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Sixty-fourth
Legislative Assembly
of North Dakota

SENATE BILL NO. 2319

Introduced by

Senator Bowman

A BILL for an Act to create and enact a new section to chapter 38-08 of the North Dakota Century Code, relating to applications for tax reduction for a horizontal well; to amend and reenact section 38-08-08 of the North Dakota Century Code, relating to the integration of fractional tracts; and to provide for retroactive application.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. A new section to chapter 38-08 of the North Dakota Century Code is created and enacted as follows:

Notification of force pooled royalty owners of costs.

An operator must notify each force pooled royalty owner of a property of all associated costs of the drilling and completion of a well and provide an affidavit of fulfilling this requirement to the oil and gas division, before the operator may certify a horizontal, horizontal reentry, or two-year inactive well as a qualifying well for purposes of eligibility for a tax incentive under chapter 57-51.1.

SECTION 2. AMENDMENT. Section 38-08-08 of the North Dakota Century Code is amended and reenacted as follows:

38-08-08. Integration of fractional tracts.

1. When two or more separately owned tracts are embraced within a spacing unit, or when there are separately owned interests in all or a part of the spacing unit, then the owners and royalty owners thereof may pool their interests for the development and operation of the spacing unit. In the absence of voluntary pooling, the commission upon the application of any interested person shall enter an order pooling all interests in the spacing unit for the development and operations thereof. Each such pooling order must be made after notice and hearing, and must be upon terms and conditions that are just and reasonable, and that afford to the owner of each tract or interest in

the spacing unit the opportunity to recover or receive, without unnecessary expense, that owner's just and equitable share. Operations incident to the drilling of a well upon any portion of a spacing unit covered by a pooling order must be deemed, for all purposes, the conduct of such operations upon each separately owned tract in the drilling unit by the several owners thereof. That portion of the production allocated to each tract included in a spacing unit covered by a pooling order must, when produced, be deemed for all purposes to have been produced from such tract by a well drilled thereon. For the purposes of this section and section 38-08-10, any unleased mineral interest pooled by virtue of this section before August 1, 2009, is entitled to a cost-free royalty interest equal to the acreage weighted average royalty interest of the leased tracts within the spacing unit, but in no event may the royalty interest of an unleased tract be less than a one-eighth interest. An unleased mineral interest pooled after ~~July 31, 2009~~December 31, 2014, is entitled to a cost-free royalty interest equal to the ~~acreage weighted average~~same royalty interest of the leased tracts ~~within the spacing unit or, at the operator's election,~~of the state in the same county. The remainder of the unleased interest must be treated as a lessee or cost-bearing interest.

2. Each such pooling order must make provision for the drilling and operation of a well on the spacing unit, and for the payment of the reasonable actual cost thereof by the owners of interests in the spacing unit, plus a reasonable charge for supervision. In the event of any dispute as to such costs, the commission shall determine the proper costs. If one or more of the owners shall drill and operate, or pay the expenses of drilling and operating the well for the benefit of others, then, the owner or owners so drilling or operating shall, upon complying with the terms of section 38-08-10, have a lien on the share of production from the spacing unit accruing to the interest of each of the other owners for the payment of the owner's or owners' proportionate share of such expenses. All the oil and gas subject to the lien must be marketed and sold and the proceeds applied in payment of the expenses secured by such lien as provided for in section 38-08-10.

3. In addition to any costs and charges recoverable under subsections 1 and 2, if the owner of an interest in a spacing unit elects not to participate in the risk and cost of drilling a well thereon, the owner paying for the nonparticipating owner's share of the

drilling and operation of a well may recover from the nonparticipating owner a risk penalty for the risk involved in drilling the well. The recovery of a risk penalty is as follows:

a. If the nonparticipating owner's interest in the spacing unit is derived from a lease or other contract for development, the risk penalty is two hundred percent of the nonparticipating owner's share of the reasonable actual costs of drilling and completing the well and may be recovered out of, and only out of, production from the pooled spacing unit, as provided by section 38-08-10, exclusive of any royalty or overriding royalty.

b. If the nonparticipating owner's interest in the spacing unit is not subject to a lease or other contract for development, the risk penalty is fifty percent of the nonparticipating owner's share of the reasonable actual costs of drilling and completing the well and may be recovered out of production from the pooled spacing unit, as provided by section 38-08-10, exclusive of any royalty provided for in subsection 1.

c. At the time the owner recovers for the nonparticipating owner's share of the drilling and operation costs of a well and any assessed penalty, the nonparticipating owner may chose to become a paying owner. If the nonparticipating owner chooses to become a paying owner, the royalty interest is converted to a working interest, proportionately reduced to the interest that the paying owner has in the spacing unit, which benefits the paying owner with all of the revenue attributable to that interest and burdens the paying owner with all of the costs associated with that interest. If the nonparticipating owner chooses not to become a paying owner, the royalty interest is increased to twenty percent of the revenues attributable to the interest that nonparticipating owner has in the spacing unit.

d. The owner paying for the nonparticipating owner's share of the drilling and operation of a well may recover from the nonparticipating owner a risk penalty for the risk involved in drilling and completing the well only if the paying owner has made an unsuccessful, good-faith attempt to have the unleased nonparticipating owner execute a lease or to have the leased nonparticipating owner join in and participate in the risk and cost of drilling the well. Before a risk penalty may be imposed, the paying owner must notify the nonparticipating owner with proof of service that the paying owner intends to impose a risk penalty and that the nonparticipating owner may object to the risk penalty by either responding in opposition to the petition for a risk penalty or if no such petition has been filed, by filing an application or request for hearing with the industrial commission.

4. A nonparticipating owner may request in writing and the paying owner shall provide a year-end accounting that includes the costs and risk penalty as defined in subsection 2 and 3 that have been paid by the paying owner on behalf of the nonparticipating owner. The paying owner has until the end of January following the request to provide the accounting.