214-775-5070

NON-PARTICIPATING ROYALTY INTERESTS

Non-Participating Royalty Interests (NPRI) is one of the most confusing terms that come up in oil and gas or other mineral leasing situations. Let's take a look at each portion of the phrase so we can better understand it – starting with "interests."

The meaning of interests, in this situation, indicates that someone owns a share, or interest, in the mineral production. Royalty indicates that the interest is only in the royalty, or percentage share of the values of the minerals sold. That means the interest holder does not receive any part of bonuses, rental payments, surface damages or shut-in payments. They only get the designated percentage of royalties. And, non-participating means that the interest owner does not get to make decisions regarding the leasing, exploration, or development.

So, if you add all that up, basically you have someone who gets paid a portion of the ongoing royalties from mineral extraction – and only the royalties. The mineral rights owner makes all the decisions about leasing and selling, keeps all bonuses and other payments, and only shares the designated percentage of royalties with the NPRI owner.

NPRI's can acquire their interests in several common ways. A mineral rights owner may transfer a non-participating royalty interest to a child or other family member as a gift, while still maintaining control of his or her land and rights to a great degree. Some mineral rights owners choose to sell a portion of their royalties in order to receive a lump sum of cash earlier than through royalty checks alone. Again, they will retain their decision-making authority. And, some NPRI owners have received their interests through inheritance.

Non-participating royalty interests can be good for both parties, then. The mineral rights owner maintains decision-making control while potentially receiving cash up-front. And, the NPRI owner is due royalties that may pay back an initial investment many times over – and they generally participate in no other costs of production. State mineral laws and court cases have, to some degree, impacted NPRIs in various states. So, you should have an attorney review any mineral interest agreement that you decide to participate in.

So, what does a basic non-participating royalty interest look like in real life? Say Rancher Smith has a good hunch that there is plenty of natural gas underneath his ranch. Smith knows that natural gas prices are low, but he thinks that they'll go up in a year or so. In the meantime, he really needs a new tractor. So, Smith sells a 1/32 NPRI for $25,000 to Farmer Jones, who was retiring and looking for a steady source of income down the road.

One year later the natural gas market was still a little low, but after another year Smith leases his oil and gas rights for a large bonus and a 1/8 royalty. Jones, then, gets 1/4 of the royalty (1/4 x 1/8 = 1/32) and Smith gets the other 3/4 of the 1/8 (or 3/32 of the total royalty). As you can see, Smith made the decisions on when and to whom he leased the rights, and Jones gets his cut without doing anything more than buying in up front.

That is the best we can do to explain basic non-participating royalty interests, but keep in mind what we said earlier – the mineral rights laws in each state dictate how NPRIs are handled in that state.

Be sure you have good legal advice when participating in one of these complex financial transactions.

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