2013 HOUSE FINANCE AND TAXATION

HB 1179

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1179
January 21, 2013
Job #17482

☐ Conference Committee

Committee Clerk Signature Mary Brucker

Explanation or reason for introduction of bill/resolution:

A Bill relating to the oil extraction tax exemption for stripper wells.

Minutes:

Attached testimony #1, 2

Chairman Belter: Opened hearing on HB 1179.

Representative Drovdal: Introduced bill. This is really a bill to define a stripper well. A stripper wells are defined by the depth and by the production. If they're from 0-60 they produce 10 barrels or something then from 6,000 to 10,000 it's 15-20 barrels. If it produces less than that it qualifies as a stripper well and if it's above 10,000 its 30 barrels which is what we are dealing with in western North Dakota. I have no idea how they define stripper fields. Mr. Helms can help define that. But once they qualify my understanding is that all the wells in that field will qualify as stripper wells. When they qualify the tax rate goes from the current 11 ½% down to the 5% production tax. In other words the extraction tax is forgiven on the stripper wells and any other wells that come in will also qualify as stripper wells and have a lower tax rate. To encourage them to get all the oil out of the fields and get a return on their investment we exempted the tax. Instead of qualifying for a stripper well field each well on its own will have to qualify for whatever barrels we set for daily production. If this passes I would like to see an increase to 30 barrels to 50 barrels a day so as the fields get weaker they will take the time and the money to go in and redo them. I understand that the Bakken and Three Forks fields will drop to 50% of their original production and in the next 12 months it will drop another 50% of that so after two years you are at 25%. If oil prices drop down a bit and that company decides that they don't want to finish the field or the infield drilling they may be able to qualify for a stripper well within a year or two. If it's then defined as a field they would go in probably with new technology and get some good wells then would be at the 5%. I would hope this legislative body would reconsider the 11 ½% as it's one of the highest in the nation and I think is just digging us a big hole and we need to lower it down a couple percentage points.

Representative Haak: Is there anything we can do to improve the production by offering new technologies?

Representative Drovdal: I know we are investing in research with some of the oil money to work with the oil companies to continue to work on the technology. Private businesses are really good at working on this since that is where they are going to make their money and their investment. As a state we are always trying to look for new ideas to help them out and one of the ways is to lower the taxes to a little more reasonable rate.

Representative Haak: Once they are improved and producing more barrels do they still not pay taxes or are we collecting taxes on that after we've improved that technology?

Representative Drovdal: They will continue to pay the 5% production tax regardless and if they go in and take a well that's doing 10 barrels a day and it goes up to 300 barrels a day they are still exempt once that oil field is exempt and once that well is exempt they would still go under the 5% because that's the way they recover the money. There's very few that improve that much so it balances out by not going in and redoing them. Once they're determined as a stripper well field that distinction stays with them from there on.

Representative Haak: Do you think we should recertify these wells annually so if the technology would improve we would be updated on what they were producing?

Representative Drovdal: I don't. Knowing the percentage out there the chances of them improving it that much probably won't happen often so they would deserve that opportunity then.

Chairman Belter: Any other questions? Further testimony?

Representative Kempenich: This has been a discussion the last year or two and nationally stripper wells are probably 80% or better of production when you get into some of these older fields. I think this is just opening up the discussion on the definition of stripper wells. There are a lot of things that go into play; the depth, zones, and zones within that depth so it becomes very interesting when you're trying to define what is described as a stripper well. I think one of the things talked about was enhanced recovery and that has to be something where if companies come in to an old field and try to do enhanced recovery they should be able to recapture back some of the costs. I think we have to be very careful when taxes are kicked on and off for this. I'm sure testimony following will start the outline of what is a reasonable outcome of definitions of stripper wells.

Chairman Belter: Are there any questions of Representative Kempenich? Any further testimony in support to 1179? Any opposition to 1179?

Ron Ness, President of North Dakota Petroleum Council: See attached testimony #1.

Vice Chairman Headland: Cost associated with redoing a stripper well with new technology versus drilling a new well?

Ron Ness, President of North Dakota Petroleum Council: In today's Bakken and Three Forks world essentially what you're doing with the current technology available you're drilling your first well and if that screen is your two mile 1280 space unit at some point it becomes a stripper property a stripper well so then you can qualify that spacing unit as a stripper property. In 2012 I think your costs on that well averaged to $11 million. So now you go back in and you have to get a lot of barrels of oil by the way to recover $11 million even at $80 a barrel. When we think back to this bill and we talk about the early 90s when these wells were costing maybe $1.5 or 2.5 million and look at the costs now and the risk that company is taking. We have some very prolific areas inside the Bakken but there are people trying to step outside the Bakken taking those risks all the time. Essentially you're now drilling another well because the technology to re-enter that well and use that technology isn't as effective as providing a second well. So you'll have $20-22 million into those two wells likely.

Representative Drovdal: Once that rig and well qualifies for a stripper well the infield drilling on that spacing unit, all of them qualify. I know your organization and members are really great at trying to intimidate members when I get home. The reason for this bill is fairness and I wasn't in favor of the tax increase. Did I not also try and talk to you in November to work with you on this bill and it was last week before you came back with a response?

Ron Ness, President of North Dakota Petroleum Council: This has been a long discussion and you did approach me in November and we continue to work on this issue as you know.

Representative Haak: On average how many barrels per day does a well produce?

Ron Ness, President of North Dakota Petroleum Council: I think that is completely dependent on where you're drilling that well and which formation you're drilling that well. Typically when we're talking about the Bakken and Three Forks formation your average well today may come in at 800 barrels a day. That well is going to decline and I believe the number is 65% in the first year, 50% decline in the second year. If you end up with a Bakken well that's going to produce 250 barrels a day going forward for an extended period of time that is a good well. We have early Bakken wells that were drilled starting at sub 100 barrels of oil and those are the stripper type wells that Representative Drovdal indicated. That is considered a stripper well if it goes below 30 barrels a day for one year. The important thing for this committee to get a grasp on over all the issue whether its an oil issue or a spending issue over the next four months is that Bakken wells do this. If you stop drilling today and Bakken wells do this the oil tax revenues will follow. The biggest thing to know is that in North Dakota that oil tax trigger that was triggered off in October 2004, if the oil price is below $5250 for a period of five months the oil extraction tax essentially goes to zero. For any well drilled within the last 24 months and for the remainder of the 24 months they have left and for any new well it goes to zero. You will pay 5% only on that well plus all existing production will drop from 11 1/2 % to 9% until the oil price exceeds $5250 for a period of five months. I would contend that if that happens over the next biennium you will be in special session in a very short order trying to figure out how to replace over $2 billion of lost tax revenue. This is the issue we've been trying to make over the last sessions. It's 130% swing that nobody can predict that price. We would like some certainty. Some of the issues on the back end are the areas with room for discussion as Representative Drovdal indicated.

Representative Marie Strinden: In the spirit of Representative Drovdal's request for fairness, what do the property owners that aren't lucky enough a stripper well on their property say about the inequality of the taxes that they are paying?

Ron Ness, President of North Dakota Petroleum Council: I'm not sure of any royalty owners that would find themselves lucky enough to have a stripper well. You've invested $10-11 million in that well then you're not lucky. You don't want your well to be a failure. I don't know any business in the world that operates like that. You want that well to be as productive as possible. The stripper property law as it stands today encourages that investor or company to reinvest back into that same property. Unfortunately under today's technology you think you can make that well better.

Representative Marie Strinden: I'm just curious whether or not there has been conversation in the industry about the inequity that Representative Drovdal was talking about?

Ron Ness, President of North Dakota Petroleum Council: I think that was part of my last statement. There are inequities all over any tax structure. Every tax structure has things beneficial to some and not beneficial to others and today we are talking about it being beneficial if you're in a good zone where you could improve your economics and the return for the investors and the state. If you produce more oil you pay more taxes. In the spirit of looking at the entire oil tax structure it is very complicated. There are many tax triggers and incentives based upon that major price difference of $5250 so I think you have to look at the whole picture and that's what we're saying.

Representative Drovdal: You mentioned the fiscal cliff that we will face if the oil revenue drops off under a number of different circumstances. Can we determine how much sales tax revenue because Williston went from one of the lowest to number one in the state because of oil?

Ron Ness, President of North Dakota Petroleum Council: That is a concern of what policy makers and all of us in North Dakota should be concerned about and is one of the reasons this bill is before you. The legacy fund is to ensure that the oil wells are producing for the next generations and have something to ensure that the revenue source is always there. We will be releasing our 2011 economic impact study over the next month or so and that will have some information in there. There's a reason Williston has become the number one city in terms of sales tax collections and that's because essentially every one of these Bakken wells in addition to the $11 million you pay in gross production and extraction taxes you pay about $330,000 per well in sales tax on all of your pipe and sand so when you take that times 2500 wells we drilled last year each of those wells pays $330,000 in sales tax. I think that's somewhere in the $600 million range of sales tax.

Representative Drovdal: I wanted to clarify your other comment where you state it's about $11 million but the last I heard it was about $7 million in the wells it takes less than a month to drill. I know the price of labor for truck drivers has gone down since then. Is that true that's its $11 million per well now?

Ron Ness, President of North Dakota Petroleum Council: I had an operator in my office last week with a major development plan in McKenzie County and his projected cost was $11.2 million. We've been in that $9 or 13 million range. Operators are working hard to try and reduce their costs.

Representative Klein: Do you agree that we need to have a better definition of stripper wells and field so that there's a standard method instead of what's going on now?

Ron Ness, President of North Dakota Petroleum Council: We would agree in the heart of the Bakken area in some of those early wells drilled but that's the tradeoffs in the tax policy. This bill eliminates it for all oil producing areas. We agree that's its part of a bigger discussion on an overall plan for the state of North Dakota to ensure that there is some type of tax revenues that are adequate to ensure what we need to pay for as far as oil and gas related impacts and also that the investors have some type of certainty. If you're trying to plan a project a Bakken is very unique and you will be making plans a long way out. If your tax increment could vary by 130% that is going to make a difference in how you're going to propose to make your plans in the future of these fields.

Representative Klein: What's the average amount of time for a stripper well? Or do they eventually completely fail?

Ron Ness, President of the North Dakota Petroleum Council: That number is going to depend completely on what kind of formation you're in. The intent and encouragement of the stripper provisions itself were that you keep those wells going on for a very long period of time because it requires about as many people to run a stripper well as it does a typical North Dakota oil well. In 1999 when North Dakota's oil prices collapsed to a point where wells weren't economical at any level especially stripper wells so Governor Schaffer went to Washington to try and encourage them to maintain some of the federal tax provisions on stripper properties and some of those other programs.

Representative Froseth: I believe we need to do some changing on the stripper well properties and definitions of them. This is a completely different oil structure now than it was from 1950s to the 1980s. I presume most of the present day stripper wells cost less than $1 million to drill than originally. I think they deserve that definition and that tax break they are getting. They could go into the same hole as the Bakken well and go out another mile further horizontally and produce 1000 barrels a day for a while. This needs to be changed somehow. Can you bring in some kind of suggestion that we can start working with?

Ron Ness, President of the North Dakota Petroleum Council: I think we would be more than happy to work with the committee. This bill covers one small segment of a big issue. The Bakken and Three Forks properties are unique. I think we are more than receptive to the discussion.

Chairman Belter: Any more questions of Mr. Ness? Further testimony in 1179?

Bill Shalhoob, Greater North Dakota Chamber: See attached testimony #2 in opposition.

Chairman Belter: Are there any questions? Any other testimony to 1179? Any neutral testimony to 1179? Are there any questions of Lynn Helms?

Lynn Helms, Director of the Department of Mineral Resources: The industrial commission hasn't take a stand on this bill but you're dealing with one of the more complicated issues incorporated in oil and gas taxes so a little information may be appropriate. Stripper wells and stripper well properties were designed to help the 80 pound weakling in the oil patch which are the oil wells that produce 20% of the United States' production and were at one time a very significant part of oil and gas production in North Dakota. The design is that it still requires one full time job to keep a stripper well operating so you maintain jobs and gross production tax revenue for the county by incentivizing stripper wells. The stripper well property concept is designed to encourage people to work over those wells, to water flood around those wells to re-drill those wells and that's something that's been done successfully in formations like the Spearfish, Tyler, Mission Canyon, Red River, etc. We have about 2,800 stripper wells operating in the state and that's out of 8,100 total wells. About 500 of those wells are stripper well properties. Stripper well or stripper well property is a lifetime exemption from the oil extraction tax that is pool specific. It doesn't exempt the land around that well in all formations for all time. It's for the pool that well is producing from, it might be Madison, Bakken, Red River, etc. It's designed to encourage someone who has a poor performing well to do some work on that well. In most cases a stripper well property is totally uneconomic to re-drill, it would cost 5-6 times as much as a re-entry of that stripper well bore to increase the production. It rewards people for taking that extreme risk when you already know that you have an 80 pound weakling on your hands. This bill doesn't take into account the ability to differentiate between the 80 pound weakling and the 800 pound gorilla and that is the Bakken and Three Forks. The Bakken and Three Forks are drilled on 1280 acre spacing units so the entire spacing unit for all their layers qualifies as a stripper well property. In much of the Bakken and Three Forks area you are going to infield drill with three to seventeen additional wells, all of them will come in at or greater than the initial production of the first well. Stripper well properties are designed to take the spacing unit over the water flood unit that surrounds a very weak marginal well and give it preferential tax treatment to encourage investment in very expensive and risky processes like re-drills, work overs and water floods. It has been successfully implemented in all these formations that lie outside the Bakken and Three Forks core area but the problem is that it doesn't apply well to an unconventional resource where you can move over 660 feet and drill a brand new 1000 barrel a day well. The average North Dakota well makes 90 barrels of oil a day, not a lot and there are a lot of wells out there not making much oil. That means that these 2800 stripper wells are like 10-11 barrel a day wells; they are marginal producers. They are being contrasted with these high rate and high decline Bakken and Three Forks wells. A thoughtful policy would differentiate between the 80 pound weakling and the 800 pound gorilla and treat them differently.

Vice Chairman Headland: I'm not suggesting that any oil company would do this but would it be possible to go into a Bakken or Three Forks pool or 1280 spacing and manipulate a well to be a stripper well then allowing the rest of your development on that 1280 spacing to produce the 800 pound gorilla?

Lynn Helms, Director of the Department of Mineral Resources: I'm not going to say it would be impossible but it would be extremely difficult. To qualify for stripper well property status you have to produce the well for twelve consecutive months at maximum efficient rate. We have a petroleum engineer review every one of these applications to make sure the well was operating for almost every day of the month. We sometimes allow a well to be down one to three days if we know there was a work over or something going on but we wouldn't allow a well to be shut in. The inspectors also review if they have artificial lift on the well, if they took the artificial lift off, did they shut the pumping unit down, or do something to manipulate that production. Since it's a lifetime exemption you have to have twelve consecutive months at maximum efficient rate below the qualification number in order to qualify and we are really careful with these.

Representative Froseth: It is your agency to determine whether it is a stripper status or not?

Lynn Helms, Director of the Development of Mineral Resources: Yes it is. It is our statutory responsibility in how you achieve stripper well or stripper well property status.

Representative Klein: You used the term lift. Would you explain what that refers too?

Lynn Helms, Director of the Development of Mineral Resources: Most of the wells come in naturally flowing when they are brand new. At some point the flow rate at what the well will produce at is below economic levels or significant profit could be made by putting one of those donkey heads on it, a pumping unit, or a gas lift, or an electric submersible pump, or something like that in the well then that's called artificial lift. It's a 100 year old technology. We check that very carefully to make sure that well if it has artificial lift on it during that qualification period that it does have artificial lift on it and they didn't just shut it down for that time to qualify the well and then start it back up again.

Representative Trottier: In trying to keep the state budget safe in the next biennium, we hear there could be a bubble that could be burst if oil prices go down; we also hear that in agriculture. We need to be careful and watch our budget for the next biennium than probably we ever have before. Where does the oil industry fit into that?

Lynn Helms, Director of the Development of Mineral Resources: I would agree. We are at a stage where we need to make a decision whether we're going to follow in Texas' or Alaska's footsteps. Alaska became overly dependent on oil tax revenue and still is and they're in a situation now where their equivalent of a legacy fund is not sustainable beyond 2020 and they are trying to figure out how to get out of that box. Texas has maintained a fairly low oil tax with incentives similar to what we have but they don't have the tax trigger which is really a huge risk. That doubles down as a price drop for the state, not only does the price drop but it brings about less drilling and less production then it brings a lower tax rate. That is probably the biggest variable that we need to deal with. The fact that we're going to drill 8000 Bakken and Three Forks spacing units and somewhere in the eight to ten year range of their life they would qualify under current law as stripper well properties means that in eight to ten years from now we start to see all Bakken and Three Forks drilling exempt from the oil extraction tax. That presents a serious risk to long term oil tax revenues. Those seem to be the biggest issues that need to be tackled and dealt with this session.

Representative Drovdal: You mentioned Texas and Alaska with North Dakota being right in the middle of it, one of the things about Alaska is that most of the land is owned by the federal government and most drilling up there is on private land. I'm not familiar with Texas. Is that the same case in Texas or is that land mostly private?

Lynn Helms, Director of the Development of Mineral Resources: Texas is even more private than North Dakota. We have about 90% private and state land, Texas is in excess of 95%. Alaska is about 90% federal. The production in Alaska is coming off state lands. The problem with Alaska's tax rate is they raised it up to about 25% so they have incentives for exploring for oil and no incentives for producing it. Texas is at 4 ½% or 5% and we have to find that sweet spot somewhere in between. Texas is more like North Dakota than Alaska is. This bill doesn't make those differentiations between the formations and wells that I consider 80 pound weaklings and the new guy.

Representative Drovdal: You say North Dakota is 90% private but in the oil area in western North Dakota that percentage between public and private land is considerably different isn't it?

Lynn Helms, Director of the Development of Mineral Resources: It certainly is. When you move into the 17 oil and gas producing counties that federal ownership jumps to about 27% so it almost triples and so it's about 10% statewide and about 27% in the oil and gas producing counties.

Representative Kelsh: Can you give me a quick break down on how much of the drilling in Texas is shale versus off shore and how that compares to North Dakota?

Lynn Helms, Director of the Development of Mineral Resources: These are going to be very rough numbers. There are currently about 800 rigs running in Texas, 230 of those are in the Eagle Ford shale play and there are 500 rigs running in the Permian but about half of them are doing shale. Roughly 500 of the 800 are doing shale plays, 300 are doing conventional gas, oil plays, and enhanced oil recovery. By contrast in North Dakota 187 rigs this morning, 95% shale, and 5% non-shale.

Chairman Belter: Any other questions? Any of neutral testimony on 1179? If not I will close the hearing on HB 1179.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1179
February 5, 2013
Job #18338

☐ Conference Committee

Committee Clerk Signature Mary Brucker

Explanation or reason for introduction of bill/resolution:

A Bill relating to the oil extraction tax exemption for stripper wells.

Minutes:

Attached amendments #1 and 2

Chairman Belter: Representative Drovdal do you have amendments?

Representative Drovdal: Distributed amendments. See attached #1.

Chairman Belter: You increased the barrels from 30 to 50?

Representative Drovdal: From 35 to 50 to qualify. If they produce less than 50 barrels a day for a year they would qualify as a stripper well. I increased that because of the cost of maintaining these wells and continuing to flow is a lot higher than the vertical so I figured they needed a little higher level to qualify.

Chairman Belter: That language would apply to new stripper wells?

Representative Drovdal: Correct, new stripper wells. That grandfathers in the old ones. I have the exact same amendment that does not grandfather in the amendments if the committee decided they would rather go that way. The one I passed out grandfathers the current wells out there. I found out that currently there are 70 wells in the Bakken and Three Forks fields that are getting the exemption and they are averaging 125 barrels a day. The fiscal note that came along with it is projecting that trend will continue and by the end of the next biennium there will be 210 wells in that same production area and that's where the $105 million comes from. In the Petroleum News dated February 3, 2013 from Hess Corporation said their cost is down 30 percent and it was Mr. Ness who said their costs went up when he was opposing this. It went from $13.4 million to $9 million for a cost of a well right now but to maintain it takes a lot of work on the rigs which is why I raised that barrel.

Representative Marie Strinden: You said that the existing stripper wells would be exempt so does that mean they would be exempt along with the existing stripper well property too?

Representative Drovdal: Since they are already drilled it is water under the bridge and I thought we would just leave them the way they are. They would have bumped from 5 to 11 ½%.

Representative Marie Strinden: That entire property would be exempt it is just the new ones going forward?

Representative Drovdal: Correct. This would only apply to new wells from now on.

Representative Froseth: Distributed amendments #2 and explained. See attached amendments. Presently the tribes get 20% of the 5% taxes being charged on those wells and if we remove this exemption they will get 50% of the extraction tax so they will actually get 70% tribal and then 50% of that would go to the state. It will be a benefit to the tribe. There's no reason they should get a 60 month exemption on those non-tribal wells. They have about 100% production on those wells so there's no reason to have an incentive to drill wells on those non-tribal lands anymore.

Representative Zaiser: Could you repeat those percentages?

Representative Froseth: Those wells are subject to the 5% production tax for five years and the tribe gets 20% of that 5% and the rest goes to the state. This way with repealing that exemption of 6 ½% there will be the full 11 ½% charged on tax to those wells. In the tribal pact the tribe gets 50% and the state gets 50 percent. The tribe will end up getting more money now on those wells as well as the state.

Representative Klein: That's only on non-tribal land now?

Representative Froseth: Yes. This is on private land within the reservation boundaries.

Representative Marie Strinden: Do we still need incentives for these companies to drill oil?

Representative Froseth: The success ratio for these wells is 100% so incentives aren't necessary for five years.

Representative Drovdal: When we put those exemptions into place there hadn't been a well drilled on a reservation for over 20 years.

Vice Chairman Headland: It will increase the tax to the mineral owner though, correct?

Representative Froseth: Yes it will and it will increase the revenue to the state.

Chairman Belter: What are the committee's wishes?

Representative Froseth: Made a motion to move his amendments 1003.

Representative Zaiser: Seconded.

Voice vote: MOTION CARRIED.

Representative Drovdal: Made a motion to move the 1002 amendments.

Representative Klein: Seconded.

VOICE VOTE: MOTION CARRIED.

Chairman Belter: What are the committee's wishes on HB 1179?

Representative Klein: Made a motion for a DO PASS AS AMENDED.

Representative Drovdal: Seconded.

Vice Chairman Headland: I think we'll have to have a new fiscal note with the addition of the fee lands and the 50% of that 6 ½% coming to the state so I'm assuming the fiscal note is going up.

Representative Froseth: This won't affect the wells that have that exemption now and it will remain in effect until that exemption has expired and so it would be for new wells drilled from now on. It's just an estimate of how many wells might be drilled in the next two years on those properties.

Chairman Belter: I think this needs to go to appropriations. We have a motion for a Do Pass as Amended and rerefer to appropriations.

Vice Chairman Headland: We have these other bills sitting out there that have eluded to what is being done on this bill and I'm not sure I can vote for this bill the way it is because it's a huge tax increase unless we are going to make it part of a bigger package where we end up reducing revenues so I'm going to resist this bill.

Representative Drovdal: It is definitely a plus and I'm not proud of that either but the important thing is that we need to have this definition changed at the end of legislation and if we push this forward they are going to be melted in to one bill. I think it is important that we continue this until we see what happens with the other bill because there is a lot of resistance on that.

Representative Froseth: I have the same amendment drafted for another bill for tax reduction on oil wells. I believe Senator Cook's bill also has that provision in his bill. If not I intend to amend it in there so it's in every bill we see.

Representative Owens: You stated you believed the exemption was for any new wells not any current wells, was that your intent?

Representative Froseth: Yes, it would become effective June 30, 2013 so any wells drilled before this would come under the old regulation.

Representative Owens: On page 1 line 4 I don't see where it says for new wells anywhere or is that just based on the date?

Representative Froseth: It would take affect for any activity after June 30, 2013.

ROLL CALL VOTE: 11 YES 3 NO 0 ABSENT
MOTION CARRIED FOR DO PASS AS AMENDED AND REREFER TO APPROPRIATIONS.

Representative Drovdal will carry this bill.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1179
February 12, 2013
Job #18766

☐ Conference Committee

Committee Clerk Signature	Mary Brucker

Explanation or reason for introduction of bill/resolution:

A Bill relating to the oil extraction tax exemption for stripper wells.

Minutes:

Chairman Belter: I would like a motion to reconsider our action where we did a Do Pass.

Representative Froseth: Made a motion to reconsider.

Representative Dockter: Seconded.

Representative Froseth: This is the bill that I have an amendment drafted that will remove the six month exemption on the extraction taxes on non-tribal lands on the reservation. There is a bill in the Senate that is being worked on right now and they would not like to have that amendment attached to any other bill and for that reason I made the motion to reconsider our action where we approved this amendment and did a Do Pass.

VOICE VOTE: MOTION CARRIED.

Chairman Belter: We have the bill before us now.

Representative Froseth: Made a motion to reconsider our action to strip the amendment 1003.

Representative Owens: Seconded.

VOICE VOTE: MOTION CARRIED.

Representative Drovdal: The bill now sits with redefining stripper wells to the individual in the Bakken and Three Forks formation leaving the other definitions as they are. It will also increase the bill requirement from the 35-50 and that is still on the bill.

Representative Drovdal: Made a motion for a DO PASS AS AMENDED.

Representative Klein: Seconded.

ROLL CALL VOTE TAKEN: 13 YES 0 NO 1 ABSENT
MOTION CARRIED.

Representative Drovdal will carry this bill.

FISCAL NOTE
Requested by Legislative Council
01/11/2013

Bill/Resolution No.: HB 1179

1 A. **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.*

	2011-2013 Biennium		2013-2015 Biennium		2015-2017 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues				$105,300,000		
Expenditures						
Appropriations						

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

	2011-2013 Biennium	2013-2015 Biennium	2015-2017 Biennium
Counties			
Cities			
School Districts			
Townships			

2 A. **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 1179 eliminates stripper well properties for purposes of the existing oil extraction tax exemption for stripper wells.

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.*

The provisions of HB 1179 require each well to be qualified as a stripper well based on each well's production levels, closing off the ability for an entire property to be deemed a stripper property on the basis of production from older, original wells.

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.*

If enacted, it is estimated that HB 1179 will prevent at least 75 stripper properties from being designated, thereby preventing the oil extraction tax exemption for strippers from applying to an estimated 225 high-producing wells. This will result in an estimated increase in oil extraction tax revenue of $105.3 million in the 2013-15 biennium, and potentially much more in subsequent biennia. This increase in oil extraction tax revenue will increase distributions to the legacy, resources trust, strategic investment and improvements and education trust funds.

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

Telephone: 328-3402

Date Prepared: 01/19/2013

13.0329.01004
Title.02000

Adopted by the Finance and Taxation Committee
February 5, 2013

YR
2/6/13
1 of 2

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1179

Page 1, line 1, after "Act" insert "to create and enact a new subsection to section 57-51.1-01 of the North Dakota Century Code, relating to definition of stripper well in the Bakken and Three Forks formations;"

Page 1, line 4, after "for" insert "stripper well properties and"

Page 1, line 4, after the semicolon insert "to repeal subsection 8 of section 57-51.1-03 of the North Dakota Century Code, relating to the oil extraction tax exemption for wells within an Indian reservation;"

Page 1, line 13, remove the overstrike over "~~well properties~~" and insert immediately thereafter "or individual stripper"

Page 1, line 23, remove the overstrike over "~~well property~~" and insert immediately thereafter "or individual stripper"

Page 2, after line 3, insert:

"**SECTION 3.** A new subsection to section 57-51.1-01 of the North Dakota Century Code is created and enacted as follows:

"Stripper well" means a well inside the Bakken or Three Forks formations for which the 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 fifty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] during any preceding consecutive twelve-month period. "Stripper well" also includes a well inside the Bakken or Three Forks formations which was drilled and completed before July 1, 2013, and was considered part of a stripper well property for purposes of this chapter on June 30, 2013."

Page 2, line 6, remove the overstrike over the first "~~property~~"

Page 2, line 6, remove the overstrike over the second "~~property~~"

Page 2, line 6, remove "well"

Page 2, line 6, overstrike "whose" and insert immediately thereafter "outside the Bakken and Three Forks formations for which the"

Page 2, line 7, remove the overstrike over "~~per well~~"

Page 2, line 18, remove the overstrike over "~~property~~" and insert immediately thereafter "or stripper well"

Page 2, line 22, remove the overstrike over "~~property~~" and insert immediately thereafter "or individual stripper well"

Page 2, line 24, remove the overstrike over "~~well property's~~" and insert immediately thereafter "<u>or individual stripper</u>"

Page 2, after line 24, insert:

"**SECTION 7. REPEAL.** Subsection 8 of section 57-51.1-03 of the North Dakota Century Code is repealed."

Renumber accordingly

Date: 2-5-13
Roll Call Vote #: 1

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment Froseth 1003

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep Froseth Seconded By Rep. Zaiser

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter			Rep. Scot Kelsh		
Vice Chairman Craig Headland			Rep. Steve Zaiser		
Rep. Matthew Klein			Rep. Jessica Haak		
Rep. David Drovdal			Rep. Marie Strinden		
Rep. Glen Froseth					
Rep. Mark Owens					
Rep. Patrick Hatlestad					
Rep. Wayne Trottier					
Rep. Jason Dockter					
Rep. Jim Schmidt					

Total (Yes) ______ No ______

Absent ______

Floor Assignment ______

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

Voice Vote

Motion Carried.

Date: 2-5-13
Roll Call Vote #: 2

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment 1002

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Drovdal Seconded By Rep. Klein

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter			Rep. Scot Kelsh		
Vice Chairman Craig Headland			Rep. Steve Zaiser		
Rep. Matthew Klein			Rep. Jessica Haak		
Rep. David Drovdal			Rep. Marie Strinden		
Rep. Glen Froseth					
Rep. Mark Owens					
Rep. Patrick Hatlestad					
Rep. Wayne Trottier					
Rep. Jason Dockter					
Rep. Jim Schmidt					

VOICE VOTE. MOTION CARRIED.

Total (Yes) No

Absent

Floor Assignment

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

1 Nay

MOTION CARRIES

Date: 2-5-13
Roll Call Vote #: 3

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

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. Klein Seconded By Rep. Drovdal

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter	√		Rep. Scot Kelsh	√	
Vice Chairman Craig Headland		√	Rep. Steve Zaiser	√	
Rep. Matthew Klein	√		Rep. Jessica Haak	√	
Rep. David Drovdal	√		Rep. Marie Strinden	√	
Rep. Glen Froseth	√				
Rep. Mark Owens		√			
Rep. Patrick Hatlestad	√				
Rep. Wayne Trottier	√				
Rep. Jason Dockter	√				
Rep. Jim Schmidt		√			

Total (Yes) 11 No 3

Absent Ø

Floor Assignment Rep. Drovdal

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

Date: 2-12-13
Roll Call Vote #: 1

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

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. Froseth Seconded By Rep. Dockter

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter			Rep. Scot Kelsh		
Vice Chairman Craig Headland			Rep. Steve Zaiser		
Rep. Matthew Klein			Rep. Jessica Haak		
Rep. David Drovdal			Rep. Marie Strinden		
Rep. Glen Froseth					
Rep. Mark Owens					
Rep. Patrick Hatlestad					
Rep. Wayne Trottier					
Rep. Jason Dockter					
Rep. Jim Schmidt					

Total (Yes) ____________ No ____________

Absent ____________

Floor Assignment ____________

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

Voice Vote
Motion Carried.

Date: 2-12-13
Roll Call Vote #: 2

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number ______

Action Taken: ~~☒ Do Pass~~ ☐ Do Not Pass ~~☒ Amended~~ ☐ Adopt Amendment 01003 - REMOVE amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Froseth Seconded By Rep Owens

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter			Rep. Scot Kelsh		
Vice Chairman Craig Headland			Rep. Steve Zaiser		
Rep. Matthew Klein			Rep. Jessica Haak		
Rep. David Drovdal			Rep. Marie Strinden		
Rep. Glen Froseth					
Rep. Mark Owens					
Rep. Patrick Hatlestad					
Rep. Wayne Trottier					
Rep. Jason Dockter					
Rep. Jim Schmidt					

Total (Yes) ______ No ______

Absent ______

Floor Assignment ______

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

Voice Vote
Motion carried

Date: 2-12-13
Roll Call Vote #: 3

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1179

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. Drovdal Seconded By Rep. Klein

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter	✓		Rep. Scot Kelsh	✓	
Vice Chairman Craig Headland	✓		Rep. Steve Zaiser	—	
Rep. Matthew Klein	✓		Rep. Jessica Haak	✓	
Rep. David Drovdal	✓		Rep. Marie Strinden	✓	
Rep. Glen Froseth	✓				
Rep. Mark Owens	✓				
Rep. Patrick Hatlestad	✓				
Rep. Wayne Trottier	✓				
Rep. Jason Dockter	✓				
Rep. Jim Schmidt	✓				

Total (Yes) 13 No 0

Absent 1

Floor Assignment Rep. Drovdal

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

REPORT OF STANDING COMMITTEE

HB 1179: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** and **BE REREFERRED** to the **Appropriations Committee** (11 YEAS, 3 NAYS, 0 ABSENT AND NOT VOTING). HB 1179 was placed on the Sixth order on the calendar.

Page 1, line 1, after "Act" insert "to create and enact a new subsection to section 57-51.1-01 of the North Dakota Century Code, relating to definition of stripper well in the Bakken and Three Forks formations;"

Page 1, line 4, after "for" insert "stripper well properties and"

Page 1, line 4, after the semicolon insert "to repeal subsection 8 of section 57-51.1-03 of the North Dakota Century Code, relating to the oil extraction tax exemption for wells within an Indian reservation;"

Page 1, line 13, remove the overstrike over "~~well properties~~" and insert immediately thereafter "or individual stripper"

Page 1, line 23, remove the overstrike over "~~well property~~" and insert immediately thereafter "or individual stripper"

Page 2, after line 3, insert:

"**SECTION 3.** A new subsection to section 57-51.1-01 of the North Dakota Century Code is created and enacted as follows:

"Stripper well" means a well inside the Bakken or Three Forks formations for which the 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 fifty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] during any preceding consecutive twelve-month period. "Stripper well" also includes a well inside the Bakken or Three Forks formations which was drilled and completed before July 1, 2013, and was considered part of a stripper well property for purposes of this chapter on June 30, 2013."

Page 2, line 6, remove the overstrike over the first "~~property~~"

Page 2, line 6, remove the overstrike over the second "~~property~~"

Page 2, line 6, remove "well"

Page 2, line 6, overstrike "whose" and insert immediately thereafter "outside the Bakken and Three Forks formations for which the"

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Page 2, line 18, remove the overstrike over "~~property~~" and insert immediately thereafter "or stripper well"

Page 2, line 22, remove the overstrike over "~~property~~" and insert immediately thereafter "or individual stripper well"

Page 2, line 24, remove the overstrike over "~~well property's~~" and insert immediately thereafter "or individual stripper"

Page 2, after line 24, insert:

"**SECTION 7. REPEAL.** Subsection 8 of section 57-51.1-03 of the North Dakota Century Code is repealed."

Renumber accordingly

REPORT OF STANDING COMMITTEE

HB 1179: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **DO PASS** (13 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING). HB 1179 was placed on the Eleventh order on the calendar.

2013 TESTIMONY

HB 1179

NORTH DAKOTA PETROLEUM COUNCIL

120 N. 3rd Street • Suite 200 • P.O. Box 1395 • Bismarck, ND 58502-1395
Phone: 701-223-6380 • Fax: 701-222-0006 • Email: ndpc@ndoil.org

House Bill 1179

House Finance and Tax Committee

January 21, 2013

Chairman Belter and members of the Committee, my name is Ron Ness. I am President of the North Dakota Petroleum Council. The Petroleum Council represents more than 400 companies involved in all aspects of the oil and gas industry including oil and gas production, refining, pipeline, transportation, mineral leasing, consulting, legal work, and oil field service activities in North Dakota. Our members produced 98% of the more than 200 million barrels of oil produced in North Dakota last year. I appear before you today in opposition to House Bill 1179.

The budget projection for 2013 – 2015 biennium indicates that the oil and gas industry will pay more than five billion in oil and gas production taxes. I believe **HB 1179 is the only tax increase bill I've seen this session other than a couple of fee or fine increases.** Over the past nine years the oil industry and royalty owners have seen their composite tax rate increase every year since the price based tax incentives triggered off in October of 2004. HB 1179 would once again result in an increase the overall composite tax rate. How much should one industry pay?

Stripper properties, or marginal wells, are the foundation of the domestic oil industry. Marginal or low producing oil wells represent 20% of our nation's domestic oil production. Oil industry investment is always driven by price and economics and keeping a favorable tax rate to encourage re-investment in a 2nd well after the first has not worked is good policy. The wells we are referring to in this bill typically include marginal Bakken and Three Forks wells that weren't necessarily productive or economic the first time and now with new technology might be much more productive with a second well in that field but the operator and investors might have $20 million into those two wells. I'm not sure we want to discourage that risk taker. In addition, this bill also includes other oil producing formations which are not as prolific as the Bakken or Three Forks and the operators project might be based on having a lower fixed tax rate for additional wells.

History on Stripper Wells in North Dakota:

"Stripper wells" were exempted from the oil extraction tax under Section 3 of Initiated Measure No. 6 which was passed by the voters of North Dakota in November, 1980. In 1981, the legislature approved HB 1651 which added the concept of a "stripper well property." HB 1651 was introduced by Majority Leader Strinden, approved by the delayed bills committee, and had an effective date of January 1, 1981, which was the also effective date of Measure No. 6. So stripper properties have always been exempt from the gross production tax.

"Stripper well properties" were a concept under the federal Emergency Petroleum Act of 1973 which, in response to the Arab oil embargo, attempted to freeze buyer/seller relationships as they existed in 1972. That's the reason for the reference in the stripper property definition to any 12-month period following December 31, 1972. Stripper oil was basically decontrolled under the EPAA. The so-called Gypsy Rose Lee Rule ("once a stripper always a stripper") was incorporated from the Federal price control rules. Decontrolled prices, like reduced taxes, were intended to provide an incentive to development as well as to prevent premature abandonment, and that was accomplished by maintaining stripper property status for new wells on stripper properties.

The industry does support a comprehensive revision of the state's overall oil tax structure which would include changes in the stripper property provisions to acknowledge new technologies in the Bakken and Three Forks formations as long as it's balanced with other changes that provide certainty to the industry and investors. The oil and gas industry is paying more than its fair-share in taxes to North Dakota. This bill represents a tax increase. We urge a Do Not Pass on HB 1179. I would be happy to answer any questions.

9

Greater North Dakota Chamber

Testimony of Bill Shalhoob
Greater North Dakota Chamber of Commerce
HB 1179
January 21, 2013

Mr. Chairman and members of the committee, My name is Bill Shalhoob and I am here today representing the Greater North Dakota Chamber of Commerce, the champions for business in North Dakota. GNDC is working to build the strongest business environment possible through its more than 1,100 business members as well as partnerships and coalitions with local chambers of commerce from across the state. GNDC also represents the National Association of Manufacturers and works closely with the U.S. Chamber of Commerce. As a group we stand in opposition to HB 1182 and urge a do not pass from your committee on the bill.

GNDC has been among the principle advocates for fair and balanced taxation at a level that supports the needs of the state but returns all excess revenues to the tax payers of North Dakota. We support an oil tax structure that is competitive with other major producing states. As the Bakken formation transitions from exploration to development, North Dakota will once again compete for investment with emerging shale plays in other states. The state's oil tax structure may have to be adjusted to acknowledge technological advancements that impact stripper well properties, while still encouraging exploration outside of the core Bakken and Three Forks areas to ensure oil production in other formations.

Given our current reliance on oil taxes we cannot support an increase and an even greater dependence on them. The stripper well exemption dates back to 1981 and was put into place and kept for a good policy reason, to encourage production from wells whose production would make them operate at a loss or at best be marginally profitable without the exemption. That reason is still valid today. Let's be careful in eliminating exemptions and credits. We would support a study or legislation that will look at the our oil taxes now and in the future both from need and competitive sides and tried to develop a long term plan for oil taxes as they relate to income, property and sales taxes in our future. At some point as they increase exponentially, we meet our infrastructure needs and shale plays become more competitive we may have to consider adjusting the tax.

Thank you for the opportunity to appear before you today in opposition to HB 1179. I would be happy to answer any questions.

Champions for Business

PO Box 2639 P: 701-222-0929
Bismarck, ND 58502 F: 701-222-1611

www.ndchamber.com

13.0329.01002
Title.

Prepared by the Legislative Council staff for
Representative Drovdal
January 22, 2013

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1179

Page 1, line 1, after "Act" insert "to create and enact a new subsection to section 57-51.1-01 of the North Dakota Century Code, relating to definition of stripper well in the Bakken and Three Forks formations;"

Page 1, line 4, after "for" insert "stripper well properties and"

Page 1, line 13, remove the overstrike over "~~well properties~~"

Page 1, line 13, after "~~properties~~" insert "or individual stripper"

Page 1, line 23, remove the overstrike over "~~well property~~"

Page 1, line 23, after "~~property~~" insert "or individual stripper"

Page 2, after line 3, insert:

"**SECTION 3.** A new subsection to section 57-51.1-01 of the North Dakota Century Code is created and enacted as follows:

"Stripper well" means a well inside the Bakken or Three Forks formations 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 fifty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] during any preceding consecutive twelve-month period. "Stripper well" also includes a well inside the Bakken or Three Forks formations which was drilled and completed before July 1, 2013, and was considered part of a stripper well property for purposes of this chapter on June 30, 2013."

Page 2, line 6, remove the overstrike over "~~property~~"

Page 2, line 6, remove the overstrike over "~~property~~"

Page 2, line 6, remove the second "well"

Page 2, line 6, after ""~~property~~well"" insert "outside the Bakken and Three Forks formations"

Page 2, line 7, remove the overstrike over "~~per well~~"

Page 2, line 18, remove the overstrike over "~~-property~~"

Page 2, line 18, after "property" insert "or stripper well"

Page 2, line 22, remove the overstrike over "~~property~~"

Page 2, line 22, after "property" insert "or individual stripper well"

Page 2, line 24, remove the overstrike over "~~well property's~~"

Page 2, line 24, after "property's" insert "or individual stripper"

13.0329.01003
Title.

Prepared by the Legislative Council staff for
Representative Froseth
January 24, 2013

#*
9

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1179

Page 1, line 4, after the semicolon insert "to repeal subsection 8 of section 57-51.1-03 of the North Dakota Century Code, relating to the oil extraction tax exemption for wells within an Indian reservation;"

Page 2, after line 24, insert:

"**SECTION 6. REPEAL.** Subsection 8 of section 57-51.1-03 of the North Dakota Century Code is repealed."

Renumber accordingly