FIRST ENGROSSMENT

Sixtieth
Legislative Assembly
of North Dakota

ENGROSSED SENATE BILL NO. 2397

Introduced by

Senators Wardner, Lyson, O'Connell

Representatives Belter, Onstad, Wieland

A BILL for an Act to amend and reenact sections 57-51.1-02, 57-51.1-03, and 57-51.1-03.1 of the North Dakota Century Code, relating to oil extraction tax rates, exemptions, and rate reductions; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-51.1-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-02. Imposition of oil extraction tax. There is hereby imposed an excise tax, to be known as the "oil extraction tax", upon the activity in this state of extracting oil from the earth, and every owner, including any royalty owner, of any part of the oil extracted is deemed for the purposes of this chapter to be engaged in the activity of extracting that oil.

<u>1.</u> ~~The~~ <u>For oil produced from wells drilled and completed before July 1, 2008, the</u> rate of tax is six and one-half percent of the gross value at the well of the oil extracted, except that the rate of tax is four percent of the gross value at the well of the oil extracted ~~in the following situations:~~ <u>that meets one of the requirements of subsection 3.</u>

<u>2.</u> <u>For oil produced from wells drilled and completed after June 30, 2008, the rate of tax is four percent of the gross value at the well of the oil extracted, including the oil extracted that meets one of the requirements of subsection 3.</u>

~~1.~~ <u>3.</u> <u>a.</u> For oil produced from wells drilled and completed after April 27, 1987, commonly referred to as new wells, and not otherwise exempt <u>or subject to a reduced tax rate</u> under section 57-51.1-03;

~~2.~~ <u>b.</u> For oil produced from a secondary or tertiary recovery project that was certified as qualifying by the industrial commission before July 1, 1991;

~~3.~~ c. For oil that does not qualify as incremental oil but is produced from a secondary or tertiary recovery project that is certified as qualifying by the industrial commission after June 30, 1991;

~~4.~~ d. For incremental oil produced from a secondary or tertiary recovery project that is certified as qualifying by the industrial commission after June 30, 1991, and which production is not otherwise exempt or subject to a reduced tax rate under section 57-51.1-03; or

~~5.~~ e. For oil produced from a well that receives an exemption pursuant to subsection 4 of section 57-51.1-03 after June 30, 1993, and which production is not otherwise exempt or subject to a reduced tax rate under section 57-51.1-03.

4. However, if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period, then the rate of tax on oil extracted from all taxable wells is six and one-half percent for wells subject to subsection 1 and four percent for wells subject to subsection 2, as a percentage of the gross value at the well of the oil extracted until the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period, in which case the rate of tax reverts to four percent of the gross value at the well of the oil extracted for any wells subject to a reduced rate under ~~subsections 1~~ subdivisions a through ~~5~~ e of subsection 3.

SECTION 2. AMENDMENT. Section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-03. Exemptions ~~from oil extraction tax~~ and rate reductions. The following activities are specifically exempted from, or subject to a reduced rate under, the oil extraction tax:

1. The activity of extracting from the earth any oil that is exempt from the gross production tax imposed by chapter 57-51.
2. The activity of extracting from the earth any oil from a stripper well property.
3. For a well drilled and completed as a vertical well before July 1, 2008, the initial production of oil from the well is exempt from any taxes imposed under this chapter for a period of fifteen months, except that oil produced from any well drilled

and completed as a horizontal well is exempt from any taxes imposed under this chapter for a period of twenty-four months.

<u>For a well drilled and completed as a vertical well after June 30, 2008, the initial production of oil from the well is subject to a tax of two percent of the gross value at the well of the oil extracted for a period of fifteen months, except that oil produced from any well drilled and completed as a horizontal well after June 30, 2008, is subject to a tax of two percent of the gross value at the well of the oil extracted for a period of twenty-four months.</u>

Oil recovered during testing prior to well completion is exempt from the oil extraction tax. The exemption <u>or rate reduction</u> under this subsection becomes ineffective if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period. However, the exemption <u>or rate reduction</u> is reinstated if, after the trigger provision becomes effective, the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period.

4. The production of oil from a qualifying well that was worked over is exempt from any taxes imposed under this chapter for a period of twelve months, beginning with the first day of the third calendar month after the completion of the work-over project.

The exemption provided by this subsection is only effective if the well operator establishes to the satisfaction of the industrial commission upon completion of the project that the cost of the project exceeded sixty-five thousand dollars or production is increased at least fifty percent during the first two months after completion of the project. A qualifying well under this subsection is a well with an average daily production of no more than fifty barrels of oil during the latest six calendar months of continuous production. A work-over project under this subsection means the continuous employment of a work-over rig, including recompletions and reentries. The exemption provided by this subsection becomes ineffective if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period. However, the exemption is reinstated if, after the trigger provision becomes effective, the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period.

5. a. The incremental production from a secondary recovery project which has been certified as a qualified project by the industrial commission after July 1, 1991, is exempt from any taxes imposed under this chapter for a period of five years from the date the incremental production begins.

b. The incremental production from a tertiary recovery project which has been certified as a qualified project by the industrial commission subsequent to June 30, 1991, is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins.

c. For purposes of this subsection, incremental production is defined in the following manner:

(1) For purposes of determining the exemption provided for in subdivision a and with respect to a unit where there has not been a secondary recovery project, incremental production means the difference between the total amount of oil produced from the unit during the secondary recovery project and the amount of primary production from the unit. For purposes of this paragraph, primary production means the amount of oil which would have been produced from the unit if the secondary recovery project had not been commenced. The industrial commission shall determine the amount of primary production in a manner which conforms to the practice and procedure used by the commission at the time the project is certified.

(2) For purposes of determining the exemption provided for in subdivision a and with respect to a unit where a secondary recovery project was in existence prior to July 1, 1991, and where the industrial commission cannot establish an accurate production decline curve, incremental production means the difference between the total amount of oil produced from the unit during a new secondary recovery project and the amount of production which would be equivalent to the average monthly production from the unit during the most recent twelve months

of normal production reduced by a production decline rate of ten percent for each year. The industrial commission shall determine the average monthly production from the unit during the most recent twelve months of normal production and must upon request or upon its own motion hold a hearing to make this determination. For purposes of this paragraph, when determining the most recent twelve months of normal production the industrial commission is not required to use twelve consecutive months. In addition, the production decline rate of ten percent must be applied from the last month in the twelve-month period of time.

(3) For purposes of determining the exemption provided for in subdivision a and with respect to a unit where a secondary recovery project was in existence before July 1, 1991, and where the industrial commission can establish an accurate production decline curve, incremental production means the difference between the total amount of oil produced from the unit during the new secondary recovery project and the total amount of oil that would have been produced from the unit if the new secondary recovery project had not been commenced. For purposes of this paragraph, the total amount of oil that would have been produced from the unit if the new secondary recovery project had not been commenced includes both primary production and production that occurred as a result of the secondary recovery project that was in existence before July 1, 1991. The industrial commission shall determine the amount of oil that would have been produced from the unit if the new secondary recovery project had not been commenced in a manner that conforms to the practice and procedure used by the commission at the time the new secondary recovery project is certified.

(4) For purposes of determining the exemption provided for in subdivision b and with respect to a unit where there has not been a secondary recovery project, incremental production means the difference between the total amount of oil produced from the unit during

the tertiary recovery project and the amount of primary production from the unit. For purposes of this paragraph, primary production means the amount of oil which would have been produced from the unit if the tertiary recovery project had not been commenced. The industrial commission shall determine the amount of primary production in a manner which conforms to the practice and procedure used by the commission at the time the project is certified.

(5) For purposes of determining the exemption provided for in subdivision b and with respect to a unit where there is or has been a secondary recovery project, incremental production means the difference between the total amount of oil produced during the tertiary recovery project and the amount of production which would be equivalent to the average monthly production from the unit during the most recent twelve months of normal production reduced by a production decline rate of ten percent for each year. The industrial commission shall determine the average monthly production from the unit during the most recent twelve months of normal production and must upon request or upon its own motion hold a hearing to make this determination. For purposes of this paragraph, when determining the most recent twelve months of normal production the industrial commission is not required to use twelve consecutive months. In addition, the production decline rate of ten percent must be applied from the last month in the twelve-month period of time.

(6) For purposes of determining the exemption provided for in subdivision b and with respect to a unit where there is or has been a secondary recovery project and where the industrial commission can establish an accurate production decline curve, incremental production means the difference between the total amount of oil produced from the unit during the tertiary recovery project and the total amount of oil that would have been produced from the unit if the tertiary recovery project had not been commenced. For purposes of this paragraph, the total

amount of oil that would have been produced from the unit if the tertiary recovery project had not been commenced includes both primary production and production that occurred as a result of any secondary recovery project. The industrial commission shall determine the amount of oil that would have been produced from the unit if the tertiary recovery project had not been commenced in a manner that conforms to the practice and procedure used by the commission at the time the tertiary recovery project is certified.

d. The industrial commission shall adopt rules relating to this exemption that must include procedures for determining incremental production as defined in subdivision c.

6. The production of oil from a two-year inactive well, as determined by the industrial commission and certified to the state tax commissioner, is exempt for a period of ten years after the date of receipt of the certification.

The exemption under this subsection becomes ineffective if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period. However, the exemption is reinstated if, after the trigger provision becomes effective, the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period.

7. The production of oil from a horizontal reentry well, as determined by the industrial commission and certified to the state tax commissioner, is exempt for a period of nine months after the date the well is completed as a horizontal well.

The exemption under this subsection becomes ineffective if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period. However, the exemption is reinstated if, after the trigger provision becomes effective, the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period.

8. The initial production of oil from a well is exempt from any taxes imposed under this chapter for a period of sixty months if:

a. The well is located within the boundaries of an Indian reservation;

b. The well is drilled and completed on lands held in trust by the United States for an Indian tribe or individual Indian; or

c. The well is drilled and completed on lands held by an Indian tribe if the interest is in existence on August 1, 1997.

SECTION 3. AMENDMENT. Section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-03.1. Stripper well, new well, work-over, and secondary or tertiary project certification for tax exemption or rate reduction - Filing requirement. To receive the benefits of a tax exemption or tax rate reduction, a certification of qualifying well status prepared by the industrial commission must be submitted to the tax commissioner as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property under subsection 2 of section 57-51.1-03, the industrial commission's certification must be submitted to the tax commissioner within eighteen months after the end of the stripper well property's qualification period.
2. To receive, from the first day of eligibility, a tax exemption <u>or rate reduction</u> under subsection 3 of section 57-51.1-03 and a rate reduction on production from a new well under section 57-51.1-02, the industrial commission's certification must be submitted to the tax commissioner within eighteen months after a new well is completed.
3. To receive, from the first day of eligibility, a tax exemption under subsection 4 of section 57-51.1-03 and a rate reduction for a work-over well under section 57-51.1-02, the industrial commission's certification must be submitted to the tax commissioner within eighteen months after the work-over project is completed.
4. To receive, from the first day of eligibility, a tax exemption under subsection 5 of section 57-51.1-03 and a tax rate reduction under section 57-51.1-02 on production from a secondary or tertiary project, the industrial commission's certification must be submitted to the tax commissioner within the following time periods:
   a. For a tax exemption, within eighteen months after the month in which the first incremental oil was produced.

b. For a tax rate reduction, within eighteen months after the end of the period qualifying the project for the rate reduction.

5. To receive, from the first day of eligibility, a tax exemption or the reduction on production for which any other tax exemption or rate reduction may apply, the industrial commission's certification must be submitted to the tax commissioner within eighteen months of the completion, recompletion, or other qualifying date.

6. To receive, from the first day of eligibility, a tax exemption under subsection 6 of section 57-51.1-03 on production from a two-year inactive well, the industrial commission's certification must be submitted to the tax commissioner within eighteen months after the end of the two-year inactive well's qualification period.

If the industrial commission's certification is not submitted to the tax commissioner within the eighteen-month period provided in this section, then the exemption or rate reduction does not apply for the production periods in which the certification is not on file with the tax commissioner. When the industrial commission's certification is submitted to the tax commissioner after the eighteen-month period, the tax exemption or rate reduction applies to prospective production periods only and the exemption or rate reduction is effective the first day of the month in which the certification is received by the tax commissioner.

SECTION 4. EFFECTIVE DATE. This Act is effective for oil extracted after June 30, 2007.