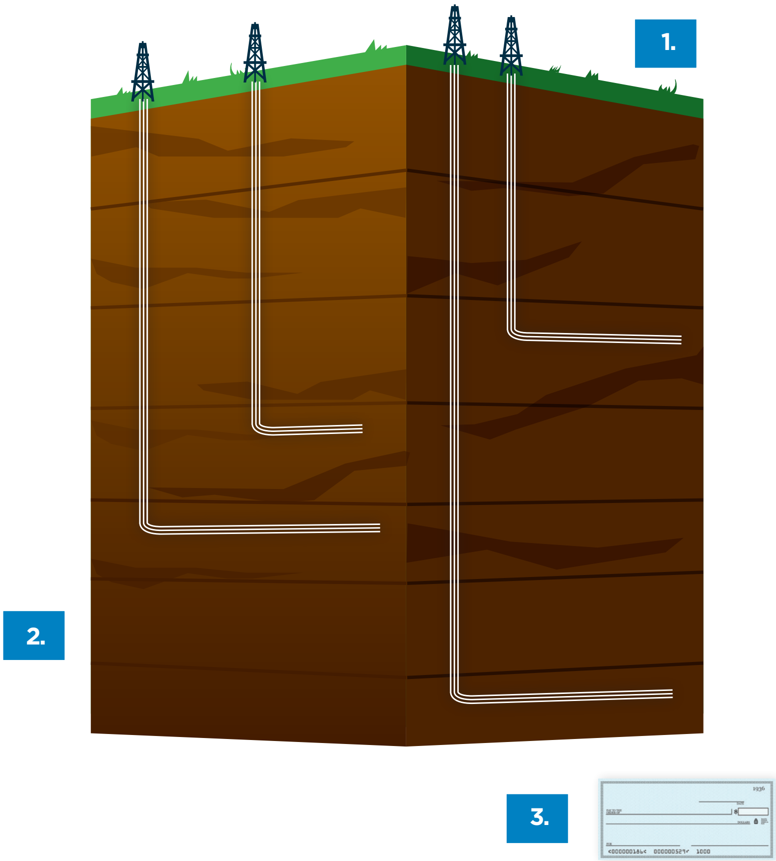
# USING ROYALTIES IN A 1031 EXCHANGE

RESOURCE ROYALTY, LLC
UNCONVENTIONAL ROYALTY

# WHAT ARE ROYALTIES?

**A ROYALTY IS A PERCENTAGE OF REVENUE PAID** to a land owner (aka mineral owners) from the production of oil and gas on his or her property.




**WE DO NOT DRILL**

## HOW DO MINERAL OWNERS GET PAID A ROYALTY?

**1.** Mineral Owners own interest in the sub-surface real estate—everything from the crust to the core—and are entitled to compensation for everything that is produced from their land.

**2.** As energy companies drill wells and produce hydrocarbons, they are required to pay a royalty to the mineral owners. The energy company, known as the operator, pays all drilling and operating expenses and assumes all drilling risks and liabilities.

**3.** Mineral Owners receive monthly royalty checks from the companies operating on their properties. This payment is generally 15-25%** of the gross revenue produced from the property and is free and clear of any operational costs and drilling risks.

***This percentage range is not guaranteed and will vary based on individual lease agreements.*

# 1031 "INTO" AND "OUT OF" ROYALTIES

## ROYALTIES ARE LIKE-KIND TO REAL ESTATE

Royalties & mineral rights are considered real property[1] and are deemed to be "like-kind" to traditional real estate, qualifying them to be used in a 1031 exchange[2].

Individuals engaging in a 1031-Exchange can use royalties and minerals as an exchange solution. Subsequently, if they are looking to "exchange out of" minerals/royalties, they are able to purchase any other "like-kind" asset.

1. *See IRS Revenue Ruling 55-526; 88-78; 73-428*

2. *IRS Private Letter Ruling 8237017 (June 11, 1982) states that "[t]he working interests presently held by the Owners and the overriding royalty interests to be held by them are, accordingly, properties of a like kind within the meaning of Section 1031(a) of the Code, since each is a continuing interest in real property . . ."*

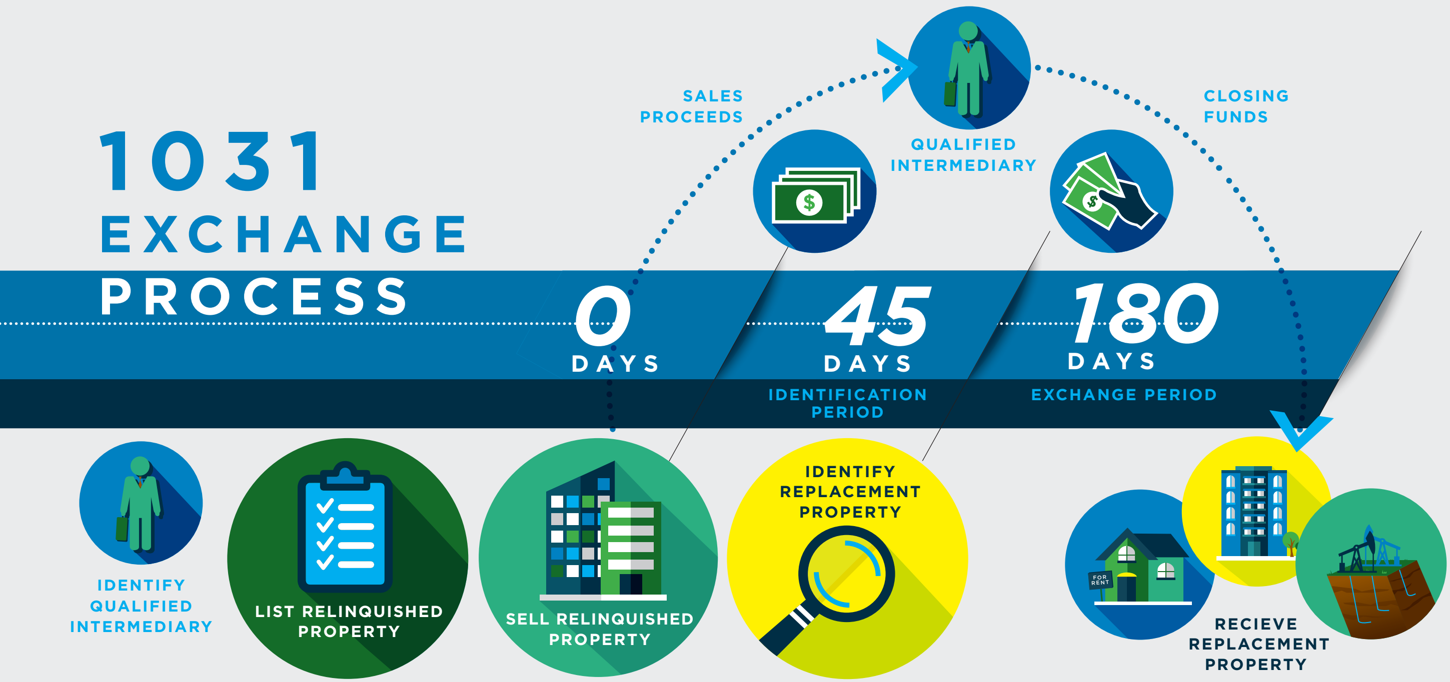
# WHAT IS A 1031 EXCHANGE?

## THANKS TO IRC SECTION 1031…

Investors are able to defer all of their capital gain taxes from the sale of an investment property if they reinvest the proceeds into a new, "like-kind" property.

**IRC SECTION 1031 (A)(1) STATES:**

*"No gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment, if such property is exchanged solely for property of like-kind which is to be held either for productive use in a trade or business or for investment."*



# IDENTIFICATION RULES

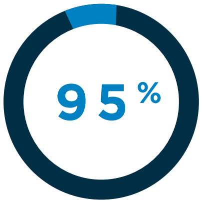
**INVESTORS HAVE THE CHOICE OF THREE DIFFERENT** identification rules for identifying replacement properties. They only need to comply with one of these rules to conduct an exchange.

## 3 PROPERTY RULE

Investors can Identify three replacement properties regardless of their total value. Investors can then choose to exchange into one individual property or all three.

## 95% RULE

Investors can identify any number of replacement properties, regardless of their total value, as long as the replacement properties acquired amount to at least 95% of the total value of all the identified properties.





## 200% RULE

Investors can identify any number of replacement properties so long as their total value does not exceed 200% of the total value of the relinquished property.

# ROYALTIES VS. DST'S & TIC'S

| | ROYALTIES | DELAWARE STATUTORY TRUST (DST) | TENANTS IN COMMON (TIC) |
|---|---|---|---|
| **1031 EXCHANGE ELIGIBLE?** | YES | YES | YES |
| **PASSIVE CASH FLOW?** | YES* | YES | YES |
| **DEBT USED?** | NO – NO LEVERAGE IS USED OR ACCEPTED | LEVERAGE IS OFTEN USED & ACCEPTED | LEVERAGE IS OFTEN USED & ACCEPTED |
| **OWNERSHIP** | DIRECT TITLE:<br>INVESTORS HOLD TITLE AND HAVE FULL OWNERSHIP OF THEIR INTEREST | BENEFICIAL INTEREST IN TRUST:<br>INVESTORS DO NOT HOLD THE TITLE AND HAVE LIMITED CONTROL OVER THEIR INVESTMENT AND ARE SOLELY RELIANT TO THE SPONSOR | FULL OWNERSHIP OF PRO-RATA SHARE OF TITLE:<br>EACH INVESTOR OWNS AN UNDIVIDED, PRO-RATA SHARE OF TITLE TO THE PROPERTY |
| **LIQUIDITY** | FULL CONTROL:<br>OWNERS HAVE FULL CONTROL OF THE LIQUIDITY OF THEIR INTEREST. | CONTROLLED BY SPONSOR:<br>TRADITIONAL LIQUIDITY LOCK-UPS<br>THE SPONSOR HAS FULL CONTROL OVER SELLING THE PROPERTY PRIOR TO THE END OF THE LOCK-UP PERIOD. | FULL CONTROL OF INTEREST ONLY:<br>OWNERS HAVE FULL CONTROL OF THE LIQUIDITY OF THEIR UNDIVIDED INTEREST ONLY. THE SALE OF THE PROPERTY CAN'T BE DONE WITHOUT THE CONSENT OF ALL THE OWNERS. |


*Royalty income generally is treated as portfolio income and does not offset passive losses.*

# CHARACTERISTICS OF ENERGY ROYALTIES

## IN A 1031 EXCHANGE

**1. PORTFOLIO DIVERSIFICATION:**
Royalties & minerals provide an opportunity for investors to step away from traditional real estate and diversify into a different asset class with exposure to different economics.

**2. TRANSACTION SIZE FLEXIBILITY:**
Private Royalty Ownership is a 1031-Exchange alternative that allows you customize your investment level. Whether you sell your property for $100,000 or $5,000,000 you can exchange the exact proceeds into oil and gas royalties.

**3. CURRENT CASH FLOW:**
Low distributions based on compressed capitalization rates have left many traditional real estate investors hungry for higher rates of return. Minerals & Royalties have the potential to experience an acceleration in cash flow caused by the drilling of additional wells by oil & gas operators.

**4. INVESTOR INDEPENDENCE:**
Owners of undivided interests in royalty properties are not locked into an ownership structure that links them to other investors in the same property. Each owner is free to exercise control over holding period and exit strategy to suit individual investment objectives.

**5. CAN BE USED TO AVOID “CASH BOOT”:**
The purchase of minerals & royalties can be used to consume any remaining exchange proceeds that an individual may have from the sale of their relinquished property or properties.

**6. TAX ADVANTAGED INCOME:**
Royalty income is allotted a 15% tax depletion allowance, meaning that 15% of the income received is tax sheltered.

*“The meek shall inherit the Earth, but not its mineral rights.”*

*– J. PAUL GETTY*

***RESOURCE ROYALTY*** *is a provider of mineral and royalty portfolios eligible for 1031 "like-kind" exchanges.*

*With an estimated 12 million mineral owners[1] in the United States and nearly $40 million paid in royalty payments annually[2], minerals and royalties bring an institutional-grade investment without institutional level minimums.*

*These deeded and titled assets provide investors with current cash flow, a natural hedge against inflation and a low correlation to the equities market.*

*Now available to the retail market, individuals have the opportunity to diversify away from traditional brick and mortar real estate into this alternative asset class.*

*[1] National Association of Royalty Owners (NARO)*

*[2] https://www.wsj.com/articles/mineral-rights-can-make-you-rich-1499638593*

# ALL INVESTMENTS HAVE RISKS...

- This material may contain forward-looking statements that are based on expectations and assumptions that are subject to risk and uncertainties.
- Oil and gas Mineral Interests and Royalty Interests are illiquid investments. In addition, the oil and gas market is affected by many factors, such as general economic conditions, oil and natural gas pricing, financing markets, supply and demand, and other factors that are beyond the Offeror's control. All these factors could restrict an investor's ability to sell their mineral/royalty interests.
- Operators are not obligated to drill or keep wells in production
- There is no assurance that the Offering will achieve all or any of its investment objectives.
- Production rates may be variable from region to region.
- There is no assurance that targets will be met.
- There is no assurance that additional drilling will take place or will achieve successful results.
- Investment in oil and gas royalties is speculative and involves a high degree of risk; investors should be able to bear the complete loss of their investment.
- This is neither an offer to sell nor a solicitation of an offer to buy interests in an Offering as offers are made solely pursuant to the PPM.
- Prospective investors should consult their own advisors to evaluate the tax consequences of an investment.
- Securities offered through JCC Advisors, LLC, member FINRA/SIPC.
- Resource Royalty, LLC and JCC Advisors, LLC are not affiliated.

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