

CROSS TIMBERS ROYALTY TRUST

Form 10-Q

October 25, 2010

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q**

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

For the quarterly period ended September 30, 2010

OR

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

Commission File Number: 1-10982

**Cross Timbers Royalty Trust**

(Exact name of registrant as specified in its charter)

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|   |  |
|---|--|
| <b>Texas</b><br>(State or other jurisdiction of<br>incorporation or organization)<br><b>U.S. Trust, Bank of America</b><br><b>Private Wealth Management</b> | <b>75-6415930</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>P.O. Box 830650, Dallas, Texas</b><br>(Address of principal executive offices)   | <b>75283-0650</b><br>(Zip Code)                              |
| <b>(877) 228-5084</b><br><br>(Registrant's telephone number, including area code)   |  |

NONE

(Former name, former address and former fiscal year, if change 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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

|   |  |
|---|--|
| Large accelerated filer <input type="checkbox"/>  | Accelerated filer <input type="checkbox"/>         |
| Non-accelerated filer <input checked="" type="checkbox"/> (Do not check if a smaller reporting company) | Smaller reporting company <input type="checkbox"/> |

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes  No

Indicate the number of units of beneficial interest outstanding, as of the latest practicable date:

Outstanding as of October 1, 2010

6,000,000

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**CROSS TIMBERS ROYALTY TRUST**

**FORM 10-Q FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2010**

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**GLOSSARY OF TERMS**

The following are definitions of significant terms used in this Form 10-Q:

|   |   |
|---|---|
| <i>Bbl</i>  | Barrel (of oil)   |
| <i>Mcf</i>  | Thousand cubic feet (of natural gas)  |
| <i>MMBtu</i>  | One million British Thermal Units, a common energy measurement  |
| <i>net proceeds</i>   | Gross proceeds received by XTO Energy from sale of production from the underlying properties, less applicable costs, as defined in the net profits interest conveyances   |
| <i>net profits income</i>   | Net proceeds multiplied by the applicable net profits percentage of 75% or 90%, which is paid to the trust by XTO Energy. Net profits income is referred to as royalty income for income tax purposes.  |
| <i>net profits interest</i>   | An interest in an oil and gas property measured by net profits from the sale of production, rather than a specific portion of production. The following defined net profits interests were conveyed to the trust from the underlying properties:<br><br><i>90% net profits interest</i> interests that entitle the trust to receive 90% of the net proceeds from the underlying properties that are royalty or overriding royalty interests in Texas, Oklahoma and New Mexico<br><br><i>75% net profits interests</i> interests that entitle the trust to receive 75% of the net proceeds from the underlying properties that are working interests in Texas and Oklahoma |
| <i>royalty interest</i><br><i>(and overriding</i><br><i>royalty interest)</i> | A nonoperating interest in an oil and gas property that provides the owner a specified share of production without any production expense or development costs  |
| <i>underlying properties</i>  | XTO Energy's interest in certain oil and gas properties from which the net profits interests were conveyed. The underlying properties include royalty and overriding royalty interests in producing and nonproducing properties in Texas, Oklahoma and New Mexico, and working interests in producing properties located in Texas and Oklahoma  |
| <i>working interest</i>   | An operating interest in an oil and gas property that provides the owner a specified share of production that is subject to all production expense and development costs  |

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**CROSS TIMBERS ROYALTY TRUST**

**PART I - FINANCIAL INFORMATION**

*Item 1. Financial Statements.*

The condensed financial statements included herein are presented, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in annual financial statements have been condensed or omitted pursuant to such rules and regulations, although the trustee believes that the disclosures are adequate to make the information presented not misleading. These condensed financial statements should be read in conjunction with the financial statements and the notes thereto included in the trust's latest Annual Report on Form 10-K. In the opinion of the trustee, all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the assets, liabilities and trust corpus of the Cross Timbers Royalty Trust at September 30, 2010, and the distributable income and changes in trust corpus for the three- and nine-month periods ended September 30, 2010 and 2009, have been included. Distributable income for such interim periods is not necessarily indicative of distributable income for the full year.

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Bank of America, N.A., as Trustee

for the Cross Timbers Royalty Trust:

We have reviewed the accompanying condensed statement of assets, liabilities and trust corpus of the Cross Timbers Royalty Trust as of September 30, 2010 and the related condensed statements of distributable income and changes in trust corpus for the three- and nine-month periods ended September 30, 2010 and 2009. These condensed financial statements are the responsibility of the trustee.

We conducted our review in accordance with standards established by the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying condensed financial statements are prepared on a modified cash basis as described in Note 1, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Based on our review, we are not aware of any material modifications that should be made to the condensed financial statements referred to above for them to be in conformity with the basis of accounting described in Note 1.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the statement of assets, liabilities and trust corpus of the Cross Timbers Royalty Trust as of December 31, 2009, and the related statements of distributable income and changes in trust corpus for the year then ended (not presented herein), included in the trust's 2009 Annual Report on Form 10-K, and in our report dated February 22, 2010, we expressed an unqualified opinion on those financial statements. In our opinion, the information set forth in the accompanying condensed statement of assets, liabilities and trust corpus as of December 31, 2009 is fairly stated, in all material respects, in relation to the statement of assets, liabilities and trust corpus included in the trust's 2009 Annual Report on Form 10-K from which it has been derived.

KPMG LLP

Fort Worth, Texas

October 25, 2010

**Table of Contents****CROSS TIMBERS ROYALTY TRUST****Condensed Statements of Assets, Liabilities and Trust Corpus**

|  | <b>September 30,<br/>2010</b><br>(Unaudited) | <b>December 31,<br/>2009</b> |
|--|--|------------------------------|
| <b>ASSETS</b>  |  |                              |
| Cash and short-term investments  | <b>\$ 1,413,026</b>                          | \$ 1,067,595                 |
| Interest to be received  | <b>28</b>                                    | 9                            |
| Net profits interests in oil and gas properties - net (Note 1)                   | <b>14,986,650</b>                            | 16,188,498                   |
|  | <b>\$ 16,399,704</b>                         | \$ 17,256,102                |
| <b>LIABILITIES AND TRUST CORPUS</b>  |  |                              |
| Distribution payable to unitholders  | <b>\$ 1,413,054</b>                          | \$ 1,067,604                 |
| Trust corpus (6,000,000 units of beneficial interest authorized and outstanding) | <b>14,986,650</b>                            | 16,188,498                   |
|  | <b>\$ 16,399,704</b>                         | \$ 17,256,102                |

The accompanying notes to condensed financial statements are an integral part of these statements.

**Table of Contents****CROSS TIMBERS ROYALTY TRUST****Condensed Statements of Distributable Income (Unaudited)**

|   | Three Months Ended<br>September 30 |              | Nine Months Ended<br>September 30 |              |
|---|------------------------------------|--------------|-----------------------------------|--------------|
|   | 2010                               | 2009         | 2010                              | 2009         |
| Net profits income                              | <b>\$ 4,142,789</b>                | \$ 2,894,511 | <b>\$ 13,011,163</b>              | \$ 8,089,015 |
| Interest income                                 | <b>43</b>                          | 29           | <b>185</b>                        | 183          |
| Total income                                    | <b>4,142,832</b>                   | 2,894,540    | <b>13,011,348</b>                 | 8,089,198    |
| Administration expense                          | <b>79,542</b>                      | 129,458      | <b>366,078</b>                    | 365,632      |
| Distributable income                            | <b>\$ 4,063,290</b>                | \$ 2,765,082 | <b>\$ 12,645,270</b>              | \$ 7,723,566 |
| Distributable income per unit (6,000,000 units) | <b>\$ 0.677215</b>                 | \$ 0.460847  | <b>\$ 2.107545</b>                | \$ 1.287261  |

The accompanying notes to condensed financial statements are an integral part of these statements.



**Table of Contents****CROSS TIMBERS ROYALTY TRUST****Condensed Statements of Changes in Trust Corpus (Unaudited)**

|                                       | Three Months Ended<br>September 30 |               | Nine Months Ended<br>September 30 |               |
|---------------------------------------|------------------------------------|---------------|-----------------------------------|---------------|
|                                       | 2010                               | 2009          | 2010                              | 2009          |
| Trust corpus, beginning of period     | <b>\$ 15,378,318</b>               | \$ 16,922,528 | <b>\$ 16,188,498</b>              | \$ 17,255,761 |
| Amortization of net profits interests | <b>(391,668)</b>                   | (253,276)     | <b>(1,201,848)</b>                | (586,509)     |
| Distributable income                  | <b>4,063,290</b>                   | 2,765,082     | <b>12,645,270</b>                 | 7,723,566     |
| Distributions declared                | <b>(4,063,290)</b>                 | (2,765,082)   | <b>(12,645,270)</b>               | (7,723,566)   |
| Trust corpus, end of period           | <b>\$ 14,986,650</b>               | \$ 16,669,252 | <b>\$ 14,986,650</b>              | \$ 16,669,252 |

The accompanying notes to condensed financial statements are an integral part of these statements.

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**CROSS TIMBERS ROYALTY TRUST**

**Notes to Condensed Financial Statements (Unaudited)**

**1. Basis of Accounting**

The financial statements of Cross Timbers Royalty Trust are prepared on the following basis and are not intended to present financial position and results of operations in conformity with U.S. generally accepted accounting principles ( GAAP ):

- Net profits income recorded for a month is the amount computed and paid by XTO Energy Inc., the owner of the underlying properties, to Bank of America, N.A., as trustee for the trust. On June 25, 2010, XTO Energy became a wholly owned subsidiary of Exxon Mobil Corporation. The merger is not expected to have a material effect on trust annual distributable income, financial position or liquidity. Net profits income consists of net proceeds received by XTO Energy from the underlying properties in the prior month, multiplied by net profit percentages of 90% for the 90% net profits interests, and 75% for the 75% net profits interests.

Costs deducted in the calculation of net proceeds for the 90% net profits interests generally include applicable taxes, transportation, marketing and legal costs, and do not include production expense or development costs. For the 75% net profits interests, costs deducted in the calculation of net proceeds include production expense, development costs, applicable taxes, transportation, marketing and legal costs, operating charges and other costs.

- Net profits income is computed separately for each of five conveyances under which the net profits interests were conveyed to the trust. If monthly costs exceed revenues for any conveyance, such excess costs must be recovered, with accrued interest, from future net proceeds of that conveyance and cannot reduce net proceeds from the other conveyances.
- Interest income, interest to be received and distribution payable to unitholders include interest to be earned from the monthly record date (last business day of the month) through the date of the next distribution to unitholders.
- Trust expenses are recorded based on liabilities paid and cash reserves established by the trustee for liabilities and contingencies.
- Distributions to unitholders are recorded when declared by the trustee.

The financial statements of the trust differ from those prepared in conformity with U.S. GAAP because revenues are recognized when received rather than accrued in the month of production, expenses are recognized when paid rather than when incurred, and certain cash reserves may be established for contingencies which would not be accrued under U.S. GAAP. This comprehensive basis of accounting other than U.S. GAAP corresponds to the accounting permitted for royalty trusts by the U.S. Securities and Exchange Commission, as specified by Staff Accounting Bulletin Topic 12:E, Financial Statements of Royalty Trusts.

Most accounting pronouncements apply to entities whose financial statements are prepared in accordance with U.S. GAAP, directing such entities to accrue or defer revenues and expenses in a period other than when such revenues were received or expenses were paid. Because the trust's financial statements are prepared on the modified cash basis, as described above, most accounting pronouncements are not applicable to the trust's financial statements.



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The initial carrying value of the net profits interests of \$61,100,449 represents XTO Energy's historical net book value on February 12, 1991, the creation date of the trust. Amortization of the net profits interests is calculated on a unit-of-production basis and is charged directly to trust corpus. Accumulated amortization was \$46,113,799 as of September 30, 2010 and \$44,911,951 as of December 31, 2009.

### **2. Contingencies**

Several states have enacted legislation to require state income tax withholding from nonresident recipients of oil and gas proceeds. After consultation with its state tax counsel, XTO Energy has advised the trustee that it believes the trust is not subject to these withholding requirements. However, regulations are subject to change by the various states, which could change this conclusion. Should the trust be required to withhold state taxes, distributions to the unitholders would be reduced by the required amount, subject to the unitholder's right to file a state tax return to claim any refund due.

### **3. Excess Costs**

Significantly lower oil prices and elevated costs caused costs to exceed revenues on properties underlying the Texas working interest for January through April 2009 and on properties underlying the Oklahoma working interest for February through April 2009. However, these excess costs did not reduce net proceeds from the remaining conveyances. XTO Energy advised the trustee that increased oil prices and decreased costs led to the full recovery of excess costs, plus accrued interest, during third quarter 2009, on properties underlying the Texas and Oklahoma working interests. Excess costs, plus accrued interest, recovered during third quarter 2009 totaled \$128,359 (\$96,269 net to the trust) on properties underlying the Texas working interest and \$278,671 (\$209,003 net to the trust) on properties underlying the Oklahoma working interest. Interest paid on these excess costs totaled \$6,995 (\$5,246 net to the trust) for the nine months ended September 30, 2009. There were no excess costs at September 30, 2010.

#### *Item 2. Trustee's Discussion and Analysis.*

The following discussion should be read in conjunction with the trustee's discussion and analysis contained in the trust's 2009 annual report, as well as the condensed financial statements and notes thereto included in this Quarterly Report on Form 10-Q. The trust's Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports are available on the trust's web site at [www.crosstimberstrust.com](http://www.crosstimberstrust.com).

### **Distributable Income**

#### **Quarter**

For the quarter ended September 30, 2010, net profits income was \$4,142,789 compared to \$2,894,511 for third quarter 2009. This 43% increase in net profits income is primarily the result of higher oil and gas prices (\$1.1 million), recovery of excess costs, plus accrued interest on the Texas and Oklahoma working interest properties in 2009 (\$0.3 million) and increased gas volumes (\$0.3 million), partially offset by decreased oil volumes (\$0.3 million). See **Net Profits Income** and **Excess Costs** below.

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After considering interest income of \$43 and administration expense of \$79,542, distributable income for the quarter ended September 30, 2010 was \$4,063,290, or \$0.677215 per unit of beneficial interest. Administrative expense for the quarter decreased 39% primarily because of the timing of expenditures. For third quarter 2009, distributable income was \$2,765,082, or \$0.460847 per unit. Distributions to unitholders for the quarter ended September 30, 2010 were:

| <b>Record Date</b> | <b>Payment Date</b> | <b>Distribution per Unit</b> |
|--------------------|---------------------|------------------------------|
| July 30, 2010      | August 13, 2010     | \$ 0.229438                  |
| August 31, 2010    | September 15, 2010  | 0.212268                     |
| September 30, 2010 | October 15, 2010    | 0.235509                     |
|                    |                     | \$ 0.677215                  |

*Nine Months*

For the nine months ended September 30, 2010, net profits income was \$13,011,163 compared to \$8,089,015 for the same 2009 period. This 61% increase in net profits income is primarily the result of higher oil and gas prices (\$5.5 million), increased gas volumes (\$0.4 million) and decreased production expense (\$0.4 million), partially offset by decreased oil volumes (\$1.0 million) and higher taxes, transportation and other costs (\$0.6 million). See *Net Profits Income* below.

After considering interest income of \$185 and administration expense of \$366,078, distributable income for the nine months ended September 30, 2010 was \$12,645,270, or \$2.107545 per unit of beneficial interest. For the nine months ended September 30, 2009, distributable income was \$7,723,566, or \$1.287261 per unit.

**Net Profits Income**

Net profits income is recorded when received by the trust, which is the month following receipt by XTO Energy and generally two months after oil production and three months after gas production. Net profits income is generally affected by three major factors:

- oil and gas sales volumes,
- oil and gas sales prices, and
- costs deducted in the calculation of net profits income.

Because properties underlying the 90% net profits interests are royalty and overriding royalty interests, they generally bear no costs other than production and property taxes, related legal costs, and marketing and transportation charges. In addition to these costs, the 75% net profits interests are subject to production expense and development costs, since the properties underlying the 75% net profits interests are working interests.

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The following is a summary of the calculation of net profits income received by the trust:

|                                 | Three Months                   |                     |                        | Nine Months                    |                     |                        |
|---------------------------------|--------------------------------|---------------------|------------------------|--------------------------------|---------------------|------------------------|
|                                 | Ended September 30 (a)<br>2010 | 2009                | Increase<br>(Decrease) | Ended September 30 (a)<br>2010 | 2009                | Increase<br>(Decrease) |
| <b>Sales Volumes</b>            |                                |                     |                        |                                |                     |                        |
| Oil (Bbls) (b)                  |                                |                     |                        |                                |                     |                        |
| Underlying properties           | 49,192                         | 55,548              | (11%)                  | 148,703                        | 166,439             | (11%)                  |
| Average per day                 | 535                            | 604                 | (11%)                  | 545                            | 610                 | (11%)                  |
| Net profits interests           | 24,421                         | 19,121              | 28%                    | 75,178                         | 50,018              | 50%                    |
| Gas (Mcf) (b)                   |                                |                     |                        |                                |                     |                        |
| Underlying properties           | 551,104                        | 507,886             | 9%                     | 1,548,653                      | 1,483,900           | 4%                     |
| Average per day                 | 6,056                          | 5,581               | 9%                     | 5,673                          | 5,436               | 4%                     |
| Net profits interests           | 486,840                        | 444,683             | 9%                     | 1,363,182                      | 1,295,472           | 5%                     |
| <b>Average Sales Prices</b>     |                                |                     |                        |                                |                     |                        |
| Oil (per Bbl)                   | \$ 69.13                       | \$ 56.90            | 21%                    | \$ 71.61                       | \$ 46.18            | 55%                    |
| Gas (per Mcf)                   | \$ 6.54                        | \$ 5.34             | 22%                    | \$ 7.23                        | \$ 5.61             | 29%                    |
| <b>Revenues</b>                 |                                |                     |                        |                                |                     |                        |
| Oil sales                       | \$ 3,400,765                   | \$ 3,160,874        | 8%                     | \$ 10,648,499                  | \$ 7,686,233        | 39%                    |
| Gas sales                       | 3,606,181                      | 2,711,361           | 33%                    | 11,201,650                     | 8,331,316           | 34%                    |
| Total Revenues                  | 7,006,946                      | 5,872,235           | 19%                    | 21,850,149                     | 16,017,549          | 36%                    |
| <b>Costs</b>                    |                                |                     |                        |                                |                     |                        |
| Taxes, transportation and other | 1,011,950                      | 852,440             | 19%                    | 3,176,436                      | 2,514,090           | 26%                    |
| Production expense (c)          | 1,122,354                      | 1,268,146           | (11%)                  | 3,387,559                      | 3,945,513           | (14%)                  |
| Development costs               | 115,678                        | 79,665              | 45%                    | 309,034                        | 502,129             | (38%)                  |
| Excess cost (d)                 | -                              | 407,030             | -                      | -                              | 6,995               | -                      |
| Total Costs                     | 2,249,982                      | 2,607,281           | (14%)                  | 6,873,029                      | 6,968,727           | (1%)                   |
| <b>Net Proceeds</b>             | <b>\$ 4,756,964</b>            | <b>\$ 3,264,954</b> | <b>46%</b>             | <b>\$ 14,977,120</b>           | <b>\$ 9,048,822</b> | <b>66%</b>             |
| <b>Net Profits Income</b>       | <b>\$ 4,142,789</b>            | <b>\$ 2,894,511</b> | <b>43%</b>             | <b>\$ 13,011,163</b>           | <b>\$ 8,089,015</b> | <b>61%</b>             |

(a) Because of the interval between time of production and receipt of royalty income by the trust, (1) oil and gas sales for the quarter ended September 30 generally represent oil production for the period May through July and gas production for the period April through June and (2) oil and gas sales for the nine months ended September 30 generally represent oil production for the period November through July and gas production for the period October through June.

(b) Oil and gas sales volumes are allocated to the net profits interests based upon a formula that considers oil and gas prices and the total amount of production expense and development costs. Changes in any of these factors may result in disproportionate fluctuations in volumes allocated to the net profits interests. Therefore, comparative discussion of oil and gas sales volumes is based on the underlying properties.

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- (c) Production expense is primarily from seven working interest properties in the 75% net profits interest. Five of these properties are not operated by XTO Energy or ExxonMobil. Production expense includes an overhead charge which is deducted and retained by the operator. As of September 30, 2010, this charge was \$34,536 per month (including a monthly overhead charge of \$2,768 which XTO Energy deducts as operator of the Penwell Unit and \$4,538 which ExxonMobil deducts as operator of the Hewitt Unit) and is subject to adjustment each May based on an oil and gas industry index.
  
- (d) See Note 3 to Condensed Financial Statements.

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The following are explanations of significant variances on the underlying properties from third quarter 2009 to third quarter 2010 and from the first nine months of 2009 to the comparable period in 2010:

### **Sales Volumes**

#### *Oil*

Oil sales volumes decreased 11% for third quarter 2010 and 11% for the first nine months of 2010 as compared with the same 2009 periods primarily because of natural production decline and the timing of cash receipts.

#### *Gas*

Gas sales volumes increased 9% for third quarter 2010 and 4% for the first nine months of 2010 as compared with the same 2009 periods. Increased gas sales volumes for the quarter and the nine-month period are primarily because of the timing of cash receipts, partially offset by natural production decline. In addition, gas sales volumes increased for the nine-month period due to increased production from new wells and workovers.

The rate of natural production decline on the underlying oil and gas properties is approximately 6% to 8% a year.

### **Sales Prices**

#### *Oil*

The average oil price increased 21% to \$69.13 per Bbl for the third quarter and 55% to \$71.61 per Bbl for the nine-month period. Oil prices are expected to remain volatile. The average NYMEX price for August and September 2010 was \$76.03 per Bbl. At October 20, 2010, the average NYMEX futures price for the following twelve months was \$84.54 per Bbl. Recent trust oil prices have averaged approximately 9% lower than the NYMEX price.

#### *Gas*

Gas prices for the third quarter increased 22% to \$6.54 per Mcf and for the nine-month period increased 29% to \$7.23 per Mcf. Natural gas prices are affected by the level of North American production, weather, crude oil and natural gas liquids prices, the U.S. economy, storage levels and import levels of liquefied natural gas. Natural gas prices are expected to remain volatile. The average NYMEX price for July and August 2010 was \$4.75 per MMBtu. At October 20, 2010, the average NYMEX futures price for the following twelve months was \$4.14 per MMBtu. Recent trust gas prices have been approximately 54% higher than the NYMEX price.



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**Costs**

*Taxes, Transportation and Other*

Taxes, transportation and other increased 19% for the third quarter and 26% for the nine-month period primarily because of increased production taxes related to higher oil and gas revenues, partially offset by decreased other deductions as a percentage of oil and gas revenues. In addition, increased taxes, transportation and other for the nine-month period was also due to increased property taxes related to the timing of expenditures.

*Production*

Production expense decreased 11% for the third quarter and 14% for the first nine months of 2010. Decreased production expense for the quarter is primarily due to decreased outside operated, repairs and maintenance and carbon dioxide injection costs, partially offset by increased labor and chemical and treating costs. Decreased production expense for the nine-month period is primarily due to decreased outside operated, repairs and maintenance, overhead on nonoperated properties and power and fuel costs, partially offset by increased chemical and treating costs.

*Development*

Development costs increased 45% for the third quarter primarily due to the timing of cash disbursements. Development costs decreased 38% for the nine-month period primarily because of decreased activity and costs related to the Texas and Oklahoma properties underlying the 75% net profits interests.

*Excess Costs*

Significantly lower oil prices and elevated costs caused costs to exceed revenues on properties underlying the Texas working interest for January through April 2009 and on properties underlying the Oklahoma working interest for February through April 2009. However, these excess costs did not reduce net proceeds from the remaining conveyances. XTO Energy advised the trustee that increased oil prices and decreased costs led to the full recovery of excess costs, plus accrued interest, during third quarter 2009, on properties underlying the Texas and Oklahoma working interests. Excess costs, plus accrued interest, recovered during third quarter 2009 totaled \$128,359 (\$96,269 net to the trust) on properties underlying the Texas working interest and \$278,671 (\$209,003 net to the trust) on properties underlying the Oklahoma working interest. Interest paid on these excess costs totaled \$6,995 (\$5,246 net to the trust) for the nine months ended September 30, 2009. There were no excess costs at September 30, 2010.

**Contingencies**

Several states have enacted legislation to require state income tax withholding from nonresident recipients of oil and gas proceeds. After consultation with its state tax counsel, XTO Energy has advised the trustee that it believes the trust is not subject to these withholding requirements. However, regulations are subject to change by the various states, which could change this conclusion. Should the trust be required to withhold state taxes, distributions to the unitholders would be reduced by the required amount, subject to the unitholder's right to file a state tax return to claim any refund due.

**Other**

On June 25, 2010, XTO Energy became a wholly owned subsidiary of Exxon Mobil Corporation. The merger is not expected to have a material effect on trust annual distributable income, financial position or liquidity.

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**Forward-Looking Statements**

Statements in this report relating to future plans, predictions, events or conditions are forward looking statements. All statements other than statements of historical fact included in this Form 10-Q including, without limitation, statements regarding the net profits interests, underlying properties, development activities, development, production and other costs and expenses, oil and gas prices and differentials to NYMEX prices, distributions to unitholders, industry and market conditions and the impact of the merger with Exxon Mobil Corporation, are forward-looking statements that are subject to risks and uncertainties which are detailed in Part I, Item 1A of the trust's Annual Report on Form 10-K for the year ended December 31, 2009, which is incorporated by this reference as though fully set forth herein. XTO Energy and the trustee assume no duty to update these statements as of any future date.

*Item 3. Quantitative and Qualitative Disclosures about Market Risk.*

There have been no material changes in the trust's market risks from the information disclosed in Part II, Item 7A of the trust's Annual Report on Form 10-K for the year ended December 31, 2009.

*Item 4. Controls and Procedures.*

As of the end of the period covered by this report, the trustee carried out an evaluation of the effectiveness of the trust's disclosure controls and procedures pursuant to Exchange Act Rules 13a-15 and 15d-15. Based upon that evaluation, the trustee concluded that the trust's disclosure controls and procedures are effective in timely recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the trust in the reports that it files or submits under the Securities Exchange Act of 1934 and are effective in ensuring that information required to be disclosed by the trust in the reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the trustee to allow timely decisions regarding required disclosure. In its evaluation of disclosure controls and procedures, the trustee has relied, to the extent considered reasonable, on information provided by XTO Energy Inc. There has not been any change in the trust's internal control over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the trust's internal control over financial reporting.

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**PART II - OTHER INFORMATION**

*Item 1.*

Not applicable.

*Item 1A. Risk Factors.*

There have been no material changes in the risk factors disclosed under Part I, Item 1A of the trust's Annual Report on Form 10-K for the year ended December 31, 2009.

*Items 2 through 5.*

Not applicable.

*Item 6. Exhibits.*

- (a) Exhibits.

**Exhibit Number  
and Description**

- |      |  |
|------|--|
| (31) | Rule 13a-14(a)/15d-14(a) Certification   |
| (32) | Section 1350 Certification   |
| (99) | Items 1A, 7 and 7A to the Annual Report on Form 10-K for Cross Timbers Royalty Trust filed with the Securities and Exchange Commission on February 23, 2010 (incorporated herein by reference) |

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**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.

CROSS TIMBERS ROYALTY TRUST

By BANK OF AMERICA, N.A., TRUSTEE

By */s/* NANCY G. WILLIS  
**Nancy G. Willis**  
**Vice President**

EXXON MOBIL CORPORATION

By */s/* PATRICK T. MULVA  
**Patrick T. Mulva**  
**Vice President and Controller**

Date: October 25, 2010

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