

An oil pumpjack is silhouetted against a dramatic sunset sky with orange and yellow clouds. The pumpjack's long arm extends from the top center towards the right. Below it, the complex metal structure of the wellhead and platform is visible, with various pipes and walkways. The overall scene is industrial and atmospheric.

Energy Working Interest Integration: An Exclusive Briefing for Tax and Financial Professionals

A Decision Stage Briefing on IRC Statutory Mechanics, K-1 Reporting Standards, and the Operating Framework for Referring Qualified Clients into Direct Working Interest Participation

SUMMIT VENTURES

CONFIDENTIAL ADVISOR BRIEFING

Executive Summary and Core Objective

Who This Briefing Is For

01

CPAs and Tax Professionals

02

RIAs and Qualified Intermediaries

03

Business Brokers and M&A Advisors

04

Estate Planning Attorneys

05

Commercial Real Estate Brokers

The Core Question

Each of you is regularly asked some version of the same question: is there a legitimate, statute-based way to reduce a client's tax exposure or redeploy sale proceeds without introducing reputational or compliance risk into the relationship.

The Core Objective

The core objective of this session is narrow and practical: walk through how direct working interest ownership in oil and gas development is structured under existing IRC provisions, what documentation and reporting your practice should expect to receive, and how Summit Ventures operates as the entrepreneurial joint venture partner behind that structure.

- ❏ This is not a product pitch. It is a technical orientation you can use to evaluate whether the category belongs in a client conversation at all, and if so, what to ask for before it does.

Context and Market Environment

Direct participation in oil and gas development is not a new or exotic category. The intangible drilling cost deduction traces to 1916 Treasury guidance and was codified as IRC Section 263(c) in the 1954 Code, making it one of the oldest targeted provisions still active in the tax code.

What has changed is client demand. Year-end income spikes from bonuses, K-1 pass-through allocations, or a liquidity event create a recurring planning problem: most conventional deduction categories are capped, phased out at higher AGI, or simply exhausted by the time a client's accountant sees the full picture in Q4.

Legislative Update

The One Big Beautiful Bill Act (signed July 2025) made 100% bonus depreciation under IRC Section 168(k) **permanent** for qualifying property, reversing the prior phase-down schedule.

Production Reality

U.S. crude oil production reached approximately **13.6 million barrels per day** in 2025 per the EIA's Annual Energy Outlook — an active, producing segment of the domestic economy.

Advisor Demand

Advisors are fielding more questions about this category now because the statutory tools are stable and the triggering client events — exits, exchanges, bonus years — are common.

Key Problem and Challenge

Reputational Risk

The reputational risk of recommending or facilitating an investment that turns out to be poorly documented, aggressively marketed, or structured in a way that does not actually hold up under IRS scrutiny. A client audit traced back to your referral is a relationship-ending event, not a minor service hiccup.

Opportunity Cost Risk

The opportunity cost risk of having no answer at all when a client specifically asks about tax-advantaged alternatives, a 1031 replacement property solution, or a place to deploy post-sale proceeds — and watching that client find a solution (and a new primary advisor) elsewhere.

The Underlying Technical Challenge

Working interest tax treatment depends entirely on how the interest is held. A direct working interest, or one held through an entity that does not limit the holder's liability, is treated differently under **IRC Section 469(c)(3)** than a limited partnership or LLC membership interest in a pooled fund.

Advisors who are not given clear documentation on which structure applies cannot responsibly evaluate the opportunity, and clients who hold the wrong structure forfeit the active income offset they were expecting.

 Structure determines eligibility. Documentation is non-negotiable.

Key Findings

Three findings should anchor how you evaluate this category for client fit.

1

IRC Section 263(c) — IDC Deduction

Treas. Reg. 1.612-4 allows a working interest holder to elect to expense intangible drilling costs (IDC) — non-salvageable expenditure such as labor, fuel, drilling mud, and site preparation — in the year incurred rather than capitalizing them. Tangible drilling costs are capitalized and depreciated separately. Industry sources commonly describe IDC as representing **60 to 85 percent** of total well cost, confirmed through the Authorization for Expenditure (AFE).

2

IRC Section 469(c)(3) — Active Income Offset

Section 263(c) governs deduction timing and classification only. The provision that determines whether that deduction can offset a client's active income (W-2, 1099, or K-1 pass-through) is IRC Section 469(c)(3), the working interest exception to the passive activity loss rules. This exception applies specifically when the interest is held directly or through an entity that does not limit liability — with **no material participation or hours test required**, a meaningfully lower bar than real estate professional status.

3

IRC Sections 611 and 613A — Percentage Depletion

These sections provide an ongoing **15 percent percentage depletion allowance** on gross income from production for independent producers once a well is generating revenue — a benefit that continues even after the client's cost basis in the property reaches zero.

Evidence: Statutory and Regulatory Grounding

The structural rules above are not marketing claims — they are drawn directly from the Code and from published guidance, which is precisely why they hold up under the scrutiny your clients' returns will eventually face.



IRC Section 465

At-risk limitation caps any deduction at the client's actual economic exposure, counting cash contributed and recourse debt only, not nonrecourse financing.



IRC Section 57(a)(2)

Treats excess IDC as an AMT preference item for independent producers, with relief generally available where excess IDC does not exceed 65% of net income from oil and gas properties for the year.



IRC Section 461(h)

The economic performance rule limits how much IDC a client can legitimately prepay in December for a well that will not spud for months, subject to a 90-day drilling exception.



Rev. Rul. 68-331

Holds that a working interest in a producing oil and gas lease is real property, like-kind to a fee interest in improved real estate, under Section 1031.



Rev. Rul. 78-135

Draws the necessary contrast: a general partnership interest itself does not qualify for 1031 treatment — the client must hold an actual direct or undivided working interest, not a fund or partnership share.

Analysis: Advisor-by-Advisor Implications

For the CPA and tax professional in the room, the throughline is straightforward: Section 469(c)(3) eligibility and Section 1031 eligibility under Rev Rul 68-331 both depend on the same structural fact — whether the client holds a direct interest or an interest in an entity that limits liability. That single documentation point should be the first thing you confirm before advising a client on either strategy, and it should be confirmable in writing, not inferred from a sales deck.



RIA and Qualified Intermediary

This category functions as a complement to, not a replacement for, the client's existing allocation or exchange strategy.



Business Broker / M&A Advisor

The relevant moment is typically the weeks following a closing, when a client is holding sale proceeds and facing a concentrated ordinary income or capital gains event with few remaining statutory offsets.



Estate Planning Attorney

Direct working interest ownership introduces a real, operationally active asset into a broader wealth transfer or diversification conversation, with its own reporting and governance characteristics distinct from securities or passive real estate holdings.



Commercial Real Estate Broker

A direct working interest is one of the few asset types that can credibly sit inside a 1031 identification alongside, or instead of, a replacement property.

Options: Three Paths for Advisors

When a client raises one of these scenarios, an advisor generally has three paths.

1

Path 1: Say Nothing

Let the client's existing advisors or a generic search result fill the gap. This carries the **opportunity cost risk** described earlier — including the risk of losing the client relationship entirely.

2

Path 2: Pooled Fund / LP Structure

Refer the client to a pooled fund or LP/LLC-structured program. May be appropriate for some clients but **structurally forecloses** the Section 469(c)(3) active income offset and the Rev Rul 68-331 like-kind analysis.

3

Path 3: Direct Working Interest Partner

Bring in a partner structured specifically around direct working interest participation, with **documentation built to withstand the scrutiny** of your own review and, eventually, the client's examination risk.

Each path has a legitimate place depending on the client's goals, liquidity needs, and risk tolerance. The point of this briefing is not to argue that direct participation is universally correct — it is to make sure you are evaluating the structural distinction with full information before recommending any of the three.

Recommendation and Summit Ventures' Role

Summit Ventures operates as a direct oil and gas entrepreneurial joint venture platform, structured so that active JV members hold a working interest position directly, consistent with the structural requirements discussed on the prior two slides. Our recommendation to this room is procedural, not promotional.

Before Any Client Conversation, Request and Review:

1 Governing Joint Operating Agreement

Language confirming direct holding status.

2 Current Tax Opinion Letter

From independent counsel addressing the IDC and depletion mechanics.

3 Sample K-1 Allocation Schedule

Reviewed before any client introduction is made.

Summit's Role in Your Practice

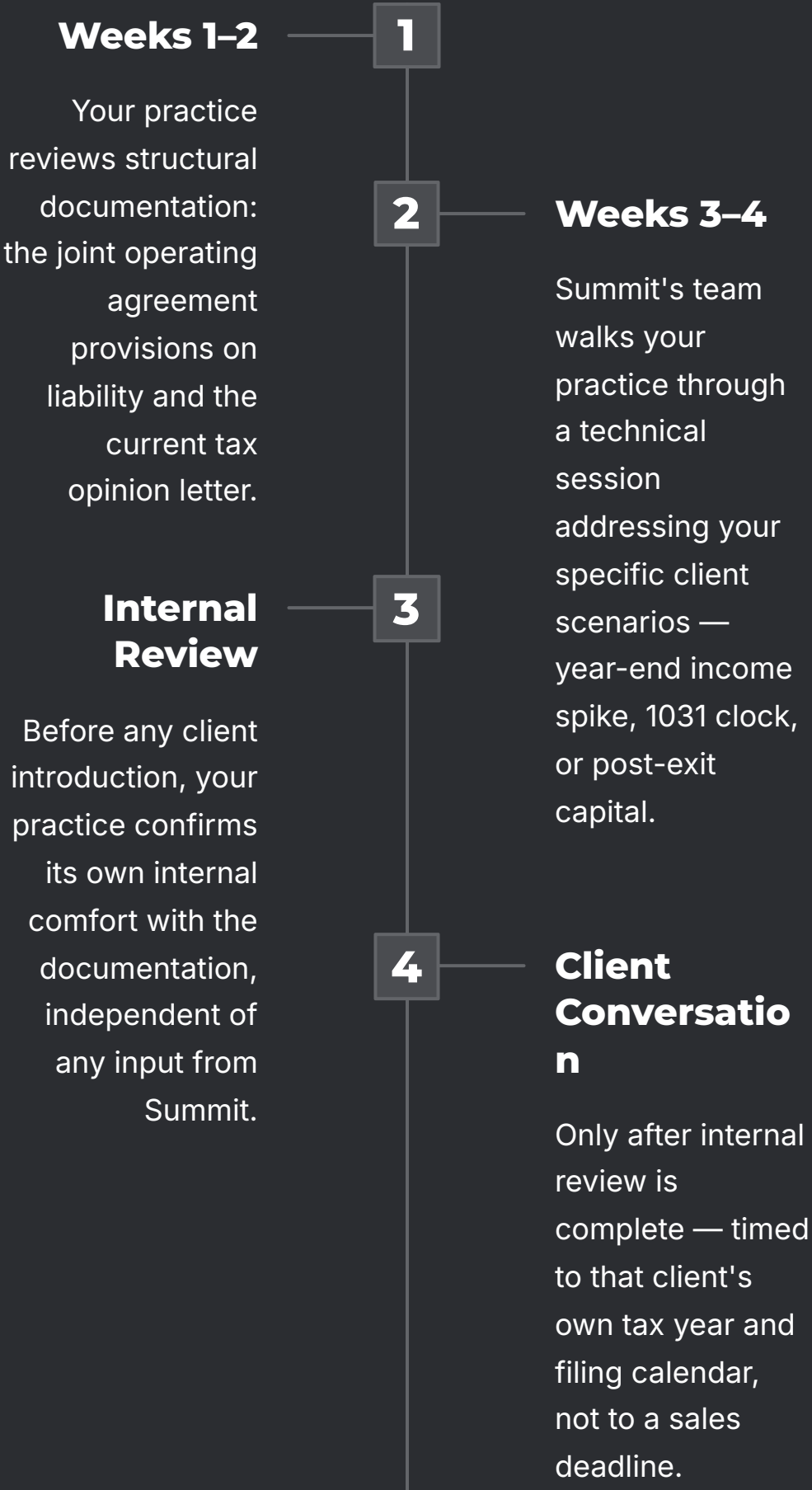
Summit's role in the relationship is to function as a **back-office educational and reporting partner** to your practice, not to replace your advisory relationship with the client.

- Direct CPA support line during filing season
- Standardized and timely K-1 delivery
- Audit-ready schedules that map cleanly to the statutory positions discussed in this briefing
- Documentation trail supporting both your workpapers and your client's return

[Request Documentation Review](#)

Timeline, Compliance Safeguards, and Summary

Advisor Evaluation Timeline



Compliance and Regulatory Safeguards

Summit provides a current tax opinion letter from independent counsel addressing the IDC, depletion, and working interest classification positions described in this briefing. K-1 allocations are delivered on a standardized schedule with a direct CPA support line available during filing season — specifically to address the complexity objection that keeps many advisors from engaging with this category during the compressed weeks of tax season. Governing documents confirm the direct holding structure required for Section 469(c)(3) and Rev Rul 68-331 analysis in writing, rather than leaving that determination to inference.

❏ Summit does not make legal or tax determinations on behalf of your client. Those determinations remain the responsibility of the client's own CPA, tax counsel, or qualified intermediary.

Summary

Direct working interest participation sits on a genuinely old and well-documented part of the tax code, anchored by IRC Section 263(c), Section 469(c)(3), Section 465, Section 57(a)(2), and Sections 611/613A, along with the real property treatment established in Revenue Ruling 68-331. The single fact that determines whether a client's interest qualifies for the active income offset and for 1031 like-kind treatment is the same in both cases: **how the interest is held.**

Summit Ventures is positioned to support that review as an entrepreneurial joint venture partner — not as a product vendor — with documentation, tax opinion letters, and K-1 reporting built around the governance and compliance standards your practice already applies to every other recommendation you make. The next step available to you is a technical documentation review, on your schedule, before any client is introduced to the structure.

[Begin Your Document...](#)

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Sources and References

IRC Section 263(c) and Treas. Reg. 1.612-4 (intangible drilling cost election). IRC Section 469(c)(3)(A) (working interest exception to passive activity loss rules), Cornell Legal Information Institute, 26 U.S.C. Section 469. IRC Section 465 (at-risk limitation). IRC Section 57(a)(2) (excess IDC as AMT preference item for independent producers). IRC Sections 611 and 613A (percentage depletion allowance). IRC Section 461(h) (economic performance, 90-day drilling exception). Revenue Ruling 68-331, 1968-1 C.B. 352 (working interest in producing oil and gas lease as like-kind real property under Section 1031). Revenue Ruling 78-135 (general partnership interest does not qualify for Section 1031 treatment). One Big Beautiful Bill Act (signed July 2025) and IRS Notice 2026-11 (permanent 100 percent bonus depreciation under IRC Section 168(k)). U.S. Energy Information Administration, Annual Energy Outlook 2026 (U.S. crude oil production data).