



EXCHANGES OF OIL, GAS AND MINERAL INTERESTS

Oil, gas and mineral interests are real estate interests which qualify for a like-kind exchange with any other qualifying real estate interest including -

- A fee interest in real estate
- Fractional ownership interests
- 30+ year leasehold interests
- Other oil, gas and mineral interests
- Conservation easements
- Transferable development rights
- Right-of-way easements
- Water rights
- Mutual irrigation ditch stock

A mineral interest is a perpetual interest on all of the minerals on a parcel of land including oil and gas, coal, gold, sand, gravel, water, etc.

There are several different kinds of ownership of oil, gas and mineral interests which include –

- Mineral rights which are a part of fee ownership of the ground.
- Mineral rights which are owned separately from ownership of the ground.
- A mineral lease granted to a lessee by the owner of the mineral rights.
- A royalty interest which can be viewed as a form of rent received by the owner of the mineral rights.

A mineral lease gives the lessee the right to extract the mineral for a period of time, or until exhaustion of the mineral. Mineral leases are sometimes referred to as a working interest or an operating interest. The lessee is the operator who is extracting the mineral. A mineral lease can be subleased to other operators.

An exchange of a working or operating interest might include equipment or other tangible personal property which would need be viewed as a multi-asset exchange (more than one kind of property).

A production payment is a right to the mineral in place for a specified sum of money, payable out of a specified percentage of the mineral production. It is a “carved out production payment” and is not considered real property for exchange purposes.

Depletion expense can be deducted by the owner of an operating or royalty interest. There are two types of depletion: percentage depletion and cost depletion. Taxpayers use the method that yields the highest deduction.

Intangible drilling costs are operating costs to extract the mineral. Costs for fuel, preparation of a site, and wages are examples of intangible drilling costs

Mineral property exchanges may be subject to recapture under Section 1254 if deductions were taken for depletion or intangible drilling costs on the relinquished property. The replacement property must be both like-kind and natural resource recovery property (Section 1254 property) to avoid recapture.

Talk to your tax advisor when you are anticipating a sale of a mineral interest. Call us at 888-367-1031 or email us at 1031@1031cpas.com if we can assist with questions about an exchange of your mineral interest. See our Exchange Manual and visit us at www.1031cpas.com. 1031 Corporation is the Intermediary of choice for real estate professionals, CPAs and investors.

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