



# Oklahoma-NARO

National Association of Royalty Owners Oklahoma Chapter  
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<http://www.naro-us.org/oklahoma>

Summer 2015

## PRESIDENT'S REPORT

The recent state convention for Oklahoma NARO was a resounding success! Located in historic downtown Tulsa, our convention chair, Janet Yeager, along with OK President Mason Mungle and Jerry Simmons and his NARO staff, provided a fun and fact filled three day event. The convention began with a tour of the Oklahoma Aquarium and ended with attendees dodging the Oklahoma spring weather. And, I know that all who attended are looking forward to the 2016 Oklahoma NARO convention located at the beautiful and recently renovated Marriott Tulsa Hotel Southern Hills April 27 - 29, 2016.

Convention 2015 featured numerous educational seminars including Mineral Management 101 and 102, wealth transference, geology of Oklahoma, Oklahoma Corporation Commission website navigation, to an informative question and answer session with a panel of experts; Dub Peace, David Sikes and Terry Stowers and moderated by Mason Mungle on pooling in Oklahoma. We were also fortunate to have Oklahoma Corporation Commissioner, Dana Murphy, and Oklahoma Secretary of Energy and Environment, Michael Teague, update us on the issues they are facing including seismicity and water usage and disposal that are at the forefront of Oklahoma's oil and gas industry. Terry Stowers also updated us on the efforts of the Coalition of Surface and Mineral Owners at the state capital including the status of very important pending legislation.

As the incoming president of Oklahoma NARO, I feel fortunate to serve with a board dedicated to serve the mineral owners of this great state. Mason Mungle, past president, left a legacy of education and commitment that should sustain us for many years to come.

I plan to continue his passion for educating our mineral owners and empowering them to be a voice

for their mineral rights. With the pressing issues in the oil and gas industry, it is imperative for mineral owners to become more active; to stand together as a unified voice not only to protect their rights but also to educate the public as to advantages and services this industry provides our country.

There is power in numbers! We are a membership driven organization. Recruiting new members is not just a duty of the board; it is a duty that every mineral owner needs to fulfill for our collective voice to be heard. Each member of OK-NARO needs to contact other mineral owners and encourage them to join NARO. Also, we need to encourage other minerals owners to attend the state convention held April 27-29, 2016.

In the future, we will strive to keep you informed; request your assistance when action is necessary; and assist you in your effort to protect your legacy for generations to come.

*Dick McCalla*, OK-NARO President



# 2015 Lease Offers Received in Oklahoma

Lease offer for \$650/acre, 3 years, and 3/16 royalty received in 4-13N-13W of Blaine County, OK

Lease offer for \$300/acre, 3 years, and 3/16 royalty received in 31-6S-8E of Bryan County, OK

Lease offer for \$35/acre, 3 years, and 3/16 royalty received in 30-6N-5E of Cimarron County, OK

Lease offer for \$100/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$50/acre) received in 24-2N-8E of Coal County, OK

Lease offer for \$350/acre, 3 years, and 3/16 royalty (or 1/4 royalty and no bonus) received in 32-9N-2E of Coal County, OK

Lease offer for \$750/acre, 3 years, and 3/16 royalty received in 12-15N-15W of Custer County, OK

Lease offer for \$450/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$300/acre) received in 35-16N-19W of Dewey County, OK

Lease offer for \$600/acre, 3+2 years, and 3/16 royalty received in 1-18N-16W of Dewey County, OK

Lease offer for \$400/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$250/acre) received in 27-20N-25W of Ellis County, OK

Lease offer for \$1000/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$700/acre) received in 24-6N-5W of Grady County, OK

Lease offer for \$325/acre, 3 years, and 3/16 royalty received in 7-6N-9E of Hughes County, OK

Lease offer for \$2000/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$1500/acre) received in 36-16N-7W of Kingfisher County, OK

Lease offer for \$150/acre, 3 years, and 3/16 royalty received in 8-5N-3W of McClain County, OK

Lease offer for \$1750/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$850/acre) received in 31-6N-4W of McClain County, OK

Lease offer for \$200/acre, 3+2 years, or \$350 for 5 years, and 3/16 royalty received in 36-12N-12E of Okmulgee County, OK

Lease offer for \$100/acre, 3 years, and 3/16 royalty received in 15-7N-3E of Pottawatomie County, OK

Lease offer for \$150/acre, 3 years, and 3/16 royalty received in 31-7N-3E of Pottawatomie County, OK

Lease offer for \$2600/acre, 3 years, and 3/16 royalty (or 1/5 royalty and \$2000/acre) received in 27-15N-25W of Roger Mills County, OK

Lease offer for \$200/acre, 3 years, and 3/16 royalty (or 1/5 royalty and no bonus) received in 15-7N-3E of Pottawatomie County, OK

# Royalty Owner Advocacy Committee Report

## Report submitted by Terry L. Stowers, Chair

*“Success usually comes to those who are too busy to be looking for it.” (Henry David Thoreau).*

Oklahoma mineral owners’ were successful on our number one issue this Session – to encourage Oklahoma Legislators to avoid these types of headlines: “Fracking Bans Could Affect Retirees Relying On Mineral Rights” CBS Denver; “Denton fracking ban quickly draws two lawsuits after passing” Dallas Morning News; “Denton’s fracking ban: Is it a reasonable prohibition or the taking of mineral rights?” Dallas Business Journal. To accomplish our goal, we joined with the Oklahoma Oil & Gas Association and Oklahoma Independent Petroleum Association to sponsor SB809 by Pro Tem Brian Bingman and Speaker Jeff Hickman which we believed correctly balanced state, county and municipal regulation of oil and gas activities, while protecting both surface owners’ and mineral owners’ private property interests. SB809 prevents municipalities from effectively banning drilling and fracking within municipal boundaries. Governor Fallin’s Press Release follows:

*Gov.Fallin Signs Legislation Reaffirming Corporation Commission as Regulator of Oil, Gas Industry*

*OKLAHOMA CITY – Governor Mary Fallin n Friday signed a bill reaffirming the Corporation Commission as the sole regulator of Oklahoma’s oil and natural gas industry. The bill aims to preserve a unified regulatory framework for the industry and prevent a confusing patchwork of inconsistent municipal regulations across the state.*

*Fallin said today that Oklahoma has led the nation in developing rigorous standards for oil and gas production. A patchwork of regulations that vary across the state would be inconsistent with the goal of reasonable, easily understood regulations and could damage the state’s economy and environment, she said.*

*Senate Bill 809 reaffirms that the Oklahoma Corporation Commission is the primary entity charged with establishing a unified regulatory framework for the energy industry, emphasizing environmentally responsible policies. SB 809 prohibits municipalities from issuing moratoriums or bans on drilling while preserving their ability to adopt reasonable ordinances, rules and regulations concerning traffic issues, noise, fencing requirements and placing of drilling rigs.*

*“The Corporation Commission is aggressively but fairly regulating Oklahoma’s energy industry,” said Fallin. “The Commission has nationally recognized experts along with direct access to multiple agencies and multi-state organizations that municipalities would not have. For example, the Commission is using scientific analysis from the Oklahoma Geological Survey and providing additional oversight on hundreds of underground injection wells linked to increased seismic activity. As more information and science become available, the Commission will use it to responsibly regulate or even put a stop to some drilling activity that could cause earthquakes or damage to the environment.*

*“Corporation Commissioners are elected by the people of Oklahoma to regulate the oil and gas industry. They are best equipped to make decisions about drilling and its affect on seismic activity, the environment and other sensitive issues. We need to let these experts do their jobs. The alternative is to pursue a patchwork of regulations that, in some cases, could arbitrarily ban energy exploration and damage the state’s largest industry, largest employers and largest taxpayers,” said Fallin.*

For a third year in a row, expansion of the 2011 Shale Reservoir Development Act (the drilling of extended horizontal laterals) was a hot topic at the Capitol. HB2177 would have accomplished this expansion. However, for a third year in a row, it was met with opposition by OIPA. While HB2177 stalled out in the final days for the 2015 Legislative Session, the brisk debate highlighted a significant divide between the horizontal and vertical producers which has been bubbling for several years now. It is our hope and belief that we can turn this divide into constructive talks this fall and find some workable solutions for a number of issues that continue to face the oil and gas industry, which includes you, the mineral owners.

# Using Decimal Interest to Estimate Royalty Payments

By: Frederick M. “Mick” Scott CMM, RPL  
Oklahoma NARO Communication/Education Committee, Chair

A gas well on a 640-acre drilling and spacing unit is allowed to drain gas from under 640 acres. Similarly, an oil well on a 160-acre drilling and spacing unit is allowed to produce the oil underlying its spacing unit. This means that everyone who owns mineral rights under an established drilling and spacing unit will share in the proceeds from any wells that are drilled. Those outside the unit would not.

Say you own 40 acres of minerals under a 640-acre drilling and spacing unit. You would get more royalty in the unit than someone who only owned 20 acres (twice as much) but would get less than someone who owned 80 acres (half as much). The amount of acres you own proportionate to the whole unit is what determines your ownership percentage in the unit, and thus your “decimal interest.”

Decimal interest is used by the purchaser of the production to determine what you are paid and is shown on those division orders you are asked to sign shortly after a new well comes on line, as well as on the royalty checks you later receive. It's important to make sure the decimal interest shown is correct before signing the division order.

To determine your decimal interest, take the number of acres you own in the unit (40, for example) and divide it by the number of acres in the unit (640, for example.) This will give you what's called a “working interest” decimal, and would apply to you only if you were participating in the well by paying your share of the costs associated with drilling it. In this example it would be .0625.

Since the lease you signed gave the oil company the right to drill the well instead of you, you won't be participating in the well so we'll continue on and multiply the working interest decimal of .0625 by the royalty on your lease (3/16 for example, which is .1875 in decimal form).  $.0625 \times .1875$  is .01171875. This will be your “decimal interest.”

The decimal interest represents your “royalty interest” in the unit, proportionate to your ownership in the whole 640-acre unit. Had you owned the 200 acres rather than only 40, your decimal interest would have been figured thusly:

$$200/640 \times .1875 = .05859375.$$

As you can see, you can plug any numbers you like into this formula. Once you have your decimal interest, multiply it by the gross revenue from the well in a given month (shown on your check stub). The result is approximately what your gross royalty would be for that month. Note that in some cases the gross revenue for a given month could be spread over two or more of your check stubs so check for that.

Now that you know how decimal interest is used to figure royalty payments, you can also use the formula to estimate what your royalty payments might be in a hypothetical well that hasn't even been drilled yet. A decent gas well might produce 30,000 MCF of gas per month. “MCF” is an acronym for “thousand-cubic-feet” so 30,000 MCF is really shorthand for 30,000,000 (thirty million) cubic feet of gas.

Let's assume natural gas sells for about \$6 per MCF (wishful thinking these days.) If a well had sales of 30,000 MCF in a month that would mean it produced \$180,000 in gross revenue for that month. Multiply the \$180,000 figure by your decimal interest to arrive at your gross royalty for the month. In our example, 40 acres of minerals owned in a 640-acre unit at 3/16 royalty would come out to \$2,109.38 for that month ( $180,000 \times .01171875 = \$2,109.38$ ).

Alternatively, if you don't know how many acres you own, or want to confirm your royalty payments are being calculated on what you do own, you can take the decimal interest shown on your check stubs (sometimes called “owner decimal”; “payment



decimal” etc.) and multiply it by the unit size if known (i.e. 640 acres) then divide by the royalty amount. The result is the net acres they are paying you on in the unit. For example:  $.01171875 \times 640 / .1875 = 40$  acres.

If you don't know the unit size or royalty, you'll need to contact the operator of the well or perhaps the person who leased you. In addition, a copy of the lease (showing the royalty) will be filed with the county clerk in the county where the minerals are located.



# The Use of Limited Liability Companies in Estate Planning

By Kimberley McCullough, Attorney

Many families have considered using a limited liability company (LLC) to accomplish their estate planning goals and when utilized properly, LLCs can be an effective estate planning tool. This article will discuss the advantages of making an LLC part of the plan to preserve your wealth, including mineral interests, and pass that wealth on to future generations.

An LLC is a type of business entity created by state statute. In order to form and operate an LLC, it is necessary to file articles of organization and create an operating agreement between the members that will govern how the LLC will operate. Assets are then transferred to the LLC in exchange for membership interests. Thus, the members of the LLC now own membership interests in the LLC that owns the assets, instead of owning the assets themselves.

Once properly organized, the LLC provides numerous benefits in achieving a family's estate planning objectives. The following are a few of the chief advantages:

## Separation of Ownership and Control of Assets

The owners of an LLC are referred to as members. The management of an LLC can be vested in either all the members of the LLC, creating a member-managed LLC, or management can be separated from ownership in a manager-managed LLC.

Because management of an LLC does not have to be based on ownership, parents or grandparents can transfer assets held by an LLC to the next generation while still maintaining control of the assets. This facilitates the younger generations in becoming familiar with the challenges and rewards of ownership, while being guided by the judgment of the more experienced generation. This structure can also prevent members who are not managers from withdrawing as members and cashing out their interest, and can place restrictions on the transfer of their membership interest.

## Asset Protection

The LLC can provide multiple levels of creditor protection if properly drafted and organized. Members of an LLC can be protected from the claims and debts of the LLC, contrary to a general partnership or even a limited partnership in which a general partner is still responsible for company debts.

Further, LLC assets can be protected from creditors of the LLC members. The operating agreement can be drafted so that creditors of an LLC member would not automatically receive member status as a result of attachment of a debt, but instead would be granted a charging order that would only allow the creditor to receive distributions that the member would have been entitled to receive. Although this does not render the creditor completely powerless, it does allow a more favorable position to negotiate a settlement.

Finally, the transfer of family assets to an LLC can allow a family member to keep such assets segregated and preserve their status as "separate property" in the event of a divorce.

## Estate and Gift Tax Planning

The utilization of LLCs in estate and gift tax planning allows families to decrease the value of assets that will eventually be subject to gift and/or estate taxes. This reduction of value is accomplished through the use of valuation discounts because a membership interest in an LLC is considered less valuable than outright ownership of the asset itself. The two main types of discounts that are generally recognized in valuing the membership interest in an LLC are the lack of marketability discount and the minority interest discount.

The lack of marketability discount is based on the principle that a family member's interest in the LLC cannot be easily sold to an independent third party due to restrictions in the LLC's operating agreement, such as transfer restrictions and the inability of the member to convert their interest to cash.



The minority interest discount reflects the member's lack of control over the decision-making in the LLC. If the LLC member does not have the ability to force distributions or liquidation, then a buyer would not be inclined to pay for the full value of the assets in purchasing the member's interest in the LLC.

Perhaps the best way to illustrate the use of LLCs in estate and gift tax planning is through an example: Assume that a married couple owns farm land and mineral interests worth \$5,000,000. They form an LLC and convey the property to the LLC in exchange for membership interest in the LLC. We can suppose, only for purposes of this example, that due to the terms in this LLC's operating agreement, the combined discounts for lack of marketability and minority interest would be 35%.

If the outright value of the LLC assets is \$5,000,000 and we take the discounts totaling 35% for lack of marketability and minority interest, then the value of the LLC assets for estate tax purposes would be \$3,250,000.

This 35% discount could also be applied to gifts of LLC membership interests. If the couple gives their daughter a 10% interest in the LLC, the value of that 10% interest before discounts would be \$500,000. Taking into account the discounts totaling 35%, the gift tax value of the LLC membership interest transferred to the daughter would be \$325,000.

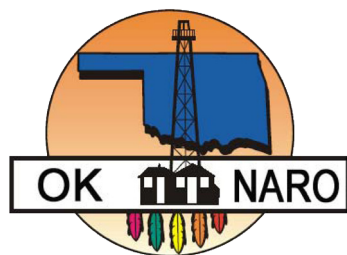
As you can see, the use of discounts in valuing the assets of an LLC for gift and estate tax purposes can be very beneficial. However, it is important to consult with a lawyer and accountant if you plan to use valuation discounts because the IRS has challenged the use of discounts in situations that have involved improper formation and operation of the LLC. None of the figures or values shown here should be used or relied on and you should seek independent counsel should you decide to utilize discounts.

While this summary represents a few of the key reasons to consider incorporating the use of an LLC in your estate plan, there are many other motivations to take into account, including: the use of an LLC to maintain ownership of assets within your family, avoidance of probate, and having the option to be taxed as a corporation, partnership or disregarded entity.

Careful consideration should be given in determining whether the use of an LLC would be beneficial to your family's plan for wealth preservation. As always, you should consult with your own advisors to decide which tools work best for your situation, but by being informed about your options, you have already taken the first step.



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