**DIAMONDBACK Energy**

April 8, 2020

The Honorable Chairman Wayne Christian
The Honorable Commissioner Christi Craddick
The Honorable Commissioner Ryan Sitton
Railroad Commission of Texas
P.O. Box 12967
Austin, Texas 78711-2967

electronically via RRCconference@rrc.texas.gov

Subject: *Comments on Motion Requesting a Market Demand Hearing and Market Demand Order Effective for May 2020 Production (the "Motion") and Request to testify.*

Dear Chairman Christian and Commissioners Craddick and Sitton:

Diamondback Energy, Inc. ("Diamondback" or the "Company") is an independent oil and natural gas company headquartered in Midland, Texas. We are one of the fastest growing and most efficient operators in the Permian Basin, having grown from less than 3,000 barrels of net production per day in 2012 to over 300,000 barrels per day today. This growth has been predicated on being a low-cost operator, and we firmly believe that in a commodity-based business, the low-cost operator wins. In addition to being dedicated industry professionals, we are Texans first and foremost. Diamondback employs over 700 people today after starting with less than ten, and we believe that a competitive free market is what provides for the stewardship of the land and resource of our great state. Therefore, after detailed review of the Motion, Diamondback is opposed to the Railroad Commission ("RRC" or the "Commission") issuing any rule or order prorating production of oil and gas in the State of Texas to meet reasonable market demand.

As the Motion indicates, the Texas Natural Resource Code (TNRC) Sec. 85.046(10) defines production in excess of reasonable market demand as "waste." Our industry has constantly endured time periods where supply has outstripped demand, and vice versa, hence the highly cyclical nature of our business. Our industry, through the free market, has always reacted to these imbalances by calling on production growth and capital spend if demand exceeds supply, and calling for a reduction in capital spend and production when the opposite is true.

Today, given current oil prices, the market is clearly calling for less capital spend and less production, which is happening in real time. The global market, including here in Texas, with no intervention from the government, is already in a massive correction: US listed public operators have already cut capital by an average of at least 40% versus original budget expectations, over 100 operated drilling rigs have been dropped in North America in the last two weeks (over 60 last week alone), economic shut-ins on an individual well basis are occurring, and, in some cases, force majeure has been declared by some North American refineries to cut back on their feedstock given lack of downstream demand. There are thousands of planned wells that will not be drilled as a result of the economic and health crisis our world is currently facing, and the effects of this crisis will not, and should not, be limited to the Permian Basin or other Texas oilfields versus the rest of the world or the United States.

The free market is efficiently and effectively taking out millions of barrels per day of higher cost oil production in real-time, just as a free market is designed to do. Just yesterday, one of the largest oil and gas operators in the United States announced it was curtailing its production by ~30% for two months due to economic reasons. The market is working as quickly as it ever has in our industry's history, and the Commission determining the reasonable market demand in Texas and then instituting a prorationing of production is merely an unnecessary and symbolic gesture.

Global oil supply and demand have rarely ever been in balance, implying for all the years that supply outstripped demand, there was "waste." This includes the last four years when production growth from the United States, primarily from Texas, outstripped global oil demand growth and OPEC cut their production to try to balance the oil market. This production growth increased US market share at the expense of the OPEC cartel, which has controlled prices for almost fifty years through its manipulation of production levels, the antithesis of a free market practice. Supply and demand were also imbalanced in the late 1980s, 2001, and during the Great Recession in 2008 and 2009, but there were no calls to prorate production through regulation during these prolonged industry recessions, instead the free market corrected these imbalances.

We agree that global supply is significantly greater than global demand today due in large part to the massive demand shock associated with the global coronavirus pandemic, but that should not be a call to arms for the Commission to interfere in the economy and institute proration. It is simply not necessary and, in the long run, will prove to be harmful to the industry and our global competitiveness.

Global demand for oil is expected to be oversupplied by between 15 and 20 million barrels per day in the second quarter of 2020, far outweighing the impact of a cut of all of Texas' production of over 5 million barrels per day, let alone a symbolic cut of 10% - 20% of current production. Unfortunately for the majority of producers in Texas, even if production is cut by 20% throughout the state, there will still be significant forced shut-ins due to economics or lack of market access. Further, the market demand for oil in Texas has always been exceeded by supply produced in the state. Texas, as a standalone economy, would be the sixth or seventh largest oil exporter in the world, which is what has fueled this great state's economy for generations, and will for many more. The status of the state of Texas as a net exporter has never been deemed "waste," and this should not be the time to start.

The assertion that without government action, Texas operators will "shut-in wells in an *ad hoc* and haphazard manner that will heighten industry disruption and cause economic waste" is a theory laid out in the Motion. In reality, no sign of such operational chaos is occurring. It is absolutely incumbent upon the RRC to ensure fairness of rules and access of production for all complying operators in Texas. The assertion that "the Commission must act promptly to ensure the shut-in process takes place in an equitable and orderly manner" is essentially asking the public sector to step-in and interfere in the private, free market that is the lifeblood of this state's economy. The Motion itself makes the argument that such action is inappropriate and unnecessary. Specifically, paragraph 8 of the Motion states that the oil marketers have already requested "that suppliers take steps to reduce oil production in response to the pandemic because of the impact on supply and transportation chains" on a case by case basis. This economic practice and mechanism is working exactly as it should be, with oil marketers using their legal contracts with various operators as the baseline to determine any potential curtailments. Can the Commission really pro-rate production better, more fairly and more orderly than the producers and marketers looking at their internal sales and transportation contracts, well-level costs, well-level production data, lease obligations, hedge positions, and crude blends when determining what needs to be shut in?

Simply put, interference by the government to choose the business winners and losers will have unintended consequences that are completely avoidable and not remotely necessary or supported by any data or economic forecast. Diamondback specifically has signed multi-year firm sales agreements with our large marketing partners to ensure almost all of our oil production flows in both good times and bad. We have strategically invested over $300 million towards the construction of new pipelines to transport our oil production from West Texas to the Gulf Coast to ensure our barrels are made available to the most liquid markets in the world. These investments have been made on behalf of our shareholders, who own the Company, to ensure their investment in Diamondback is made safer as a result of these investments. Our willingness, along with the willingness of others in our industry, to purchase this "flow assurance" directly improves the infrastructure that has allowed this industry to grow and thrive. Should the government intervene in this process, rather than the free market, our shareholders will evaluate their investments in oil and gas in Texas differently. We have already heard from some of our largest shareholders that even the concept of prorationing being debated has led them to reconsider the cost of allocating capital to Texas operators versus other opportunities in global oil and gas, thus directly and negatively impacting the value of oil and gas properties in Texas. Put simply, Texas, which has consistently had the most certain regulatory environment in the United States, and potentially the world, has now introduced an element of regulatory uncertainty simply because this intervention is being discussed, let alone given serious consideration of implementation.

Our industry, like virtually every other industry, will be completely redefined as a result of this global pandemic. We are a state that is rich in natural resources, but none of the testimony or facts on the ground support the emotional pleas of operators that the RRC must approve unfair market treatment to protect resources or the supporting and surrounding economy. We have enormous issues in front of our industry today. Having to navigate and spend time and resources to deal with proration in the midst of human suffering is a diversion of valuable time and resources for which we will be judged poorly. Diamondback believes that not only as a Company and an industry, but also as individuals, we should be grateful for the opportunities that this state gives us and the independence it provides.

I am available to testify at the virtual conference on Tuesday, April 14, 2020, and our CEO, Travis Stice, and I are available any time to answer questions or give additional comments on our position about the need for a May 2020 production market demand order.

Respectfully submitted,

Kaes Van't Hof
Chief Financial Officer
Diamondback Energy, Inc.