarter of 2014 compared to the second quarter of 2013.

In June 1994, PNR entered into a Gas Transportation Agreement ("Gas Transportation Agreement") with Western Resources, Inc. ("WRI") for a primary term of five years commencing June 1, 1995. This contract has renewed on a year-to-year basis being effective June 1, 2001. The contract is renewed a year in advance, so PNR extended the contract to June 1, 2015. Pursuant to the Gas Transportation Agreement, WRI agreed to compress and transport up to 160 MMcf per day of gas and redeliver such gas to PNR at the inlet of PNR's Satanta Plant. PNR agreed to pay WRI a fee of \$0.06 per Mcf escalating 4% annually as of June 1, 1996. This Gas Transportation Agreement was assigned to Oneok Field Services.

The Trust income distribution for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013.

Royalty income attributable to the Hugoton Royalty increased to \$1,486,567 in the second quarter of 2014 from \$347,058 in the second quarter of 2013 primarily due to the settlement discussed above, increases in natural gas and natural gas liquids prices, increases in natural gas and natural gas liquids volumes and reduced operating costs from the Hugoton Royalty Properties, offset in part by increased capital expenditures. The average price received in the second quarter of 2014 for natural gas and natural gas liquids sold from the Hugoton Royalty Properties was \$5.19 per Mcf and \$43.98 per barrel, respectively, as compared to \$3.65 per Mcf and \$31.22 per barrel, respectively, in the second quarter of 2013. Net production of natural gas attributable to the Hugoton Royalty increased to 75,141 Mcf in the second quarter of 2014 from 57,339 Mcf in the second quarter of 2013. Net production of natural gas liquids attributable to the Hugoton Royalty increased to 4,888 barrels in the second quarter of 2014 from 4,413 barrels in the second quarter of 2013. Actual production volumes from the Hugoton properties increased to 114,331 Mcf of natural gas and decreased to 7,424 barrels of natural gas liquids in the second quarter of 2014 as compared to 108,565 Mcf of natural gas and 8,352 barrels of natural gas liquids for the same period in 2013. The increase in natural gas volumes and decrease in natural gas liquids volumes was due primarily to changes in plant recoveries during the second quarter of 2014 compared with the second quarter of 2013.

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The Hugoton capital expenditures were \$10,419 in the second quarter of 2014, as compared to \$0 in the second quarter of 2013. Operating costs were \$303,872 in the second quarter of 2014, a decrease of approximately 2% as compared to \$309,069 in the second quarter of 2013.

### *San Juan Basin*

Royalty income from the San Juan Basin Royalty Properties is calculated and paid to the Trust on a state-by-state basis. Substantially all of the royalty income from the San Juan Basin Royalty Properties is attributable to the Royalty Properties located in the State of New Mexico.

Royalty income from the San Juan Basin New Mexico was \$937,512 during the second quarter of 2014 as compared with Royalty income of \$218,210 during the second quarter of 2013. This increase in Royalty income was due primarily to an increase in natural gas and natural gas liquids prices, increased production of natural gas, decreased capital expenditures and decreased operating costs for the second quarter of 2014 compared to the second quarter of 2013. Net production attributable to the San Juan Basin Royalty Properties located in New Mexico was 136,885 Mcf of natural gas and 14,425 barrels of natural gas liquids in the second quarter of 2014, as compared to 38,518 Mcf of natural gas and 4,116 barrels of natural gas liquids in the second quarter of 2013. The average price received in the second quarter of 2014 for natural gas and natural gas liquids sold from the San Juan Basin Royalty Properties located in the State of New Mexico was \$4.19 per Mcf and \$25.24 per barrel, respectively, compared to \$2.84 per Mcf and \$26.44 per barrel during the same period in 2013. Actual production volumes of natural gas attributable to the San Juan Basin Royalty Properties located in the State of New Mexico increased to 198,029 Mcf in the second quarter of 2014 from 167,520 Mcf of natural gas for the same period in 2013. Actual production volumes of natural gas liquids attributable to the San Juan Basin Royalty Properties located in the State of New Mexico increased to 22,566 barrels in the second quarter of 2014 from 21,941 barrels for the same period in 2013.

Capital expenditures on these properties were \$61,845 in the second quarter of 2014, a decrease of approximately 83% as compared to \$362,334 in the second quarter of 2013, primarily due to decreased developmental drilling. Operating costs were \$359,640 in the second quarter of 2014, a decrease of approximately 4% as compared to \$375,798 in the second quarter of 2013.

The Trust's interest in the San Juan Basin was conveyed from PNR's working interest in 31,328 net producing acres in northwestern New Mexico and southwestern Colorado. Substantially all of the natural gas produced from the San Juan Basin is currently being sold on the spot market.

Royalty income from the San Juan Basin Colorado Royalty Properties was \$63,581 during the second quarter of 2014, compared to \$125,136 during the second quarter of 2013. This decrease in Royalty income was due primarily to increased operating costs and decreased natural gas production in the second quarter of 2014 compared to the second quarter of 2013, offset in part by an increase in the price received for natural gas in the second quarter of 2014 compared to the second quarter of 2013. Net production attributable to the San Juan Basin Royalty Properties located in Colorado was 17,512 Mcf of natural gas during the second quarter of 2014 with 53,083 Mcf of natural gas attributable to the Trust during the second quarter of 2013. The average price received in the second quarter of 2014 for natural gas sold from the San Juan Basin Colorado Properties was \$3.63 per Mcf, as compared to average price of \$2.36 per Mcf for the second quarter of 2013. Actual production volumes attributable to the San Juan Basin Colorado Properties decreased to 46,654 Mcf of natural gas in the second quarter of 2014 from 67,806 Mcf of natural gas for the same period in 2013.

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Operating costs on these properties were \$70,275 in the second quarter of 2014 as compared to \$34,882 in the second quarter of 2013 due primarily to increased labor and supervision costs.

By letter dated April 28, 2014, ConocoPhillips notified the Trustee that it became aware of an issue regarding the payment of general and administrative invoices on behalf of the Trust. Specifically, ConocoPhillips was unable to locate documentation to support the reimbursement of expenses attributable to its overriding interest and, as a result, was suspending such payments. The Trustee provided to ConocoPhillips on May 2, 2014, the letter agreement, dated April 30, 1991, whereby Conoco Inc. agreed to assume 33% of the Trustee expenses allocated to the San Juan Properties and the matter was subsequently resolved. For the three months ended June 30, 2014, the amount of such payments by ConocoPhillips was approximately \$111,000.

### Six Months Ended June 30, 2014 and 2013

#### Financial Review

	Six Months Ended June 30,	
	2014	2013
Royalty income	\$ 3,732,244	\$ 1,729,479
Interest income	35	84
General and administrative expense	(89,843)	(90,133)
Distributable income	\$ 3,642,436	\$ 1,639,430
Distributable income per unit	\$ 1.9545	\$ 0.8797
Units outstanding	1,863,590	1,863,590

The Trust's Royalty income was \$3,732,244 for the six months ended June 30, 2014, an increase of approximately 116% as compared to \$1,729,479 for the six months ended June 30, 2013, primarily as a result of increased natural gas and natural gas liquids prices and production volumes and lower capital expenditures, offset in part by increased operating costs in the first six months of 2014 as compared to the first six months of 2013. In addition, the Trust income distribution for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013.

The distributable income of the Trust for each period includes the Royalty income received from the working interest owners during such period, plus interest income earned to the date of distribution. Trust administration expenses are deducted in the computation of distributable income. Distributable income for the six months ended June 30, 2014 was \$3,642,436, representing \$1.9545 per unit, compared to \$1,639,430, representing \$0.8797 per unit, for the six months ended June 30, 2013.

During 2011, the Trustee withheld \$1.0 million for future unknown contingent liabilities and expenses in accordance with the Trust Indenture. As of June 30, 2014 the \$1.0 million is included in cash and short term investments.

*Operational Review*

*Hugoton Field*

Natural gas and natural gas liquids revenue from the Hugoton field attributable to the Royalty accounted for approximately 37% of the Royalty income of the Trust during the six months ended June 30, 2014.

Royalty income attributable to the Hugoton Royalty Properties increased to \$1,934,277 for the six months ended June 30, 2014 from \$709,144 for the same period in 2013 primarily due to higher prices for natural gas and natural gas liquids, increased natural gas and natural gas liquids production volumes and lower operating costs, offset in part by an increase in capital expenditures from the Hugoton Royalty Properties in the first six months of 2014 compared to the first six months of 2013. In addition, the Trust income distribution for the month of April 2014 included \$881,595. The Trustee engaged an independent consulting firm to audit revenues and expenses of certain working interest owners. As a result of the audit, the Trustee entered into a Settlement Agreement with one of the working interest owners, pursuant to which such working interest owner agreed to pay the Trust for certain audit exceptions noted by the Trustee for the calendar years 2006 through 2013. The average price received in the first six months of 2014 for natural gas and natural gas liquids sold from the Hugoton field was \$4.51 per Mcf and \$39.44 per barrel, respectively, compared to \$3.58 per Mcf and \$31.75 per barrel, respectively, during the same period in 2013. Net production attributable to the Hugoton Royalty Properties increased to 143,991 Mcf of natural gas and 10,225 barrels of natural gas liquids for the six months ended June 30, 2014 as compared to 119,219 Mcf of natural gas and 8,893 barrels of natural gas liquids for the six months ended June 30, 2013. Actual production volumes attributable to the Hugoton Royalty Properties increased to 228,986 Mcf of natural gas and decreased to 16,339 barrels of natural gas liquids in the six months ended June 30, 2014 as compared to 225,330 Mcf of natural gas and 16,828 barrels of natural gas liquids for the same period in 2013. The increase in natural gas volumes and decrease in natural gas liquids volumes was due primarily to changes in plant recoveries during the second quarter of 2014 compared with the second quarter of 2013.

Capital expenditures on these properties were \$19,161 during the six months ended June 30, 2014, an increase of approximately 100% as compared to \$0 during the six months ended June 30, 2013. Operating costs were \$603,708 during the six months ended June 30, 2014, a decrease of approximately 4% as compared to \$631,701 during the six months ended June 30, 2013.

*San Juan Basin*

Royalty income from the San Juan Basin New Mexico was \$1,667,808 for the first six months of 2014 compared to \$807,719 for the first six months of 2013. The increase in Royalty income was due primarily to reduced capital expenditures, increased natural gas and natural gas liquids prices and higher production volumes, offset in part by increased operating costs in the first six months of 2014 from the San Juan Basin properties compared to the same period in 2013. The average price received in the six months ended June 30, 2014 for natural gas and natural gas liquids sold from the San Juan Basin Royalty Properties located in the state of New Mexico was \$3.77 per Mcf and \$26.19 per barrel, respectively, compared to \$2.74 per Mcf and \$25.94 per barrel, respectively, during the same period in 2013. Net production attributable to the San Juan Basin Royalty located in New Mexico was 256,609 Mcf of natural gas and 26,786 barrels of natural gas liquids for the six months ended June 30, 2014 as compared to 140,186 Mcf of natural gas and 16,335 barrels of natural gas

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liquids for the six months ended June 30, 2013. Actual production volumes attributable to the San Juan Basin Royalty Properties increased to 383,658 Mcf of natural gas and decreased to 44,494 barrels of natural gas liquids in the six months ended June 30, 2014 as compared to 335,903 Mcf of natural gas and 44,573 barrels of natural gas liquids for the same period in 2013.

San Juan-New Mexico capital expenditures were \$116,766 during the six months ended June 30, 2014, a decrease of approximately 74% as compared to \$449,850 during the six months ended June 30, 2013. This decrease is due to decreased developmental drilling activity during the six months ended June 30, 2014 when compared to the six months ended June 30, 2013. Operating costs were \$717,088 during the six months ended June 30, 2014, an increase of approximately 10% as compared to \$650,849 during the six months ended June 30, 2013. The increase in operating costs is due primarily to small increases primarily due to surface maintenance across the majority of the properties.

Royalty income from the San Juan Basin Colorado Royalty Properties was \$130,159 for the six months ended June 30, 2014, compared to \$212,616 during the same period in 2013. The decrease in Royalty income was primarily the result of increased operating costs and decreased natural gas production, offset in part by higher natural gas prices in the six months ended June 30, 2014 compared to the same period in 2013. Net production attributable to the San Juan Basin Royalty Properties located in Colorado was 42,106 Mcf of natural gas during the six months ended June 30, 2014 with 86,972 Mcf of natural gas attributable to the Trust during the same period in 2013. The average price received for the six months ended June 30, 2014 for natural gas sold from the San Juan Basin Colorado Properties was \$3.09 per Mcf, compared to \$2.44 per Mcf received during the same period in 2013. Actual production volumes attributable to the San Juan Basin Colorado Properties decreased to 95,485 Mcf of natural gas for the six months ended June 30, 2014 as compared to 114,067 Mcf of natural gas for the same period in 2013.

Operating costs on these properties were \$164,934 for the six months ended June 30, 2014, an increase of approximately 149% as compared to \$66,295 in the same period in 2013 due primarily to increased labor and supervision costs.

By letter dated April 28, 2014, ConocoPhillips notified the Trustee that it became aware of an issue regarding the payment of general and administrative invoices on behalf of the Trust. Specifically, ConocoPhillips was unable to locate documentation to support the reimbursement of expenses attributable to its overriding interest and, as a result, was suspending such payments. The Trustee provided to ConocoPhillips on May 2, 2014, the letter agreement, dated April 30, 1991, whereby Conoco Inc. agreed to assume 33% of the Trustee expenses allocated to the San Juan Properties and the matter was subsequently resolved. For the six months ended June 30, 2014, the amount of such payments by ConocoPhillips was approximately \$141,000.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

The Trust does not engage in any operations, and does not utilize market risk sensitive instruments, either for trading purposes or for other than trading purposes. The Trust's monthly distributions are highly dependent upon the prices realized from the sale of natural gas. Natural gas prices can fluctuate widely on a month-to-month basis in response to a variety of factors that are

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beyond the control of the Trust and the working interest owners. Factors that contribute to price fluctuation include, among others:

political conditions worldwide, in particular political disruption, war or other armed conflict in or affecting oil producing regions;

worldwide economic conditions;

weather conditions, including hurricanes and tropical storms in the Gulf of Mexico;

the supply and price of foreign natural gas;

the level of consumer demand;

the price and availability of alternative fuels;

the proximity to, and capacity of, transportation facilities; and

the effect of worldwide energy conservation measures.

Moreover, government regulations, such as regulation of natural gas transportation and regulation of greenhouse gas and other emissions associated with fossil fuel combustion and price controls, can affect product prices in the long term.

### **Item 4. Controls and Procedures.**

*Evaluation of Disclosure Controls and Procedures.* The Trustee maintains disclosure controls and procedures designed to ensure that information required to be disclosed by the Trust in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed by the Trust in the reports that it files or submits under the Exchange Act is accumulated and communicated by the working interest owners to The Bank of New York Mellon Trust Company, N.A., as Trustee of the Trust, and its employees who participate in the preparation of the Trust's periodic reports as appropriate to allow timely decisions regarding required disclosure.

As of the end of the period covered by this report, the trust officer acting on behalf of the Trustee responsible for the administration of the Trust conducted an evaluation of the Trustee's disclosure controls and procedures. The officer acting on behalf of the Trustee concluded that the Trust's disclosure controls and procedures were effective.

Due to the contractual arrangements of (i) the Trust Indenture and (ii) the rights of the Trust under the Conveyance regarding information furnished by the working interest owners, the Trustee relies on information provided by the working interest owners, including (i) the status of litigation, (ii) historical operating data, plans for future operating and capital expenditures and reserve information, (iii) information relating to projected production, and (iv) conclusions regarding reserves by their internal reserve engineers or other experts in good faith. See Part I Item 1A. "Risk Factors Trust unitholders and the Trustee have no control over the operation or development of the Royalty Properties and have little influence over operation or development" and " The Trustee relies upon the working interest owners for information regarding the Royalty Properties" in the Trust's Annual Report on Form 10-K for the year ended December 31, 2013 for a description of certain risks relating to these

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arrangements and reliance, including filings such as this filing outside the time periods specified notwithstanding effective disclosure controls and procedures of the Trustee regarding information under its control.

The officer acting on behalf of the Trustee has not conducted a separate evaluation of the disclosure controls and procedures with respect to information furnished by the working interest owners. The Trustee notes that it is conducting an ongoing review of certain information and calculations by the working interest owners, along with an outside joint venture auditor. See "Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources" under Item 7 on Form 10-K for the year ended December 31, 2013 for information concerning controls and procedures with respect to the Royalty.

*Changes in Internal Control over Financial Reporting.* In connection with the evaluation by the Trustee of changes in internal control over financial reporting of the Trust that occurred during the Trust's last fiscal quarter, no change in the Trust's internal control over financial reporting was identified that has materially affected, or is reasonably likely to materially affect, the Trust's internal control over financial reporting. The Trustee notes for purposes of clarification that it has no authority over, has not evaluated and makes no statement concerning the internal control over financial reporting of the working interest owners.

**PART II OTHER INFORMATION****Item 1. Legal Proceedings.**

There are no pending legal proceedings to which the Trust is a named party. The Trustee has been advised by PNR, ConocoPhillips and BP that it is subject to litigation in the ordinary course of business for certain matters that include the Royalty Properties. While each of the working interest owners has advised the Trustee that it does not currently believe any of the pending litigation will have a material adverse effect net to the Trust, in the event such matters were adjudicated or settled in a material amount and charges were made against Royalty income, such charges could have a material impact on future Royalty income.

**Item 1A. Risk Factors.**

There have not been any material changes from risk factors previously disclosed in Item 1A to Part 1 of the Trust's Annual Report on Form 10-K for the year ended December 31, 2013.

**Item 6. Exhibits.**

(Asterisk indicates exhibit previously filed with the Securities and Exchange Commission and incorporated herein by reference. The Bank of New York Mellon Trust Company, N.A. is the successor trustee to JPMorgan Chase Bank, N.A. JPMorgan Chase Bank, N.A. was formerly known as The Chase Manhattan Bank and was successor by mergers to the original name of the Trustee, Texas Commerce Bank National Association).

		SEC File or Registration Number	Exhibit Number
4(a)*	Mesa Royalty Trust Indenture between Mesa Petroleum Co. and Texas Commerce Bank National Association, as Trustee, dated November 1, 1979	2-65217	1(a)
4(b)*	Overriding Royalty Conveyance between Mesa Petroleum Co. and Texas Commerce Bank, as Trustee, dated November 1, 1979	2-65217	1(b)
4(c)*	First Amendment to the Mesa Royalty Trust Indenture dated as of March 14, 1985 (Exhibit 4(c) to Form 10-K for year ended December 31, 1984 of Mesa Royalty Trust)	1-7884	4(c)
4(d)*	Form of Assignment of Overriding Royalty Interest, effective April 1, 1985, from Texas Commerce Bank National Association, as Trustee, to MTR Holding Co. (Exhibit 4(d) to Form 10-K for year ended December 31, 1984 of Mesa Royalty Trust)	1-7884	4(d)
4(e)*	Purchase and Sale Agreement, dated March 25, 1991, by and among Mesa Limited Partnership, Mesa Operating Limited Partnership and Conoco, as amended on April 30, 1991 (Exhibit 4(e) to Form 10-K for year ended December 31, 1991 of Mesa Royalty Trust)	1-7884	4(e)
31	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002		
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002		





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