2011 HOUSE FINANCE AND TAXATION

HB 1467

2011 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1467
January 31, 2011
#13680

☐ Conference Committee

Committee Clerk Signature Mary Brucker

Explanation or reason for introduction of bill/resolution:

A Bill relating to oil extraction tax rates and exemptions; and to provide an effective date.

Minutes: *See attached testimony #1A and B.*

Representative Kempenich: Sponsor. Support. Please refer to attached testimony #1 A and B. This bill reflects what is going on in today's industry in the oil patch. This is a bill that triggers tax reductions as prices fall. If you remember two years ago our trigger system was close for just about the whole period and then it started to go up again and never reflected really what was going on in the oil field. As a result of that in April there was about 105 rigs drilling and dropped down to about 30 some rigs to keep drilling to hold leases otherwise they pretty much stacked out. It was December of 2009 before they started spooling back up again. The rest is history and through 2010 they've been increasing like crazy. This bill is in response to that. Once you stack those rigs out those crews dissipate and if the money is there they will come back in usually but a lot of times they find something else to do. It helped me out as I had two guys help me combine that fall but they were making $300 a day and I only paid them $100 a day. So this does create quite a thing to have these rigs stack out. Referred to attached testimony. I used Flint Hills as an example as Tesoro doesn't do a daily posting. If it drops below $65/barrel a day and stays there for a calendar month you would see a 2% drop. If this stayed at below $65/barrel for four months it could stay at 9 ½%, it just follows a trigger down to where it is today roughly $45/barrel and then it could drop off to the 5%. Every 30 days they pretty much change a lot in the oil field. It is more reflective of where the break evens come into play. For this biennium there is no fiscal note on it.

Chairman Wesley R. Belter: Is this for all wells and just new wells?

Representative Kempenich: This would be for all of what is going on out there. When the Bakken drops off they pretty much have those wells paid for the first 18 months. The cost of doing things out there has gotten higher also. Five or six years ago a water truck was at $65-70/hour and now they are up to $125-40 now, it's doubled in price. So this reflects what happens as prices start dropping.

Representative Glen Froseth: The elimination of all these exemptions of these incentives...

Representative Kempenich: There isn't any elimination of any incentives. The only things we eliminated was the way they trigger it off the MYMEX. We still have the stripper well exemptions. We didn't touch any of the low producing wells.

Representative Glen Froseth: There are a lot of things crossed out in the bill.

Representative Kempenich: Yes there is and most of it is all the same language dealing with the old trigger. We didn't do anything with stripper wells; we just left it as it was.

Representative Glen Froseth: If the price drops for a month, now the price has to fluctuate for six months before new rates apply. Is this going to create a bookkeeping nightmare for the Tax Department if the price teeters on $65 or $68 every other day?

Representative Kempenich: I don't think so. It has to stay at below $65 for a full calendar month. If it's back and forth it isn't going to trigger it.

Vice Chairman Craig Headland: You mentioned in your area the wells drilled are different; they don't pump like Bakken wells. We just had Representative who said they are drilling in the Bakken formation saying they would like a flat simple tax. Are the producers where you live a step down?

Representative Kempenich: There is no real impact on it. I think anybody would look for some type of a break as prices drop down the cost of operating drops. It's based on production end prices so anything that breaks even could be $30 a barrel on some of those older wells that are already paid for. As it drops down it gets closer where they look for an incentive to keep investing your new one. They are taking money from past wells to pay for new wells. It takes capital to drill new wells. So this would keep them exploring as prices drop. I'm not looking at today's prices because most production is within 24 months and after that it levels off and you'll see that in the Bakken and in our country too. You can tell over the years that your production keeps dropping down because you don't have to have as many tanks sitting there as they get older. There is upkeep and maintenance on them. It's not that there is all profit coming out of these wells, there is good money but there is maintenance on them too.

Representative Shirley Meyer: This piece of legislation is irrelevant currently but in the event it drops to a trigger price we are looking at a $1.4 billion fiscal note, right?

Representative Kempenich: Yes. We are looking at that anyway. If you hit the trigger, assuming it goes all the way down to the 5%, we are looking at that anyways. This could actually take a lot longer than six months to get to the 5% because if oil would drop down to $65/barrel and stay there for a number of months it could stay at 9 ½% for six months and never drop all they way off. But what it does is more of a transition type and it transitions the same was coming back up again too. There is no fiscal note and it is hard to quantify what it would be because you would have to base it on production of what it would drop off at. The worst case scenario would be $1.4 billion but that could happen even with the current situation.

Representative Shirley Meyer: You've got the trigger in here but then on page 5 it says "if the average price is less than $45" is that just the set trigger?

Representative Kempenich: Yes, that is just the set price. There are three spots where it drops; 65, 55, and 45.

Representative Shirley Meyer: It doesn't matter what the Flint Hills posting price is?

Representative Kempenich: No, that is what triggers all these prices is the Flint Hills or the Tax Commission, whatever is available at that time. When you read through it on page 5 it goes through and the first page is where the average price is and then it follows on page 4 and 5 that's where it follow through. It wouldn't qualify, you would have to drop below 45 for a month to get it to trigger on to the 5%.

Representative Lonny B. Winrich: The bill defines the average price of oil as posted by Flint Hills Resources or as determined by the Tax Commissioner from available indices" but if I look at this sheet you passed out from Flint Hill Resources there are about six different rigs of North Dakota oil. Are you going to average all of them?

Representative Kempenich: No. We could average them out but I was thinking of the light sweet crude when I did this.

Representative Lonny B. Winrich: So that should be amended in?

Representative Kempenich: It could be. North Dakota sour is what we have a lot of in our area, it's high sulfur low gravity oil. A good chunk of the oil pumped today is the light sweet in the Bakken.

Representative Lonny B. Winrich: You talked about your trigger mechanism as requiring the price to drop below a certain level for a full calendar month. Does that mean if the price dropped below 65 on January 15 and stayed there until February 25 that wouldn't trigger a drop although it's over 30 days?

Representative Kempenich: It has to be a calendar month. It gets confusing if you don't do it over a calendar month.

Chairman Wesley R. Belter: No further testimony in support. No opposition. No neutral testimony. Closed hearing on HB 1467.

2011 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1467
February 7, 2011
#14155

☐ Conference Committee

Committee Clerk Signature	Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to oil extraction tax rates and exemptions; and to provide an effective date.

Minutes: *See attached amendments #1.*

Chairman Wesley R. Belter: Distributed amendments and reviewed. Please refer to attached amendments #1.

Representative Shirley Meyer: The trigger is reset every year.

Chairman Wesley R. Belter: Inaudible.

Representative Shirley Meyer: If that is your intent, the trigger is reset every year. If you fall below the trigger price for five consecutive months then the exemptions and incentives trigger on. But it has to go to five months consecutively below the trigger. So what does this do?

Chairman Wesley R. Belter: It leaves the triggers where they were in the original legislation in 2007. Inaudible.

Representative Shirley Meyer: What we passed was to set the exemptions based on a trigger. The trigger is formulated over yearly average, West Texas Intermediate minus $2.50 and that establishes your trigger. I don't know if you're asking if you want the trigger to remain the same as it was in 2007 what it is today or if that is the intent then you are just locking in the trigger price at lower.

Chairman Wesley R. Belter: When I was visiting with John Walstad it was my understanding that the trigger would be $52.50.

Representative Shirley Meyer: Our trigger is at $46.79.

Chairman Wesley R. Belter: He was using the figure $52.50.

Representative Shirley Meyer: In the information I passed out to you he doesn't get to use any trigger on 4679 because that is the trigger and that is based on data every month

average from the North Dakota Tax Department. I don't understand if you are just locking the trigger in at the 2007 trigger or if you're...I can't see one difference other than your changing one year from 2012 to 2013. Are you just locking in your trigger?

Chairman Wesley R. Belter: That is my understanding that we are keeping the same triggers.

Representative Shirley Meyer: My question is why you would want to do that because your trigger price is set in December for the following year and why you'd want to lock in the trigger on a year that....It's based on oil. Entire year of 2011 it is $46.78.

Representative Patrick Hatlestad: My understanding of this bill is we take the existing bill and instead of letting it expire in 2012 we extend it one year. So whatever we are doing now will continue and if we adjust that every December then I would think it would continue.

Chairman Wesley R. Belter: We are extending current legislation for one year.

Representative Shirley Meyer: I guess my question is then I didn't realize that the bill dealing with the oil extraction tax did not have a sunset on it so it is automatically extended, is it not?

Representative Glen Froseth: If you look at the title it is section 57-51.1-03 deals with exemptions. A lot of those exemptions are the sunset on June 30, 2012. This basically extends the exemptions which also the trigger price would come into play in a lot of those exemptions. Some of those exemptions already have run out like the very last paragraph is already obsolete that sunset itself like the first 75,000 barrels produced in the Bakken. All the reset pertain to the stripper well exemptions and all exemptions that we presently have. The trigger price does affect a lot of the exemptions.

Representative Shirley Meyer: So the intent of this is to leave the exemptions in place for another year? And you're not addressing the trigger at all?

Chairman Wesley R. Belter: We are keeping current in effect for one additional year.

Representative Shirley Meyer: I guess my point is when the trigger price is $46.78 and the price of oil is running around $90 this doesn't mean anything. None of the exemptions or your incentives will trigger on anyway.

Chairman Wesley R. Belter: That's true.

Representative Shirley Meyer: I understand.

Chairman Wesley R. Belter: Inaudible because speaker wasn't on.

Representative Shirley Meyer: In the event that oil falls out falls below the trigger for five consecutive months then according to this all your exemptions and incentives will stay on which will cost the state of North Dakota a lot of money.

Chairman Wesley R. Belter: Inaudible because speaker wasn't on.

Representative Shirley Meyer: Mr. Walstad, I was concerned about the trigger and if this affected the trigger or not.

John Walstad, Tax Department: There are two triggers in existing law; the ancient trigger and I can't tell you what price per barrel that sits at now, it was indexed for price changes. What this bill would affect is the short term trigger in subsection 9 and on the amendment sheet it is on page 5. This is the trigger provision that was plugged in toward the end of last session when the price just missed triggering the exemptions under the ancient trigger. This trigger ended up only being in place from May to October because that's the way the pricing went. The price structure of this trigger is $55/barrel on the low end and $70/barrel on the high end. For this trigger to kick in the price would have to drop for one full calendar month, it's not five months under this trigger, one month under $55/barrel then this reduction would kick in again. This is not a full exemption but it drops the rate to 2% for the first 75,000 barrels or $4 ½ million of gross value at the well for the first 18 months from a horizontal well. Under the legislation from last session this trigger provision is set to expire June 30, 2012. Representative Belter's amendment would extend that expiration one more year so it would stay in place through next legislative session. If the legislature thinks it's appropriate then it can be continued.

Representative Shirley Meyer: We're just talking about the secondary trigger?

John Walstad: It's the new and improved trigger to extend it for one more year than what it is scheduled to do under current law. There is no other change to anything in this bill. It's a new bill basically.

Chairman Wesley R. Belter: The $55 you talked about that's not in the bill?

John Walstad: It's in the bill on page 5 subsection 9. (Read this portion of the bill). Those numbers are there because I put them there, I didn't dream them up. Someone told me those are the numbers. Industry told some committee member less than $55 we have a problem and at $70 or more we are okay. That's where the numbers came from. I don't know if those numbers are still the right numbers from the industry's point of view.

Chairman Wesley R. Belter: I don't know if this is good or bad.

Representative Shirley Meyer: Made a motion to move the amendment.

Representative Patrick Hatlestad: Seconded.

Voice vote taken: MOTION CARRIED TO MOVE THE AMENDMENTS.

Representative Shirley Meyer: Made a motion for a DO PASS WITH AMENDMENTS.

Representative Bette Grande: Seconded.

A roll call vote was taken: YES 13 NO 0 ABSENT 1

MOTION CARRIED—DO PASS WITH AMENDMENTS.
Representative Glen Froseth will carry HB 1467.

FISCAL NOTE

Requested by Legislative Council
02/10/2011

Amendment to: HB 1467

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2009-2011 Biennium		2011-2013 Biennium		2013-2015 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2009-2011 Biennium			2011-2013 Biennium			2013-2015 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

Engrossed HB 1467 extends for one additional year an existing triggered oil extraction tax rate reduction.

B. **Fiscal impact sections:** *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

If enacted, Engrossed HB 1467 is expected to have no impact in the 2011-13 biennium as oil prices are forecasted to exceed those that would trigger the oil extraction tax rate decrease provided for in this bill.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*
   A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

   B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

   C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*

Name:	Kathryn L. Strombeck	**Agency:**	Office of Tax Commissioner
Phone Number:	328-3402	**Date Prepared:**	02/10/2011

FISCAL NOTE

Requested by Legislative Council
01/19/2011

Bill/Resolution No.: HB 1467

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2009-2011 Biennium		2011-2013 Biennium		2013-2015 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2009-2011 Biennium			2011-2013 Biennium			2013-2015 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

HB 1467 replaces the existing oil extraction tax price trigger with new thresholds that would reduce the oil extraction tax rate from 6.5% to 4.5%, 2.5%, or 0% depending on average oil prices.

B. **Fiscal impact sections:** *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

If enacted, HB 1467 is expected to have no impact in the 2011-13 biennium as oil prices are forecasted to exceed those that would trigger any of the oil extraction tax rate decreases provided for in this bill.

However, if the forecast is incorrect and prices fall to the lowest threshold provided for in HB 1467 ($45 per barrel), and remain there throughout the biennium, the oil price decrease alone would result in a drop in total oil tax revenues of approximately $800 million. In addition to that price-related drop in revenue, enactment of HB 1467 could result in an additional revenue loss of $600 million as the oil extraction tax rate triggered to zero. The forecast assumes this does not occur.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*
   A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

   B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

   C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*

Name:	Kathryn L. Strombeck	**Agency:**	Office of Tax Commissioner
Phone Number:	328-3402	**Date Prepared:**	01/28/2011

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Prepared by the Legislative Council staff for
Representative Belter
February 3, 2011

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PROPOSED AMENDMENTS TO HOUSE BILL NO. 1467

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact section 57-51.1-03 of the North Dakota Century Code, relating to a triggered oil extraction tax rate reduction; to provide an effective date; and to provide an expiration date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-03. (Effective through June 30, ~~2012~~2013) Exemptions from oil extraction tax.

The following activities are specifically exempted from 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, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.

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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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, 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, 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.

9. The first seventy-five thousand barrels or the first four million five hundred thousand dollars of gross value at the well, whichever is less, of oil produced during the first eighteen months after completion, from a horizontal well drilled and completed after April 30, 2009, is subject to a reduced tax rate of two percent of the gross value at the well of the oil extracted under this chapter. A well eligible for a reduced tax rate under this subsection is eligible for the exemption for horizontal wells under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion. The rate reduction under this subsection becomes effective on the first day of the month following a month for which the average price of a barrel of crude oil is less than fifty-five dollars. The rate reduction under this subsection becomes ineffective on the first day of the month following a month in which the average price of a barrel of crude oil exceeds seventy dollars. If the rate reduction under this subsection is effective on the date of completion of a well, the rate reduction applies to production from that well for up to eighteen months after completion, subject to the other limitations of this subsection. If the rate reduction under this subsection is ineffective on the date of completion of a well, the rate reduction under this subsection does not apply to production from that well at any time.

(Effective after June 30, ~~2012~~2013) Exemptions from oil extraction tax. The following activities are specifically exempted from 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, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.

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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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, 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, 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.

9. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a horizontal well drilled and completed in the Bakken formation after June 30, 2007, and before July 1, 2008, is subject to a reduced tax rate of two percent of the gross value at the well of the oil extracted under this chapter. A well eligible for a reduced tax rate under this subsection is eligible for the exemption for horizontal wells under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

SECTION 2. EFFECTIVE DATE - EXPIRATION DATE. This Act is effective for taxable events occurring after June 30, 2011, and is effective through June 30, 2013, and is thereafter ineffective."

Renumber accordingly

Date: 2-7-11
Roll Call Vote # 1

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1467

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Meyer Seconded By Rep. Hatlestad

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley R. Belter			Scot Kelsh		
Vice Chair. Craig Headland			Shirley Meyer		
Glen Froseth			Lonny B. Winrich		
Bette Grande			Steven L. Zaiser		
Patrick Hatlestad					
Mark S. Owens					
Roscoe Streyle					
Wayne Trottier					
Dave Weiler					
Dwight Wrangham					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

VOICE VOTE

MOTION CARRIED

Date: 2-7-11
Roll Call Vote # 2

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1467

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☒ Do Pass ☐ Do Not Pass ☒ Amended ☐ Adopt Amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Meyer Seconded By Rep. Grande

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley R. Belter	✓		Scot Kelsh	AB	
Vice Chair. Craig Headland	✓		Shirley Meyer	✓	
Glen Froseth	✓		Lonny B. Winrich	✓	
Bette Grande	✓		Steven L. Zaiser	✓	
Patrick Hatlestad	✓				
Mark S. Owens	✓				
Roscoe Streyle	✓				
Wayne Trottier	✓				
Dave Weiler	✓				
Dwight Wrangham	✓				

Total (Yes) 13 No Ø

Absent 1

Floor Assignment Rep. Froseth

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1467: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (13 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING). HB 1467 was placed on the Sixth order on the calendar.

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact section 57-51.1-03 of the North Dakota Century Code, relating to a triggered oil extraction tax rate reduction; to provide an effective date; and to provide an expiration date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-03. (Effective through June 30, ~~2012~~2013) Exemptions from oil extraction tax.

The following activities are specifically exempted from 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, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.

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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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.

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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, 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, 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.

9. The first seventy-five thousand barrels or the first four million five hundred thousand dollars of gross value at the well, whichever is less, of oil produced during the first eighteen months after completion, from a horizontal well drilled and completed after April 30, 2009, is subject to a reduced tax rate of two percent of the gross value at the well of the oil extracted under this chapter. A well eligible for a reduced tax rate under this subsection is eligible for the exemption for horizontal wells under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion. The rate reduction under this subsection becomes effective on the first day of the month following a month for which the average price of a barrel of crude oil is less than fifty-five dollars. The rate reduction under this subsection becomes ineffective on the first day of the month following a month in which the average price of a barrel of crude oil exceeds seventy dollars. If the rate reduction under this subsection is effective on the date of completion of a well, the rate reduction applies to production from that well for up to eighteen months after completion, subject to the other limitations of this subsection. If the rate reduction under this subsection is ineffective on the date of completion of a well, the rate reduction under this subsection does not apply to production from that well at any time.

(Effective after June 30, ~~2012~~2013) Exemptions from oil extraction tax.
The following activities are specifically exempted from 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, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.

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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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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.

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SECTION 2. EFFECTIVE DATE - EXPIRATION DATE. This Act is effective for taxable events occurring after June 30, 2011, and is effective through June 30, 2013, and is thereafter ineffective."

Renumber accordingly

2011 SENATE FINANCE AND TAXATION

HB 1467

2011 SENATE STANDING COMMITTEE MINUTES

Senate Finance and Taxation Committee
Lewis and Clark Room, State Capitol

HB 1467
3/16/2011
Job Number 15522

☐ Conference Committee

A. Bittmiller

Explanation or reason for introduction of bill/resolution:

Relating to a triggered oil extraction tax rate reduction

Minutes: Written Testimony Attached

Chairman Cook opened the hearing on HB 1467.

John Walstad, Legislative Council – The bill as introduced did a number of things, what it does now is not too much and the change you will see on page 1 line 7 one year is added to the effectiveness of the first version of this section and the only thing affected by that is subsection 9 over on page 6 subsection 9 as you recall was enacted last session. Shortly after the old trigger for reductions was narrowly missed, this triggered provision was put in place, took effect May 1, 2009 and ceased to be effective at the end of September 2009 and it was a 75,000 barrel or $4.5 million of value reduced rate 2% instead of 6.5%.

Chairman Cook asked for testimony in favor of HB 1467. No one came forward.

Chairman Cook asked for testimony opposed to HB 1467. No one came forward.

Chairman Cook asked for neutral testimony for HB 1467.

Representative Carlson – (See attached testimony A and A1, amendments for HB 1467)

Representative Meyer – (See attached testimony B and B1in favor of proposed amendments)

Vice Chairman Miller – What makes an area more competitive than another?

Representative Meyer – For example, weather, what makes it more competitive, when you have a lease that's up in 5 years and the oil companies out there are pushing the gun, many are going to expire here shortly. They have to have a well spudded before that lease is held. With that, once they get that done, then they look around, what is more economical, what makes a well being drilled more economical, what makes that more competitive, your tax structure, your weather is a huge one for North Dakota, and location. We are discounted because of pipeline constraints, our trucks are full, our tank batteries are full,

our pipelines are full, and if our oil companies want to get oil on that line, the pipeline companies will say, how much of a discount are you willing to take to let us put your oil on the line.

Senator Triplett – One thing that concerns me about this new way of doing things suggests that what we are trying to encourage is maximum production because the oil companies will get a lower tax rate if they push the production up and it is my personal opinion that what we ought to be trying to establish is sustainable production because it seems to me that we have just had a pretty rigorous lesson over the last couple of years in the hardships to all of our communities in rushed production. I understand what you're saying, there is a reason that everyone is rushing so hard and pushing so hard to get their leases held but do we really want to incentivize continued rush like this or is there a way we can look to incentivize a more steady long term sustainable level of production?

Representative Meyer – I believe this bill does do that. We have had this wild ride if you will, just for the lease holds but then we do want to keep them here. We do not want them looking at other states and take their drilling rig to LA or TX. If we do a project like this, not that it will increase drilling per say but it will keep them there. It will keep the oil companies here because of a more sustained tax rate. When they look around at the economies and we've got the highest oil tax in the nation and they look around after they've got their lease held, maybe they are going to try somewhere with a more favorable tax rate.

Senator Triplett – I get the premise I'm just saying in terms of where the reductions were pegged in terms of production. In terms of that level of production the best tax rate that they are offered is when we get to the 700,000 barrels per day. I'm curious what kind of traffic that's going to require to get to that level of production and is that the right number, is that the right place to be for the lowest tax rate?

Representative Meyer – I looked at it as 700,000 barrels a day, what it would do for the state of North Dakota. I represent a lot of people out there, oil companies, royalty owners, and also my surface owners. It's an issue we are dealing with, however, the oil industry has kept many young farmers and ranchers out there farming and ranching. The oil industry right now is sustaining our farming and ranching habit. It's all hopefully when we looked at the projections and the dates in here are infrastructure will have come along and hopefully it will all fall into place. Hopefully when we hit 700,000 barrels a day we are a little smarter than we are right now in dealing with the impacts and the state of North Dakota will benefit from this for years.

John Olson, Lobbyist, Continental Resources – I want to introduce to you the CEO and the Chairman of the Board of Continental Resources. He's a good corporate and personal friend to many of us here in North Dakota.

Harold Hamm, Continental Resources – I've had the opportunity the last few years to travel across the state and find out what everybody's interest is, especially the areas that we work in out west. One of the first questions that come up is, is this thing going to last or are we in for another bust. It takes me a little bit to answer that because really what we are dealing with is something that's kind of subject to a bust even though we are working with a big resource up here and our team has scoped that. We think the potential of it is huge but

its high cost production. It's a fragile resource that we are dealing with. We are a long way from market; we have to ship this to Midwest refineries and other places.

Senator Burckhard – I understand North Dakota is a long way from the market so it costs more to produce, but on a per barrel basis does it cost more to produce oil in the Gulf or in North Dakota?

Harold Hamm, Continental Resources – It costs more to produce oil here. Our operating costs are higher and wells are deep.

Senator Triplett – If I understand this amendment correctly the tax will go down by .5% at each of the 4 triggers on production at which point the top rate would be 9.5%, is that correct?

Harold Hamm, Continental Resources – Yes

Senator Triplett – It stays there even if it later declines, is that correct? In terms of talking about my concern which is sustainability of oil production over the long term can you explain to me how that accomplishes that objective because it seems to me that what this tax structure would do is encourage the oil companies to get to that 700,000 barrels per day of production to establish the reduced rate and then beyond that even if production declines there's no offsetting increase. How does this accomplish the states goal of long term sustainability?

Harold Hamm, Continental Resources – My estimation of production may hopefully of oil price will stay above the threshold that we've talked about and the service cost don't creep too badly that we may see a million barrels a day and that's been predicted by people other than myself. We are not going to quit producing oil and drilling wells just because we got over that last quarter of a percent threshold I can assure you.

Senator Dotzenrod – I would just like to add to what's been said, I think all of us in North Dakota really appreciate the work the companies have done and invested their money and their stockholders money here. I think every taxpayer in the state has really benefitted from the work that you have all done. I wanted to ask about what would be the appropriate approach? Two years ago we did pass a bill that provided this trigger and what we heard from companies at that time was that in a low priced oil environment this tax really becomes a problem. They wanted and we passed a trigger that is in place today that says if oil prices go down there's a reduction in the tax in an attempt to try to make it a little easier to deal with the burden of that tax. When the price got above $70-$75 per barrel then this tax would go back to where we had it originally and that the message that I recall from those hearings is that if you get in to a good price environment that it's kind of a win-win situation. The oil companies can make some money, the state has got tax revenue, the royalty owner is getting their money, and everyone is making some money. Based on where we are today with the kind of number of rigs that are coming to North Dakota and the activity that's in North Dakota it's really hard for me to see why we've got a problem that needs to be dealt with by reducing the tax in a more permanent way when it appears the market is working, we are getting a response from the market, and people are coming here to really take advantage of it and to pursue what they can in the state. It seems to me the

policy we adopted 2 years ago really had a good argument for it. I'm having a little harder time understanding how in this current environment why we would feel it would be necessary to do anything other than what we've got in place right now.

Harold Hamm, Continental Resources – I think that's the problem that we have. In a $100 environment nobody has a problem. I've been in this business 44 years now and the price goes down as much as it comes up and it will go back. Right now that threshold that was put in there 2 years ago is not the lower threshold that we need to produce out here because service costs went up. Already that's obsolete. I think this is the best way to fix it and I think this amendment will do that and take care of it long term and everybody comes out on it. At these numbers going forward it's a good fix and it takes us back just a little bit from the boom bust. It gets us back from failure.

Ron Ness, North Dakota Petroleum Council – (See attached testimony C in favor of the proposed amendments)

Senator Triplett – What happens to this consensus that we seem to have developing right now if Alaska or other major oil producing states start dropping their taxes in order to try to incentivize the oil industry back to their states?

Ron Ness, North Dakota Petroleum Council – We have sent 2 people representing the Petroleum Council to Alaska in the last 2 months talking about how we've worked together on things like the pipeline authority and all those things. Alaska's tax rate I believe is 25%.

Senator Triplett – Do you see any similar conversations going on in any other states?

Ron Ness, North Dakota Petroleum Council – I have the unique opportunity to be one of the few oil lobbyists in the country that deal with this every session. I just don't see this issue popping up across other states.

Senator Dotzenrod – Normally a policy maker or tax policy or government would use a tax cut at a time when a business is having some difficulty. If we pass an oil tax cut in the middle of an oil boom what are we going to do when things do get difficult?

Ron Ness, North Dakota Petroleum Council – I think that's what we've always done. We've waited and then it's too late. What these guys are saying is that this is a unique resource; let us plan for the long haul. During the lease hold activity we are going to have a rush mentality and the cost of those leases expiring is probably a lot greater than what we could ever provide for an incentive here. In the subsequent phases of this thing, this resource is so incredible.

Chairman Cook closed the hearing on HB 1467.

2011 SENATE STANDING COMMITTEE MINUTES

Senate Finance and Taxation Committee
Lewis and Clark Room, State Capitol

HB 1467
3/21/2011
Job Number 15760

☐ Conference Committee

A. Bittmiller

Explanation or reason for introduction of bill/resolution:

Relating to a triggered oil extraction tax rate reduction

Minutes: Committee Work

Chairman Cook opened discussion on HB 1467.

Senator Hogue – I'll move a Do Pass on HB 1467.

Seconded by **Senator Dotzenrod**.

Senator Triplett – We are saying then passing this as is we are not considering Representative Carlson's amendments at all?

Chairman Cook – The motion is Do Pass that is correct.

Senator Triplett requested a little time to visit with a few people regarding some questions she has.

Chairman Cook closed discussion on HB 1467.

2011 SENATE STANDING COMMITTEE MINUTES

Senate Finance and Taxation Committee
Lewis and Clark Room, State Capitol

HB 1467
3/21/2011
Job Number 15759

☐ Conference Committee

A. Bittmiller

Explanation or reason for introduction of bill/resolution:

Relating to a triggered oil extraction tax rate reduction

Minutes: Committee Work

Chairman Cook opened discussion on HB 1467.

Senator Triplett – I think it's worth having a serious conversation about oil and gas tax policy in this interim and unfortunately there hasn't been a vehicle to do that on the Senate side yet. I think the bill that was in on the House side was killed apparently with the idea that the conversation would be had later in the session and apparently now we are later in the session. There is a benefit in streamlining our tax policy in this state. The offer that's on the table right now to get rid of a couple of decades worth of exemptions in return for reducing the top side of the tax rate is intriguing to me, not that I'm exactly willing at the moment to offer Representative Carlson's amendments, but I think there are ideas in there that need discussion. I think this is a reasonable time to be thinking about streamlining our tax code.

Chairman Cook – There is some wisdom in getting rid of the exemptions, the question is going to come down to how much is it going to cost us. We see this bill would cost us 2.5% to get rid of all of them over a period of time and I like the way the bill is put together and we have a motion before us.

Chairman Cook – Ask the clerk to take the roll. (6-1-0)

Carried by **Vice Chairman Miller**.

Date: 3-21-11
Roll Call Vote # 1

2011 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1467

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☒ Do Pass ☐ Do Not Pass ☐ Amended ☐ Adopt Amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Senator Hogue Seconded By Senator Dotzenrod

Senators	Yes	No	Senators	Yes	No
Dwight Cook – Chairman	X		**Jim Dotzenrod**	X	
Joe Miller – Vice Chairman	X		**Connie Triplett**		X
Randy Burckhard	X				
David Hogue	X				
Dave Oehlke	X				

Total (Yes) 6 No 1

Absent 0

Floor Assignment Senator Miller

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1467, as engrossed: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **DO PASS** (6 YEAS, 1 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1467 was placed on the Fourteenth order on the calendar.

2011 TESTIMONY

HB 1467

Testimony #1
A

FLINT HILLS RESOURCES CRUDE OIL POSTINGS
P.O. BOX 2917, WICHITA, KS 67201

Effective 7:00 A.M., on dates shown below, and subject to its division orders as amended and supplemented, contracts and other agreements, FLINT HILLS RESOURCES, LP will pay the following prices per barrel of 42 U.S. gallons for merchantable crude oil purchased and delivered into pipelines or facilities authorized by FLINT HILLS RESOURCES, LP, in the fields or area designated below. The following prices are for informational purposes only, do not constitute an offer, and are subject to change or revisions without notice.

Effective Date	01/03/11	01/04/11	01/05/11	01/06/11	Jan	GVT
Bulletin	20110001	20110002	20110003	20110004	EDQ	ADJ
COLORADO						
Colorado D-J Basin	87.0000 *	84.7500 *	85.7500 *	83.7500 *	85.0726	E
NORTH DAKOTA						
North Dakota Light Sour	77.7800 *	75.5300 *	76.5300 *	74.5300 *	75.9887	B
North Dakota Light Sweet	81.7500 *	79.5000 *	80.5000 *	78.5000 *	79.9194	C
North Dakota Medium Sour	71.8600 *	69.6100 *	70.6100 *	68.6100 *	70.1268	B
North Dakota Northern Area	73.0000 *	70.7500 *	71.7500 *	69.7500 *	71.2016	C
North Dakota Sour	63.0000 *	60.7500 *	61.7500 *	59.7500 *	61.2500	B
North Dakota Southern Area	80.0000 *	77.7500 *	78.7500 *	76.7500 *	78.2339	C
TEXAS						
Eagle Ford	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	N
Eagle Ford Condensate	87.0000 *	84.7500 *	85.7500 *	83.7500 *	85.0726	N
Eagle Ford Light	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	N
Eagle Ford West	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	N
Eagle Ford West Condensate	87.0000 *	84.7500 *	85.7500 *	83.7500 *	85.0726	N
Eagle Ford West Light	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	N
Giddings Sweet Texas	86.0000 *	83.7500 *	84.7500 *	82.7500 *	84.0726	C
Gulf Coast Mix	86.0000 *	83.7500 *	84.7500 *	82.7500 *	84.0726	C
Pearsall Sweet	85.7500 *	83.5000 *	84.5000 *	82.5000 *	83.8226	C
South Texas Heavy	86.2500 *	84.0000 *	85.0000 *	83.0000 *	84.3226	H
South Texas Light Sweet	86.2500 *	84.0000 *	85.0000 *	83.0000 *	84.3226	C
[illegible]th Texas Sour	79.2500 *	77.0000 *	78.0000 *	76.0000 *	77.3226	D
[illegible]th Texas Sweet	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	N
South Texas Valley Sweet	86.0000 *	83.7500 *	84.7500 *	82.7500 *	84.0726	C
Upper Texas Gulf Coast	86.2500 *	84.0000 *	85.0000 *	83.0000 *	84.3226	C
West Texas/New Mexico Intermediate	88.0000 *	85.7500 *	86.7500 *	84.7500 *	86.0726	C
WYOMING						
Wyoming Asphaltic Sour	64.5000 *	62.2500 *	63.2500 *	61.2500 *	62.8306	L
Wyoming Heavy Sour, using FHR's published gravity scale L	69.8500 *	67.6000 *	68.6000 *	66.6000 *	68.1845	L
Wyoming Medium Sour, using FHR's published gravity scale L	70.9500 *	68.7000 *	69.7000 *	67.7000 *	69.2845	L
Wyoming Sweet	81.5000 *	79.2500 *	80.2500 *	78.2500 *	79.7339	C
Wyoming/Montana General Sour	65.5000 *	63.2500 *	64.2500 *	62.2500 *	63.8306	L

The above prices are based on the use of 100% tank tables or automatic measuring equipment acceptable to us or the pipeline company receiving the oil for our account, with customary adjustment of volume for temperature and full deduction for basic sediment and water. The foregoing schedule of prices is subject to deduction without notice for trucking, pipeline gathering, market adjustments, and other related changes on crude oil purchased from leases.

* DENOTES CHANGE

Printed: 01/31/2011

HB [redacted]7
Oil E[redacted]action tax

Testimony #1
B

11.5%

2%

9.5%

A drop of 2% for a price drop to $65 a barrel
For a full calendar month

2%

7.5%

A drop of 2% for a price
drop to $55 for a full
Calendar month

2½%

5%

A drop of 2½% for a
price drop to $45 for a
full Calendar month

Price based on Flint Hills Posted Price
light sweet crude

A

SUMMARY OF OIL TAX AMENDMENTS

I. Tax rate

a. The 6.5% OET would be reduced in 0.5% increments based on production levels with a maximum reduction of 2.5%. The first 0.5% reduction occurs when production reaches 425,000 BOPD and takes effect on the first day of the third calendar month following a period of three consecutive calendar months in which statewide average daily production exceeds 425,000 barrels.
b. Subsequent 0.5% reductions occur at 500,000, 575,000, 650,000 and 700,000 BOPD.
c. All price triggers are eliminated. Once a rate reduction level is reached, the rate is locked in regardless of price or if production declines. If production increases to the next level, the rate is reduced by another 0.5% and is again locked.
d. The tax rate applies to production from all new wells and all existing production in the State.

II. Secondary recovery units, tertiary recovery projects, and incremental production

There are no changes to the OET incentives on incremental production. (for example, the five year exemption on the 6.5% OET incentive on incremental production from a waterflood unit remains in effect). All other production is taxed at whatever rate is in effect under Section I, above.

III. Stripper wells and Stripper Properties

a. The OET tax exemption for stripper wells based on 10, 15 and 30 BOPD rates remains in effect.
b. Stripper "properties" are retained, however, "once a stripper, always a stripper" is modified as to Bakken pool properties.
c. Once statewide production reaches the 425,000 BOPD level, any new well spud thereafter on a Bakken pool stripper property is not a stripper well until production from that well meets the requirements of the definition for a stripper well.

IV. Tribal and Reservation Lands

There are no changes to the current taxation statutes relating to Tribal lands or lands lying within the boundaries of the Fort Berthold Reservation.

Prepared by the North Dakota Legislative Council
staff for Representative Carlson
March 2011

TRANSPORTATION INFRASTRUCTURE FUNDING - 2011 LEGISLATIVE ACTION

The table below details transportation infrastructure funding in addition to regular transportation funding provided to the Department of Transportation included in the executive budget and the additional transportation infrastructure funding reflecting legislative action through crossover.

2011 Legislative Assembly Action to Provide Additional Transportation Infrastructure Funding (Amounts Shown in Millions)

	Executive Budget	Legislative Action Through Crossover	Increase (Decrease)
House Bill No. 1012			
State road projects in areas affected by oil and gas development (highway fund with money transferred from the permanent oil tax trust fund; however, the Senate removed the transfer from Senate Bill No. 2015)	$228.6	$228.6	
County and township road projects in areas affected by oil and gas development (highway fund with money transferred from the permanent oil tax trust fund; however, the Senate removed the transfer from Senate Bill No. 2015)	142.0	142.0	
Transportation funding distributions to counties, cities, and townships for the 2009-11 biennium (general fund)		25.0	$25.0
Transportation funding distributions to counties, cities, and townships for the 2011-13 biennium (general fund)		25.0	25.0
House Bill No. 1013			
Energy infrastructure and impact grants (oil and gas impact grant fund)	100.0	100.0	
Senate Bill No. 2325			
County and township road reconstruction program to support agriculture and economic development (permanent oil tax trust fund)		73.6	73.6
Total	$470.6	$594.2	$123.6

SUMMARY OF LEGISLATIVE ACTION THROUGH CROSSOVER AFFECTING ADDITIONAL TRANSPORTATION INFRASTRUCTURE FUNDING

Land Department

Engrossed House Bill No. 1013 provides $100 million of energy infrastructure and impact grant funding during the 2011-13 biennium. This is an increase of $92 million from the 2009-11 total grant funding amount of $8 million. The executive recommendation also included $100 million for 2011-13 oil and gas impact grant funds.

Engrossed House Bill No. 1013 provides authority to the Board of University and School Lands to award and distribute energy infrastructure and impact grants from money deposited in the oil and gas impact grant fund. Annual distributions are limited to 60 percent of the biennial appropriation for energy infrastructure and impact grants. The board is provided authority to create an advisory committee to assist in making grant award determinations. The bill changes the name of the Energy Development Impact Office to the Energy Infrastructure and Impact Office. The bill allocates 35 percent of the grant funds to cities of 10,000 or more that are impacted by oil and gas development and 65 percent to other cities, counties, school districts, and other political subdivisions. The bill provides that of the large cities' share of energy infrastructure and impact grants, one city may not receive more than 60 percent of the funds available each biennium.

Senate Bill No. 2132 also affects oil and gas impact grants awarded by the Land Department. Of the money in the oil and gas impact grant fund, the bill designates $8 million for cities of fewer than 7,500 or counties of fewer than 10,000. Grants to one city or county may not exceed $500,000 per biennium. The bill requires a local match of $1 for each $1 awarded.

Department of Transportation

Engrossed House Bill No. 1012 provides $228.6 million from the highway fund with money transferred from the permanent oil tax trust fund for state roadway projects in areas affected by oil and gas development and $142 million from the highway fund with money transferred from the permanent oil tax trust fund for county and township roadway projects in areas affected by oil and gas development. Funding for the roadway projects was also included in the executive recommendation. The $370.6 million transfer from the permanent oil tax trust fund to the highway fund was included in Senate Bill No. 2015; however, the Senate removed this transfer.

Senate Bill No. 2325 provides the Department of Transportation with $73.6 million from the permanent

oil tax trust fund for county and township road projects to support agriculture and economic development. The funding is to be distributed for projects based on an Upper Great Plains Transportation Institute report regarding roadway needs related to agriculture and economic development.

State Treasurer

Engrossed House Bill No. 1012 provides funding to the State Treasurer for transportation funding distributions of $25 million from the general fund during both the 2009-11 and 2011-13 bienniums to eligible counties, cities, and townships in non-oil and gas-producing areas. The funding is to be distributed to eligible counties, cities, and townships based on the amount of funding received by these entities from the highway tax distribution fund compared to total funding received by all eligible counties, cities, or townships from the highway tax distribution fund during the previous state fiscal year.

State Infrastructure Fund

House Bill No. 1451 repeals the permanent oil tax trust fund at the end of the 2009-11 biennium and renames the "lands and minerals trust fund" the "state infrastructure fund." The bill deposits the first $300 million of the state share of oil and gas tax revenue in the general fund, deposits the next $300 million of the state share of oil and gas tax revenue in the property tax relief sustainability fund, and deposits the remaining state share of oil and gas tax revenue in the "state infrastructure fund." The estimated 2011-13 biennium funding to be deposited in the state infrastructure fund is $78.3 million. Funding in the state infrastructure fund is designated for one-time expenditures relating to improving state infrastructure subject to legislative appropriations. The bill provides legislative intent that funding should be appropriated only to the extent that funds are estimated to be available at the beginning of the biennium in which the appropriations are authorized.

SUMMARY OF EXECUTIVE RECOMMENDATION FOR ADDITIONAL TRANSPORTATION INFRASTRUCTURE FUNDING

Land Department

The executive recommendation increased the maximum amount of oil and gas tax revenues that may be deposited in the oil and gas impact grant fund by $92 million per biennium, from $8 million to $100 million. The fund is used for providing oil and gas development impact grants and the administration of the oil and gas development impact grant program.

The executive recommendation transferred the authority to award grants to counties, cities, school districts, and other taxing districts pursuant to North Dakota Century Code Chapter 15-01 from the energy development impact director to the Board of University and School Lands. The executive recommendation:

- Provided authority to the Board of University and School Lands to award and distribute oil and gas impact grants from money deposited in the oil and gas impact grant fund.
- Created an Oil and Gas Impact Grant Advisory Committee.
- Defined the membership and duties of the committee.
- Required the commissioner serve as chairman of the Oil and Gas Impact Grant Advisory Committee.
- Required the energy development impact director serve as a member of the Oil and Gas Impact Grant Advisory Committee.
- Allocated 35 percent of the grant funds to cities of 10,000 or more.
- Allocated 65 percent to other cities, counties, school districts, and other political subdivisions.

Department of Transportation

The executive recommendation provided $228.6 million from the highway fund with money transferred from the permanent oil tax trust fund for state road projects in areas affected by oil and gas development. The executive recommendation also provided $142 million from the highway fund with money transferred from the permanent oil tax trust fund for county and township roadway projects in areas affected by oil and gas development. The funding for county and township road projects is to be distributed by the Department of Transportation based on a report prepared by the Upper Great Plains Transportation Institute that details transportation infrastructure needs in areas affected by oil and gas development.

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Expected

$7[illegible]0 per barrel

165 - 200[illegible]

	Barrels per day	wells	tax	Annual GPT	Revenue Legacy	OE[illegible]	
2008	171,947	4,221	0.096	$235,353,071		$216,524,826	
2009	218,432	4,595	0.099	$298,978,748		$292,999,173	
2010	309,670	5,349	0.102	$423,860,625		$440,815,050	
2011	390,000	6,300	0.115	$533,812,500	$104,093,438	$589,862,813	current rate is 11.5% - 5% gross production tax + 6.5% extraction tax
2012	460,000	8,300	0.110	$629,625,000	$226,665,000	$528,885,000	lower rate to 11% at 425,000 barrels per day - 5% gross production tax + 6% extraction tax
2013	530,000	9,300	0.105	$725,437,500	$239,394,375	$558,586,875	lower rate to 10.5% at 500,000 barrels per day - 5% gross production tax + 5.5% extraction tax
2014	600,000	10,300	0.100	$821,250,000	$246,375,000	$574,875,000	lower rate to 10% at 575,000 barrels per day - 5% gross production tax + 5% extraction tax
2015	670,000	11,300	0.095	$917,062,500	$247,606,875	$577,749,375	lower rate to 9.5% at 650,000 barrels per day - 5% gross production tax + 4.5% extraction tax
2016	710,000	12,300	0.090	$971,812,500	$233,235,000	$544,215,000	lower rate to 9% at 700,000 barrels per day - 5% gross production tax + 4% extraction tax
2017	710,000	13,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2018	710,000	14,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2019	710,000	15,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2020	710,000	16,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2021	710,000	17,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2022	710,000	18,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2023	710,000	19,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2024	710,000	20,300	0.090	$971,812,500	$233,235,000	$544,215,000	
2025	710,000	21,300	0.090	$971,812,500	$233,235,000	$544,215,000	
				$13,345,312,500	$3,396,484,688	$8,272,109,063	

$72 - $76 - $10 Lower than market

$60 per barrel

135 – 155 rigs

	Barrels per day wells	wells	tax	Annual GPT	Revenue Legacy	OET	
2008	171,947	4,221	0.096	$235,353,071		$216,524,826	
2009	218,432	4,595	0.099	$298,978,748		$292,999,173	
2010	309,670	5,349	0.102	$423,860,625		$440,815,050	
2011	380,000	6,150	0.115	$520,125,000	$101,424,375	$574,738,125	current rate is 11.5% - 5% gross production tax + 6.5% extraction tax
2012	415,000	7,000	0.115	$568,031,250	$221,532,188	$516,908,438	
2013	450,000	7,850	0.110	$615,937,500	$221,737,500	$517,387,500	lower rate to 11% at 425,000 barrels per day - 5% gross production tax + 6% extraction tax
2014	485,000	8,700	0.110	$663,843,750	$238,983,750	$557,628,750	
2015	525,000	9,550	0.105	$718,593,750	$237,135,938	$553,317,188	lower rate to 10.5% at 500,000 barrels per day - 5% gross production tax + 5.5% extraction tax
2016	545,000	10,400	0.105	$745,968,750	$246,169,688	$574,395,938	
2017	560,000	11,250	0.105	$766,500,000	$252,945,000	$590,205,000	
2018	575,000	12,100	0.100	$787,031,250	$236,109,375	$550,921,875	lower rate to 10% at 575,000 barrels per day - 5% gross production tax + 5% extraction tax
2019	590,000	12,950	0.100	$807,562,500	$242,268,750	$565,293,750	
2020	600,000	13,800	0.100	$821,250,000	$246,375,000	$574,875,000	
2021	610,000	14,650	0.100	$834,937,500	$250,481,250	$584,456,250	
2022	620,000	15,500	0.100	$848,625,000	$254,587,500	$594,037,500	
2023	630,000	16,350	0.100	$862,312,500	$258,693,750	$603,618,750	
2024	640,000	17,200	0.100	$876,000,000	$262,800,000	$613,200,000	
2025	650,000	18,050	0.095	$889,687,500	$240,215,625	$560,503,125	lower rate to 9.5% at 650,000 barrels per day - 5% gross production tax + 4.5% extraction tax
				$11,326,406,250	$3,511,459,688	$8,531,487,188	

$50 per barrel

105 – 125 rigs

	Barrels per day wells	wells	tax	Annual GPT	Revenue Legacy	OET	
2008	171,947	4,221	0.096	$235,353,071		$216,524,826	
2009	218,432	4,595	0.099	$298,978,748		$292,999,173	
2010	309,670	5,349	0.102	$423,860,625		$440,815,050	
2011	380,000	6,000	0.115	$520,125,000	$101,424,375	$574,738,125	current rate is 11.5% - 5% gross production tax + 6.5% extraction tax
2012	392,500	6,700	0.115	$537,234,375	$209,521,406	$488,883,281	
2013	405,000	7,400	0.115	$554,343,750	$216,194,063	$504,452,813	
2014	417,500	8,100	0.115	$571,453,125	$222,866,719	$520,022,344	
2015	430,000	8,800	0.110	$588,562,500	$211,882,500	$494,392,500	lower rate to 11% at 425,000 barrels per day - 5% gross production tax + 6% extraction tax
2016	442,500	9,500	0.110	$605,671,875	$218,041,875	$508,764,375	
2017	455,000	10,200	0.110	$622,781,250	$224,201,250	$523,136,250	
2018	467,500	10,900	0.110	$639,890,625	$230,360,625	$537,508,125	
2019	480,000	11,600	0.110	$657,000,000	$236,520,000	$551,880,000	
2020	492,500	12,300	0.110	$674,109,375	$242,679,375	$566,251,875	
2021	505,000	13,000	0.105	$691,218,750	$228,102,188	$532,238,438	lower rate to 10.5% at 500,000 barrels per day - 5% gross production tax + 5.5% extraction tax
2022	517,500	13,700	0.105	$708,328,125	$233,748,281	$545,412,656	
2023	530,000	14,400	0.105	$725,437,500	$239,394,375	$558,586,875	
2024	542,500	15,100	0.105	$742,546,875	$245,040,469	$571,761,094	
2025	555,000	15,800	0.105	$759,656,250	$250,686,563	$584,935,313	
				$9,598,359,375	$3,310,664,063	$8,062,964,063	

$40 per barrel

65 – 85 rigs

Constant at 350,000 barrels per day

Total Oil Tax Revenue Collections
Contained in Governor's Budget Forecast
And Assuming Additional Production Over Forecasted Levels
Including Computation of Rate Reduction Proposal (Proposed Amendments to HB 1467)

Scenario	Assumptions	FY 2012	FY 2013	11-13 Biennium	FY 2014	FY 2015	13-15 Biennium
Governor's Budget (1)	Price	$ 72.00	$ 75.00		$ 78.00	$ 81.00	
	Production	405,000	425,000		445,000	465,000	
	Tax Rate	11.5%	11.5%		11.5%	11.5%	
	Gross Revenue	$ 978,500,000	$ 1,062,600,000	$ 2,041,100,000	$ 1,311,257,025	$ 1,422,889,538	$ 2,734,146,563
Higher Production (2)	Price	$ 72.00	$ 75.00		$ 78.00	$ 81.00	
	Production	425,000	500,000		575,000	650,000	
	Tax Rate	11.5%	11.5%		11.5%	11.5%	
	Gross Revenue	$ 1,155,991,500	$ 1,416,656,250	$ 2,572,647,750	$ 1,694,320,875	$ 1,988,985,375	$ 3,683,306,250
Higher Production And Rate Reduction (3)	Price	$ 72.00	$ 75.00		$ 78.00	$ 81.00	
	Production	425,000	500,000		575,000	650,000	
	Tax Rate	11.0%	10.5%		10.0%	9.5%	
	Gross Revenue	$ 1,105,731,000	$ 1,293,468,750	$ 2,399,199,750	$ 1,473,322,500	$ 1,643,074,875	$ 3,116,397,375

Revenue Comparisons	11-13 Biennium	13-15 Biennium
Revenue gain (over Gov's Budget) due to higher production:	$ 531,547,750	$ 949,159,688
Revenue loss due to rate reduction (from higher production scenario):	$ (173,448,000)	$ (566,908,875)
Revenue gain (over Gov's Budget) from higher production including rate reductions:	$ 358,099,750	$ 382,250,813

(1) Governor's Budget does not contain a forecast for 2013-15 biennium. Price and production assumptions were continued in a linear manner

(2) Higher production assumptions were amounts needed to trigger first 4 of 5 rate reductions in HB 1467. Assumes 1 rate reduction per year

(3) Rate reductions are assumed to be in place for full fiscal year. Provisions in the bill require a five-month delay before the first rate reduction could occur.

Prepared By: Office of Tax Commissioner, Kathryn Strombeck, March 7, 2011

11.0597.02003
Title.

Prepared by the Legislative Council staff for
Representative Carlson
March 14, 2011

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1467

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact sections 57-51.1-01, 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 and exemptions; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 57-51.1-01 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-01. Definitions ~~for oil extraction tax.~~

For ~~the~~ purposes of ~~the oil extraction tax law, the following words and terms shall have the meaning ascribed to them in this section~~this chapter:

1. "Average daily production" of a well means the qualified maximum total production of barrels of oil from the well during a calendar month ~~period~~ divided by the number of calendar days in that ~~period,~~month and "qualified maximum total production" of a well means that the well must have been maintained at the maximum efficient rate of production as defined and determined by rule adopted by the industrial commission ~~in furtherance of its authority~~ under chapter 38-08.

2. "Average ~~price" of a barrel of crude oil means the monthly average of the daily closing price for a barrel of west Texas intermediate cushing crude oil, as those prices appear in the Wall Street Journal, midwest edition, minus two dollars and fifty cents. When computing the monthly average price, the most recent previous daily closing price must be considered the daily closing price for the days on which the market is closed~~statewide daily production" means the number of barrels of oil produced from wells within this state during a calendar month divided by the number of calendar days in that month, as determined by the industrial commission.

3. ~~"Horizontal reentry well" means a well that was not initially drilled and completed as a horizontal well, including any well initially plugged and abandoned as a dry hole, which is reentered and recompleted as a horizontal well.~~

~~4. "Horizontal well" means a well with a horizontal displacement of the well bore drilled at an angle of at least eighty degrees within the productive formation of at least three hundred feet [91.44 meters].~~

~~5.~~ "Oil" means petroleum, crude oil, mineral oil, casinghead gasoline, and all liquid hydrocarbons that are recovered from gas on the lease incidental to the production of the gas.

~~6.~~4. "Property" means the right which arises from a lease or fee interest, as a whole or any designated portion thereof, to produce oil. A producer shall treat as a separate property each separate and distinct producing reservoir subject to the same right to produce crude oil~~; provided, that such~~ if the reservoir is recognized by the industrial commission as a producing formation that is separate and distinct from, and not in communication with, any other producing formation.

~~7.~~5. "Qualifying secondary recovery project" means a project employing water flooding~~. To be eligible for the tax reduction provided under section 57-51.1-02, a secondary recovery project must be certified as qualifying by the industrial commission and the project operator must have achieved for six consecutive months an average production level of at least twenty-five percent above the level that would have been recovered under normal recovery operations. To be eligible for the tax exemption provided under section 57-51.1-03 and subsequent thereto the rate reduction provided under section 57-51.1-02, a secondary recovery project must be~~ and certified as qualifying by the industrial commission, and the project operator must have obtained incremental production as defined in ~~subsection 5 of section 57-51.1-03~~rules of the industrial commission.

~~8.~~6. "Qualifying tertiary recovery project" means a project for enhancing recovery of oil which meets the requirements of section 4993(c), Internal Revenue Code of 1954, as amended through December 31, 1986, and includes the following methods for recovery:

a. Miscible fluid displacement.

b. Steam drive injection.

c. Microemulsion.

d. In situ combustion.

e. Polymer augmented water flooding.

f. Cyclic steam injection.

g. Alkaline flooding.

h. Carbonated water flooding.

i. Immiscible carbon dioxide displacement.

j. New tertiary recovery methods certified by the industrial commission.

It does not include water flooding, unless the water flooding is used as an element of one of the qualifying tertiary recovery techniques described in this subsection, or immiscible natural gas injection. ~~To be eligible for the tax reduction provided under section 57-51.1-02, a tertiary recovery project must be certified as qualifying by the industrial commission, the project operator must continue to operate the unit as a qualifying tertiary recovery project, and the project operator must have achieved for at least one month a production level of at least fifteen percent above the level that would have been recovered under normal recovery operations.~~ To be eligible for the tax exemption provided under section 57-51.1-03 ~~and subsequent thereto the rate reduction provided under section 57-51.1-02~~, a tertiary recovery project

must be certified as qualifying by the industrial commission, the project operator must continue to operate the unit as a qualifying tertiary recovery project, and the project operator must have obtained incremental production as defined in ~~subsection 5 of section 57-51.1-03~~rules of the industrial commission.

~~9.~~7. "Royalty owner" means an owner of what is commonly known as the royalty interest and shall not include the owner of any overriding royalty or other payment carved out of the working interest.

~~10.~~8. "Stripper well property" means a "property" whose average daily production of oil, excluding condensate recovered in nonassociated production, per well did not exceed ten barrels per day for wells of a depth of six thousand feet [1828.80 meters] or less, fifteen barrels per day for wells of a depth of more than six thousand feet [1828.80 meters] but not more than ten thousand feet [3048 meters], and thirty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] during any preceding consecutive twelve-month period. Wells which did not actually yield or produce oil during the qualifying twelve-month period, including disposal wells, dry wells, spent wells, and shut-in wells, are not production wells for the purpose of determining whether the stripper well property exemption applies.

~~11. "Trigger price" means thirty-five dollars and fifty cents, as indexed for inflation. By December thirty-first of each year, the tax commissioner shall compute an indexed trigger price by applying to the current trigger price the rate of change of the producer price index for industrial commodities as calculated and published by the United States department of labor, bureau of labor statistics, for the twelve months ending June thirtieth of that year and the indexed trigger price so determined is the trigger price for the following calendar year.~~

~~12. "Two-year inactive well" means any well certified by the industrial commission that did not produce oil in more than one month in any consecutive twenty-four month period before being recompleted or otherwise returned to production after July 31, 1995. A well that has never produced oil, a dry hole, and a plugged and abandoned well are eligible for status as a two-year inactive well.~~

SECTION 2. 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~~Oil extraction tax rate.

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.

The 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~~:

1. ~~For oil produced from wells drilled and completed after April 27, 1987, commonly referred to as new wells, and not otherwise exempt under section 57-51.1-03;~~Six percent beginning on the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds four hundred twenty-five thousand barrels per day, which must remain the rate unless a lower rate is determined under subsections 2 through 5.

2. Five and one-half percent beginning on the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds five hundred thousand barrels per day, which must remain the rate unless a lower rate is determined under subsections 3 through 5.

3. Five percent beginning on the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds five hundred seventy-five thousand barrels per day, which must remain the rate unless a lower rate is determined under subsection 4 or 5.

4. Four and one-half percent beginning on the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds six hundred fifty thousand barrels per day, which must remain the rate unless a lower rate is determined under subsection 5.

5. Four percent beginning on the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds seven hundred thousand barrels per day.

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

~~3. 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. 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 under section 57-51.1-03; or~~

~~5. 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 under section 57-51.1-03.~~

~~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 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 through 5.~~

SECTION 3. AMENDMENT. Section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-03. ~~(Effective through June 30, 2012)~~ Exemptions from oil extraction tax.

The following activities are specifically exempted from 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. A well spud on a Bakken pool stripper well property on or after the first day of the third calendar month following a period of three consecutive calendar months in which average statewide daily production exceeds four hundred twenty-five thousand barrels per day is not a stripper well under this subsection until production from that well meets the requirements of the definition for stripper well status under section 57-51.1-01.

3. ~~For a well drilled and completed as a vertical well, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.~~

~~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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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~~the exemption ~~that~~under this subsection which 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, 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, 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.~~4. 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.

~~9. The first seventy-five thousand barrels or the first four million five hundred thousand dollars of gross value at the well, whichever is less, of oil produced during the first eighteen months after completion, from a horizontal well drilled and completed after April 30, 2009, is subject to a reduced tax rate of two percent of the gross value at the well of the oil extracted under this chapter. A well eligible for a reduced tax rate under this subsection is eligible for the exemption for horizontal wells under~~

~~subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion. The rate reduction under this subsection becomes effective on the first day of the month following a month for which the average price of a barrel of crude oil is less than fifty-five dollars. The rate reduction under this subsection becomes ineffective on the first day of the month following a month in which the average price of a barrel of crude oil exceeds seventy dollars. If the rate reduction under this subsection is effective on the date of completion of a well, the rate reduction applies to production from that well for up to eighteen months after completion, subject to the other limitations of this subsection. If the rate reduction under this subsection is ineffective on the date of completion of a well, the rate reduction under this subsection does not apply to production from that well at any time.~~

~~**(Effective after June 30, 2012) Exemptions from oil extraction tax.** The following activities are specifically exempted from 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, 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. Oil recovered during testing prior to well completion is exempt from the oil extraction tax. 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.~~

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 that does not use carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter for a period of ten years from the date the incremental production begins. Incremental production from a tertiary recovery project that uses carbon dioxide and which has been certified as a qualified project by the industrial commission is exempt from any taxes imposed under this chapter 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, 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, 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.~~

~~9. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a horizontal well drilled and completed in the Bakken formation after June 30, 2007, and before July 1, 2008, is subject to a reduced tax rate of two percent of the gross value at the well of the oil extracted under this chapter. A well eligible for a reduced~~

~~tax rate under this subsection is eligible for the exemption for horizontal wells under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.~~

SECTION 4. 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 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 5. EFFECTIVE DATE. This Act is effective for taxable events occurring after June 30, 2011."

Renumber accordingly

B

STATE OF NORTH DAKOTA

OFFICE OF STATE TAX COMMISSIONER

Cory Fong, Commissioner

ANNUAL OIL TRIGGER PRICE ADJUSTMENT

TO: **North Dakota Oil Producers and Purchasers**

FROM: **Office of State Tax Commissioner**

SUBJECT: **Notification of Oil Trigger Price Adjustment for Calendar Year 2011**

DATE: **December 31, 2010**

In keeping with the provisions of North Dakota Century Code (N.D.C.C.) § 57-51.1-01, the Tax Commissioner has determined that the oil trigger price for the calendar year January 1, 2011, through December 31, 2011, is $46.78.

For your information, the following steps determined the trigger price for calendar year 2011:

STEP 1 - The annual average of the industrial commodities producer price index, commodity code 03 thru 15, as published by the U.S. Department of Labor, Bureau of Labor Statistics, for fiscal year 2010 was computed from the data shown below.

July	2009	174.6
August	2009	177.7
September	2009	176.9
October	2009	177.8
November	2009	180.1
December	2009	180.4
January	2010	184.6
February	2010	183.6
March	2010	185.6
April	2010	187.0
May	2010	187.2
June	2010	186.4
Annual Average		181.83

STEP 2 - A base rate adjustment of 1.31761 was computed by dividing the 2010 fiscal year average price index of 181.83 by the base rate index of 138.0, which was determined using the 2001 fiscal year average (i.e., 181.83 / 138.0 = 1.31761).

STEP 3 - The effective trigger price of $46.78 for calendar year 2011 was computed by multiplying $35.50 times the base rate adjustment of 1.31761 (i.e., $35.50 X 1.31761 = $46.78).

In accordance with N.D.C.C. § 57-51.1, if the average price of a barrel of crude oil (i.e., monthly average daily closing price for a barrel of west Texas intermediate Cushing crude oil minus two dollars and fifty cents) exceeds the trigger price for each month in any consecutive five-month period, certain exemptions and rate reductions become ineffective. The exemptions and rate reductions are subsequently reinstated if the average price is less than the trigger price for each month in any consecutive five-month period.

The trigger price adjustment is published on the Office of State Tax Commissioner's web site located at: www.nd.gov/tax. If you have any questions regarding this notification, please contact the Oil and Gas Tax Section at 701.328.3657 or by email at oiltax@nd.gov.

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19505.01

Prepared by the North Dakota Legislative Council staff

January 2011

Shirley

OIL TAX-RELATED INFORMATION FOR THE 2011-13 BIENNIUM

This memorandum provides information regarding statutory provisions relating to oil and gas gross production tax, oil extraction tax, the permanent oil tax trust fund, the oil and gas research fund, and the oil and gas impact grant fund; the legacy fund; oil prices and production; oil tax-related revenues and distributions for the 2009-11 biennium to date; and oil tax revenue projections for the 2011-13 biennium.

OIL AND GAS GROSS PRODUCTION TAX (NORTH DAKOTA CENTURY CODE CHAPTER 57-51)

The gross production tax on oil is 5 percent of the gross value at the well on oil produced. The gross production tax on gas is four cents times the gas base rate adjustment for each fiscal year as calculated by the Tax Department. Shallow gas produced during the first 24 months of production from and after the date of first sales of gas from a well completed or recompleted in a shallow gas zone after June 30, 2003, is exempted from the gross production tax. The oil and gas gross production tax is distributed per formula to the legacy fund, the oil and gas research fund, oil and gas impact grant fund (up to $8 million per biennium under current law), the state general fund or the permanent oil tax trust fund, and political subdivisions within producing counties.

OIL EXTRACTION TAX (CHAPTER 57-51.1)

The oil extraction tax rate is 6.5 percent, but the rate may be reduced or oil may be exempt as determined by a trigger price. The trigger price is defined in statute as $35.50 as indexed for inflation. The current trigger price is $46.79. If the average price of a barrel of oil exceeds the trigger price for each month in any consecutive five-month period, the oil extraction tax is 6.5 percent. If the average price of a barrel of oil is less than the trigger price for each month in any consecutive five-month period, the tax rate is reduced or oil is exempted for the following activities:

- For oil produced from any well drilled and completed as a vertical well after April 27, 1987, there is no extraction tax levied for the first 15 months, and thereafter the rate is 4 percent.
- For oil produced from any well drilled and completed as a horizontal well after April 27, 1987, there is no extraction tax levied for 24 months, and thereafter the rate is 4 percent.
- For incremental production from qualifying secondary recovery projects that have used up the five-year exemption from the date incremental production begins, the rate is 4 percent.
- For incremental production from qualifying tertiary recovery projects that do not use carbon dioxide which have used up the 10-year exemption from the date incremental production begins, the rate is 4 percent.
- For oil produced from a qualifying well that was "worked over" there is no extraction tax levied for 12 months, beginning with the first day of the third calendar month after the completion of the workover project, and thereafter the rate is 4 percent.
- For oil produced from a certified two-year inactive well there is no extraction tax levied for 10 years after the date of receipt of certification, and thereafter the rate is 6.5 percent.
- For oil produced from a certified horizontal reentry well there is no extraction tax levied for nine months after the date the well is completed as a horizontal well, and thereafter the rate is 6.5 percent.

The following activities are specifically exempt from the oil extraction tax without regard to the trigger price:

- Production from stripper wells.
- Incremental production from a qualifying secondary recovery project is exempt for five years from the date incremental production begins.
- Incremental production from a qualifying tertiary recovery project that does not use carbon dioxide is exempt for 10 years from the date incremental production begins.
- Incremental production from a qualifying tertiary recovery project that uses carbon dioxide is exempt from the date the incremental production begins.
- The initial production of oil from a well is exempt from any oil extraction tax for a period of 60 months if it meets any of the following conditions:
  - Is located within the boundaries of an Indian reservation;
  - Is on lands held in trust for an Indian tribe or individual Indian; or
  - Is on lands held by an Indian tribe as of August 1, 1997.

Under the July 1, 2008, agreement between the Governor and the Three Affiliated Tribes of the Fort Berthold Reservation, wells on trust lands are subject to a tax of 11.5 percent and wells on nontrust lands are subject to a tax of 5 percent. Tax revenue from

wells on trust lands are divided evenly between the tribe and state, and tax revenue from wells on nontrust lands are allocated 80 percent to the state and 20 percent to the tribe. The effect of the agreement is to allow the exemption only for wells on nontrust lands within the reservation.

A contingent rate reduction in the oil extraction tax, which can only go into effect if the trigger price rate reduction is not in effect, reduces the oil extraction tax rate for horizontal wells from 6.5 percent to 2 percent during the time the rate reduction is in effect. The rate reduction becomes effective on the first day of the month following a month for which the average price of a barrel of crude oil is less than $55. The contingent rate becomes ineffective on the first day of the month following a month for which the average price of a barrel of crude oil exceeds $70. The contingent rate reduction applies to oil produced during the first 18 months after completion for a horizontal well drilled and completed after April 30, 2009, and is limited to the first 75,000 barrels or the first $4.5 million of gross value at the well of oil produced from the well. If the rate reduction is effective on the date of completion of a well, the rate reduction applies to production from that well for up to 18 months after completion, even if the price of oil rises to more than $70. If the rate reduction is ineffective on the date of completion of a well, the rate reduction does not apply to production from that well at any time. The contingent rate reduction was in effect from May 1, 2009, through October 31, 2009. During October 2009, the average price of a barrel of crude oil exceeded $70. North Dakota Century Code defines the average price of a barrel of crude oil used to determine the trigger and contingent rate reduction to be the monthly average of the daily closing price for a barrel of West Texas intermediate Cushing crude oil minus $2.50.

The oil extraction tax is allocated as follows:

- Thirty percent to the legacy fund beginning July 1, 2011.
- Twenty percent to the resources trust fund for water development projects.
- Ten percent to the foundation aid stabilization fund.
- Ten percent to the common schools trust fund.
- Sixty percent to the state general fund or the permanent oil tax trust fund after allocation to the oil and gas research fund.

The constitutional and statutory provisions for distribution of the oil extraction tax will exceed 100 percent beginning July 1, 2011. The 2011 Legislative Assembly may wish to consider statutory changes to ensure the distribution formula for the oil extraction tax does not exceed 100 percent.

PERMANENT OIL TAX TRUST FUND (SECTION 57-51.1-07.2)

Section 57-51.1-07.2 (1997 Senate Bill No. 2366) establishes a permanent oil tax trust fund and provides that all revenues deposited in the general fund during a biennium derived from taxes imposed on oil and gas under Chapters 57-51 (Oil and Gas Gross Production Tax) and 57-51.1 (Oil Extraction Tax) which exceed $71 million are to be transferred by the State Treasurer to the permanent oil tax trust fund. The State Treasurer is to transfer the interest earnings on the fund to the general fund as they accrue. The principal of the permanent oil tax trust fund may only be spent upon a two-thirds vote of the members elected to each house of the Legislative Assembly.

LEGACY FUND

The 2009 Legislative Assembly enacted House Concurrent Resolution No. 3054, which was approved by North Dakota voters in the 2010 general election and which creates a new section to Article X of the Constitution of North Dakota to create a new North Dakota legacy fund. The measure will become effective July 1, 2011. The constitutional measure provides that 30 percent of all revenues derived from taxes imposed on oil and gas be transferred to the legacy fund. The principal and earnings of the legacy fund accruing prior to June 30, 2017, may not be expended until after June 30, 2017, and then may only be spent upon a two-thirds vote of the members elected to each house of the Legislative Assembly. Expenditures from the fund are limited to 15 percent of the principal during a biennium. Earnings of the fund accruing after June 30, 2017, will be transferred to the state general fund.

OIL AND GAS RESEARCH FUND (SECTION 57-51.1-07.3)

Section 57-51.1-07.3 (2003 Senate Bill No. 2311) establishes the oil and gas research fund. Section 57-51.1-07.3 provides that 2 percent of the state's share of the oil and gas gross production tax and oil extraction tax revenues, up to $4 million per biennium, is to be deposited into the oil and gas research fund. All money deposited in the oil and gas research fund is appropriated as a continuing appropriation to the Oil and Gas Research Council.

OIL AND GAS IMPACT GRANT FUND

Section 57-51-15 (1989 House Bill No. 1302) establishes the oil and gas impact grant fund for deposit of revenue from oil and gas gross production taxes. Section 57-51-15 provides that one-third of one percent of the gross value of oil at the well, up to $8 million per biennium, is to be deposited into the oil and gas impact grant fund. Money in the oil and gas impact grant fund is disbursed by the Energy Development Impact Office of the Land Department as grants to local units of government affected by oil and gas development activity. The executive budget recommends increasing the allocation to the oil and gas impact grant fund to a maximum of $100 million.

OIL AND GAS TAX REVENUE DISTRIBUTION FLOWCHART

Attached as an appendix is a flowchart reflecting the distribution of oil and gas tax revenues for the 2011-13 biennium based on current law.

OIL PRICES AND PRODUCTION

The following table provides information from the Department of Mineral Resources relating to average North Dakota oil prices and daily production levels for the 2009-11 biennium through November 2010:

	Average North Dakota Oil Price	Average Daily Production of Barrels of Oil
July 2009	$54.87	227,880
August 2009	$61.41	232,365
September 2009	$59.26	238,172
October 2009	$65.52	240,041
November 2009	$67.06	245,854
December 2009	$63.96	242,107
January 2010	$68.57	236,176
February 2010	$67.58	261,223
March 2010	$71.20	277,454
April 2010	$71.26	284,492
May 2010	$60.10	298,283
June 2010	$63.14	314,696
July 2010	$67.35	321,163
August 2010	$69.07	328,883
September 2010	$67.95	341,385
October 2010	$74.41	342,094 (preliminary)
November 2010	$75.60 (preliminary)	342,247 (preliminary)

OIL AND GAS TAX REVENUES

The following table provides information on actual monthly distributions of oil and gas tax revenues for the 2009-11 biennium to date through December 2010:

	Actual Monthly Distributions								
	General Fund	Permanent Oil Tax Trust Fund	Oil and Gas Research Fund	Oil and Gas Impact Fund	Resources Trust Fund	Common Schools Trust Fund	Foundation Aid Stabilization Fund	Political Subdivisions	Total
August 2009	$28,814,213	$89,005[1]	$588,045	$1,205,112	$3,708,878	$1,854,439	$1,854,439		$38,114,131
September 2009	14,115,128	124,131[1]	288,064	1,510,131	3,620,364	1,810,182	1,810,182	$14,452,459	37,730,641
October 2009	23,881,587	159,105[1]	487,380	1,424,978	4,266,878	2,133,439	2,133,439	10,070,975	44,557,781
November 2009	4,189,072	19,731,466	484,475	1,585,995	3,651,341	1,825,671	1,825,671	6,983,331	40,277,022
December 2009		28,942,441	585,855	1,707,402	4,147,702	2,073,851	2,073,851	6,289,856	45,820,958
January 2010		30,594,234	622,853	566,382	4,324,659	2,162,329	2,162,329	6,732,783	47,165,569
February 2010		30,856,996	625,085		4,358,550	2,179,275	2,179,275	5,695,998	45,895,179
March 2010		28,518,377	318,243		3,964,773	1,982,386	1,982,386	4,420,759	41,186,924
April 2010		40,420,799			5,245,925	2,622,963	2,622,963	6,616,346	57,528,996
May 2010		43,175,692			5,693,977	2,846,988	2,846,988	5,582,773	60,146,418
June 2010		88,721,611			11,847,487	5,923,743	5,923,743	5,648,302	118,064,886
July 2010								4,565,549	4,565,549
August 2010		43,461,105			5,600,893	2,800,447	2,800,447	4,387,448	59,050,340
September 2010		31,761,664			6,343,686	3,171,843	3,171,843	21,528,772	65,977,808
October 2010		43,241,561			6,513,183	3,256,591	3,256,591	12,084,863	68,352,789
November 2010		44,174,395			6,256,551	3,128,276	3,128,276	9,036,237	65,723,735
December 2010		52,063,832			7,520,245	3,760,123	3,760,123	9,777,874	76,882,197
Total	$71,000,000	$526,036,414	$4,000,000	$8,000,000	$87,065,092	$43,532,546	$43,532,546	$133,874,325	$917,040,923

[1]This amount reflects a portion of the first $700,000 of the state's share of oil extraction tax revenue produced from wells within the exterior boundaries of the Fort Berthold Reservation which is required to be deposited in the permanent oil tax trust fund pursuant to Section 57-51.1-07.4.

DISTRIBUTION OF OIL AND GAS GROSS PRODUCTION TAXES TO POLITICAL SUBDIVISIONS

Oil and gas gross production taxes are apportioned to the state and counties pursuant to Section 57-51-15. From the tax equal to the first 1 percent of gross value at the well of oil production, a direct allocation of $500,000 is provided for a city in an oil-producing county which has a population of 7,500 or more and more than 2 percent of its employment engaged in the mining industry. The allocation is increased to $1 million if the city's employment in the mining industry exceeds 7.5 percent of its total employment. Also from the tax equal to the first 1 percent of value of oil produced is a biennial allocation to the oil and gas impact grant fund up to $8 million. Any amounts remaining from the first 1 percent are allocated to the state general fund.

After deduction of the amounts provided for above, remaining annual revenue from the tax is allocated as follows:

1. The first $2 million is allocated to the county.

2. The next $1 million is allocated 75 percent to the county and 25 percent to the state general fund.
3. The next $1 million is allocated 50 percent to the county and 50 percent to the state general fund.
4. The next $14 million is allocated 25 percent to the county and 75 percent to the state general fund.
5. All annual revenue remaining after the above allocations is allocated 10 percent to the county and 90 percent to the state general fund.

The table below provides information on the distribution of the oil and gas gross production taxes for oil produced from July 2009 through October 2010 for oil-producing counties and oil extraction tax and oil and gas gross production tax for Fort Berthold based on information from the State Treasurer. The amounts include distributions to cities and school districts within the counties:

County	2009-11 Biennium to Date Actual Revenue for Oil Production Through October 2010
Billings	$7,349,021
Bottineau	5,314,550
Bowman	12,822,533
Burke	5,170,272
Divide	6,519,075
Dunn	13,456,243
Golden Valley	1,851,773
Hettinger	471
McHenry	89,239
McKenzie	14,406,359
McLean	423,384
Mercer	17,085
Mountrail	23,992,458
Renville	2,641,890
Slope	1,712,126
Stark	5,167,542
Ward	195,445
Williams	13,847,714
Fort Berthold	18,897,145
Total	$133,874,325

2011-13 PRELIMINARY REVENUE FORECAST

The table below presents information on estimated oil and gas tax revenue based on the Office of Management and Budget's revised revenue forecast for the 2009-11 biennium and the executive revenue forecast for the 2011-13 biennium:

	2009-11 Biennium Legislative Forecast (May 2009)[1]	Revised 2009-11 Biennium Forecast[2] (December 2010)	Executive 2011-13 Biennium Forecast[3] (December 2010)
General fund	$71,000,000	$71,000,000	$71,000,000
Permanent oil tax trust fund	323,092,000	886,261,921	607,271,039
Legacy fund			612,468,299[4]
Political subdivisions	101,211,208	168,759,700	247,196,952
Oil and gas research fund	4,000,000	4,000,000	4,000,000
Oil and gas impact grant fund	8,000,000	8,000,000	100,000,000
Common schools trust fund	25,554,341	68,472,199	99,906,177
Foundation aid stabilization fund	25,554,341	68,472,199	99,906,177
Resources trust fund	51,108,682	136,944,397	199,812,353
Total oil and gas tax revenue	$609,520,572	$1,411,910,416	$2,041,560,997

[1]The legislative forecast estimated oil prices to range from $40 to $45 per barrel in the first year of the 2009-11 biennium and $50 to $55 per barrel in the second year. The daily production rate was estimated to average approximately 213,000 barrels for the 2009-11 biennium.

[2]The revised 2009-11 biennium forecast reflects actual collections for fiscal year 2010 and revised estimates for fiscal year 2011 based on an average price per barrel of $67 and an average daily production rate of 366,250 barrels.

[3]The executive forecast for the 2011-13 biennium estimates oil prices to average from $72 per barrel in the first year of the 2011-13 biennium and $75 per barrel in the second year. The estimated average daily production rate ranges from 390,000 barrels per day to 405,000 barrels per day for the first year of the biennium and from 405,000 barrels per day to 425,000 barrels per day in the second year.

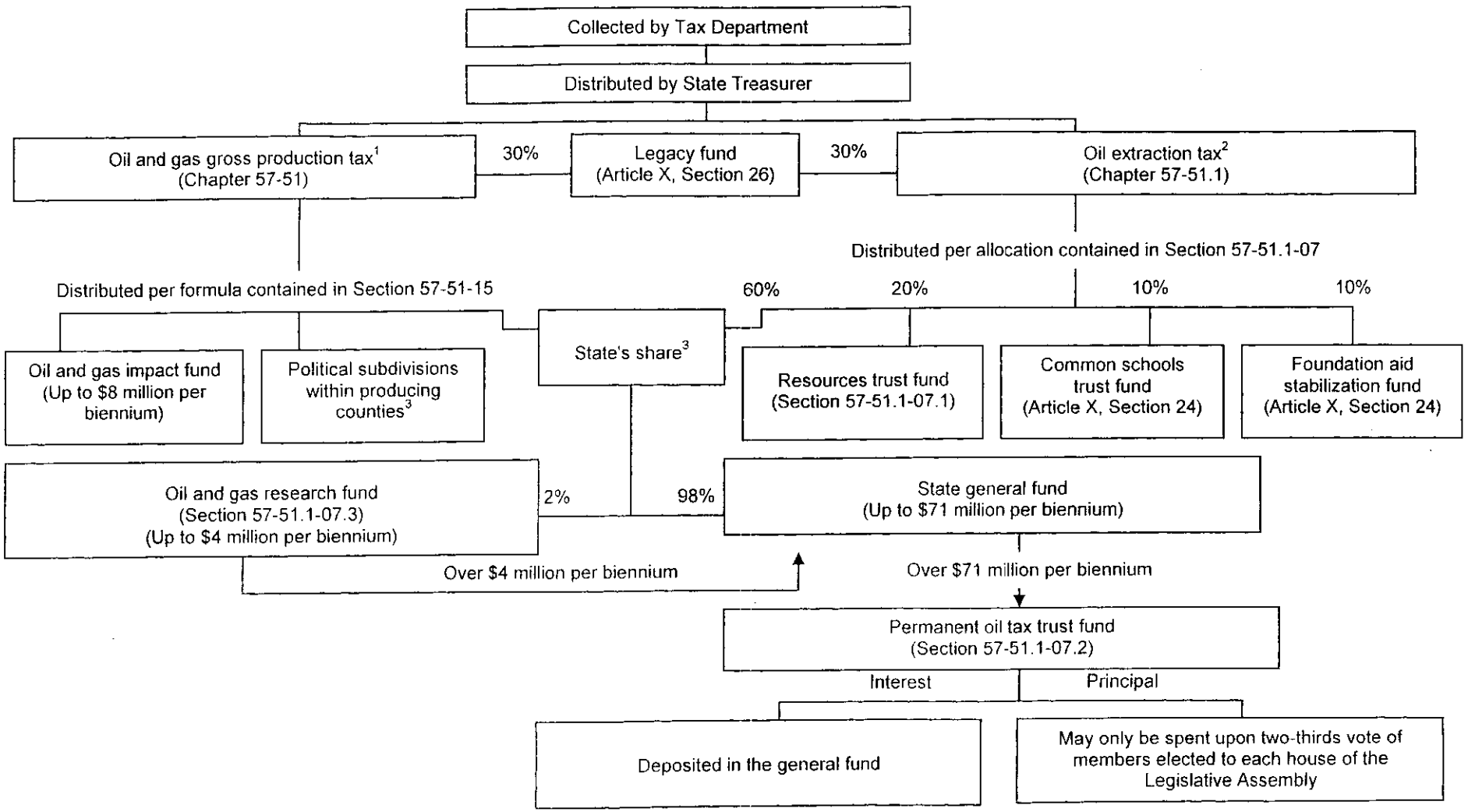
[4]Passage of constitutional measure No. 1 in the November 2010 general election resulted in the creation of a legacy fund. The legacy fund will receive 30 percent of oil and gas gross production and oil extraction taxes beginning July 1, 2011, resulting in $612.47 million estimated to be deposited in the legacy fund rather than the permanent oil tax trust fund during the 2011-13 biennium.

ATTACH:1

Prepared by the North Dakota Legislative Council staff

January 2011

Oil and Gas Tax Revenues Distribution of Funds for the 2011-13 Biennium Based on Current Law



[1]The gross production tax on oil is 5 percent of the gross value at the well on oil produced. The gross production tax on gas is four cents times the gas base rate adjustment for each fiscal year as calculated by the Tax Department.

[2]The oil extraction tax is 6.5 percent of the gross value at the well and 4 percent in certain situations.

[3]The oil and gas gross production tax is distributed to the political subdivisions and to the state general fund based on each county's production and city populations.

NORTH DAKOTA PETROLEUM COUNCIL

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House Bill 1467

Senate Finance & Taxation Committee

March 16, 2011

Chairman Cook and Members of the Committee. My name is Ron Ness and I am the president of the North Dakota Petroleum Council. The North Dakota Petroleum Council represents 280 companies involved in all aspects of the oil and gas industry and has been representing the industry since 1952. Our members produced nearly 98% of the 113 million barrels of oil produced in North Dakota in 2010. We also represent 47 of the top 50 oil producers in the state. I appear before you today in support of HB 1467.

The Bakken is an amazing resource. It provides great jobs, great wealth, population growth, and energy for our nation. Along with that, as we all know, it creates great challenges for our state and industry as we go forward. Fortunately, the growth in oil tax revenues has made investing in those challenges and funding the needs rather easy in North Dakota, while nearly all other states struggle to balance their budgets. Even with our infrastructure challenges, our state is experiencing tremendous budget surpluses enabling us to increase funding to education, water projects, and creating the Legacy Fund, while still having the ability to provide massive tax relief to our citizens in the form of property, income, and corporate taxes.

To put this all in perspective, it was only a decade ago when we collected oil and gas production taxes at $60 million for an entire biennium, while today we are now collecting nearly $60 million per month with an expected two billion in the next biennium, or even much more. These amounts

do not account for the lease and royalty income that is pouring into state coffers like never before. Yes, it is easy for us to vote for beneficial projects and tax relief now when the surplus is there. It's great fun, but we have to be cautious and look long term.

At today's high oil prices, the great Bakken recovery rates we are seeing in many parts of western North Dakota, and with a record 174 rigs drilling, it is easy to paint a rosy picture. But history teaches us it is easy to become complacent and short-sighted with potentially catastrophic results.

With the current level of activity and current economics, it would only be logical for you to ask, "Why should the legislature consider changing its oil and gas tax policy now, and why would the industry even suggest it at this time of good economics and high prices?" We are developing what has become a known and vast resource that we never knew existed. We need a long-term plan over the next several decades, not months or years, to maximize this long-term, vast resource, for the benefit of everyone. In addition, at some point, shouldn't the industry be directly included in the tax relief being provided in North Dakota?

The oil and gas tax rate was raised 130% in 1980 at a time when all things seemed rosy. Government spending was rising and there didn't seem to be an issue -- and then it all crashed. High taxes and low prices effectively halted all development and the state's over reliance on production taxes sent us into a budgetary free fall. For the past 30 years, the North Dakota Legislature has struggled with the right oil and gas tax policy and over time has adopted a complex tax structure with more than a dozen incentives and price triggers. Over the years, these efforts to adjust the tax policy since 1980 did sustain our industry and benefit the state as well, but today we have a vast resource previously unknown or unreachable which requires careful and serious evaluation of our tax policy going forward.

The proposed amendment to HB 1467 is unique and not something we have considered previously. It provides for a gradual step-down of the tax rate which only occurs if the production is there to ensure adequate revenues will be available to fund the infrastructure needs. If we reach these levels, the

revenue stream becomes enormous and much larger than ever anticipated. Once again, if you solely look at today's prices and activity, naturally, one will wonder why lower the oil tax? However, the concept is not to look just at today, next month, or next year, but to look forward in terms of decades. For the State of North Dakota, it will create predictability for long-term tax collections by eliminating the 130% swing in tax rates from 5% to 11.5% and create a flat rate. In future times of low prices, and if history teaches us anything, we know low prices will also occur. It will be a tax increase to the State and provide more revenue to the state when it's needed. This is what a flat rate does – it evens it out over time. Predictability and simplicity – nobody knows what the price will be in the future; but, if we know the tax rate, we have reduced the uncertainty, which provides more predictability, which helps the state and industry.

The Bakken play is an intensive capital cost venture where companies are budgeting billions of dollars over many years to come. We've seen how these investments to date have improved technology and ultimate recovery of oil. Yet, as of today, we only recover a small amount of oil from the reservoir rock. To maximize this vast resource and achieve even higher recovery rates with the continued advancement in expensive technology over the next several decades, billions and billions of dollars of capital will be required in times of both high prices, and low, to maintain and develop this resource. A long term fiscal tax policy, one that is fair, competitive and simplified, helps companies raise and meet their capital investment requirements, which in turn will be reflected in the higher ultimate recovery of oil produced and corresponding revenue to the State of North Dakota and its citizens. At these prices, and with the current success rate, industry is going to drill many wells and produce lots of additional oil. It's the potential decades of drilling after that we should be looking at by passing this type of oil tax structure -- when times are good.

We urge you to support a fair, competitive, and predictable oil tax structure for North Dakota's future.

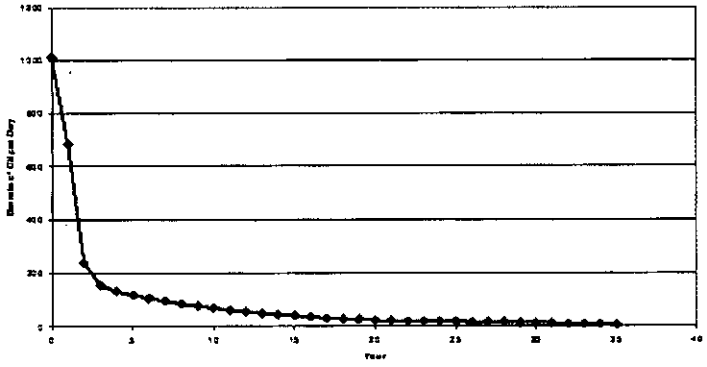
OIL REVENUE & USE OF OIL REVENUE

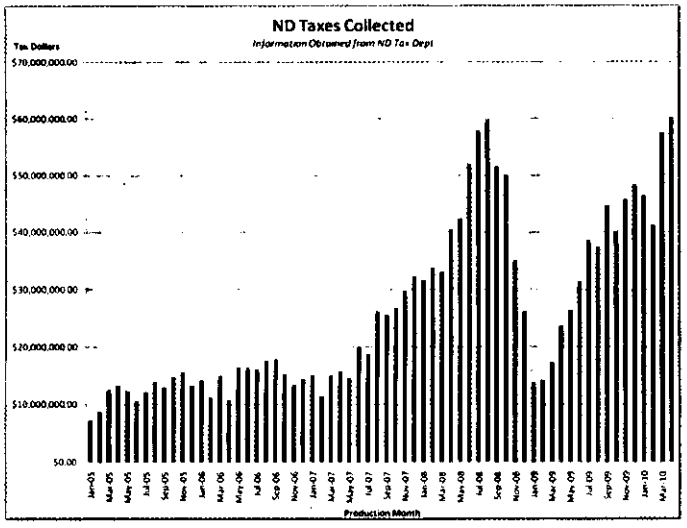
	Production & Extraction	Production & Extraction	Production & Extraction	Extraction 6.5%	Extraction 6.5%	Extraction 6.5%	Production 5%	Production 5%	Production 5%		
	Permanent Oil Trust	Legacy Fund	General Fund	Resources Trust Fund	Common Schools Trusts	Stabilization Foundation Aid	Impact Fund	Counties Production Formula	Research Oil & Gas	Total Oil Rev 2011-13	
End (09-11)	620.1	0	0	128.5	1.4B	134	0	0	0		
Rev (11-13)	608.3	618.6	71	199.8	100	100	100	247	3	2047.7	M
				Repay 3.5						2.0477	B
				Int. 1.1							
Totals	1228.4	618.6	71	328.3	1.5B	234	100	247	3		
(in millions)											
		Locked Savings	Deposit in General Fund	Water Commission Water Projects	Elementary & Secondary Funding (part of interest and rev is pd out in Foundation aid)	Locked Savings for Elementary & Secondary	Grants Oil & Gas Counties	Formula Oil & Gas Counties In Lieu of Property Tax	Research New Tech		
		State Wide	State Wide	State Wide	State Wide	State Wide	Oil & Gas Counties	Oil & Gas Counties	Oil & Gas Industry		

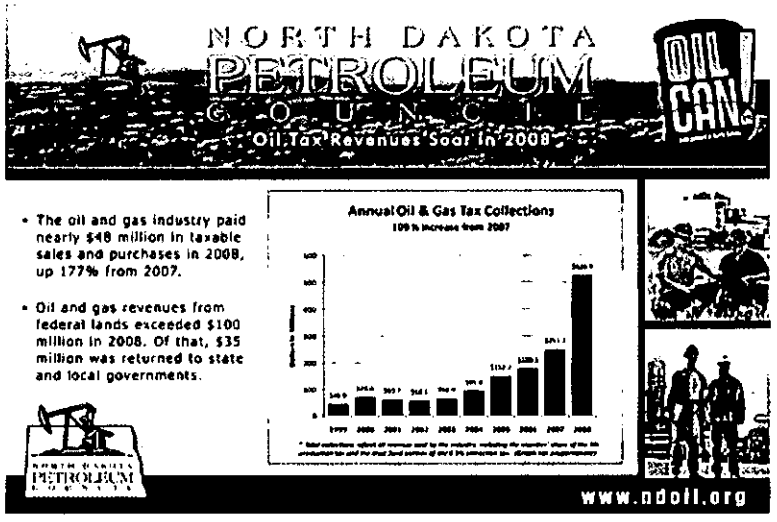
DHS	1.5	State Wide			
Higher Ed	2.3				
Tribal College	1		Oil Counties Infrastructure Support		
State Road Project	228.6	Oil Counties	State Roads in oil country	229	M
County & Township	142	Oil Counties	County roads and Township roads	142	M
Property Tax (11-13)	46.8	State Wide	Oil & Gas Impact Grants	100	M
Property Tax (13-15)	341.8	State Wide	Oil & Gas Production Tax	247	M
General Fund	232	State Wide	DOT Funds - State/Federal Highway Funds	240	M
Ending (11-13)	232	State Wide			
				958	M

Proposed Governor's Budget 2011-13

Typical Bakken Well Production







NORTH DAKOTA
PETROLEUM
COUNCIL

Tax Rate Should be Comparable to Other Oil-producing States

- Majority (52%) either agree (46%) or strongly agree (6%) that the oil industry in ND should be taxed at a rate that is comparable to the taxes charged by other oil-producing states.