



NM STATE LAND OFFICE

2025 RMD INDUSTRY TRAINING

Audit Bureau
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AUDIT BUREAU

DISCLAIMER

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AUDIT TEAM



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AGENDA

Define the Role of an Audit

What We Do and Why It Matters?

Audit Process

- Types of Audits
- Scope Selection
- Audit Process (Start to Finish)

Our Commitment to You

AuditBoard
New Audit Management System!!

Why Are Audits Helpful?

- Audit Challenges



WHAT WE DO AND WHY IT MATTERS?

- Ensure our Trust Beneficiaries receive their entitled share of royalties
 - 22 Beneficiaries (Common Schools, Hospitals, Universities and Community Institutions)
- Collaborative, educational, and innovative approach to our audits
 - Ensure the accuracy in reporting and distribution of royalties
 - Each lease is linked to a specific beneficiary
 - Each lease prefix identifies the Royalty Rate
- Our goal is to audit 80% of royalties in 4-5 year cycles
- Compliance with contract terms (Lease / Cooperative Agreements)
- Audits also help **YOU** correct issues that can potentially **save** everyone **time and money!**



What Triggers an Audit?

AUDIT PROCESS

- Random Selections
 - 4-5 year cycles
 - Large – midsize companies will go through Field Audits
- Close outs
- Mergers / Acquisitions / Name Changes
- Affiliations / Joint Ventures
- Referrals
 - Intra-agency (compliance reviews, request for refunds, etc.)
 - Discrepancies found during an audit in which other entities have shared interest



Types of Audits

AUDIT PROCESS

Desk Audits

- Smaller companies
- Specific properties identified through a prior audit of another company OR referral
- Scope **not** large enough to warrant travel to the company
- ***Request for Refund**
 - Referral from Compliance Bureau
 - Specific properties identified through a prior audit of another company OR referral
 - Scope **not** large enough to warrant travel to the company

Field Audits

- Larger companies
- Scope large enough to warrant travel
- Auditors onsite for 1-2 weeks

Trespass

- Identified production without an active lease contract
- Royalties due on these schedules are 100%
- Beware of Termination Notices on PUN(s) or Contracts
 - COMM Agreements
- Upon filing a return, a PUN error may result, and remitted royalties will go into suspense



Desk Audit vs. Field Audit

AUDIT PROCESS

Desk Audit

1. Pre-Audit
 - Scope selection
 - Creating Draft Schedules
 2. Engagement Packet
 - Engagement Letter
 - Draft Schedules
 - Draft schedules are based on index price
 3. Company Response – 30 days
 - Provide settlement statements
 4. Final Schedules
 5. Audit Findings Summary
 6. Company files amendments and remit royalties
 7. Interest Assessment(s) will be generated
 8. Company to pay Interest Assessment(s)
 9. All done!
- Desk Audits are not as formal as Field Audits and often have a much smaller scope.
 - Our Draft Schedules are based on assumptions based on C-115 reports and OGR2 reports, and valued at Index Price.
 - Once you receive the Engagement Letter and Draft Schedules, we will need your data to update our schedules with more accurate information, such as pricing, allocations, etc.



Desk Audit vs. Field Audit

AUDIT PROCESS

Field Audit

1. Pre-Audit
 1. Scope selection
 2. Notify Company and coordinate field dates
2. Engagement Packet
 1. Engagement Letter
 1. Scope
 2. Required Documents*
 3. Audit Questionnaire
 4. Audit Confirmation
 2. Schedule Introductory Call
3. Company Response
 1. 3-4 months to upload Required Documents
 2. Schedule document and system walkthroughs
4. Field Work (1-2 weeks)
 1. Opening meeting Monday morning
 1. Expectations for the audit
 2. Walkthroughs / questions
 2. Testing / building schedules
 3. 80-100% of draft schedules should be provided before departing
 4. Findings and Discussion Meeting before departing
5. Final Schedules
 1. Company has 30 days to review and approve schedules
6. Audit Findings Letter
7. Company files amendments and remit royalties
 1. When amending returns, all previously booked lines must be backed out verbatim. New lines will be booked to Transaction Code 55.
8. Interest Assessment(s) will be generated
9. Company to pay Interest Assessment(s)
10. All done! (See you in 4 – 5 years! ☺)

****We do not close out audits – all properties are subject to re-audit.**

Please refrain from making amendments to previously audited properties and let us know if you need to make any amendments.



Desk Audit vs. Field Audit **AUDIT PROCESS**

Field Audit – Required Documents

At a **minimum** the following documents must be provided:

1. Settlement Statement for all scoped properties and periods
2. Allocation Schedules (if applicable)
 1. Central Delivery Point (CDP's)
3. DOI's
4. Contract Terms
5. Cross-reference of wells and settlement statements (when there are multiple statements and wells)
6. Transportation and processing invoice statements
7. Netback pricing and calculation methods

****If you need it to calculate your royalty returns, we will need it too.**



Scope Development

*same for Desk and Field Audits

AUDIT PROCESS

1. Volume

Review volumes reported to OCD on the C-115 returns to volumes reported on the OGR2 form, factoring in the State's Net Interest (SNI).

3. Price and Variance

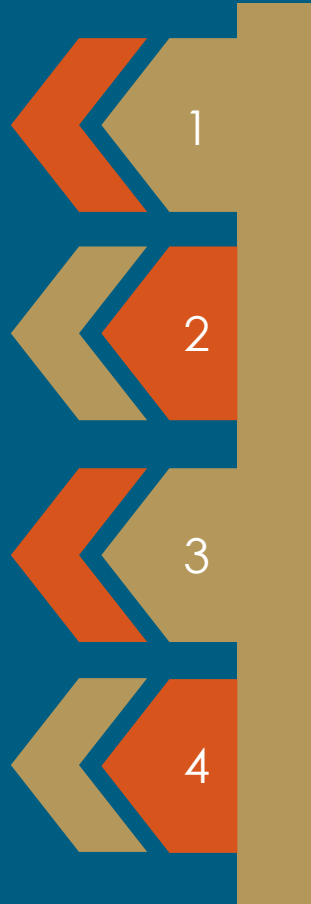
Wellhead price review – a per-volume value comparison to other remitters and other properties in the same field or area.

2. Value

Review of gross and net proceeds as well as per volumes values reported to the Land Office.

4. Deductions

% of gross proceeds, comparison to other remitters and other properties in the same field or area.





Scope Development

*same for Desk and Field Audits


AUDIT PROCESS

1. Volume Review: Review volumes reported to OCD on the C-115 returns to volumes reported on the OGR2 form, factoring in the State's Net Interest (SNI).


1. Convert wellhead mcf volumes to the NM standardized Pressure Base of 15.025

OCD


NMSLO



Sale YR	Sale MTH	PUN	Prop Name	Pool IDN	C-115 Disposition	SNI	SNI Volume	Roy Volume	Roy Diff
2023	08	1234567	TRAINING	4567	16,727	100%	16,727	16,727 ✓	0 ✓



Sale YR	Sale MTH	PUN	Prop Name	Pool IDN	C-115 Disposition	SNI	SNI Volume	Roy Volume	Roy Diff
2023	08	1234567	TRAINING	4567	16,727	100%	16,727	8,364 !	8,363



Sale YR	Sale MTH	PUN	Prop Name	Pool IDN	C-115 Disposition	SNI	SNI Volume	Roy Volume	Roy Diff
2023	08	1234567	TRAINING	4567	16,727	50% ☆	8,364	8,364 ✓	0 ✓



Scope Development

*same for Desk and Field Audits

AUDIT PROCESS

2. Value Review: Review of gross and net proceeds as well as per volumes values reported to the Land Office.

Example 1:
Volume Review

Sales Year	Sales Month	PUN	Property name	Pool	C115 Disposition	SNI	SNI Volume	Remitted Volume	Difference
2023	8	1234567	TRAINING	96830	16,727	100%	16,727	11,621	5,106

Value Review

Sales MTH / YR	PUN	Lease	PC	Trns Cd	Ams Len	Vol MCF	NGL Gal	BTU No.	GRSS PRCDS	Deducts	Roy Paid
823	1234567	B01234	3	51 Y		11,621	-	1,302	13,815	3,521	1,287
823	1234567	B01234	7	51 Y		-	104,570	-	27,087	13,872	1,652

- Volume discrepancy
 - Underreported volumes
 - -0- MCF reported on product code 7
- No monetary audit finding
- Amended reporting necessary





Scope Development

*same for Desk and Field Audits

AUDIT PROCESS

2. Value Review: Review of gross and net proceeds as well as per volumes values reported to the Land Office.

Example 2:
Volume Review

Sales Year	Sales Month	PUN	Property name	Pool	C115 Disposition	SNI	SNI Volume	Remitted Volume	Difference
2023	8	1234567	TRAINING	96830	16,727	100%	16,727	11,621	5,106

Value Review

Sales MTH / YR	PUN	Lease	PC	Trns Cd	Ams Len	Vol MCF	NGL Gal	BTU No.	GRSS PRCDS	Deducts	Roy Paid
823	1234567	B01234	3	51 Y		11,621	-	1,302	13,000	3,521	1,185
823	1234567	B01234	7	51 Y		-	104,570	-	27,087	13,872	1,652

- Volume discrepancy
- Gross proceeds differs from settlement statement
- Audit needed





Scope Development

*same for Desk and Field Audits

AUDIT PROCESS

3. Price and Variance Review

- Price comparison as a per-volume / value comparison to other remitters and other properties in the same area
- Underreported volumes due to -0- MCF reported on product code 7 line
- Reporting Gallons in MCF field
- No reporting on Negative Gross Revenue
- No reporting on Negative Net Revenue
- No reporting on newly acquired properties
- Reporting on incorrect basis – Takes/Entitlements
- Reporting to incorrect:
 - SNI
 - PUN
 - Product Code
 - Allocation
 - Pressure Base



Scope Development

*same for Desk and Field Audits

AUDIT PROCESS

4. Deductions

Allowable

- Post production costs that make the product merchantable

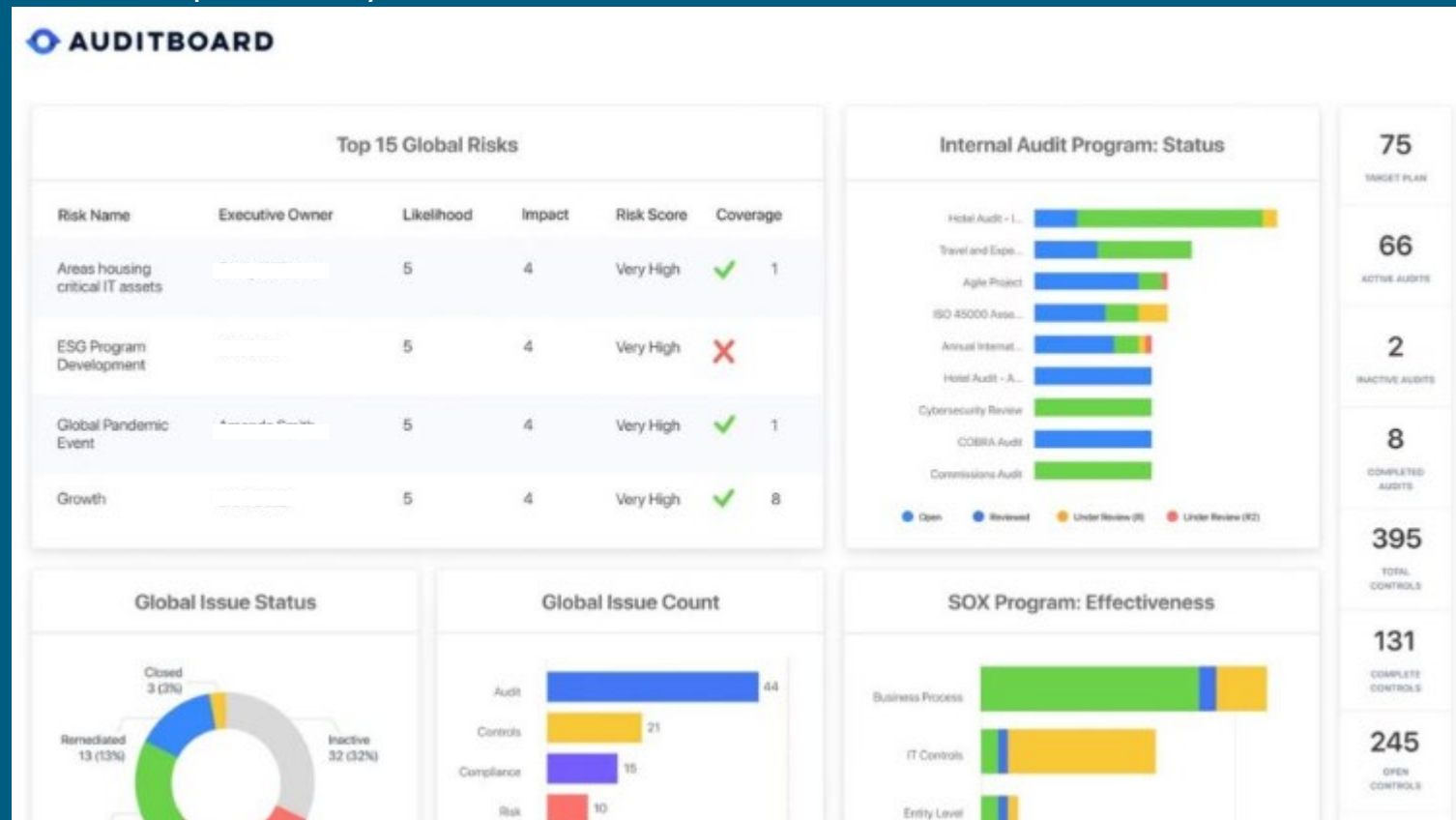
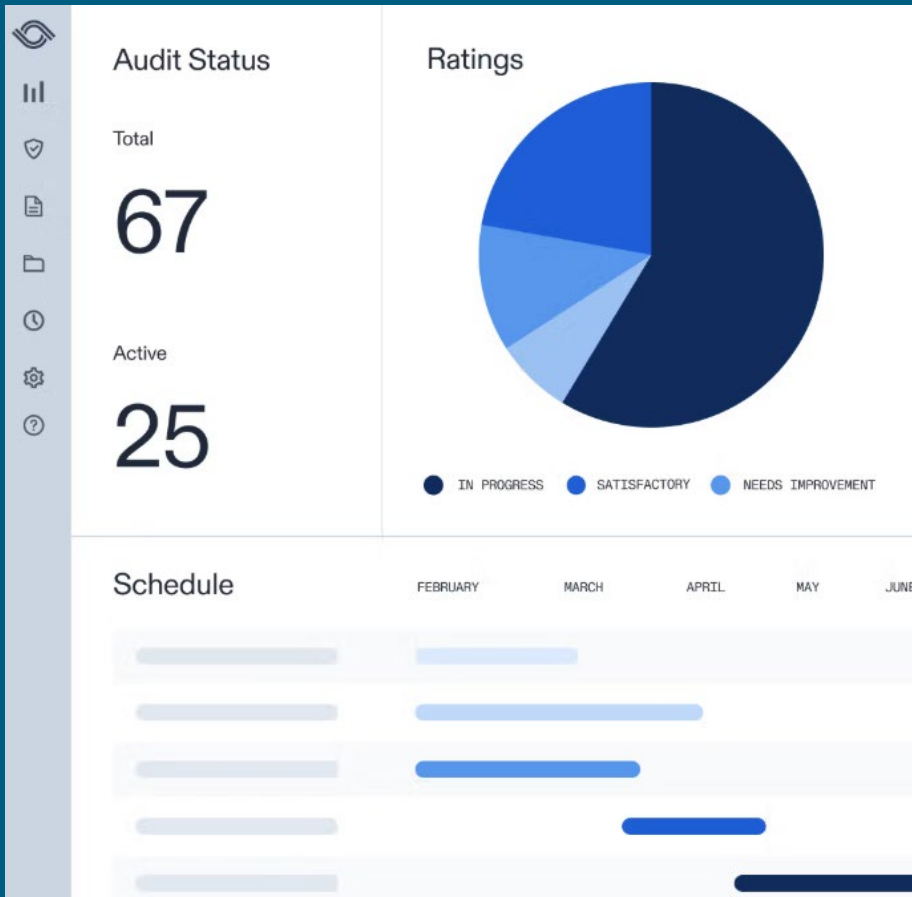
Non-Allowable

- New Mexico Gas Processors Tax
- Low volume fees, throughput fees, or low margin fees
- Metering fees
- Penalties
- Marketing Fees
- Any other costs incurred that **do not** make the product merchantable



OUR COMMITMENT TO CONSISTENCY AND INNOVATION

**Examples only!





WHY ARE AUDITS HELPFUL?

Audit Challenges

- Operator changes / Acquisitions
 - Effective dates of royalty burdens
 - Transaction Service Agreement
- Takes vs Entitlement Reporting
 - Takes = Uniform land owner, beneficiaries, and royalty rates
 - Entitlements = all different (similar to federal royalty)
- Reporting to Incorrect PUN(s)
 - Volume discrepancies
 - Over / under payments of royalties
 - Affects the distribution of monies to beneficiaries
- UNITS
 - PA wells or NP wells
 - UNIT phases
 - UNIT Comms
 - Consent / Non consent wells
 - DOI's
- CDP's (Central Delivery Point)
 - Settlement statements
 - Incorrect allocations
- Netback Pricing
 - Weighted Average Sales Price (WASP) Calculations
- Affiliated Sales
 - Tracing – first arm's length sale



HOW CAN YOU BE PROACTIVE AND AVOID POTENTIAL ISSUES?

Tools Available to You

PUN / Lease Inquiry Screen

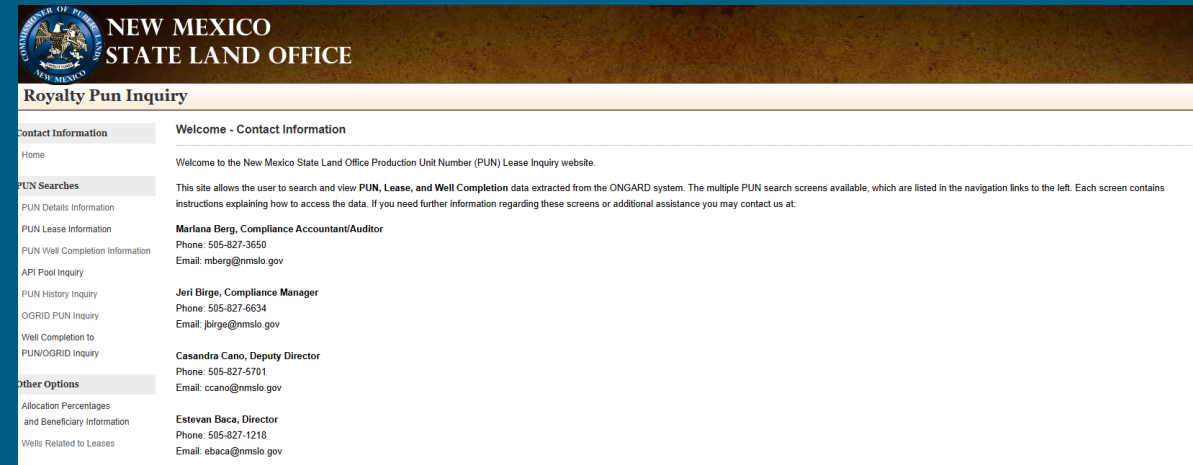
Royalty Pun Inquiry

C-115 to Royalty Volume Check

- Ensure MCF and Oil / Condensate BBLs Tie
- Identify Product Code Errors
 - Product Code 7 mcf plug
 - Oil Reported As Gas **OR** Gas Reported As Oil
- Identify Negative Revenue Not Reported

CSV Template With Lease Rate Verification Tool

- Verify Lease Royalty Rate on Return is Correctly Calculated
- Royalty Management Forms
- Royalty Online Filing



QUESTIONS?

None, it's all crystal clear!





LET'S WORK TOGETHER!



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