

Who's Minding Your Minerals?



Chapter 1

*Step by Step Procedure in Drilling,
Completing and Producing a Well:*

A) *Geology* 1

B) *Land* 1

C) *Drilling* 2

D) *Completion* 2

E) *Production* 3

F) *Payments of Royalties* 4

CHAPTER 1

STEP BY STEP PROCEDURE IN DRILLING, COMPLETING & PRODUCING A WELL

A) Geology:

The *geologist* is actually the inventor of the well. The geologist reviews maps, seismic and topographic information along with other technical data to determine if your land or minerals have the potential to produce oil, gas or other hydrocarbons. Geologists usually work for companies to develop *prospects*. The company that the geologists work for, is commonly known as the *operator*. A prospect can be small (encompassing a portion of a *section*) or large (encompassing several sections).

B) Land:

The operator then instructs a *landman* to determine the ownership underlying the prospect. The landman goes to the County Courthouse in which the prospect is located and performs a *record check*. The landman begins at statehood, with a *patent*, and reviews all *conveyances* affecting the land. This includes not only the *mineral ownership*, but the *surface ownership* and any *leasehold ownership* on the property. Upon completion of the record check, the operator instructs the landman to negotiate the purchase of *oil and gas leases* with the mineral owners.

After the leases have been secured in the prospect, the operator then may need to file a *spacing application* with the *Oklahoma Corporation Commission (OCC)*. Spacing simply defines the formations that they propose to drill and develop, and defines the *size of the unit*. Unit sizes vary from 2.50 acres (very shallow oil wells) to 640.00 acres (deeper gas wells).

Another application the operator may have to file with the Oklahoma Corporation Commission is a **pooling application**. Pooling allows the operator to proceed with the drilling of a well even if leases are not granted by all mineral owners. The pooling application will name all parties who are unlocatable, unagreeable, or owners with questionable title. If you have already granted an oil & gas lease, you will not be named in this application. However, if you received your interest through an estate that was not probated in Oklahoma, that party will more than likely be named and your address will be used for notification purposes.

C) Drilling:

A representative of the operator will negotiate and compensate the **surface owner** of the particular **tract** (or tracts) directly affected by the **drilling** of a well. This includes the actual **location** of the rig, access to the location, and possibly the purchase of water, if it is available and needed during drilling operations.

The operator will contract with service companies to prepare the location, drill the well, test the well, monitor and report progress and results, etc. There are so many specialists involved in the actual drilling of the well that I can't even begin to name them all. This by far is the most expensive step of the process.

D) Completion:

After the well has been drilled to a predetermined depth, and if it has shown productive qualities, the drilling rig will be removed and a smaller completion rig will be moved in. The **completion** process is like the drilling process in that many, many steps are involved before the actual **production equipment** is in place and connected to a supply.

E) Production:

The well is connected through pipelines and valves to a *tank battery*, which holds the oil produced, and/or a *pipeline*, which carries the gas produced to a central plant. The *oil production* is held in the tank battery on location and when the battery is full and warrants a pick up, a tank truck is called in to measure and remove the oil. Depending on the productive ability of the well, there may be oil sales every month or every six months. Therefore if you own royalties under a well that produces small amounts of oil, you may not be paid each month for it. Oil royalties are paid in the month that the oil is picked up and sold, not the month that it was produced.

If the well is capable of *gas production*, the operator then has to find a market or pipeline to accept the gas that is produced from the well. This can sometimes be a lengthy process because of the lack of existing pipelines in the area. Sometimes pipelines have to be expanded to reach the well, or new pipelines constructed entirely. Unfortunately we have no storage facilities for gas at the wellsite that enables us to produce a well and remove the gas as we do the oil.

When a market is established and connection to the pipeline is in place, then *gas sales* begin. A meter is placed at the wellsite that measures gas flowing into a main pipeline. This meter is the basis for the payment of royalties under the well. Gas sale payments will be paid monthly because all gas produced is immediately sold through the pipeline.

Sometimes during initial testing or other conditions, a well will produce gas that is not sold. The gas will be vented (released) and no income will be obtained from this because gas was not sold.

Who's Minding Your Minerals?



Chapter 2

Understanding Legal Descriptions:

- A) Townships and Ranges 5*
- B) Section Pattern 6*
- C) Tract Descriptions 7*

F) Payments of Royalties:

The operator retains a *title attorney* to examine the county records and prepare a *title opinion*. This title opinion will show the *decimal interest* of not only working interest owners, but royalty owners as well. It will also detail and make *requirements* that need to be satisfied before funds can be distributed to an owner with less than marketable title. The operator then attempts to *cure* the title opinion requirements, usually by contracting a landman, so *division orders* can be prepared and sent to all parties for execution.

The division order will show the decimal interest you will receive on income (gas or oil) from the well. The decimal interest shown on the division order should agree with your records and you will be instructed later in the book on how to determine your decimal interest. If this doesn't agree with your calculations, contact the operator. He will be happy to explain his calculations or adjustments.

See *Chapter 6-D* for examples of typical royalty checks. This will help you to understand the income on not only your share of the well, but the income on the entire well.

Comments:

The receipt of the division order may be the only notification that you, as a mineral owner, will receive if a productive well has been drilled. However, if a well was drilled and if it was a *dry hole*, you may never be advised of it. It would be nice if the operator could keep the mineral owners informed as to their intentions, actions or results, but this isn't possible. With Oklahoma minerals divided among multiple owners, the costs involved in notifying individual owners would be astronomical.

You can periodically check on the progress of your minerals by contacting either the landman to whom you leased the property, the Oklahoma Corporation Commission or the operator. This takes time, research and resources which may not be feasible for you. However, we provide a service for this type of inquiries. The fees are nominal and are fully described in *Chapter 8 - Other Services Available*.

CHAPTER 2

UNDERSTANDING LEGAL DESCRIPTIONS

A) *Township and Ranges:*

Oklahoma and many other states are based on a grid type system. It is like a multiplication table. The *township* and *range* is how you locate these minerals. Exhibit #1 below shows a sample of the system used in township and range division. Townships run north and south; ranges run east and west. See *Chapter 6-A* for a map on the entire state of Oklahoma. This will help you pinpoint the area your minerals are in.

EXHIBIT #1 - *Township and Range Patterns*

T2N R3W	T2N R2W	T2N R1W	T2N R1E	T2N R2E	T2N R3E
T1N R3W	T1N R2W	T1N R1W	T1N R1E	T1N R2E	T1N R3E
T1S R3W	T1S R2W	T1S R1W	T1S R1E	T1S R2E	T1S R3E
T2S R3W	T2S R2W	T2S R1W	T2S R1E	T2S R2E	T1S R3E

Starting at the township dividing line (A), move up to T1N, up another block to T2N, etc. The south townships are numbered in the same manner. If you move down from (A) one block you are in T1S, down another block to T2S, etc.

Ranges progress in the same manner, although the directions change. Starting at line (B), move to the left and you are in R1W, move left another block to R2W, move left another block to R3W. If you move right from (B) you will be in R1E, right another block to R2E, right another block to R3E and so on.

Each of the blocks shown on Exhibit #1 contains 36 sections. Exhibit #2 shows the layout of the 36 sections within each township.

B) Section Pattern:

After you have located the township and range coordinates, you are then ready for your next test. Exhibit #2 below gives a diagram of a typical township. The entire area below covers 36 square miles, while each section covers 1 square mile or 640.00 acres.

EXHIBIT #2 - Section Patterns

6	5	4	3	2	1
7	8	9	10	11	12
18	17	16	15	14	13
19	20	21	22	23	24
30	29	28	27	26	25
31	32	33	34	35	36

Section 1 is located in the top right corner of every township, and the sections progress left (Section 2), left again (Section 3) and so on, until you reach the western boundary of the township at Section 6.

Move down and you are at Section 7, then right (Section 8), right again (Section 9) and so on until you reach the eastern boundary of the township at Section 12.

Movement again is down to Section 13 and begin the left movement as described in Sections 1 through 6 above.

When you reach the western boundary again the pattern follows that of Section 7 through 12. This alternating pattern is used throughout the state of Oklahoma (and other grid based states).

Because the earth is round, most townships are adjusted (or corrected) and not every section will contain exactly 640 acres. Corrections are only made on the sections that border the north township line and the west range line. The *correctional sections* will only be Sections 1, 2, 3, 4, 5, 6, 7, 18, 19, 30 and 31. Only the portion of the individual section that border the township and range lines are adjusted. When adjustments are made in a tract it will be referred to as Lot 1, Lot 2, etc. See *Chapter 6-B* to locate lots in a correctional section.

With the knowledge you have gained, you should now understand how to pinpoint the *section, township and range (S-T-R)* your mineral interest is in.

C) *Tract Description:*

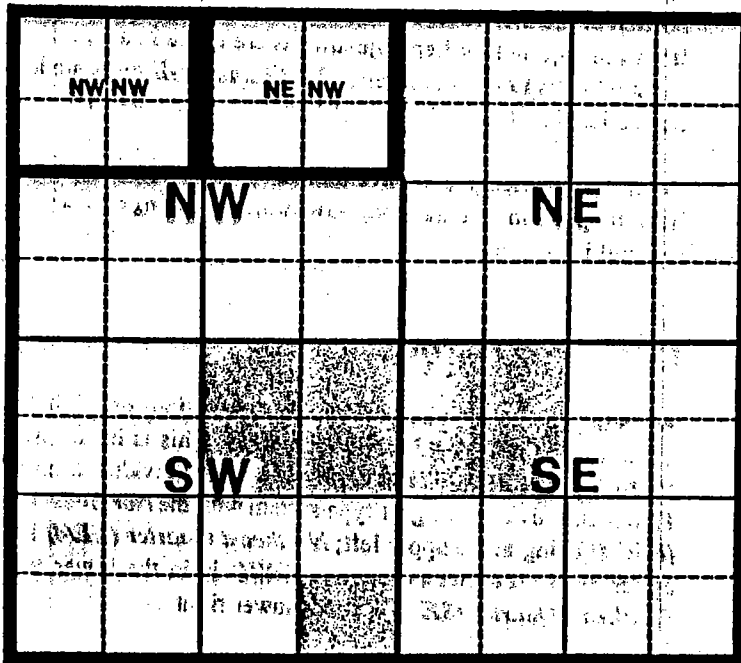
We will proceed to those weird little descriptions of the individual tracts in which your minerals are owned. This is by far the most confusing aspect. Exhibit #3 on Page 8 is an individual section plat. This is also divided in a grid-type system with the *Northwest Quarter (NW/4)* being in the upper left; *Northeast Quarter (NE/4)* is in the upper right; *Southwest Quarter (SW/4)* is in the lower left; and *Southeast Quarter (SE/4)* is in the lower right.

Each quarter section contains 160 acres and when they are divided again, the quarter-quarter section contains 40 acres. The division concept is the same one as described on Page 7, but instead of starting with an entire section, we start with only a quarter section.

Where do you think the Northwest Quarter of the Northwest Quarter (NW/4 NW/4) would be? If you have understood the basic concept so far, you are well on your way to *minding your minerals!* The location of the NW/4 NW/4 is in the uppermost left corner of the NW/4. Now locate the NE/4 NW/4. Are you correct again?

The most important thing to understand here is, when plotting out your description, start from the **BACK AND WORK FORWARD!** A general rule of thumb here is when saying the description aloud, insert the words "of the" between every description. This will get you in the habit of locating the correct quarter when you start.

EXHIBIT #3- Section Plat



Use Exhibit #3 on Page 8 to find the following tracts:

**NE/4 (of the) SW/4
and
NW/4 (of the) SE/4**

The location of these two 40-acre tracts are shaded, but were you able to do it on your own?

Tracts can break down as small as 2.50 acres but for now we will only go down to 10-acre tracts. The concept is the same...remember it! Where would the following tract be located?

SE/4 (of the) SE/4 (of the) SW/4

Start at the end of the description the SW/4. Now find the SE/4 within the SW/4. Now find the SE/4 within the SE/4 of the SW/4. The correct location of this 10-acre tract is also shaded.

If you were successful in these exercises, then I have all the confidence in the world that **YOU CAN MIND YOUR MINERALS!**

Use the Mineral Inventory Forms provided in Chapter 5-B to not only inventory each parcel you own, but also plat them out. Granted, you will not be able to fill in every blank, but as time goes by, documents will be discovered that will help to complete the "mineral puzzle."

Who's Minding Your Minerals?



Chapter 3

Title and Fractional Ownership:

- A) Grandpa's Land 10*
- B) Descent & Distribution 12*

CHAPTER 3

*

TITLE AND FRACTIONAL OWNERSHIP

Oklahoma, like many other oil producing states, has severed (divided) mineral ownership. This simply means that there may be several fractional mineral owners under a particular tract and the surface owner may or may not own any of the mineral rights.

Each mineral tract can have many different surface tracts. If each of the different surface owners owns mineral rights under his surface tract, then the mineral tracts would be divided to coincide with the surface tracts. If the different surface owners do not own any of the mineral rights, there would only be one tract. Grandpa's story below is a simple example of fractional ownership and tract division.

A) Grandpa's Land:

Grandpa came to Oklahoma in the land run and was granted the NW/4 (160.00 gross acres) by the USA. This included all surface and all mineral rights.

During the Dust Bowl he was forced to start selling pieces of his property. He sold the first piece, the NW/4 NW/4 (40 gross acres), to Neighbor Bob without reserving any of the mineral rights. After this conveyance, Grandpa no longer owned surface or minerals in the NW/4 NW/4.

Grandpa still couldn't make ends meet so he sold another piece, however he had wised up to the fact that he could reserve all or a portion of the minerals under this tract. A deed was given to Banker Don for all surface rights in the SW/4 NW/4 (40 gross acres), but Grandpa reserved 1/2 of the mineral rights for himself. After this conveyance, Grandpa owned 1/2 of the minerals in the SW/4 NW/4 but still owned all surface and mineral rights in the E/2 NW/4.

After years of struggling, Grandpa couldn't keep up with the taxes so he sold the rest of his farm to Neighbor Bob and moved west. Grandpa wanted to retain all the mineral rights under the surface he had left, so a deed was given to Neighbor Bob for surface rights only in the E/2 NW/4.

After all of the conveyances noted above, the NW/4 (which was one tract originally) is now divided into three tracts, not because of the surface, but because of the minerals. A tract is defined and divided by common mineral ownership. The ownership to the NW/4 would now be as follows:

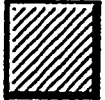
(Diagrams below on each tract coincide with the plat on Page 12)

Tract #1 (NW/4 NW/4) 40.00 acres surface - Neighbor Bob (all)



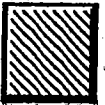
40.00 acres minerals - Neighbor Bob (all)

Tract #2 (SW/4 NW/4) 40.00 acres surface - Banker Don (all)



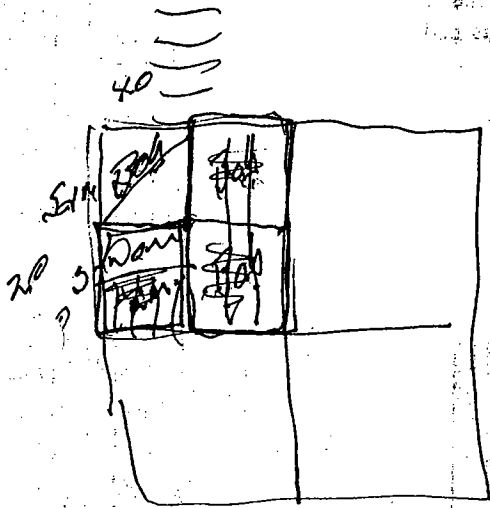
20.00 acres minerals - Banker Don (1/2)
20.00 acres minerals - Grandpa (1/2)

Tract #3 (E/2 NW/4) 80.00 acres surface - Neighbor Bob (all)

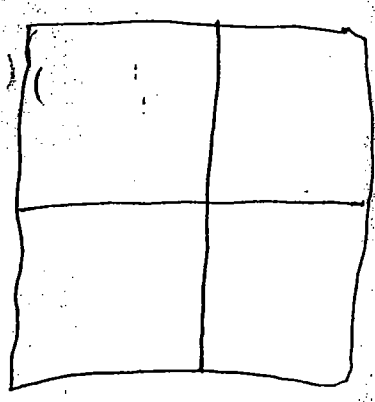


80.00 acres minerals - Grandpa (all)

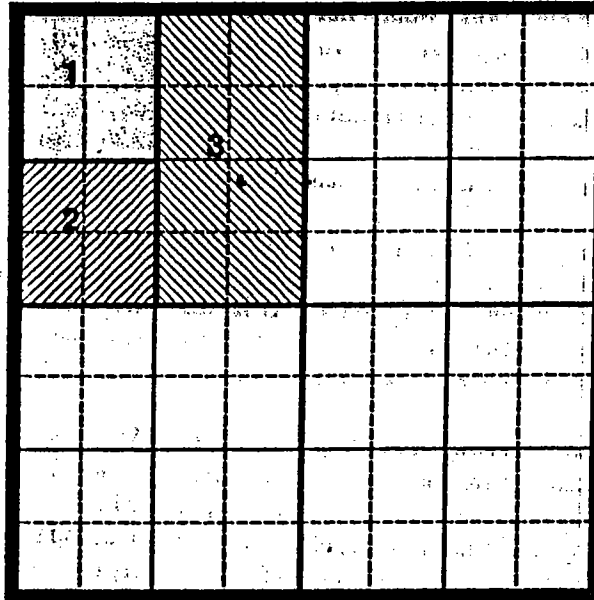
If Grandpa were alive and leasing today, the leased premises would be the SW/4 NW/4 and E/2 NW/4 (120.00 gross acres and 100.00 net mineral acres).



100 min Ac



Plat showing the three tracts described on Page 11:



B) Descent and Distribution:

Now we will discuss the changes in title after Grandpa dies. Let's say that Grandpa moved to California, married, had children and then died. The only time title moves clearly (with no questions as to the validity) is:

- 1) If Grandpa made a conveyance of the property to his heirs or another party, OR
- 2) If Grandpa's estate was probated in any county in Oklahoma. Probated simply means that a judicial determination has been made by a court in Oklahoma as to the disposition of Grandpa's assets and property.

Let's say Grandpa died in California and his estate was probated in California and Grandma received all of his interest via a last will and testament. Title would not move clearly to Grandma unless she petitioned and probated his will and estate in Oklahoma. I am not saying that she has no claim to the property if she doesn't probate his estate in Oklahoma, but that it has just created a "title gap" (also called a cloud). If Grandma wanted to lease this property, she would have to supply documentation to the landman, evidencing her claim to the land.

If Grandpa did not have a will, then Oklahoma laws of intestate distribution would be followed as to the heirship and percentage acquired by his widow and children. If he did leave a will but it was not probated in Oklahoma, these guidelines would also have to be followed to assure that the oil and gas lease covered all his interest.

Documents known as *Proof of Death & Heirships* (See *Chapter 6-D* for an example) are commonly prepared for cases like this. The affidavit simply states who owned the property (record title owner); the legal description of the property; the name of the spouse (the date of death if applicable); and all children born to the property owner. If any (or all) of the heirs of Grandpa are deceased, the affidavit will detail the dates of their deaths and the heirs of their estates. Proof of death and heirships are an acceptable document for leasing, but if production is obtained and if the mineral ownership is large, an operator may require that judicial determination is made prior to disbursing funds. This would not only be judicial determination of Grandpa's estate, but Grandma's and any other parties involved in the chain of title leading to your interest.

If the property was acquired in *joint tenancy* then the whole estate will go to the survivor. Upon the death of the survivor, with no will, the estate (or property) will be divided among the heirs.

The tables on Pages 14 through 16 show the percentage each heir would receive. The percentage changed on July 1, 1985, so it is important to know the date of death. The percentages also change if: a) the property was not acquired by joint industry; b) the decedent was married more than once; c) the property was acquired outside the covenant of marriage; d) the decedent was married at the time of his death; and e) the decedent left a surviving spouse.

The term "issue" refers only to children (natural born or adopted). If a child predeceases the owner of the property, but left issue, then his share would be divided equally among his issue (children). For example, Grandpa and Grandma are both dead and they had four children. All of the children are still alive, except for one. The child who died was married and had two children at the time of his death. Only the two children would share equally his 1/4th interest in the property. This is also referred to as "right of representation." The property would not be divided three ways, for each living child, but would also include the issue of any predeceased heirs.

As you can see, this gets very complicated. It is important for your heirs not only to know about the property, but also know about your entire family (date of their births, date of their deaths, their spouses and children, etc.). With the passing of each generation, some of this knowledge is lost and will never be fully known. If you cannot provide the information needed to establish a claim to the property, you cannot be leased or be paid for royalties.

The purpose of the table below is in no way intended to be an interpretation of the Oklahoma Statutes, but merely an example of the most common situations that occur when a person dies without a will.

Before After
7/1/85 7/1/85

1) Decedent married only once or decedent married more than once and the mineral interest was acquired during the marriage:

- a) Left surviving spouse and one child (or its issue):

Surviving spouse	one-half	one-half
Child (or its issue)	one-half	one-half

- b) Left surviving spouse and more than one child (or its issue):

Surviving spouse	one-third	one-half
Children (divided equally)	two-thirds	one-half

- c) Left surviving spouse, no children but mother and/or father:

Surviving spouse	all	all
------------------	-----	-----

	Before	After
	7/1/85	7/1/85

1) Decedent married only once (continued)

d) Left surviving spouse, no children, no surviving parent, but surviving brothers & sisters (or their issues):

Surviving spouse	all	all
------------------	-----	-----

e) No surviving spouse and one child (or its issue):

Child (or its issue)	all	all
----------------------	-----	-----

f) No surviving spouse and more than one child (or their issues):

Children share in equal portions	all	all
----------------------------------	-----	-----

g) No surviving spouse, no children, but mother and father:

Mother & father (divide equally)	all	all
-------------------------------------	-----	-----

h) No surviving spouse, no children, no surviving parents, but left surviving brothers & sisters (or their issues):

Brothers & sisters (divided equally)	all	all
---	-----	-----

i) No surviving spouse, no children, no surviving parents, no surviving brothers & sisters (or their issues):

State of Oklahoma	all	all
-------------------	-----	-----

2) Decedent was married more than once and acquired mineral interest prior to marriage:

a) Left surviving spouse and one child (or its issue):

Surviving spouse	one-half	one-half
Child (or its issue)	one-half	one-half

b) Left surviving spouse and more than one child (or their issues):

divide equally

Before After
7/1/85 7/1/85

2) Decedent married more than once (continued)

c) Left surviving spouse, no children, but
mother and/or father: divide equally

d) Left surviving spouse, no children, no
surviving parents, but surviving brothers
and sisters (or their issues): divide equally

(Same distribution as Part 1 [e through i] if no surviving spouse)

Comments:

During the leasing process the heirs to the estate may desire to divide the property differently from the guidelines above. For example, Grandpa left a widow and four children and the children all agree that their mother should receive the income from bonuses, rentals and royalties during her lifetime. In cases like this, the landman would prepare an oil and gas lease for the mother and a document known as a *Ratification of Oil and Gas Lease* (See *Chapter 6-D* for an example) for each of the children to sign. The ratification simply states that the children agree with the terms and provisions of the lease signed by their mother, but they wish to forego any money due to them until after her death. The children would all own a *reversionary interest* until the death of their mother.

Another type of reversionary interest is a *life estate*. A life estate is usually created when an owner conveys his interest to a third party (or parties) but retains the benefits of the property for his lifetime. The third parties are known as the *remaindermen*. The remaindermen will own a reversionary interest (an interest that does not vest until a specific condition is met) on this property. Again, during the leasing process, an oil and gas lease would be taken on the life tenant, and ratifications would be taken from the remainderman. By creating a life estate, the life tenant would receive full benefits of the mineral interest for his lifetime, and upon his death, this mineral interest would automatically be vested to the remaindermen. Also, by creating a life estate you would avoid the need for judicial determination of your estate.

Ratifications are required to protect the operator and the interest being leased. The reason for this is if a lease was taken from a life tenant and ratifications were not obtained from the remainderman, upon the death of the life tenant this interest could be construed as open (not subject to the terms and conditions of any oil and gas lease) and operators usually will not take this risk.

The most important thing to remember here is to leave a will. If you do not direct the disposal of your property, the state of Oklahoma will and it may not be the way you want it! Another important thing to remember is to make yourself easy to locate. File *affidavits* at the county courthouses to not only notify the public of address changes, but also of name changes. See *Chapter 6-D Sample Documents* for an example of an affidavit of address change and an affidavit of identity (name change).

Another important thing to remember is to execute all documents exactly as your name appears. Let's say that Grandpa conveyed an interest to "Bradley Sean Keen" and he now uses the name "Brad S. Keen" for all legal documents. If he were to sign an oil and gas (or any other document) any way other than Bradley Sean Keen it would be incorrect. A new document would have to be prepared for re-execution or an affidavit of identity would have to be recorded to clear up any title questions. The exact name that title is acquired in will be used on all documents regarding this property. If you are no longer using (or signing) the name that property was acquired in, you should point this out to the party who is preparing the documents. He will then style the document correctly the first time (i.e. Bradley Sean Keen, also known as Brad S. Keen).

Many times when women acquire property in their maiden name, marry, move away, divorce and remarry, it makes it almost impossible for a landman to locate and lease their property. This not only results in the loss of bonus income, but also royalty payments on producing wells. The landman is required to research all avenues to locate the mineral owner and if they are not successful, then this mineral interest will be pooled. The bonus money paid under the pooling and any income from producing wells will be placed in suspense. After a specific period of time passes, and no claim has been made to the money, it is turned over to the State of Oklahoma, Unclaimed Property Section.

Use this book as a tool to make a claim to your minerals and to make yourself accessible. Documents are provided in *Chapter 6-D* to be used as an example in preparing affidavits for address and/or name changes. We do, however, provide a service for this type of document preparation for a nominal fee. See *Chapter 8-A Document Preparation Services* for the forms that need to be completed and returned should you wish us to prepare your affidavits.

See *Chapter 7-C Other State Agencies* for the address to the Unclaimed Property Section of the State of Oklahoma. You can make a written inquiry to this department if you believe you have monies in suspense. This inquiry should include not only your name, but the names of any party whom you may have received your interest from.

Who's Minding Your Minerals?



Chapter 4

The Leasing Process:

<i>A) Leased Premises</i>	<i>19</i>
<i>B) Primary Term</i>	<i>20</i>
<i>C) Royalty</i>	<i>21</i>
<i>D) Bonus Consideration</i>	<i>21</i>
<i>E) Other Special Provisions</i>	
<i>Top-Leases</i>	<i>22</i>
<i>Options</i>	<i>22</i>

CHAPTER 4



THE LEASING PROCESS

An *oil and gas lease* is a formal written agreement where the *mineral owner*, known as the *lessor*, grants the right to explore for oil, gas and other hydrocarbons (for a specific period of time), to an individual (or an entity), known as the *lessee*.

Most oil and gas lease forms are preprinted and the specifics negotiated and agreed to by both parties (lessor and lessee) will be incorporated into the lease. An example of a typical oil and gas lease form can be found in *Chapter 6-D*.

A) Leased Premises:

This is the *legal description* of the *tract* (or tracts) that your minerals underlie in a specific section, township and range. The *gross acres* of the tract will also be shown. The term "gross acres" is confusing to most people because they assume that since the lease shows 160.00 gross acres they should be paid their bonus based on 160.00 acres. This is incorrect as the bonus is calculated on the number of *net mineral acres* owned and you may only own a fractional interest under the entire tract. Additionally the tracts can be described differently, and still cover the same land. Be sure you are familiar with how to plot an individual tract description (see *Chapter 2-C*). The following is an example of the different ways a tract can be described and still be the same:

$$\begin{array}{rcl} \text{NW/4 and NE/4} & = & \text{N/2} \\ (160) + (160) & & (320) \end{array}$$

$$\begin{array}{rcl} \text{SW/4 SE/4 and NW/4 SE/4} & = & \text{W/2 SE/4} \\ (40) + (40) & & (80) \end{array}$$

SW/4 SW/4 and NW/4 SW/4 and NE/4 SW/4 (40 + 40 + 40)	=	N/2 SW/4 and SW/4 SW/4 (80 + 40)
	OR	W/2 SW/4 and NE/4 SW/4 (80 + 40)
	OR	SW/4 less the SE/4 SW/4 (160 - 40)

B) Primary Term:

This is the length of time the lessor (we'll say it's Grandpa) has granted the lessee the right to drill a well. The *primary term* can vary but is usually a period of three to five years. Grandpa agreed to grant a five-year lease which was dated March 2, 1996. Grandpa's lease will expire automatically, with the absence of production, March 2, 2001.

However, if at the expiration date, a well has been commenced (started), Grandpa's lease would still be in force and effect until operations are finished. If Lady Luck is smiling on us all and the well is good, Grandpa's interest would now be *held by production* and the lease would remain in force as long as the well continues to produce.

On the other hand, if a *dry hole* was drilled, or if there was never a well drilled during the primary term, Grandpa's lease will expire under its own terms on March 2, 2001. At this time, Grandpa's interest is open and he is free to lease this mineral interest again.

C) Royalty:

This is the percentage that Grandpa would retain on proceeds from a producing well. Let's say Grandpa agreed to a 1/8th royalty (12.50%). This means the lessee pays 100% of the cost to drill, complete and produce a well, and in return, receives 7/8ths (87.50%) of the production proceeds. The standard royalty is 1/8th. However, depending on the area and activity, the royalty may be greater.

See *Chapter 5-A* to understand how to calculate your *decimal interest* in a well based on your royalty. See *Chapter 6-D* for an example of an oil royalty check and a gas royalty check. This will help you understand the meaning of each figure.

D) Bonus Consideration:

Another plus in mineral ownership is when you agree to lease, you are paid a *bonus*. This is calculated on the *net mineral acres* owned times the *bonus price per acre*. Grandpa agreed to a price of \$50 bonus per acre and because most leases are "*paid-up*" there would be \$1 added to the bonus, for prepayment of the rentals, for every year, after the first year, of the primary term. By prepaying the rentals on a lease, this keeps the lessee from having to remit yearly rental payments on every lease. The total bonus price per acre for a five-year paid-up oil and gas lease would be \$54; \$50 (bonus and 1st year) + \$1 (2nd year) + \$1 (3rd year) + \$1 (4th year) + \$1 (fifth and final year) = \$54 per net mineral acre.

Total bonus = \$5,940.00 (110.00 [net acres owned] x \$54.00)

The bonus payments are usually in the form of a *bank draft*. After the lease has been executed and notarized, the bank draft and lease are taken to the *collection department* of your bank. They forward all documents to the lessee's bank for payment. The draft will state the number of days, from receipt, in which payment is to be made. This is usually 30 days and allows time for examination, approval and allocation of funds for your lease.

