

NORTH EUROPEAN OIL ROYALTY TRUST
Form 10-Q
August 30, 2018

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended July 31, 2018 or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from . . . to . . .

Commission file number 1-8245

NORTH EUROPEAN OIL ROYALTY TRUST

(Exact name of registrant as specified in its charter)

Delaware _____ 22-2084119

(State of organization) (IRS Employer I.D. No.)

43 West Front Street, Suite 19A, Red Bank, New Jersey 07701

(Address of principal executive offices)

(732) 741-4008

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Edgar Filing: NORTH EUROPEAN OIL ROYALTY TRUST - Form 10-Q

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ___ No ___

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ___ No

<u>Class</u>	<u>Outstanding</u> as of July 31, 2018
Units of Beneficial Interest	9,190,590

PART I -- FINANCIAL INFORMATIONItem 1. Financial Statements.

	<u>2018</u>	<u>2017</u>
ASSETS		
Current assets -- Cash and cash equivalents	\$1,878,517	\$2,126,005
Producing gas and oil royalty rights, net of amortization (Notes 1 and 2)	—	1
Total Assets	\$1,878,518	<u>\$2,126,006</u>
LIABILITIES AND TRUST CORPUS		
Current liabilities -- Distributions to be paid to unit owners, paid August 2018 and paid November 2017	\$1,746,212	\$2,021,929
Trust corpus (Notes 1 and 2)	1	1
Undistributed earnings	<u>132,305</u>	<u>104,076</u>
Total Liabilities and Trust Corpus	<u>\$1,878,518</u>	<u>\$2,126,006</u>

The accompanying notes are an integral part of these financial statements.

	<u>2018</u>	<u>2017</u>
Gas, sulfur and oil royalties received	\$1,900,082	\$1,974,441
Interest income	<u>1,228</u>	<u>1,230</u>
Trust Income	<u>\$1,901,310</u>	<u>\$1,975,671</u>
Non-related party expenses	(117,742)	(115,679)
Related party expenses (Note 3)	<u>(15,937)</u>	<u>(19,298)</u>
Trust Expenses	<u>(133,679)</u>	<u>(134,977)</u>
Net Income	<u>\$1,767,631</u>	<u>\$1,840,694</u>
Net income per unit	<u>\$0.19</u>	<u>\$0.20</u>
Distributions per unit paid or to be paid to unit owners	<u>\$0.19</u>	<u>\$0.20</u>

The accompanying notes are an integral part of these financial statements.

	<u>2018</u>	<u>2017</u>
Gas, sulfur and oil royalties received	\$5,724,343	\$5,617,957
Interest income	<u>3,842</u>	<u>2,806</u>
Trust Income	<u>\$5,728,185</u>	<u>\$5,620,763</u>
Non-related party expenses	(582,264)	(547,831)
Related party expenses (Note 3)	<u>(62,867)</u>	<u>(57,312)</u>
Trust Expenses	<u>(645,131)</u>	<u>(605,143)</u>
Net Income	<u>\$5,083,054</u>	<u>\$5,015,620</u>
Net income per unit	<u>\$0.55</u>	<u>\$0.55</u>
Distributions per unit paid or to be paid to unit owners	<u>\$0.55</u>	<u>\$0.54</u>

The accompanying notes are an integral part of these financial statements.

	<u>2018</u>	<u>2017</u>
Balance, beginning of period	\$104,076	\$62,476
Net income	<u>5,083,054</u>	<u>5,015,620</u>
	5,187,130	5,078,096
Less:		
Current year distributions paid or to be paid to unit owners	<u>5,054,825</u>	<u>4,962,919</u>
Balance, end of period	<u>\$132,305</u>	<u>\$115,177</u>

The accompanying notes are an integral part of these financial statements.

2018

2017

The accompanying notes are an integral part of these financial statements.

NORTH EUROPEAN OIL ROYALTY TRUST

NOTES TO FINANCIAL STATEMENTS

(Unaudited)

(1) Summary of significant accounting policies:

Basis of accounting -

The accompanying financial statements of North European Oil Royalty Trust (the "Trust") are prepared in accordance with the rules and regulations of the SEC. Financial statement balances and financial results are presented on a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States ("GAAP basis"). In the opinion of management, all adjustments that are considered necessary for a fair presentation of these financial statements, including adjustments of a normal, recurring nature, have been included.

On a modified cash basis, revenue is earned when cash is received and expenses are incurred when cash is paid. GAAP basis financial statements disclose revenue as earned and expenses as incurred, without regard to receipts or payments. The modified cash basis of accounting is utilized to permit the accrual for distributions to be paid to unit owners (those distributions approved by the Trustees for the Trust). The Trust's distributable income represents royalty income received by the Trust during the period plus interest income less any expenses incurred by the Trust, all on a cash basis. In the opinion of the Trustees, the use of the modified cash basis of accounting provides a more meaningful presentation to unit owners of the results of operations of the Trust.

The results of any interim period are not necessarily indicative of the results to be expected for the fiscal year. These financial statements should be read in conjunction with the financial statements that were included in the Trust's Annual Report on Form 10-K for the year ended October 31, 2017 (the "2017 Form 10-K"). The Statements of Assets, Liabilities and Trust Corpus included herein contain information from the Trust's 2017 Form 10-K.

Producing gas and oil royalty rights -

The rights to certain gas and oil royalties in Germany were transferred to the Trust at their net book value by North European Oil Company (the "Company") (see Note 2). The net book value of the royalty rights has been reduced to one dollar (\$1) in view of the fact that the remaining net book value of royalty rights is de minimis relative to annual royalties received and distributed by the Trust and does not bear any meaningful relationship to the fair value of such rights or the actual amount of proved producing reserves.

Federal and state income taxes -

The Trust, as a grantor trust, is exempt from federal income taxes under a private letter ruling issued by the Internal Revenue Service. The Trust has no state income tax obligations.

Cash and cash equivalents -

Cash and cash equivalents are defined as amounts deposited in bank accounts and amounts invested in certificates of deposit and U. S. Treasury bills with original maturities generally of three months or less from the date of purchase. The investment options available to the Trust are limited in accordance with specific provisions of the Trust Agreement. As of July 31, 2018, the uninsured amount held in the Trust's U.S. bank accounts was \$1,622,802. In

addition, the Trust held Euros 4,870, the equivalent of \$5,715, in its German bank account at July 31, 2018.

Net income per unit -

Net income per unit is based upon the number of units outstanding at the end of the period. As of both July 31, 2018 and 2017, there were 9,190,590 units of beneficial interest outstanding.

New accounting pronouncements -

The Trust is not aware of any recently issued, but not yet effective, accounting standards that would be expected to have a significant impact on the Trust's financial position or results of operations.

(2) Formation of the Trust:

The Trust was formed on September 10, 1975. As of September 30, 1975, the Company was liquidated and the remaining assets and liabilities of the Company, including its royalty rights, were transferred to the Trust. The Trust, on behalf of the owners of beneficial interest in the Trust, holds overriding royalty rights covering gas and oil production in certain concessions or leases in the Federal Republic of Germany. These rights are held under contracts with local German exploration and development subsidiaries of ExxonMobil Corporation and the Royal Dutch/Shell Group of Companies. Under these contracts, the Trust receives various percentage royalties on the proceeds of the sales of certain products from the areas involved. At the present time, royalties are received for sales of gas well gas, oil well gas, crude oil, condensate and sulfur.

(3) Related party transactions:

John R. Van Kirk, the Managing Director of the Trust, provides office space and office services to the Trust at cost. For such office space and office services, the Trust reimbursed the Managing Director \$6,717 and \$5,311 in the third quarter of fiscal 2018 and 2017, respectively. For such office space and office services, the Trust reimbursed the Managing Director \$19,356 and \$17,947 in the first nine months of fiscal 2018 and 2017, respectively.

Lawrence A. Kobrin, a Trustee of the Trust, is a Senior Counsel at Cahill Gordon & Reindel LLP, which serves as counsel to the Trust. For the third quarter of fiscal 2018 and 2017, the Trust paid Cahill Gordon & Reindel LLP \$9,220 and \$13,987 for legal services, respectively. For the first nine months of fiscal 2018 and 2017, the Trust paid Cahill Gordon & Reindel LLP \$43,511 and \$39,365 for legal services, respectively.

(4) Employee benefit plan:

The Trust has established a savings incentive match plan for employees (SIMPLE IRA) that is available to both employees of the Trust, one of whom is the Managing Director. The Trustees have authorized the Trust to make contributions to the accounts of the employees, on a matching basis, of up to 3% of cash compensation paid to each employee effective for the 2018 and 2017 calendar years.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Executive Summary

The Trust is a passive fixed investment trust which holds overriding royalty rights, receives income under those rights from certain operating companies, pays its expenses and distributes the remaining net funds to its unit owners. As mandated by the Trust Agreement, distributions of income are made on a quarterly basis. These distributions, as determined by the Trustees, constitute substantially all of the funds on hand after provision is made for Trust expenses then anticipated.

The Trust does not engage in any business or extractive operations of any kind in the areas over which it holds royalty rights and is precluded from engaging in such activities by the Trust Agreement. There are no requirements, therefore, for capital resources with which to make capital expenditures or investments in order to continue the receipt of royalty revenues by the Trust.

The properties of the Trust, which the Trust and Trustees hold pursuant to the Trust Agreement on behalf of the unit owners, are overriding royalty rights on sales of gas, sulfur and oil under certain concessions or leases in the Federal Republic of Germany. The actual leases or concessions are held either by Mobil Erdgas-Erdol GmbH ("Mobil Erdgas"), a German operating subsidiary of the ExxonMobil Corporation ("ExxonMobil"), or by Oldenburgische Erdolgesellschaft ("OEG"). The Oldenburg concession is the primary area from which the natural gas, sulfur and oil are extracted and currently provides 100% of all the royalties received by the Trust. The Oldenburg concession (approximately 1,386,000 acres) covers virtually the entire former Grand Duchy of Oldenburg and is located in the German federal state of Lower Saxony.

In 2002, Mobil Erdgas and BEB Erdgas und Erdol GmbH ("BEB"), a joint venture of ExxonMobil and the Royal Dutch/Shell Group of Companies, formed a company, ExxonMobil Production Deutschland GmbH ("EMPG"), to carry out all exploration, drilling and production activities. All sales activities are still handled by the operating companies, either Mobil Erdgas or BEB. EMPG put out a press release in Germany on August 6, 2018 announcing the successful completion of a new sidetrack out of an existing well in eastern Oldenburg, Goldenstedt Z-12a M1. The horizontal deviation used a steerable drill bit in a miniature format in conjunction with coiled tubing. The drill bit in this instance is "about the size of a tennis ball." This is the first time this technique was used successfully in Germany. The net result of this drilling was a substantial increase in recoverable reserves for this well.

Vermilion Energy Inc. ("Vermilion"), a Canadian based international oil and gas producer, entered into a Farm-In Agreement (the "Farm-In Agreement") with Mobil Erdgas and BEB effective as of January 1, 2016. The Trust has been advised by its consultant in Germany that, based on conversations with people at EMPG and other sources, the Farm-In Agreement specifies that Vermilion has acquired an interest in various portions of a concession or areas owned by Mobil Erdgas and BEB. Three of these licenses cover the three northernmost areas of the Oldenburg concession. The Farm-In Agreement commits Vermilion to financial participation at a 50% level in 11 gross exploratory wells over the next five years. Three of these wells will be drilled in areas subject to the Trust's royalties. If a well in the area subject to the Trust's royalties is a discovery, Vermilion's participation in the production and sale will be 50%. Vermilion's participation in the development of any well does not impact the Trust's royalty interest and the sale of that gas or oil would be subject to the relevant royalty contract. Based upon statements from EMPG to the Trust's consultant, Vermilion will lead the development of its first well within the Oldenburg concession with a possible start time in 2020. The planned well-site is located in the western portion of the area designated Oldenburg-Land, the southernmost area of the three areas within the concession subject to Vermilion's Farm-In Agreement. Vermilion's well is intended to develop the Rotliegend (Red Sandstone) formation, a previously undeveloped productive zone within the concession. Additionally, according to EMPG and in accordance with the terms of the Farm-In Agreement, Vermilion will drill two other wells within the Oldenburg concession, one in

Jeverland and one in Jade-Weser. No details concerning these wells or any other activities by Vermilion are available to the Trust at this date and Vermilion is under no obligation to disclose such information.

The operating companies pay monthly royalties to the Trust based on their sales of natural gas, sulfur and oil. Of these three products, natural gas provided approximately 94% of the cumulative royalty income received in fiscal 2018. The amount of royalties paid to the Trust is primarily based on four factors: the amount of gas sold, the price of that gas, the area from which the gas is sold, and the exchange rate.

On approximately the 25th of the months of January, April, July and October, the operating companies calculate the amount of gas sold during the previous calendar quarter and determine the amount of royalties that were payable to the Trust based on those sales. This amount is divided into thirds and forms the monthly royalty payments (payable on the 15th of each month) to the Trust for its upcoming fiscal quarter. At the same time that the operating companies determine the actual amount of royalties that were payable for the prior calendar quarter, they look at the actual amount of royalties that were paid to the Trust for that period and calculate the difference between what was paid and what was payable. Additional amounts payable by the operating companies would be paid immediately and any overpayment would be deducted from the payment for the first month of the following fiscal quarter. In September of each year, the operating companies make the final determination of any necessary royalty adjustments for the prior calendar year with a positive or negative adjustment made accordingly. The Trust's German accountants review the royalty calculations on a biennial basis.

There are two types of natural gas found within the Oldenburg concession, sweet gas and sour gas. Sweet gas has little or no contaminants and needs no treatment before it can be sold. Sour gas, in comparison, must be processed at the Grossenkneten desulfurization plant before it can be sold. The desulfurization process removes hydrogen sulfide and other contaminants. The hydrogen sulfide in gaseous form is converted to sulfur in a solid form and sold separately. As needed, EMPG conducts maintenance on the plant generally during the summer months when demand is lower. The operating companies have informed the Trust that, to promote greater efficiency and cost effectiveness, the production capacity of Grossenkneten was reduced by approximately one-third through the retirement of Unit 3. With full operation of the two remaining units, raw gas input capacity would stand at approximately 400 million cubic feet ("MMcf") per day. While originally EMPG had indicated there would be no maintenance conducted during 2018, one of the two units was shut down from February to March 2018. A second shutdown for both of the units followed for the period from May 19 to June 5, 2018. This initial problem was related to an emissions control issue. However, while these repairs were being conducted, further problems were discovered with one of the units. EMPG has informed the Trust that they expect the repair work on this unit to be fully completed by the end of August 2018. While this unit is undergoing repairs, the total throughput capacity will be reduced by 40-50%.

Under one set of rights covering the western part of the Oldenburg concession (approximately 662,000 acres), the Trust receives a royalty payment of 4% on gross receipts from sales by Mobil Erdgas of gas well gas, oil well gas, crude oil and condensate (the "Mobil Agreement"). Under the Mobil Agreement, there is no deduction of costs prior to the calculation of royalties from gas well gas and oil well gas, which together accounted for approximately 98% of the cumulative royalty income received under this agreement in fiscal 2018. Historically, the Trust has received significantly greater royalty payments under the Mobil Agreement, as compared to the OEG Agreement described below, due to the higher royalty rate specified by that agreement.

The Trust is also entitled under the Mobil Sulfur Agreement to receive a 2% royalty on gross receipts of sales of sulfur obtained as a by-product of sour gas produced from the western part of Oldenburg. The payment of the sulfur royalty is conditioned upon sales of sulfur by Mobil Erdgas at a selling price above an agreed upon base price. This base price is adjusted annually by an inflation index. In the first nine months of fiscal 2018, the Trust received \$46,458 in sulfur royalties under the Mobil Sulfur Agreement. The Trust was entitled to receive sulfur royalties for the third quarter but due to the overpayment of royalties by the operating companies, the sulfur royalties were used to reduce the amount of the overpayment. In the first nine months of fiscal 2017, the Trust received \$84,405 in sulfur royalties under the Mobil Sulfur Agreement.

Edgar Filing: NORTH EUROPEAN OIL ROYALTY TRUST - Form 10-Q

Under another set of rights covering the entire Oldenburg concession and pursuant to the agreement with OEG, the Trust receives royalties at the rate of 0.6667% on gross receipts from sales by BEB of gas well gas, oil well gas, crude oil, condensate and sulfur (removed during the processing of sour gas) less a certain allowed deduction of costs (the "OEG Agreement"). Under the OEG Agreement, 50% of the field handling and treatment costs, as reported for state royalty purposes, are deducted from the gross sales receipts prior to the calculation of the royalty to be paid to the Trust.

In addition to the Oldenburg area, the Trust also holds overriding royalties at various rates on a number of currently non-producing leases of various sizes in other areas of Germany. One of these leases, Grosses Meer, was formerly active but provided no royalties during fiscal 2018, 2017 and 2016. Vermilion is scheduled to participate in a new well to be drilled in an area which includes the Grosses Meer field as well as other non-royalty areas. However, no details are available at this date, and it is unknown if the well will be sited within the area subject to the Trust's royalty interest.

On August 26, 2016, the Trust executed amendments to its existing royalty agreements with OEG and Mobil establishing a new base for the determination of gas prices upon which the Trust's royalties are determined. This new base is set as the state assessment base for natural gas used by the operating companies in their calculation of royalties payable to the State of Lower Saxony. This change reflects a shift from the use of gas ex-field prices ("contractual prices") to the prices calculated for the German Border Import gas Price ("GBIP"). For simplification purposes, we will use "GBIP" when referring to the current state assessment base.

The change to the GBIP is intended to be revenue neutral for the Trust. Additionally, this change should reduce the scope and cost of the accounting examination, eliminate ongoing disputes with OEG and Mobil regarding sales to related parties, and reduce prior year adjustments to the normally scheduled year-end reconciliation. The new pricing basis also eliminates certain costs (transportation and plant gas storage), one half of which were previously deductible prior to the royalty calculation under the agreement with OEG.

Actual gas sales from the prior calendar quarter are multiplied by the average GBIP for a period starting two months earlier and provide the basis for royalty payments to the Trust during its fiscal quarter. The average GBIP for the corresponding period of actual sales is not available due to the delay in its calculation. As of the start of calendar 2016, the average GBIP under the Mobil and OEG Royalty Agreements was and will continue to be increased by 1% and 3%, respectively.

In March of the following calendar year, an average GBIP for the prior calendar year (weighted on a monthly basis by the respective volume of imported gas) is published. In September of the following calendar year, EMPG makes a final reconciliation based upon the published yearly average GBIP increased by the respective percentage factor and the total volume of gas sold under the royalty agreements during the prior calendar year. Required additions to royalty amounts already paid are paid immediately. Required deductions from royalty amounts already paid are deducted from the next royalty payment due.

The new basis for oil prices is the published price from the State Authority for Mining, Energy and Geology. There are no percentage adjustments factored into the oil royalty calculation. There is no change in the previous methodology used with regard to the determination of royalties attributable to sales of sulfur.

The Trust itself does not have access to the specific sales contracts under which gas from the Oldenburg concession is sold. However, working under a confidentiality agreement with the operating companies, the Trust's German accountants will confirm that the volume of gas sales corresponds to the amount reported under the sales contracts and that the weighted GBIP was properly calculated and applied in the calculation of royalties payable to the Trust.

For unit owners, changes in the dollar value of the Euro have an immediate impact. This impact occurs at the time the royalties, which are paid to the Trust in Euros, are converted into U.S. dollars at the applicable exchange rate and

transferred from Germany to the United States. In relation to the dollar, a stronger Euro would yield more dollars and a weaker Euro would yield less dollars.

Seasonal demand factors affect the income from the Trust's royalty rights insofar as they relate to energy demands and increases or decreases in prices, but on average they are generally not material to the annual income received under the Trust's royalty rights.

The Trust has no means of ensuring continued income from overriding royalty rights at their present level or otherwise. The Trust's consultant in Germany provides general information to the Trust on the German and European economies and energy markets. This information provides a context in which to evaluate the actions of the operating companies. The Trust's consultant receives reports from EMPG with respect to current and planned drilling and exploration efforts. However, EMPG and the operating companies continue to limit the information flow to that which is required by German law.

The low level of administrative expenses of the Trust limits the effect of inflation on costs. Sustained price inflation would be reflected in sales prices. Sales prices along with sales volumes form the basis on which the royalties paid to the Trust are computed.

Results: Third Quarter of Fiscal 2018 versus Third Quarter of Fiscal 2017

Total royalty income received during the third quarter of fiscal 2018 was derived from sales of gas, sulfur and oil from the Trust's overriding royalty areas in Germany during the second calendar quarter of 2018. A distribution of 19 cents per unit will be paid on August 29, 2018 to owners of record as of August 17, 2018. Comparisons of total royalty income and net income for the third quarter of fiscal 2018 and 2017 are shown below.

	<u>3rd Fiscal Quarter Ended</u> <u>7/31/2018</u>	<u>3rd Fiscal Quarter Ended</u> <u>7/31/2017</u>	<u>Percentage</u> <u>Change</u>
Total Royalty Income	\$1,900,082	\$1,974,441	- 3.77%
Net Income	\$1,767,631	\$1,840,694	- 3.97%
Distribution per Unit	\$0.19	\$0.20	- 5.00%

The decrease in total royalty income for the third quarter of fiscal 2018 from the third quarter of fiscal 2017 resulted primarily from the decline in gas sales due to the interruption of processing at the Grossenkneten desulfurization plant in the February and March 2018 period in combination with the loss of processing capacity at Grossenkneten following the retirement of Unit 3. This decline more than offset the increase in gas prices and average exchange rate. There were no adjustments impacting royalties during the third quarter of fiscal 2018 or fiscal 2017. There were no royalties received under the Mobil Sulfur Agreement in either the third quarter of fiscal 2018 or fiscal 2017.

The table below is intended to illustrate trends based on actual gas sales in each fiscal quarter. Gas royalties shown in the table below are determined based on the actual physical gas sales that occurred during the second calendar quarter of 2018 and the average German Border Import gas Price for the period of February 2018 through April 2018. Under both the Mobil and OEG Agreements, lower gas sales were the primary factor contributing to the decrease in royalty income during the third quarter of fiscal 2018 in comparison to the third quarter of fiscal 2017.

	<u>2nd Calendar</u>	<u>2nd Calendar</u>			
	<u>Quarter</u>	<u>Quarter</u>	<u>Percentage</u>		
	<u>Ended</u>	<u>Ended</u>			
<u>Mobil Agreement</u>	<u>6/30/2018</u>	<u>6/30/2017</u>	<u>Change</u>		
Gas Sales (Bcf) ¹	3.593	5.500	- 34.67%		
Gas Prices ² (Ecents/Kwh) ³	1.9141	1.7406	+ 9.97%		
Average Exchange Rate ⁴	1.1705	1.1175	+ 4.74%	Gas Prices (\$/Mcf) ⁵	\$6.43 \$5.55 + 15.86%

OEG Agreement**Footnotes**

1. Billion cubic feet
2. Gas prices derived from February-April period
3. Euro cents per kilowatt hour
4. Based on average Euro/dollar exchange rates of cumulative royalty transfers
5. Dollars per thousand cubic feet

Excluding the effects of differences in prices and average exchange rates, the combination of royalty rates on gas sold from western Oldenburg results in an effective royalty rate approximately seven times higher than the royalty rate on gas sold from eastern Oldenburg. This is of particular significance to the Trust since gas sold from western Oldenburg provides the bulk of royalties paid to the Trust. For the calendar quarter ended June 30, 2018, gas sales from western Oldenburg accounted for only 30.68% of all gas sales from the Oldenburg concession. However, royalties on these gas sales provided approximately 78.75%, or \$1,437,669 out of \$1,825,601, of all royalties attributable to gas sales from the Oldenburg concession.

Trust expenses for the third quarter of fiscal 2018 decreased 0.96%, or \$1,298, to \$133,679 in comparison to \$134,977 for the third quarter of fiscal 2017. This decrease in expenses reflects the reduction in legal costs. Trust interest income received during the third quarter of fiscal 2018 was \$1,228, in comparison to \$1,230 received in the third quarter of fiscal 2017.

The current Statements of Assets, Liabilities and Trust Corpus of the Trust at July 31, 2018, compared to that at fiscal year-end (October 31, 2017), shows a decrease in assets due to lower royalty receipts during the third quarter of fiscal 2018.

Results: First Nine Months of Fiscal 2018 versus First Nine Months of Fiscal 2017

Total royalty income during the first nine months of fiscal 2018 was primarily derived from sales of gas, sulfur and oil from the Trust's overriding royalty areas in Germany during the fourth calendar quarter of 2017 and the first calendar quarter of 2018. Comparisons of total royalty income and net income for the first nine months of fiscal 2018 and 2017 are shown below.

	<u>Nine Months</u>	<u>Nine Months</u>	
	<u>Ended 7/31/2018</u>	<u>Ended 7/31/2017</u>	<u>Percentage Change</u>
Total Royalty Income	\$5,724,343	\$5,617,957	+ 1.89%
Net Income	\$5,083,054	\$5,015,620	+ 1.34%
Distribution per Unit	\$0.55	\$0.54	+ 1.85%

The increase in total royalty income in the first nine months of fiscal 2018 from the first nine months of fiscal 2017 resulted from higher royalty income totals for the first two quarters of fiscal 2018. Additionally, by the time that the operating companies had access to the data upon which to base their calculations of royalties payable in the third quarter for fiscal 2018, the Trust had already received its final payment for that quarter. As a result, the Trust received more royalties than it was owed in the final quarter of the nine-month period ended July 31, 2018, and the total royalty income for the current nine-month period is higher than it otherwise would have been. Therefore, the required negative adjustment will be offset against the scheduled royalty payments in the Trust's fourth fiscal quarter.

The table below is intended to illustrate trends based on actual gas sales in each fiscal nine-month period. Gas royalties shown in the table below are determined based on the actual physical gas sales that occurred during the fourth calendar quarter of 2017 and the first and second calendar quarter of 2018 and the average German Border Import gas Price for the period of August 2017 through April 2018. Under both the Mobil and OEG Agreements, lower gas sales were the primary factor contributing to the decline in royalty income during the first nine-month period of fiscal 2018 in comparison to the first nine-month period of fiscal 2017.

	<u>Nine Months</u>	<u>Nine Months</u>	<u>Percentage</u>	
	<u>Ended</u> <u>6/30/2018</u>	<u>Ended</u> <u>6/30/2017</u>	<u>Change</u>	
<u>Mobil Agreement</u>				
Gas Sales (Bcf)	14.447	17.923	- 19.39%	
Gas Prices(Ecents/Kwh)	1.7830	1.6465	+ 8.29%	
Average Exchange Rate	1.2041	1.0795	+ 11.54%	Gas Prices (\$/Mcf) \$6.12 \$5.08 + 20.47%

OEG Agreement

For the nine months ended 6/30/2018, gas sales from western Oldenburg accounted for only 31.25% of all gas sales from the Oldenburg concession. However, royalties on these gas sales provided approximately 79.88%, or \$4,312,708 out of \$5,399,039, of all royalties attributable to gas sales from the Oldenburg concession.

Trust expenses for the first nine months of fiscal 2018 increased 6.61% or \$39,988 to \$645,131 in comparison to \$605,143 for the prior fiscal year's equivalent period. This increase in expenses reflects accounting expenses associated with the royalty examination in Germany and an increase in the NYSE listing fee. Trust interest income received during the first nine months of fiscal 2018 increased to \$3,842 in comparison to \$2,806 received in the first nine months of fiscal 2017 due to higher interest rates in effect.

This report on Form 10-Q may contain forward-looking statements intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. Such statements address future expectations and events or conditions concerning the Trust. Many of these statements are based on information provided to the Trust by the operating companies or by consultants using public information sources. These statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those anticipated in any forward-looking statements. These include:

- risks and uncertainties concerning levels of gas production and gas sale prices, general economic conditions and currency exchange rates;
- the ability or willingness of the operating companies to perform under their contractual obligations with the Trust;
- potential disputes with the operating companies and the resolution thereof; and
- the risk factors set forth under Item 1A of the Trust's Annual Report on Form 10-K for the year ended October 31, 2017.

All such factors are difficult to predict, contain uncertainties that may materially affect actual results, and are generally beyond the control of the Trust. New factors emerge from time to time and it is not possible for the Trust to predict all such factors or to assess the impact of each such factor on the Trust. Any forward-looking statement speaks only as of the date on which such statement is made, and the Trust does not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Trust does not engage in any trading activities with respect to possible foreign exchange fluctuations. The Trust does not use any financial instruments to hedge against possible risks related to foreign exchange fluctuations. The market risk is negligible because standing instructions at the Trust's German bank require the bank to process conversions and transfers of royalty payments as soon as possible following their receipt. The Trust does not engage in any trading activities with respect to possible commodity price fluctuations.

Item 4. Controls and Procedures.

The Trust maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed by the Trust is recorded, processed, summarized, accumulated and communicated to its management, which consists of the Managing Director, to allow timely decisions regarding required disclosure, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

The Managing Director has performed an evaluation of the effectiveness of the design and operation of the Trust's disclosure controls and procedures as of July 31, 2018 based on the criteria for effective internal control over financial reporting described in the standards promulgated by the Public Company Accounting Oversight Board and the Internal Control-Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, the Managing Director concluded that the Trust's disclosure controls and procedures were effective as of July 31, 2018.

There have been no changes in the Trust's internal control over financial reporting identified in connection with the evaluation described above that occurred during the third quarter of fiscal 2018 that have materially affected or are reasonably likely to materially affect the Trust's internal control over financial reporting.

PART II -- OTHER INFORMATION

Item 1. Legal Proceedings.

The Trust is not a party to any pending legal proceedings.

Item 4. Mine Safety Disclosure.

Not applicable.

Item 6. Exhibits.

Exhibit 31. Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32. Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

NORTH EUROPEAN OIL ROYALTY TRUST

(Registrant)

/s/ John R. Van Kirk

John R. Van Kirk
Managing Director
August 30, 2018