



## DEPARTMENT OF REVENUE

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### MEMORANDUM

TO: WYOMING PETROLEUM PRODUCERS

FROM: CRAIG GRENVIK, ADMINISTRATOR, MINERAL TAX DIVISION

DATE: DECEMBER 20, 2016

SUBJECT: EXEMPT ROYALTY DETERMINATION

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The following guidance is a policy statement clarifying the Wyoming Department of Revenue's (Department) position regarding the proper determination of exempt royalties and interests (federal, state and tribal) on petroleum minerals for the reporting of Wyoming production taxes. Sample calculations are provided for clarity.

The three main questions this guidance addresses are: 1) How to calculate the exempt royalty/exempt interest in a mineral property containing one or more unitization agreements, participating areas, communitization agreements or any combination thereof. 2) How to calculate the value of the exempt royalty/exempt interest when the royalty bearing volume is different from the production tax volume for a property in a given timeframe. 3) How to adjust for a difference between royalty and tax calculations when the methodologies between the two are different.

The basis for any mineral royalty is the lease. Multiple leases are at times combined into participating areas (PA) and units. Communitization agreements (CA) tied to leases are also quite common. For Wyoming production tax reporting, however, basic building blocks are the petroleum wells themselves, which are reported to the Department as a "Mineral Group." While mineral groups are often formed from an individual lease containing a single well, many mineral groups are comprised of wells within a communitization agreement, participating area, a unit or any combination of the three.

Mineral groups containing multiple wells should be established along the "property basis." Statutorily, each property should be a lease, an entire unit, individual participating areas within a unit, or combination thereof. While the statutes are silent toward communitization agreements, this policy considers a CA to be equivalent to the statutorily provided concepts previously mentioned.

Since the Department does not have direct access to lease/unit/CA information, producers have been relied upon to establish the well groupings for mineral groups. This guidance addresses the

determination of the proper exempt interest/royalty rate in instances in which the group consists of one or more unit, PA or CA.

We present two scenarios that represent the difficulty in calculating exempt royalties and interests and the allocation of those royalties and interests. One scenario describes a mineral group comprised of wells in both a CA and a unit. The second scenario depicts a mineral group containing only one well in a CA. In the second scenario the unit still impacts the royalty calculation even though the well is on a lease distinct from the unit itself. In both instances a take-in-kind owner and the operator report production taxes based upon take volumes that do not correlate to either interest owner's entitlement percentage.

The Department's policy is to base exempt royalties on a weighted-average exempt royalty rate. This royalty rate would take into account the percentages of federal, state, fee, and tribal land, along with the respective exempt lease royalty rates, to determine a weighted-average exempt royalty rate. This calculated weighted-average exempt royalty rate should be applied to the net value after allowable transportation and processing deductions, thus resulting in a taxable value.

The Department recognizes the fact that not all calculated royalty rates are straightforward; therefore, the department has provided two mineral group scenarios that represent the calculation of a weighted-average exempt royalty rate with overlapping CA's etc., to demonstrate how the royalty rate is calculated in a complex situation. One mineral group scenario, as depicted in Unit Blue & Green (attached), demonstrates how to calculate a weighted-average exempt royalty rate for a mineral group containing a unit that is comprised of state, federal, and fee land, as well as a federal CA. The second scenario, which includes a fee well in overlapping CA Red, demonstrates how to calculate the exempt royalty rate for a mineral group containing one fee well in a CA that also overlaps a unit. In both instances a take-in-kind owner and the operator report production taxes based upon take volumes that do not correlate to either interest owner's entitlement percentage.

Severance and Ad Valorem taxes are subject to actual quantities taken rather than entitlement percentages. (Please note the difference between the "take" volumes and entitlement volumes for both the operator and the take-in-kind interest owner). Therefore, the exempt royalty percentage is applied to the actual quantity taken to determine the exempt volume. In this scenario the oil is sold after the LACT meters on the lease so transportation and processing deductions are applicable. The allowable deductions are a "given" in this scenario and are only represented here to illustrate the exempt royalty percentage is applied to the net value after deductions and *not* applied to the gross revenue. This guidance has *nothing* to do with determining the proper transportation and processing deductions. Please refer to the calculations that follow.

Under this policy, the surface location of the wellhead from which petroleum volumes are produced shall not be the basis for the determination or allocation of exempt royalties/interests for valuation purposes. This policy does not alter either the taxpayer's or the taxing jurisdiction's rights and obligations under W.S. 39-14-207(a)(iii).

Finally, in instances that the reported exempt interest/exempt royalty is not the product of the exempt royalty rate multiplied by the net value of the production being reported (see example below), taxpayers shall notify the Department in writing and specify the reason for the difference. In the event the taxpayer is subsequently audited, and the royalty audit has been paid on the same volumes as those taxed, then the audited paid royalty shall be used.

The facts in the first hypothetical scenario are as follows:

Mineral Group 012345 contains the following wells: 38-20001, 38-20002, 38-20003, 38-20004, 38-20005

Mineral Group 012345 contains one Unit (Blue & Green) and one CA( C/A Red) comprised of entirely Federal property outside of the unit

Well 38-20001 is in the "Red" CA while the remaining wells are contained within the unit

The unit consolidates 6 originally independent, leases, three Federal, two private and one State lease

There are only two working interest owners in this property, Operator "Big R" and take-in kind owner "Little t".

The facts in the second hypothetical scenario are as follows:

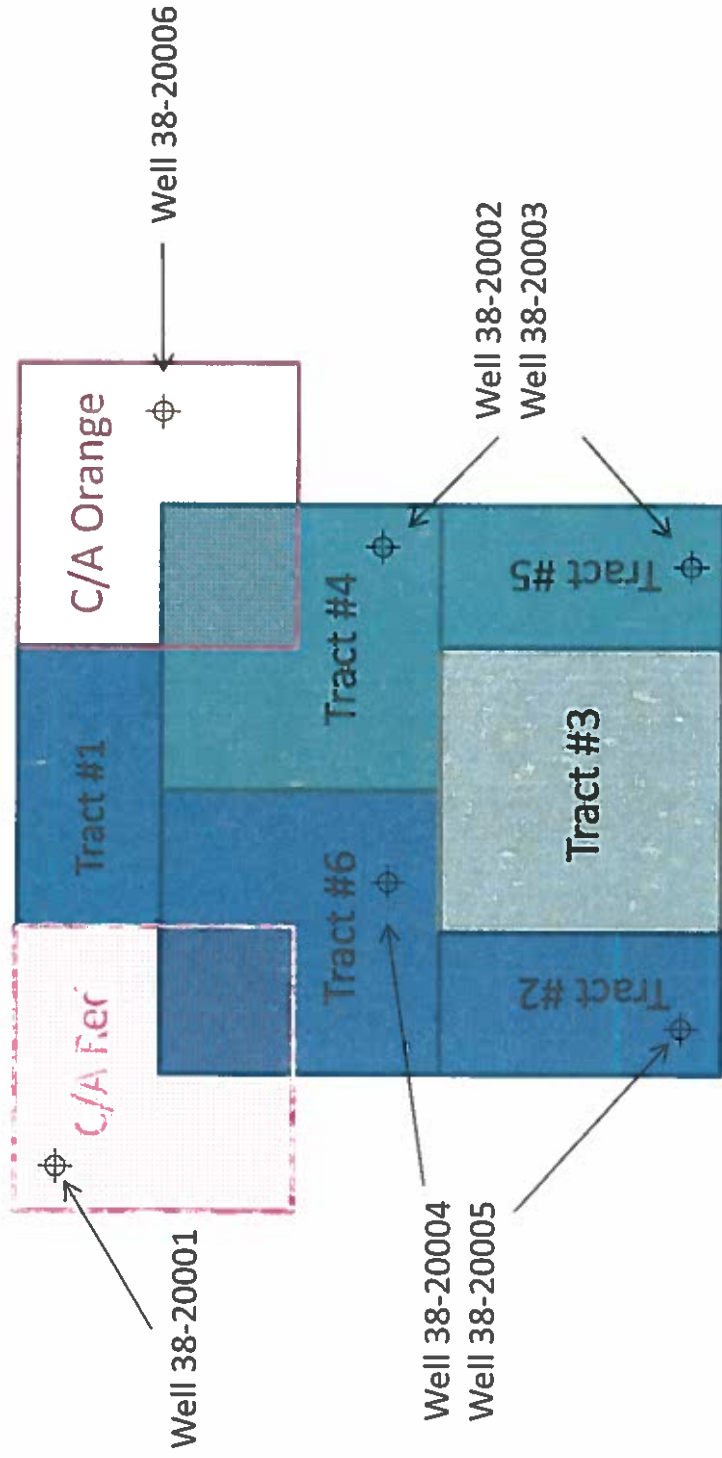
Big R is the only interest owner in Fee Lease A that is outside the Blue & Green Unit

Mineral Group 002468 is comprised of a single CA -C/A Orange

Mineral Group 0002468 contains one well: 38-20006,

Well 38-20006 is in the "Orange" CA. The acreage in the Orange CA outside the unit boundary is comprised entirely of fee land

# “BLUE & GREEN” UNIT WITH OVERLAPPING C/A’S



1. Dark Blue Tracts #1, #6, #2 are Federal Tracts; Green Tract #3 is a State Tract; and Light Blue Tracts #4 & #5 are Fee tracts for “Blue & Green Unit”
2. Mineral Group 012345 includes wells 38-20001, 38-20002, 38-20003, 38-20004, & 38-20004. Mineral Group 002468 includes well 38-20006
3. For C/A Red, acreage outside of the unit boundary is 100% federal. For C/A Orange acreage outside of the unit boundary is 100% fee.
4. All wells were drilled by the Operator and the Operator is the same for the unit and both C/A's.

Wells: 38-20002, 38-20003, 38-20004, 38-20005

Actual Total Well Production:

Operator Entitlement (5,950 times Operator Entitlement %):

Take In-Kind Entitlement (5,950 times TIK Entitlement %):

5,950

3,306

2,644

**Unit Blue & Green (mixed unit)**

Tracts	Ownership Type	Royalty Rate	Committed Acres	Tract %	Effective Unit Exempt Royalty Rate	Working Interest	Operator Acres	Take In-Kind Acres	Operator Entitlement %	Take In-Kind Entitlement %
		$a$	$b$	$c = b / \text{total } b$	$d = a * c$	$e$	$f$	$g$	$h = f / \text{total } f$	$i = g / \text{total } g$
Tract 1	Federal	12.50%	80	11.11111%	1.3889%	Operator	80	80	55.56%	44.44%
Tract 2	Federal	12.50%	80	11.11111%	1.3889%	Operator	80			
Tract 3	State	16.67%	160	22.22222%	3.7044%	Take In-Kind		160		
Tract 4	Private	0.00%	160	22.22222%	0.0000%	Take In-Kind		160		
Tract 5	Private	0.00%	80	11.11111%	0.0000%	Operator	80			
Tract 6	Federal	12.50%	160	22.22222%	2.7778%	Operator	160			
			720	100.00000%	9.2600%		400	320		

Actual Taken Volume	Price	Gross Value	Allowed Processing & Transportation Deduction	Effective Unit Exempt Royalty Rate	Net Value	Exempt Royalty	Blue&Green Unit Taxable Value
$j$	$k$	$l = j * k$	$m$	$n = \text{total } d$	$o = i * m$	$p = n * o$	$q = n - p$
Operator Takes:	\$45.25	\$181,000.00	\$8,000.00	9.2600%	\$173,000.00	\$16,019.80	\$156,980.20
Take In-Kind Takes:	\$53.50	\$104,325.00	\$4,875.00	9.2600%	\$99,450.00	\$9,209.07	\$90,240.93

**Mineral Group: 012345**

Wells: 38-20001

Actual Total Well Production:

Operator Entitlement (3,250 times Operator Entitlement %):

Take In-Kind Entitlement (3,250 times TIK Entitlement %):

3,250

2,889

361

**C/A Red (100% fed with unit overlap)**

Committed Acres	Average %	Royalty Rate	Effective Unit Exempt Royalty Rate	Operator Entitlement Percentage	Operator Interest	Take In-Kind Interest	Take In-Kind Entitlement Percentage
$a$	$b = a / \text{total } a$	$c = d * e$	$d = b * c$	$f = e * b$	$g = h * i$	$h = g * j$	$k = h * l$
Unit Blue & Green	40	25.00%	2.31500%	13.8889%	55.56%	44.4444%	11.1111%
Federal Lease "A"	120	75.00%	9.37500%	75.00%	100.00%	0.00%	0.00%
Total C/A Land	160	100.00%	11.69000%	88.8889%			11.1111%

Actual Volume	Price	Gross Value	Allowed Processing & Transportation Deduction	Effective Unit Exempt Royalty Rate	Net Value	Exempt Royalty	Min Grp 012345 Taxable Value
$l$	$j$	$k = l * j$	$i$	$n$	$m = k - i$	$o = m * n$	$p = m - o$
Operator Takes:	2,050	\$45.25	\$92,762.50	11.6900%	\$88,662.50	\$10,364.65	\$235,278.05
Take In-Kind Takes:	1,200	\$53.50	\$64,200.00	11.6900%	\$61,200.00	\$7,154.28	\$144,286.65
							Unit+C/A RED TV

Mineral Group: 002468

Wells: 38-20006

Actual Total Well Production: 4,550

Operator Entitlement (4,550 times Operator Entitlement %): 4,044

Take In-Kind Entitlement (4,550 times TIK Entitlement %): 506

**C/A Orange (100% fee land with unit overlap)**

Committed Acres	Average %	Royalty Rate	Effective Unit Exempt Royalty Rate	Operator Interest	Operator Entitlement Percentage	Take In-Kind Interest	Take In-Kind Entitlement Percentage
$a$	$b = a / \text{total } a$	$c = d \cdot 1$	$d = b \cdot c$	$e = h \cdot 1$	$f = e \cdot b$	$g = i \cdot 1$	$h = g \cdot b$
40	25.00%	9.2600%	2.31500%	55.56%	13.8889%	44.4444%	11.1111%
120	75.00%	0.0000%	0.00000%	100.00%	75.00%	0.00%	0.00%
160	100.00%		2.31500%		88.8889%		11.1111%

Unit Blue & Green

Fee Lease "A"

Total C/A Land

Actual Volume	Price	Gross Value	Allowed Processing & Transportation Deduction	Net Value	Effective Unit Exempt Royalty Rate	Exempt Royalty	C/A Taxable Value	Min Grp 002468 Taxable Value
$i$	$j$	$k = i \cdot j$	$l$	$m = k - l$	$n$	$o = m \cdot n$	$p = m - o$	$q = p$
1,550	\$45.25	\$70,137.50	\$3,100.00	\$67,037.50	2.3150%	\$1,551.92	\$65,485.58	\$65,485.58
3,000	\$53.50	\$160,500.00	\$7,500.00	\$153,000.00	2.3150%	\$3,541.95	\$149,458.05	\$149,458.05

Operator Takes:

Take In-Kind Takes:

DEPARTMENT OF INTERIOR  
BUREAU OF LAND MANAGEMENT  
CASE RECORDATION  
(MASS Serial Register Page)

01 02-25-1920;041STAT0437;30USC181  
Case Type 000000: O&G PARTICIPATING AREA  
Commodity 459: OIL & GAS  
Case Disposition: AUTHORIZED

Total Acres 720.00  
Serial Number WYW--- - BLUE & GREEN UNIT

Name & Address		Serial Number: WYW--- - BLUE & GREEN UNIT		Int Rel	% Interest
BLM-WYOMING SO/RMG	2987 PROSPECTOR DR	CASPER WY 826042968	OFFICE OF RECORD		0
BIG "R" OIL AND GAS CO.	PO BOX 645022	BUFORD WY 802173779	OPERATOR		100

Serial Number: WYW--- - BLUE & GREEN UNIT								
Mer Twp	Rng	Sec	STyp	SNr Suff	Subdivision	District/Field Office	County	Mgmt Agency
##	#####	#####	##	LOTS	8;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT
##	#####	#####	##	ALIQ	E2,E2SW,SENW;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT
##	#####	#####	##	ALIQ	ALL;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT
##	#####	#####	##	ALIQ	NENE,S2NE,S2;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT
##	#####	#####	##	ALIQ	E2NE,NESE;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT

Serial Number: WYW--- - BLUE & GREEN UNIT				
Act Date	Code	Action	Action Remark	Pending Office
12/1/1995	387	CASE ESTABLISHED		
12/1/1995	500	GEOGRAPHIC NAME	INT FRONTIER	
12/1/1995	500	GEOGRAPHIC NAME	UA-BLUE & GREEN;	
12/1/1995	868	EFFECTIVE DATE	/A/1/	
9/11/1997	580	PROPOSAL RECEIVED	/1/	
12/1/1997	595	WELL DETERMINED PAYING	/1/FEE, 80	
12/1/1997	665	PA APPROVED	/1/	
7/31/2001	658	MEMO OF 1ST PROD-ACTUAL	/2/; 38-20002	
11/16/2001	643	PRODUCTION DETERMINATION	/2/;	
2/25/2002	817	MERGER RECOGNIZED	/B/;	
11/1/2002	658	MEMO OF 1ST PROD-ACTUAL	/3/; 38-20003	
3/1/2005	517	AGRMT WITHIN UA/CA	CA-WYW CA ORANGE;	
4/1/2006	517	AGRMT WITHIN UA/CA	CA-WYW CA RED	
6/22/2006	817	MERGER RECOGNIZED	/C/;	

Serial Number: WYW--- - BLUE & GREEN UNIT				
Line Nr	Remarks	TR#	ACRES	PERCENT
001	/A/ PA ALLOCATION EFFECTIVE 12/01/1995			
002	LEASE SERIAL NO			
003	WYW LEASE X	1	80.00	11.1100
004	WYW LEASE Y	2	80.00	11.1100
005	WYW LEASE Z	6	160.00	22.2200
006	STATE	3	160.00	22.2200
007	FEE	4	160.00	22.2200
008	FEE	5	80.00	11.1100
009	TOTAL		720.00	100.00
010				
011	LANDS			
012	TR1,22N,112W,S26,E2NE,SWNE			
013	TR2,22N,112W,S22,ALL			
014	TR3,22N,112W, S15,N2SE,NESW			
015	TR4,22N,112W,S26,N2SE,SWSE,SW			
016	TR5,22N,112W,S28,E2NE,NESE			
017	TR6,22N,111W,S30,LOT 8			
019	/2/ 38-20002			
020	/B/ JOES OIL AND GAS INTO BIG "R" OIL AND GAS CO TO			
021	BIG "R" OIL AND GAS CO;			
022	/3/ 38-20003			
023	/B/ AUNT MAE'S TINY GAS CO INTO BIG "R" OIL AND GAS CO TO			
024	BIG "R" OIL AND GAS CO;			

**DEPARTMENT OF INTERIOR  
BUREAU OF LAND MANAGEMENT  
CASE RECORDATION  
(MASS Serial Register Page)**

01 02-25-1920;041STAT0437;30USC181

Total Acres

Serial Number

Case Type 000001: O&G COMMUNITIZATION AGRMT

160

WYW--- - CA ORANGE

Commodity 459: OIL & GAS

Case Disposition: AUTHORIZED

Serial Number: WYW--- - CA ORANGE

Name & Address			Int Rel	% Interest
BLM-WYOMING SO/RMG	2987 PROSPECTOR DR	CASPER WY 826042968	OFFICE OF RECORD	0
BIG "R" OIL AND GAS CO.	PO BOX 645022	BUFORD WY 802173779	OPERATOR	100

Serial Number: WYW--- - CA ORANGE

Mer Twp	Rng	Sec	STyp	SNr Suff	Subdivision	District/Field Office	County	Mgmt Agency	
##	#####	###	W	###	ALIQ	SWNE,NWSE NESW,SENW;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT

Serial Number: WYW--- - CA ORANGE

Act Date	Code	Action	Action Remark	Pending Office
3/1/2005	387	CASE ESTABLISHED		
3/1/2005	516	FORMATION	FRNR;FRONTIER	
3/1/2005	517	AGRMT WITHIN UA/CA	UA-BLUE & GREEN;	
3/1/2005	525	ACRES-NONFEDERAL	160.00;100.00% FEE	
3/1/2005	868	EFFECTIVE DATE	/A/	
4/28/2005	654	AGRMT PRODUCING	FEE,WELL 38-20006	
8/26/2010	580	PROPOSAL RECEIVED	CA RECD;	
7/27/2012	334	AGRMT APPROVED		
7/27/2012	690	AGRMT VALIDATED		

Serial Number: WYW--- - CA ORANGE

Line Nr	Remarks	AC COMMITTED	% INTEREST
001	/A/ RECAPITULATION EFFECTIVE 3/1/2005		
002	TR# LEASE SERIAL NO		
003	1 WYW BLUE & GREEN	40.00	25.00
004	2 FEE	120.00	75.00
005	TOTAL	160.00	100.00
006			
007			
008	TRACTS 1 AND 2 INVOLVE FEE LAND WITHIN THE BLUE&		
009	GREEN UNIT FRONTIER		
010	THIS CA AFFECTS ONLY THE FRONTIER PRODUCTION FROM		
011	THE WELL 38-20006.		



DEPARTMENT OF INTERIOR  
BUREAU OF LAND MANAGEMENT  
CASE RECORDATION  
(MASS Serial Register Page)

01 02-25-1920;041STAT0437;30USC181  
 Case Type 000002: O&G COMMUNITIZATION AGRMT  
 Commodity 410: NATURAL GAS  
 Case Disposition: AUTHORIZED

Total Acres 160  
 Serial Number WYW--- - CA RED

Name & Address			Serial Number: WYW--- - CA RED	
			Int Rel	% Interest
BLM-WYOMING SO/RMG	2987 PROSPECTOR DR	CASPER WY 826042968	OFFICE OF RECORD	0
BIG "R" OIL AND GAS CO.	PO BOX 645022	BUFORD WY 802173779	OPERATOR	100

Serial Number: WYW--- - CA RED								
Mer Twp	Rng	Sec	STyp	SNr Suff	Subdivision	District/Field Office	County	Mgmt Agency
##	#####	####	W ##	ALIQ	SE;	KEMMERER FIELD OFFICE	LINCOLN	BUREAU OF LAND MGMT

Serial Number: WYW--- - CA RED				
Act Date	Code	Action	Action Remark	Pending Office
4/1/2006	387	CASE ESTABLISHED		
4/1/2006	516	FORMATION	FRNR;FRONTIER	
4/1/2006	517	AGRMT WITHIN UA/CA	PA-WYW BLUE&GREEN	
4/1/2006	526	ACRES-FED INT 100%	160.00;100.0000%	
4/1/2006	868	EFFECTIVE DATE	/A/	
4/29/2006	654	AGRMT PRODUCING	WYW CA RED; 38-20001	
2/20/2007	580	PROPOSAL RECEIVED	CA RECD	
4/12/2007	334	AGRMT APPROVED		
4/12/2007	690	AGRMT VALIDATED		
6/14/2012	672	SUCCESSOR OPERATOR	/B/THE OIL PRODUCING CO/BIG "R" OIL AND GAS CO.	
9/28/2012	909	BOND ACCEPTED	;WYB000000	

Serial Number: WYW--- - CA RED				
Line Nr	Remarks	AC COMMITTED	% INTEREST	
001	/A/RECAPITULATION EFFECTIVE 04/01/2006			
002	TR# LEASE SERIAL NO			
003	1 WYW FEDERAL LEASE "A"	120.00	75.0000	
004	2 WYW BLUE & GREEN	40.00	25.0000	
005	TOTAL	160.00	100.0000	
006				
007	/B/THE OIL PRODUCING CO/BIG "R" OIL AND GAS CO. 6/14/12			