

State bid for water deals gets first test

Top officials split over plan to pump for profit in arid far West Texas
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A group of Midland oil men, joined by telecommunications millionaire Steve Smith of Austin, wants to lease 646,508 acres of state land in far West Texas -- but not for the usual purposes of oil and gas drilling or ranching.

Like other oil men these days, they're after water.

The partnership, Rio Nuevo Ltd., is the first private group to apply to the General Land Office for a lease to pump and export ground water from aquifers underneath state land in six counties. The School Land Board, an affiliate of the land office, will discuss Rio Nuevo's request Tuesday, but no vote is expected.

The negotiations are the first test of Land Commissioner Jerry Patterson's plan to strike water deals to produce more revenue from state-owned land for education, beyond the traditional sources of oil and gas royalties and ranch leases.

"It's a stand-up deal," Patterson said of Rio Nuevo's lease application. "This land, nobody has ever offered to lease it. These people want to write us a big check and royalty payments. I have a fiduciary obligation to look at that."

Agriculture Commissioner Susan Combs isn't sure the lease is a good idea. Combs, whose office oversees rural economic development, as well as farming and ranching, said large-scale pumping in drought-stricken far West Texas would devastate the region, which includes Big Bend National Park.

"You have truly irreplaceable features that depend on water in that land," she said.

Combs and West Texas water planners are also concerned because it isn't clear that Rio Nuevo will have to obey local ground water district rules on pumping and space between wells. If a leaseholder can disregard local rules, Combs said, Texas' system of ground water regulation collapses.

Combs also cautioned that the land office "has not so far had any demonstrated expertise in the area of ground water."

"So before they embark on this new adventure, I hope they would take a lot of time and look at all the issues," she said.

Combs has a family ranch in Brewster County, but it's not near the land Rio Nuevo wants to lease.

Rio Nuevo doesn't have customers -- at least none it will disclose -- and it's not clear that it has a viable plan for any water it pumps. None of the partners would comment for this story.

The partnership has ambitious plans. Rio Nuevo intends to pump at least 50,000 acre feet of water a year, or 16.3 billion gallons, from aquifers in the region known as the West Texas Bolsons, the land office says.

The biggest question is whether Rio Nuevo would have to abide by the rules of local ground water districts. Three districts, in Presidio, Jeff Davis and Brewster counties, govern land that Rio Nuevo wants to lease; the group also wants to pump water in El Paso, Culberson and Hudspeth counties.

In passing a landmark water law in 1997, the Legislature said local districts are the preferred method of regulating ground water and gave them the power to curb pumping and limit how far apart wells are located.

Commissioner Patterson said land office lawyers are researching the issue of whether state leaseholders must obey ground water district rules.

Tom Beard, an Alpine rancher and lawyer who chairs the state-created Far West Texas Regional Water Planning Group, said residents are frustrated by the lack of information about Rio Nuevo's plans and its negotiations with the land office.

The proposed deal, Beard said, is "flying in the face of three major policies of the state:" Negotiations aren't being done in public, local water districts haven't been told anything about the proposal, and the Far West Texas planning group, which is supposed to set policy, hasn't been consulted.

"I think that's terrible public policy," Beard said.

Beard said some West Texans are also wary of Rio Nuevo's political connections.

One reason is the financial tie between some Rio Nuevo partners and House Speaker Tom Craddick, R-Midland.

Four partners in Rio Nuevo are executives with Falcon Bay Operating LLC, which has an oil and gas exploration agreement with Mexco Energy Corp., where Craddick has been a director since 1998. He also owns \$204,000 worth of stock and has a consulting deal with Falcon Bay on an unrelated natural-gas prospect. Falcon Bay President Mike Ford is a lead investor in Rio Nuevo.

Craddick said he has no financial interest in the water partnership, nor is he familiar with its application to lease state land. He also said Falcon Bay has no financial interest in the water deal.

"I haven't looked at what they're doing," Craddick said. The only financial tie, he said, is that he is a director of Mexco, which has one joint venture with Falcon Bay amid many other deals the companies are exploring independently.

Patterson said he asked Craddick directly if he was involved with Rio Nuevo, "and he told me, 'No,'" Patterson said.

It's unclear how much money the state would earn from the deal. In its application, Rio Nuevo offered 20 cents an acre for rights to lease the land, about \$129,000. Patterson said the state would also earn royalties from the sale of water, but the split hasn't been determined.

Some of Rio Nuevo's partners have financial muscle.

Smith made an estimated \$100 million-plus on the 1998 sale of his stake in long-distance company Excel Communications, and he's best known for building an upscale resort in the West Texas desert town of Lajitas, which he owns. Another partner, Roger Abel, recently retired from a long career in the oil business, including stints as head of Conoco's European operations and a top position at energy giant Occidental Petroleum Corp.

During the regular legislative session, the partnership hired lobbyist Bill Messer to successfully lobby for a state law that would allow it to transport ground water down the Rio Grande to downstate customers. Some Rio Grande Valley farmers and communities also backed the bill.

Transporting water via a river is wasteful because so much evaporates. Patterson said Rio Nuevo has abandoned that idea, and that his office wouldn't sign any lease that would allow underground water to be dumped into a river for transport.

Instead, HillCo Partners' Alexis DeLee, Rio Nuevo's spokeswoman, said the partners intend to finance construction of a pipeline to customers and treatment plants for the water.

Some water experts are skeptical.

"Rio Nuevo wouldn't be the first group of oilmen to try their hand in the water business," said Jace Houston, general counsel for the Harris-Galveston Coastal Subsidence District, a Friendswood-based water authority. "So far, the efforts of these groups have only lended support to the old adage that oil and water don't mix."

A number of oil and gas men are exploring water deals.

In Hudspeth County east of El Paso, Denver billionaire Philip Anschutz and El Paso construction magnate Woody Hunt are considering selling water under land they own. Boone Pickens, the corporate raider and oil millionaire, is trying to find customers for water rights he holds in the Panhandle. He's had no takers, but he has an agreement with the Brazos River Authority to explore deals.

Houston said, "If I were doing a large water deal, I would want someone on my team like a river authority or other major water provider who has actually been through the difficult process of building consensus for a major water project. Water projects affect local citizens in an entirely different way than oil and gas projects."

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What is Rio Nuevo Ltd.?

The Midland-based partnership incorporated last year, intending to pool investments for water deals. Its partners include:

Mike Ford, Midland, president, Falcon Bay Operating LLC

Gary Martin, Midland, energy, investments

Roger Abel, Austin, former president and CEO, Occidental Petroleum Corp.'s oil and gas subsidiary

Robert Canon, Midland, Falcon Bay Operating LLC

Steve Smith, Austin, investor; owns 25,000 acres, including a resort, in Lajitas

Anthony Sam, Midland, vice president, Falcon Bay Operating LLC

Steve Cole, Midland, Falcon Bay Operating LLC

Kyle McDonnold, Midland, lawyer

Sources: Texas secretary of state; SEC filings