

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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TEXAS PACIFIC LAND TRUST  
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 Quarter Ended September 30, 2018

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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,<br>2018<br>(Unaudited) | December 31,<br>2017 |
|---|--------------------------------------|----------------------|
| <b>ASSETS</b>   |                                      |                      |
| 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           |
| <b>LIABILITIES AND CAPITAL</b>  |                                      |                      |
| 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<br>Ended<br>September 30, |           | Nine Months Ended<br>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<br>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<br>reported<br>in prior<br>year | Retrospective<br>Adjustment | As<br>reported<br>in current<br>year |
|--|------------------------------------|-----------------------------|--------------------------------------|
| Condensed Consolidated Statements<br>of Income:  |                                    |                             |                                      |
| For the three months ended September<br>30, 2017 |                                    |                             |                                      |
| Revenue  | \$42,476                           | \$ 9,501                    | \$51,977                             |
| Taxes, other than income taxes                   | 797                                | (731                        | ) 66                                 |
| Income taxes                                     | 12,687                             | 3,635                       | 16,322                               |
| Net income                                       | 26,405                             | 6,597                       | 33,002                               |
| Net income per Sub-share Certificate             | \$ 3.36                            | \$ 0.84                     | \$4.20                               |

For the nine months ended September  
30, 2017

|                                      |          |           |           |
|--------------------------------------|----------|-----------|-----------|
| Revenue                              | \$94,054 | \$ 20,623 | \$114,677 |
| Taxes, other than income taxes       | 2,219    | (2,036    | ) 183     |
| Income taxes                         | 27,945   | 8,050     | 35,995    |
| Net income                           | 58,002   | 14,609    | 72,611    |
| Net income per Sub-share Certificate | \$ 7.37  | \$ 1.85   | \$9.22    |

Condensed Consolidated Balance  
Sheets:

As of December 31, 2017

Assets:

|                                |           |         |            |
|--------------------------------|-----------|---------|------------|
| Accrued receivables            | \$ 18,206 | \$ (433 | ) \$17,773 |
| Deferred tax asset (liability) | 6,992     | (7,106  | ) (114     |

Liabilities and Capital:

|                     |          |            |           |
|---------------------|----------|------------|-----------|
| Unearned revenue    | \$41,375 | \$ (33,011 | ) \$8,364 |
| Other taxes payable | 433      | (433       | ) —       |

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|                               |        |        |         |
|-------------------------------|--------|--------|---------|
| Net proceeds from all sources | 79,997 | 25,905 | 105,902 |
|-------------------------------|--------|--------|---------|

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## Presentation of Net Periodic Pension Cost

In March 2017, the FASB issued ASU No. 2017-07, "Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost." This ASU requires employers to disaggregate the service cost component from the other components of net benefit cost in the income statement, provides explicit guidance on the presentation of the service cost component and the other components of net benefit cost in the income statement and allows only the service cost component of net benefit cost to be eligible for capitalization. The service cost component is recorded within salaries and related employee benefits expense, and the other components of net benefit costs are recorded in other income.

We adopted the new standard on January 1, 2018 applying the retrospective method. Adoption of the standard using the retrospective method required us to restate certain previously reported results as though the new standard had always been in effect.

## Effects on Operating Income and Other Income from Adoption of New Accounting Standards

Adoption of the standards related to revenue recognition and presentation of net periodic pension cost impacted our previously reported results for operating income and other income as follows (in thousands):

|   | As<br>reported<br>in prior<br>year | Retrospective<br>Adjustment | As<br>reported<br>in current<br>year |
|---|------------------------------------|-----------------------------|--------------------------------------|
| Condensed Consolidated Statements of Income:  |                                    |                             |                                      |
| For the three months ended September 30, 2017 |                                    |                             |                                      |
| Operating income <sup>(1)</sup>               | \$ 39,071                          | \$ 10,235                   | \$ 49,306                            |
| Other income                                  | 20                                 | (2                          | ) 18                                 |
| For the nine months ended September 30, 2017  |                                    |                             |                                      |
| Operating income <sup>(1)</sup>               | \$ 85,907                          | \$ 22,668                   | \$ 108,575                           |
| Other income                                  | 39                                 | (8                          | ) 31                                 |

<sup>(1)</sup> The retrospective adjustment amount includes approximately \$10.2 million and \$22.7 million for the three and nine months ended September 30, 2017, respectively, related to the adoption of the new revenue recognition guidance as discussed above. The retrospective adjustment amount related to the adoption of the presentation of net periodic pension cost had a minimal impact.

## Impact of the 2017 Tax Cuts and Jobs Act on Certain Income Tax Effects

In March 2018, the FASB issued ASU 2018-05, "Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118." The amendments in this update provide guidance on when to record and disclose provisional amounts for certain income tax effects of the 2017 Tax Cuts and Jobs Act ("Tax Reform Act"). The amendments also require any provisional amounts or subsequent adjustments to be included in net income from continuing operations.

Additionally, this ASU discusses required disclosures that an entity must make with regard to the Tax Reform Act. This ASU is effective immediately as new information is available to adjust provisional amounts that were previously recorded. The Trust has adopted this standard and will continue to evaluate indicators that may give rise to a change in our tax provision as a result of the Tax Reform Act.

### 3. Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." This ASU requires lessees to recognize a right of use asset and lease liability on the balance sheet for all leases, with the exception of short-term leases. The new guidance will also require significant disclosures about the amount, timing and uncertainty of cash flows from leases. In January 2018, the FASB issued ASU No. 2018-01, "Land Easement Practical Expedient for Transition to Topic 842" that clarifies the application of the new lease guidance to land easements. The ASU allows an optional transition practical expedient, which if elected, would not require an entity to reassess the accounting treatment on existing or expired land easements not previously accounted for as leases under the current lease guidance. Any new or modified land easements would be evaluated under the new lease guidance upon adoption of the new lease standard. In July 2018, the FASB issued ASU No. 2018-10, "Codification Improvements to Topic 842, Leases" and ASU No. 2018-11, "Leases (Topic 842) — Targeted Improvements" to set forth certain additional practical

expedients for lessors and to provide entities with an option to adopt the new lease standard with a cumulative effect at the adoption date without restating prior periods. The new lease standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, which for the Trust is the first quarter of 2019. The Trust plans to adopt the new lease standard on January 1, 2019 with a cumulative effect at the adoption date. While the assessment of the impact this ASU will have on the consolidated financial statements is ongoing, the Trust does expect to recognize a right of use asset and lease liability for our operating lease commitments on the consolidated balance sheet, but does not expect a significant impact on our consolidated results of operations or cash flows.

In February 2018, the FASB issued ASU 2018-02, "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income (Topic 220)." This ASU allows for stranded tax effects in accumulated other comprehensive income resulting from the Tax Reform Act to be reclassified as retained earnings. This standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Trust is currently evaluating the impact that ASU 2018-02 will have on our consolidated financial statements and disclosures.

In August 2018, the FASB issued ASU 2018-14, "Compensation — Retirement Benefits — Defined Benefit Plans — General (Subtopic 715-20): Disclosure Framework — Changes to Disclosure Requirements for Defined Benefit Plans." The ASU eliminates requirements for certain disclosures and requires additional disclosures under defined benefit pension plans and other post-retirement plans. The ASU is effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The Trust is currently evaluating the impact that ASU 2018-14 will have on our consolidated financial statements and disclosures.

#### 4. Property, Plant and Equipment

Property, plant and equipment, net consisted of the following as of September 30, 2018 and December 31, 2017 (in thousands):

|   | September 30,<br>2018 | December 31,<br>2017 |
|---|-----------------------|----------------------|
| Property, plant and equipment:              |                       |                      |
| Water service-related assets <sup>(1)</sup> | \$ 55,417             | \$ 18,193            |
| Furniture, fixtures and equipment           | 3,927                 | 1,786                |
| Other                                       | 597                   | —                    |
| Property, plant and equipment at cost       | 59,941                | 19,979               |
| Less: accumulated depreciation              | (1,952)               | (463)                |
| Property, plant and equipment, net          | \$ 57,989             | \$ 19,516            |

(1) Water service-related assets reflect assets related to brackish water sourcing and water re-use projects.

Depreciation expense was \$0.7 million and \$1.5 million for the three and nine months ended September 30, 2018, respectively. Depreciation expense was \$0.2 million and \$0.3 million for the three and nine months ended September 30, 2017.

#### 5. Real Estate Activity

##### Land Sales

No value has been assigned to the land held by the Trust other than parcels which have been acquired through foreclosure and a limited number of parcels which have been acquired. Consequently, no allowance for depletion is computed, and no charge to income is made, with respect thereto, and no cost is deducted from the proceeds of the land sales in computing gain or loss thereon.

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During the nine months ended September 30, 2018 and 2017, we completed the following sales of land parcels (in thousands, except number of acres):

| Date of sale                                 | Location         | Approximate number of acres sold | Contract sale price |
|--|------------------|----------------------------------|---------------------|
| For the nine months ended September 30, 2018 |                  |                                  |                     |
| February 2018                                | Loving County    | 40.0                             | \$ 1,150            |
| March 2018                                   | Culberson County | 80.0                             | 1,600               |
| August 2018                                  | El Paso County   | 15.0                             | 270                 |
| September 2018                               | Reeves County    | 31.8                             | 1,273               |
| Total  |                  | 166.8                            | \$ 4,293            |
| For the nine months ended September 30, 2017 |                  |                                  |                     |
| May 2017                                     | Loving County    | 11.02                            | \$ 220              |
| Total  |                  | 11.02                            | \$ 220              |

#### Real Estate Acquired

Real estate acquired included the following activity for the nine months ended September 30, 2018 and 2017 (in thousands, except number of acres):

|                          | Nine Months Ended September 30, 2018 |            | Nine Months Ended September 30, 2017 |            |
|--------------------------|--------------------------------------|------------|--------------------------------------|------------|
|                          | Acres                                | Book Value | Acres                                | Book Value |
| Balance at January 1,    | 10,064.78                            | \$ 1,115   | 10,064.78                            | \$ 1,115   |
| Acquisitions             | 2,883.68                             | 2,663      | —                                    | —          |
| Sales                    | —                                    | —          | —                                    | —          |
| Balance at September 30, | 12,948.46                            | \$ 3,778   | 10,064.78                            | \$ 1,115   |

#### 6. Income Taxes

Effective January 1, 2018, the statutory Federal income tax rate for the Trust decreased from 35% to 21%. The Trust's effective Federal income tax rate is less than the 21% statutory rate because taxable income is reduced by statutory percentage depletion allowed on mineral royalty income.

#### 7. Capital

The Sub-share Certificates ("Sub-shares") and the Certificates of Proprietary Interest are freely interchangeable in the ratio of one Certificate of Proprietary Interest for 3,000 Sub-shares or 3,000 Sub-shares for one Certificate of Proprietary Interest.



## Dividends

On March 16, 2018, we paid \$31.7 million in dividends representing a cash dividend of \$1.05 per Sub-share and a special dividend of \$3.00 per Sub-share for sub-shareholders of record at the close of business on March 9, 2018.

On March 16, 2017, we paid \$10.7 million in dividends representing a cash dividend of \$0.35 per Sub-share and a special dividend of \$1.00 per Sub-share for sub-shareholders of record at the close of business on March 9, 2017.

## Repurchases of Sub-shares

During the nine months ended September 30, 2018, we purchased and retired 39,768 Sub-shares. During the nine months ended September 30, 2017, we purchased and retired 88,272 Sub-shares.

## 8. Business Segment Reporting

During the periods presented, we reported our financial performance based on the following 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. We eliminate any inter-segment revenues and expenses upon consolidation.

The Land and Resource Management segment encompasses the business of managing approximately 890,000 acres of land and related resources in West Texas owned by the Trust. The revenue streams of this segment consist primarily of royalties from oil and gas, revenues from easements and leases, and land sales.

The Water Service and Operations segment encompasses the business of providing a full-service water offering to operators in the Permian Basin as well as managing agreements with energy companies and oilfield service businesses to allow such companies to explore for water, drill water wells, construct water-related infrastructure and purchase water sourced from land that we own. The revenue streams of this segment consist of revenue generated from direct sales of water as well as revenues from royalties on water service-related activity.

Segment financial results were as follows for the three and nine months ended September 30, 2018 and 2017 (in thousands):

|                                       | Three Months Ended September 30, |          | Nine Months Ended September 30, |           |
|---------------------------------------|----------------------------------|----------|---------------------------------|-----------|
|                                       | 2018                             | 2017     | 2018                            | 2017      |
| <b>Revenues:</b>                      |                                  |          |                                 |           |
| Land and resource management          | \$47,513                         | \$42,343 | \$142,642                       | \$93,209  |
| Water service and operations          | 25,655                           | 9,634    | 64,377                          | 21,468    |
| Total consolidated revenues           | \$73,168                         | \$51,977 | \$207,019                       | \$114,677 |
| <b>Net income:</b>                    |                                  |          |                                 |           |
| Land and resource management          | \$36,385                         | \$27,424 | \$109,700                       | \$59,535  |
| Water service and operations          | 14,377                           | 5,578    | 37,356                          | 13,076    |
| Total consolidated net income         | \$50,762                         | \$33,002 | \$147,056                       | \$72,611  |
| <b>Capital expenditures</b>           |                                  |          |                                 |           |
| Land and resource management          | \$909                            | \$1,682  | \$2,464                         | \$2,188   |
| Water service and operations          | 7,533                            | 2,678    | 37,542                          | 5,782     |
| Total capital expenditures            | \$8,442                          | \$4,360  | \$40,006                        | \$7,970   |
| <b>Depreciation and amortization:</b> |                                  |          |                                 |           |
| Land and resource management          | \$160                            | \$104    | \$330                           | \$123     |
| Water service and operations          | 546                              | 105      | 1,189                           | 190       |
| Total depreciation and amortization   | \$706                            | \$209    | \$1,519                         | \$313     |



The following table presents total assets and property, plant and equipment, net by segment as of September 30, 2018 and December 31, 2017 (in thousands):

|   | September 30, December 31, |            |
|---|----------------------------|------------|
|   | 2018                       | 2017       |
| Assets:   |                            |            |
| Land and resource management                          | \$ 141,934                 | \$ 97,549  |
| Water service and operations                          | 77,767                     | 22,486     |
| Total consolidated assets                             | \$ 219,701                 | \$ 120,035 |
| Property, plant and equipment, net                    |                            |            |
| Land and resource management                          | \$ 3,567                   | \$ 1,449   |
| Water service and operations                          | 54,422                     | 18,067     |
| Total consolidated property, plant and equipment, net | \$ 57,989                  | \$ 19,516  |

#### 9. Oil and Gas Producing Activities

There are a number of oil and gas wells that have been drilled but are not yet completed (“DUC”) where the Trust has a royalty interest. Currently, the Trust has identified 303 DUC wells subject to our royalty interest. The process of identifying these wells is ongoing and we anticipate updates going forward to be affected by a number of factors including, but not limited to, ongoing changes/updates to our identification process, changes/updates by Drilling Info (our main source of information in identifying these wells) in their identification process, the eventual completion of these DUC wells, and additional wells drilled but not completed by companies operating where we have a royalty interest.

#### 10. Subsequent Events

We evaluate events that occur after the balance sheet date but before consolidated financial statements are, or are available to be, issued to determine if a material event requires our amending the consolidated financial statements or disclosing the event. We evaluated subsequent events through the filing date we issued these consolidated financial statements and did not identify any subsequent events requiring disclosure.

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

### Cautionary Statement Regarding Forward-Looking Statements

Statements in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding management's expectations, hopes, intentions or strategies regarding the future. Forward-looking statements include statements regarding the Trust's future operations and prospects, the markets for real estate in the areas in which the Trust owns real estate, applicable zoning regulations, the markets for oil and gas, production limits on prorated oil and gas wells authorized by the Railroad Commission of Texas, expected competition, management's intent, beliefs or current expectations with respect to the Trust's future financial performance and other matters. All forward-looking statements in this Report are based on information available to us as of the date this Report is filed with the Securities and Exchange Commission (the "SEC"), and we assume no responsibility to update any such forward-looking statements, except as required by law. All forward-looking statements are subject to a number of risks, uncertainties and other factors that could cause our actual results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward-looking statements. These risks, uncertainties and other factors include, but are not limited to, the factors discussed in Item 1A. "Risk Factors" of Part I of our Annual Report on Form 10-K for the year ended December 31, 2017, and in Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Part II, Item 1A. "Risk Factors" of this Quarterly Report on Form 10-Q.

The following discussion and analysis should be read together with (i) the factors discussed in Item 1A. "Risk Factors" of Part I of our Annual Report on Form 10-K for the year ended December 31, 2017, (ii) the factors discussed in Part II, Item 1A. "Risk Factors," if any, of this Quarterly Report on Form 10-Q and (iii) the Financial Statements, including the Notes thereto, and the other financial information appearing elsewhere in this Report. Period-to-period comparisons of financial data are not necessarily indicative, and therefore should not be relied upon as indicators, of the Trust's future performance. Words or phrases such as "expects" and "believes", or similar expressions, when used in this Form 10-Q or other filings with the SEC, are intended to identify "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995.

### Overview

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. We were organized under a Declaration of Trust, dated February 1, 1888, to receive and hold title to extensive tracts of land in numerous counties in West Texas, previously the property of the Texas and Pacific Railway Company. Our Trustees are empowered under the Declaration of Trust to manage the lands with all the powers of an absolute owner.

Our revenues are derived primarily from oil, gas and water service-related royalties, sales of water and land, easements and leases of the land. Due to the nature of our operations, our revenue is subject to substantial fluctuations from quarter to quarter and year to year. We are a passive seller of land and do not actively solicit sales of land. In addition, the demand for, and sale price of, particular tracts of land is influenced by many factors beyond our control, including general economic conditions, the rate of development in nearby areas and the suitability of the particular tract for the ranching uses prevalent in western Texas.

We are not an oil and gas producer. Rather, our oil and gas revenue is derived from our retained perpetual non-participating oil and gas royalty interests. Thus, in addition to being subject to fluctuations in response to the market prices for oil and gas, our oil and gas royalty revenues are also subject to decisions made by the owners and operators of the oil and gas wells to which our royalty interests relate as to investments in and production from those wells. We monitor production reports by the oil and gas companies to assure that we are being paid the appropriate

royalties. We review conditions in the agricultural industry in the areas in which our lands are located and seek to keep as much of our lands as possible under lease to local ranchers.

Our revenue from easements is generated from easement contracts covering activities such as oil and gas pipelines and subsurface wellbore easements. The majority of our easements have a ten-year term. We also enter into agreements with operators and mid-stream companies to lease land from us, primarily for facilities and roads.

In prior years, we entered into agreements with energy companies and oilfield service businesses to allow such companies to explore for water, drill water wells, construct water-related infrastructure and purchase water sourced from land

that we own. Energy businesses use water for their oil and gas projects while non-energy businesses (i.e., water management service companies) operate water facilities to produce and sell water to energy businesses. We collect revenue from royalties and water sales under these legacy agreements.

Demand for water solutions is expected to grow as drilling and completion activity in the Permian Basin continues to increase. In response to that anticipated demand, the Trust formed Texas Pacific Water Resources LLC (“TPWR”) in June 2017. TPWR, a single member LLC and wholly owned subsidiary of the Trust, focuses on providing full-service water offerings to operators in the Permian Basin. These services include brackish water sourcing, produced-water gathering/treatment/recycling, infrastructure development/construction, disposal, water tracking, analytics and well testing services. TPWR is committed to sustainable water development with significant focus on the large-scale implementation of recycled water operations.

During the nine months ended September 30, 2018, the Trust invested approximately \$27.7 million in TPWR projects to develop brackish water sourcing and water re-use assets.

### Results of Operations

We operate our business in two segments: Land and Resource Management and Water Service and Operations. We eliminate any inter-segment revenues and expenses upon consolidation.

We analyze financial results for each of our reportable segments. The reportable segments presented are consistent with our reportable segments discussed in Note 8, “Business Segment Reporting” in Item 1. Financial Statements in this Quarterly Report on Form 10-Q. We monitor our reporting segments based upon revenue and net income calculated in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

For the three months ended September 30, 2018 as compared to the three months ended September 30, 2017

Revenues. Revenues increased \$21.2 million, or 40.8%, to \$73.2 million for the three months ended September 30, 2018 compared to \$52.0 million for the three months ended September 30, 2017. Net income increased \$17.8 million, or 53.8%, to \$50.8 million for the three months ended September 30, 2018 compared to \$33.0 million for the three months ended September 30, 2017.

The following is an analysis of our operating results for the comparable periods by reportable segment (in thousands):

|                               | Three months ended September |       |          |       |
|-------------------------------|------------------------------|-------|----------|-------|
|                               | 30,                          |       | 2017     |       |
|                               | 2018                         |       | 2017     |       |
| Revenues:                     |                              |       |          |       |
| Land and resource management: |                              |       |          |       |
| Oil and gas royalties         | \$31,253                     | 43 %  | \$20,481 | 39 %  |
| Easements and sundry income   | 14,591                       | 20 %  | 21,737   | 42 %  |
| Land sales and other income   | 1,669                        | 2 %   | 125      | — %   |
|                               | 47,513                       | 65 %  | 42,343   | 81 %  |
| Water service and operations: |                              |       |          |       |
| Water sales and royalties     | 18,178                       | 25 %  | 7,917    | 15 %  |
| Easements and sundry income   | 7,477                        | 10 %  | 1,717    | 4 %   |
|                               | 25,655                       | 35 %  | 9,634    | 19 %  |
| Total consolidated revenues   | \$73,168                     | 100 % | \$51,977 | 100 % |
| Net income:                   |                              |       |          |       |
| Land and resource management  | \$36,385                     | 72 %  | \$27,424 | 83 %  |
| Water service and operations  | 14,377                       | 28 %  | 5,578    | 17 %  |

Total consolidated net income    \$50,762 100%    \$33,002 100%



## Land and Resource Management

Land and Resource Management segment revenues increased \$5.2 million, or 12.2%, to \$47.5 million for the three months ended September 30, 2018 as compared with \$42.3 million for the comparable period of 2017.

Oil and gas royalties. Oil and gas royalty revenue was \$31.3 million for the three months ended September 30, 2018 compared to \$20.5 million for the three months ended September 30, 2017. Oil royalty revenue was \$24.1 million for the three months ended September 30, 2018 compared to \$17.0 million for the comparable period of 2017. This increase in oil royalty revenue is principally due to the combined effect of a 98.9% increase in crude oil production subject to the Trust's royalty interest, and a 31.0% increase in the average price per royalty barrel of crude oil received during the three months ended September 30, 2018 compared to the same period in 2017. Gas royalty revenue was \$7.1 million for the three months ended September 30, 2018, an increase of 102.8% over the three months ended September 30, 2017 when gas royalty revenue was \$3.5 million. This increase in gas royalty revenue resulted from a volume increase of 174.7% for the three months ended September 30, 2018 as compared to the same period of 2017, partially offset by a 26.5% decrease in the average price received. Additionally, oil and gas royalties for the three months ended September 30, 2017 included \$7.7 million related to an arbitration settlement with Chevron U.S.A., Inc. (the "Chevron Settlement") in September 2017.

Easements and sundry income. Easements and sundry income was \$14.6 million for the three months ended September 30, 2018, a decrease of 32.9% compared to \$21.7 million for the three months ended September 30, 2017. Easements and sundry income includes pipeline easement income, seismic and temporary permit income, lease rental income and income from material sales. The decrease in easements and sundry income is principally related to the decrease in pipeline easement income which decreased 42.5% to \$9.1 million for the three months ended September 30, 2018 compared to the three months ended September 30, 2017. Easements and sundry income is unpredictable and may vary significantly from period to period. Effective January 1, 2018, the Trust adopted the new revenue recognition accounting standard using the full retrospective method, and no longer defers revenue on its term easements. See more discussion in Note 2, "Summary of Significant Accounting Policies — Recently Adopted Accounting Guidance" for further discussion and analysis of impact on our condensed consolidated financial statements.

Land sales and other income. Land sales and other income includes revenue generated from land sales and grazing leases. For the three months ended September 30, 2018, we sold approximately 46.83 acres of land for total consideration of \$1.5 million, or approximately \$32,953 per acre. There were no land sales for the three months ended September 30, 2017.

Net income. Net income for the Land and Resource Management segment was \$36.4 million for the three months ended September 30, 2018 compared to \$27.4 million for the three months ended September 30, 2017. As discussed above, revenues for the Land and Resource Management segment increased \$5.2 million for the three months ended September 30, 2018 compared to the same period of 2017. Expenses, including income tax expense, for the Land and Resource Management segment were \$11.1 million and \$14.9 million for the three months ended September 30, 2018 and 2017, respectively. This decrease in expenses was principally due to the decrease in income tax expense related to the change in the federal income tax rate from 35% to 21% effective January 1, 2018 and an overall decrease in legal and professional fees. For the three months ended September 30, 2017, we incurred consulting fees related to a strategic review of the Trust. No such consulting fees were incurred for the three months ended September 30, 2018. See further discussion of these expenses below under "Other Financial Data — Consolidated."

## Water Service and Operations

Water Service and Operations segment revenues increased \$16.0 million, or 166.3%, to \$25.7 million for the three months ended September 30, 2018 as compared with \$9.6 million for the comparable period of 2017.

Water sales and royalties. Water sales and royalty revenues for the three months ended September 30, 2018 of \$18.2 million were more than double the amount of revenue for the comparable period of 2017. This increase is due to the Trust commencing development of brackish water sourcing, partially offset by a decrease in the royalties received from existing legacy agreements.

Easements and sundry income. Easements and sundry income for the Water Service and Operations segment includes pipeline easement royalties, lease royalties and income from temporary permits. For the three months ended September 30, 2018, the combined revenue from these revenue streams was \$7.5 million compared to \$1.7 million for the three months ended September 30, 2017.

Net income. Net income for the Water Service and Operations segment was \$14.4 million for the three months ended September 30, 2018 compared to \$5.6 million for the three months ended September 30, 2017. As discussed above, revenues for the Water Service and Operations segment increased \$16.0 million for the three months ended September 30, 2018 compared to the same period of 2017. Expenses for the Water Service and Operations segment were \$11.3 million and \$4.1 million for the three months ended September 30, 2018 and 2017, respectively. The increase in expenses during 2018 is directly related to the formation and commencement of operations of TPWR during the second quarter of 2017 and operating expenses related to the brackish water sourcing and water re-use projects placed in service in 2018 and late 2017. See further discussion of these water service-related operating expenses below under “Other Financial Data — Consolidated.”

#### Other Financial Data — Consolidated

Salaries and related employee benefits. Salaries and related employee benefits were \$3.7 million for the three months ended September 30, 2018 compared to \$0.7 million for the comparable period of 2017. The increase in salaries and related employee benefits is directly related to the increase in the number of employees from 17 employees as of September 30, 2017 to 58 as of September 30, 2018 and additional contract labor expenses for the three months ended September 30, 2018 compared to the same period of 2017.

Water service-related expenses. Water service-related expenses of \$3.7 million for the three months ended September 30, 2018, include expenses for equipment rental, propane and fuel and other equipment-related expenses associated with the brackish water sourcing and water re-use projects placed in service in 2018 and late 2017. The Trust incurred minimal water service-related expenses during the three months ended September 30, 2017.

General and administrative expenses. General and administrative expenses increased \$0.9 million to \$1.4 million for the three months ended September 30, 2018 from \$0.5 million for the same period of 2017. The increase in general and administrative expenses is primarily due to additional liability insurance and equipment costs as a result of the opening of an additional office in Midland, Texas for our TPWR operations during the second quarter of 2017.

Legal and professional expenses. Legal and professional fees decreased \$0.4 million to \$0.6 million for the three months ended September 30, 2018 from \$1.0 million for the comparable period of 2017. Legal and professional fees for the three months ended September 30, 2017 included consulting fees related to a 2017 strategic review of the Trust.

Depreciation and amortization. Depreciation and amortization was \$0.7 million for the three months ended September 30, 2018 compared to \$0.2 million for the three months ended September 30, 2017. The increase in depreciation and amortization is principally related to the Trust’s investment in water service-related assets during 2017 and 2018.

For the nine months ended September 30, 2018 as compared to the nine months ended September 30, 2017

Revenues. Revenues increased \$92.3 million, or 80.5%, to \$207.0 million for the nine months ended September 30, 2018 compared to \$114.7 million for the nine months ended September 30, 2017. Net income increased \$74.4 million, or 102.5%, to \$147.1 million for the nine months ended September 30, 2018 compared to \$72.6 million for the nine months ended September 30, 2017.

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The following is an analysis of our operating results for the comparable periods by reportable segment (in thousands):

|                               | Nine Months Ended September 30, |       |           |       |  |  |
|-------------------------------|---------------------------------|-------|-----------|-------|--|--|
|                               | 2018                            |       |           | 2017  |  |  |
| Revenues:                     |                                 |       |           |       |  |  |
| Land and resource management: |                                 |       |           |       |  |  |
| Oil and gas royalties         | \$88,078                        | 43 %  | \$43,252  | 38 %  |  |  |
| Easements and sundry income   | 49,896                          | 24 %  | 49,363    | 43 %  |  |  |
| Land sales and other income   | 4,668                           | 2 %   | 594       | — %   |  |  |
|                               | 142,642                         | 69 %  | 93,209    | 81 %  |  |  |
| Water service and operations: |                                 |       |           |       |  |  |
| Water sales and royalties     | 47,428                          | 23 %  | 19,584    | 17 %  |  |  |
| Easements and sundry income   | 16,949                          | 8 %   | 1,884     | 2 %   |  |  |
|                               | 64,377                          | 31 %  | 21,468    | 19 %  |  |  |
| Total consolidated revenues   | \$207,019                       | 100 % | \$114,677 | 100 % |  |  |
| Net income:                   |                                 |       |           |       |  |  |
| Land and resource management  | \$109,700                       | 75 %  | \$59,535  | 82 %  |  |  |
| Water service and operations  | 37,356                          | 25 %  | 13,076    | 18 %  |  |  |
| Total consolidated net income | \$147,056                       | 100 % | \$72,611  | 100 % |  |  |

#### Land and Resource Management

Land and Resource Management segment revenues increased \$49.4 million, or 53.0%, to \$142.6 million for the nine months ended September 30, 2018 as compared with \$93.2 million for the comparable period of 2017.

**Oil and gas royalties.** Oil and gas royalty revenue was \$88.1 million for the nine months ended September 30, 2018 compared to \$43.3 million for the nine months ended September 30, 2017. Oil royalty revenue was \$69.0 million for the nine months ended September 30, 2018 compared to \$33.4 million for the comparable period of 2017. This increase in oil royalty revenue is principally due to the combined effect of a 115.2% increase in crude oil production subject to the Trust's royalty interest, and a 24.2% increase in the average price per royalty barrel of crude oil received during the nine months ended September 30, 2018 compared to the same period in 2017. Gas royalty revenue was \$19.1 million for the nine months ended September 30, 2018, an increase of 94.5% over the nine months ended September 30, 2017 when gas royalty revenue was \$9.8 million. This increase in gas royalty revenue resulted from a volume increase of 156.8% for the nine months ended September 30, 2018 as compared to the same period of 2017, partially offset by a 24.8% decrease in the average price received. Additionally, oil and gas royalties for the nine months ended September 30, 2017 included \$7.7 million related to the Chevron Settlement in September 2017.

**Easements and sundry income.** Easements and sundry income was \$49.9 million for the nine months ended September 30, 2018, an increase of 1.1% compared to \$49.4 million for the nine months ended September 30, 2017. Easements and sundry income includes pipeline easement income, seismic and temporary permit income, lease rental income and income from material sales. The increase in easements and sundry income is principally related to the increase in material sales which increased 29.6% to \$4.9 million for the nine months ended September 30, 2018 from \$3.7 million for the nine months ended September 30, 2017. Easements and sundry income is unpredictable and may vary significantly from period to period. Effective January 1, 2018, the Trust adopted the new revenue recognition accounting standard using the full retrospective method, and no longer defers revenue on its term easements. See more discussion in Note 2, "Summary of Significant Accounting Policies — Recently Adopted Accounting Guidance" for further discussion and analysis of impact on our condensed consolidated financial statements.

**Land sales and other income.** Land sales and other income includes revenue generated from land sales and grazing leases. For the nine months ended September 30, 2018, we sold approximately 167 acres of land for total consideration of \$4.3 million, or approximately \$25,734 per acre. For the nine months ended September 30, 2017, we sold approximately 11.02 acres of land for total consideration of \$0.2 million, or approximately \$20,000 per acre.



Net income. Net income for the Land and Resource Management segment was \$109.7 million for the nine months ended September 30, 2018 compared to \$59.5 million for the nine months ended September 30, 2017. As discussed above, revenues for the Land and Resource Management segment increased \$49.4 million for the nine months ended September 30, 2018 compared to the same period of 2017. Expenses, including income tax expense, for the Land and Resource Management segment were \$32.9 million and \$33.7 million for the nine months ended September 30, 2018 and 2017, respectively. This decrease in expenses was principally due to the decrease in income tax expense related to the change in the federal income tax rate from 35% to 21% effective January 1, 2018 partially offset by increased salaries and related employee benefits and general and administrative expenses. See further discussion of these expenses below under “Other Financial Data — Consolidated.”

#### Water Service and Operations

Water Service and Operations segment revenues increased \$42.9 million, or 199.9%, to \$64.4 million for the nine months ended September 30, 2018 as compared with \$21.5 million for the comparable period of 2017.

Water sales and royalties. Water sales and royalty revenues for the nine months ended September 30, 2018 of \$47.4 million were more than double the amount of revenue for the comparable period of 2017. This increase is due to the Trust commencing the development of brackish water sourcing, partially offset by a decrease in the royalties received from existing legacy agreements.

Easements and sundry income. Easements and sundry income for the Water Service and Operations segment includes pipeline easement royalties, lease royalties and income from temporary permits. For the nine months ended September 30, 2018, the combined revenue from these revenue streams was \$16.9 million as compared to \$1.9 million for the nine months ended September 30, 2017.

Net income. Net income for the Water Service and Operations segment was \$37.4 million for the nine months ended September 30, 2018 compared to \$13.1 million for the nine months ended September 30, 2017. As discussed above, revenues for the Water Service and Operations segment increased \$42.9 million for the nine months ended September 30, 2018 compared to the same period of 2017. Expenses for the Water Service and Operations segment were \$27.0 million for the nine months ended September 30, 2018 as compared to \$8.4 million for the nine months ended September 30, 2017. The increase in expenses during 2018 is directly related to the formation and commencement of operations of TPWR during the second quarter of 2017 and operating expenses related to the brackish water sourcing and water re-use projects placed in service in 2018 and late 2017. See further discussion of these water service-related operating expenses below under “Other Financial Data — Consolidated.”

#### Other Financial Data — Consolidated

Salaries and related employee benefits. Salaries and related employee benefits were \$9.5 million for the nine months ended September 30, 2018 compared to \$1.6 million for the comparable period of 2017. The increase in salaries and related employee benefits is directly related to the increase in the number of employees from 17 employees as of September 30, 2017 to 58 as of September 30, 2018 and additional contract labor expenses for the nine months ended September 30, 2018 compared to the same period of 2017.

Water service-related expenses. Water service-related expenses of \$7.6 million for the nine months ended September 30, 2018, include expenses for equipment rental, propane and fuel and other equipment-related expenses associated with the brackish water sourcing and water re-use projects placed in service in 2018 and late 2017. The Trust incurred only minimal water service-related expenses during the nine months ended September 30, 2017.

General and administrative expenses. General and administrative expenses increased \$2.3 million to \$3.4 million for the nine months ended September 30, 2018 from \$1.1 million for the same period of 2017. The increase in general and administrative expenses is primarily due to additional liability insurance and equipment costs as a result of the formation and commencement of operations of TPWR during the second quarter of 2017.

Legal and professional expenses. Legal and professional fees decreased 38.3% to \$1.6 million for the nine months ended September 30, 2018 from \$2.6 million for the comparable period of 2017. Legal and professional fees for the nine months ended September 30, 2017 included consulting fees related to a 2017 strategic review of the Trust.

Depreciation and amortization. Depreciation and amortization was \$1.5 million for the nine months ended September 30, 2018 compared to \$0.3 million for the nine months ended September 30, 2017. The increase in depreciation and amortization is principally related to the Trust's investment in water service-related assets during 2017 and 2018.

### Cash Flow Analysis

For the nine months ended September 30, 2018 as compared to the nine months ended September 30, 2017 Cash flows provided by operating activities for the nine months ended September 30, 2018 and 2017 were \$130.8 million and \$65.9 million, respectively. This increase in operating cash flows is principally due to increases in oil and gas royalties collected, easements and sundry payments received and water sales and royalties collected during the nine months ended September 30, 2018 compared to the nine months ended September 30, 2017.

Cash flows used in investing activities were \$42.6 million compared to \$7.9 million for the nine months ended September 30, 2018 and 2017, respectively. The increased use of investing cash flows is due to our investment of \$37.2 million in water service-related assets during the nine months ended September 30, 2018.

Cash flows used in financing activities were \$57.2 million compared to \$37.8 million for the nine months ended September 30, 2018 and 2017, respectively. During the nine months ended September 30, 2018, the Trust paid total dividends of \$31.7 million consisting of a cash dividend of \$1.05 per Sub-share Certificate (“Sub-share”) and a special dividend of \$3.00 per Sub-share to each sub-shareholder of record at the close of business on March 9, 2018. During the nine months ended September 30, 2017, the Trust paid total dividends of \$10.7 million consisting of a cash dividend of \$0.35 per Sub-share and a special dividend of \$1.00 per Sub-share to each sub-shareholder of record at the close of business on March 9, 2017.

### Liquidity and Capital Resources

The Trust’s principal sources of liquidity are its revenues from oil, gas and water service-related royalties, easements and sundry income, and water and land sales.

Our primary liquidity and capital requirements are for capital expenditures related to our water service and operations segment, working capital and general corporate needs. As of September 30, 2018, we had cash and cash equivalents of \$110.6 million that we expect to utilize, along with cash flow from operations, to provide capital to support the growth of our business, particularly the growth of TPWR, to repurchase additional Sub-shares subject to market conditions, and for general corporate purposes. We believe that cash from operations, together with our cash and cash equivalents balances, will be enough to meet ongoing capital expenditures, working capital requirements and other cash needs for the foreseeable future.

### Off-Balance Sheet Arrangements

The Trust has not engaged in any off-balance sheet arrangements.

### Critical Accounting Policies and Estimates

This discussion and analysis of our financial condition and results of operations is based on our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and disclosures of contingent assets and liabilities. For a full discussion of our accounting policies please refer to Note 2 to the Consolidated Financial Statements included in our 2017 Annual Report on Form 10-K filed with the SEC on February 28, 2018. Our most critical accounting policies and estimates include: valuation of real estate acquired through foreclosure and gain on recognition on land sales. We continually evaluate our judgments, estimates and assumptions. We base our estimates on the terms of underlying agreements, historical experience and other factors that we believe are reasonable based on the circumstances, the results of which form our management’s basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. There have been no material changes to our critical accounting policies and estimates from the information provided in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations included in our 2017 Annual Report on Form 10-K.



New Accounting Pronouncements

For further information regarding recently issued accounting pronouncements, see Note 3, “Recent Accounting Pronouncements” in the notes to the consolidated financial statements included in Item 1. Financial Statements in this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in the information related to market risk of the Trust since December 31, 2017.

Item 4. Controls and Procedures

Pursuant to Rule 13a-15, management of the Trust under the supervision and with the participation of Tyler Glover, the Trust's Chief Executive Officer, and Robert J. Packer, the Trust's Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of the Trust's disclosure controls and procedures as of the end of the Trust's fiscal quarter covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, Mr. Glover and Mr. Packer concluded that the Trust's disclosure controls and procedures are effective in timely alerting them to material information relating to the Trust required to be included in the Trust's periodic SEC filings.

There have been no changes in the Trust's internal control over financial reporting during the Trust's most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Trust's internal control over financial reporting.

PART II  
OTHER INFORMATION

Item 1. Legal Proceedings.

Texas Pacific is not involved in any material pending legal proceedings.

Item 1A. Risk Factors

There have been no material changes in the risk factors previously disclosed in response to Item 1A. "Risk Factors" of Part I of the Trust's Annual Report on Form 10-K for the year ended December 31, 2017.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the three months ended September 30, 2018, the Trust repurchased Sub-shares as follows:

| Period                                 | Total Number of Sub-shares Purchased | Average Price Paid per Sub-share | Total Number of Sub-shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number (or Approximate Dollar Value) of Sub-shares that May Yet Be Purchased Under the Plans or Programs |
|--|--------------------------------------|----------------------------------|--|--|
| July 1 through July 31, 2018           | 4,111                                | \$ 767.01                        | —  | —  |
| August 1 through August 31, 2018       | 4,839                                | 795.31                           | —  | —  |
| September 1 through September 30, 2018 | 1,756                                | 834.18                           | —  | —  |
| Total                                  | 10,706                               | \$ 790.82                        | —  | —  |

(1) The Trust purchased and retired 10,706 Sub-shares in the open market during the three months ended September 30, 2018.

Item 3. Defaults Upon Senior Securities

Not applicable

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None



Item 6. Exhibits

EXHIBIT INDEX

EXHIBIT  
NUMBER DESCRIPTION

31.1\* Rule 13a-14(a) Certification of Chief Executive Officer.

31.2\* Rule 13a-14(a) Certification of Chief Financial Officer.

32.1\* Certification of Chief Executive Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2\* Certification of Chief Financial Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101\* The following information from the Trust's Quarterly Report on Form 10-Q for the quarter ended September 30, 2018 formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets; (ii) Condensed Consolidated Statements of Income and Total Comprehensive Income, (iii) Condensed Consolidated Statements of Cash Flows and (iv) Notes to Condensed Consolidated Financial Statements.

\* Filed or furnished herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TEXAS PACIFIC LAND TRUST  
(Registrant)

Date: November 7, 2018 By: /s/ Tyler Glover  
Tyler Glover, General Agent and  
Chief Executive Officer

Date: November 7, 2018 By: /s/ Robert J. Packer  
Robert J. Packer, General Agent and  
Chief Financial Officer