1999 SENATE FINANCE AND TAXATION

SB 2332

1999 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. 2332

Senate Finance and Taxation Committee

❑ Conference Committee

Hearing Date 01//25/99/

Tape Number	Side A	Side B	Meter #
2,332	X		4599-END
2,332		X	0-1011
Committee Clerk Signature	Sheila Ward		

Minutes:

Sen. Urlacher opened the hearing on 2332, A bill relating to allocation of oil and gas gross production tax revenue, and provide and effective date.

Sen. O'Connell - This is to change the formula, the counties could get a little bit more money under this bill. 250 well shut down at this time, and affects rural electricity, the rates will have to go up to the rest of the consumers.

Sen. Wardner- The money going to the oil impact fund, that is also taken out ?

Sen. O'Connell - I believe we have that capped at $5 million dollars.

Sen Wardner - The 21/2 % is going to the counties, the fiscal note shows they would get a plus 348,000 dollars. that would make up for impact money. The counties need to know that so they don't feel they are getting cheated on it.

Lowell Ridgeway-ND Petroleum Council - I am in support of this bill. Other issues will be addressed, such as sales tax relief, on oil equipment, there has been discussion on electric rate relief, reduction like that. The counties have to help in these depressed time also. If nothing is done, a lot of marginal production would be shut in. Well shut in, production is the obvious thing and drilling will come to a halt.

Ron Block - County Commissioner - Bottineau county had 46% of its oil production from oil stripper wells. Half of its production comes from stripper wells. We provide services to these oil well sites. 5% is interracial part of taxes in the county. 57% drop in oil collections and still provide the services for the wells.

Vicky Steiner- ND Assoc. of Oil L& Gas Producing Counties. Testimony submitted.

Sen. Urlacher - Any questions, or more testimony? With that we will close the hearing.

DISCUSSION 2-10-99. TAPE # 1 B, 735 - 735 - 1100, MOTION MADE BY SEN WARDNER TO DO NOT PASS AND SECONDED BY SEN. CHRISTMANN. VOTE WAS 6 Y 1 N 0 ABSENT OR NOT VOTING. CARRIER OF THE BILL WILL SEN. CHRISTMANN.

FISCAL NOTE

(Return original and 14 copies)

l/Resolution No.: SB 2332 | Amendment to: ____________

Requested by Legislative Council | Date of Request: 1/18/99

1. Please estimate the fiscal impact (in dollar amounts) of the above measure for state general or special funds, counties, cities, and school districts. Please provide breakdowns, if appropriate, showing salaries and wages, operating expenses, equipment, or other details to assist in the budget process. In a word processing format, add lines or space as needed or attach a supplemental sheet to adequately address the fiscal impact of the measure.

   Narrative: If enacted, SB 2332 is expected to decrease state general fund revenues by \$2.7 million and the impact grant fund revenues by \$361,000 during the 1999-2001 biennium. Overall, county revenues would increase by approximately \$348,000. However, there would be shifts among counties with some counties gaining and some losing revenues. (Note: There may be a constitutional problem with the provision to tax federal and American Indian royalties.)

2. **State** fiscal effect in dollar amounts:

	1997-99 Biennium		**1999-2001 Biennium**		**2001-03 Biennium**	
	General Fund	**Other Funds**	**General Fund**	**Other Funds**	**General Fund**	**Other Funds**
Revenues			-\$2.7 million	-\$361,000		
Expenditures						

3. What, if any, is the effect of this measure on the budget for your agency or department:
   a. For rest of 1997-99 biennium: ____________
   (Indicate the portion of this amount included in the 1999-2001 executive budget:)
   b. For the 1999-2001 biennium: \$112,400 for administrative costs
   (Indicate the portion of this amount included in the 1999-2001 executive budget:)
   c. For the 2001-03 biennium: \$62,400

4. **County, city, and school district** fiscal effect in dollar amounts:

1997-99 Biennium			**1999-2001 Biennium**			**2001-03 Biennium**		
Counties	**Cities**	**School Districts**	**Counties**	**Cities**	**School Districts**	**Counties**	**Cities**	**School Districts**
			+\$348,000					

If additional space is needed attach a supplemental sheet.

Signed: Kathryn L. Strombeck

Typed Name: Kathryn L. Strombeck

Department: Tax

Phone Number: 328-3402

Date Prepared: January 22, 1999

Date: 2-10-99

Roll Call Vote #:

1999 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 2332

Senate Senate Finance and Taxation Committee

☐ Subcommittee on

or

☐ Conference Committee

Legislative Council Amendment Number

Action Taken Do Not Pass

Motion Made By Sen. Wardner Seconded By Christmann

Senators	Yes	No	Senators	Yes	No
SENATOR URLACHER	✓				
SENATOR CHRISTMANN	✓				
SENATOR SCHOBINGER	✓				
SENATOR STENEHJEM	✓				
SENATOR WARDNER	✓				
SENATOR KINNOIN		✓			
SENATOR KROEPLIN	✓				

Total (Yes) 6 No 1

Absent

Floor Assignment Sen. Christmann

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

REPORT OF STANDING COMMITTEE

SB 2332: Finance and Taxation Committee (Sen. Urlacher, Chairman) recommends **DO NOT PASS** (6 YEAS, 1 NAY, 0 ABSENT AND NOT VOTING). SB 2332 was placed on the Eleventh order on the calendar.

1999 TESTIMONY

SB 2332

North Dakota Association of Oil & Gas Producing Counties

Bill 2332

1/25/99

Mr. Chairman and Members of the Senate Finance and Taxation Committee. My name is Vicky Steiner. I represent the North Dakota Association of Oil and Gas Producing Counties. I've worked for them for 13 years. They have 133 members: 17 counties, 53 school districts, 63 cities. The members share with the state in the 5% oil and gas gross production tax.

I've included oil and gas tax information in our packet. I've also got the grand total generated by the extraction tax. There are the two oil taxes. The gross production tax originated in 1953. In 46 years, it has never been used for exemptions. We believe it should not be used. The 6½% oil extraction tax, since 1987, has had at least 12 exemptions placed on it and its effective rate today is about 3%. You have granted millions of dollars of tax relief to our oil industry. How did it end up with so many exemptions? It started with the first one. Just like this one.

This bill is flawed in concept. It says if your industry's price falls to this level, you don't pay any taxes in the stripper well fields. Someone else picks up the tab. Not all the counties have stripper well production. McHenry County has 88% of its production from stripper wells. Burke County has 72% and Slope County has no stripper wells. As guardians of the state general fund, you decide who gets out of a tax and who picks up the additional burden. This bill says that when sour crude oil sells for $4 a barrel, the state gives about 10 cents back to producers. That dime would be better spent changing the price per barrel. That's the real problem, not the 5% gross production tax.

If you decide that the $5 million dollar fiscal note to the general fund is worth the sacrifice, then use it to make a difference in state's future economy. It's a harder route but worth the effort. Use that money to hire a public relations firm to lobby President Clinton to create a new national oil policy.

If President Clinton would form a national oil policy that included a price support for small independent oil producers, we would create job stability for the state's small independent oil producers and service companies. The gross production tax should not be used for incentives for drilling or production. It's an integral part of our state and counties economies. Thank you.

VICKY STEINER - EXECUTIVE DIRECTOR
859 Senior Ave. ~ Dickinson, ND 58601-3755 ~ Phone: (701) 225-0884 ~ Fax: (701) 227-3040
E-mail: ndoilcos@dickinson.ctctel.com ~ Web: www.ND–oilcounties.org

Ray Gedeon - Permit Operator
409 East 21st Street ~ Williston, ND 58801 ~ Evenings: (701) 572-6808 ~ E-mail: rgedeon@host1.dia

OIL AND GAS TAXES

CURRENT LAW

OIL AND GAS GROSS PRODUCTION TAX

Imposition and Rates

The oil and gas gross production tax is imposed in lieu of property taxes on oil and gas producing properties.

Oil. A 5% rate is applied to the gross value at the well of all oil produced, except royalty interest in oil produced from a state, federal or municipal holding and from an American Indian holding within the boundary of a reservation. Both the producer and the purchaser of the oil are required to submit reports to the North Dakota Tax Department on a monthly basis. The reports show the volume and taxable value of the production from each well. The producer remits the tax on oil not sold at the well. The purchaser is primarily responsible for remitting the tax when the oil is bought during a production.

Gas. The gross production tax on gas is an annually adjusted flat rate per mcf of all nonexempt gas produced in the state. The annual adjustments are made according to the average producer price index for gas fuels. Rates through June 30, 1998 are as follows:

Time Period	Tax Rate
July 1, 1993 - June 30, 1994	$.0401
July 1, 1994 - June 30, 1995	$.0415
July 1, 1995 - June 30, 1996	$.0385
July 1, 1996 - June 30, 1997	$.0345
July 1, 1997 - June 30, 1998	$.0467

Exempt from the tax is gas used on the lease for production purposes and the royalty interest in gas produced from a state, federal or municipal holding and from an American Indian holding within the boundary of a reservation.

Monthly reports to the North Dakota Tax Department are required from both the producer and the purchaser/processor of the gas. The reports show the volume produced from each well. The producer remits the tax on unprocessed gas and the purchaser/processor remits the tax on processed gas.

Distribution of Revenue

Revenue from the gross production tax is distributed under the following formula:

- One-fifth is deposited with the State Treasurer. Of this portion, 33 1/3% is allocated to the Oil and Gas Impact Grant Fund, up to a maximum of $5 million per biennium. The remainder of this portion is credited to the State General Fund.

- Four-fifths is allocated between the State General Fund and the producing county according to the following formula:

Revenue	County	State
Up to $1 million	75%	25%
$1 to $2 million	50%	50%
Over $2 million	25%	75%

However, the amount any one county can receive per fiscal year is limited according to population as follows:

Population	Maximum Distribution
Up to 3,000	$ 3.9 million
3,000 to 6,000	4.1 million
6,000 or more	4.6 million

Tax revenue distributed to a county is further split with 45% earmarked for the county general fund, 35% for the school districts within the county, and 20% to incorporated cities within the county.

Reference: North Dakota Century Code ch. 57-51.

OIL EXTRACTION TAX

Imposition and Rates

The oil extraction tax is levied on the extraction of oil from the earth. The tax rate is 6½% of the gross value at the well of crude oil. However, the rate is reduced to 4% for oil produced from the following:

- A vertical or horizontal new well, after the appropriate exemption expires.

- A well which received the workover exemption after June 30, 1993.

- Incremental oil from a qualifying secondary or tertiary recovery project, after the 5-year or 10-year exemption expires.

- Nonincremental oil from a qualifying secondary recovery project that has reached an average production level of at least 25% over normal operations for six consecutive months.

- Nonincremental oil from a qualifying tertiary recovery project that has reached a production level of at least 15% over normal operations for one month and continues to be operated as a qualifying project.

A qualifying *secondary recovery project* is a unit that uses water flooding and is certified by the North Dakota Industrial Commission. A qualifying *tertiary recovery project* is a unit that uses an enhanced recovery method which conforms with federal tax code provisions and is certified by the North Dakota Industrial Commission.

The oil extraction tax is paid monthly with the gross production tax on a combined reporting form.

Exemptions

To receive the full benefit of an exemption or the 4% reduced rate, a producer must file the Industrial Commission's certification of well status with the Tax Commissioner within 18 months of the first day of eligibility. If the producer does not file within the 18-month period, then the exemption or reduced rate begins the first day of the month in which the certification is received by the Commissioner. This requirement becomes effective on January 1, 1996.

The exemptions to the oil extraction tax are as follows:

- Royalty interest in oil extracted from a state, federal or municipal holding and from an American Indian holding within the boundary of a reservation.

- Oil extracted from a certified stripper well property. A stripper well property is property whose average daily production during a 12-month period did not exceed 10 barrels per day for a well of a depth of 6,000 feet or less, 15 barrels per day for a well of a depth of more than 6,000 feet but not more than 10,000 feet, and 30 barrels per day for a well of a depth of more than 10,000 feet.

- Oil produced during the first 15 months of production from either a vertical new well (drilled and completed after April 27, 1987) or a horizontal new well (drilled and completed after April 27, 1987 and before April 1, 1995). This exemption is subject to the "trigger" provisions described below.

- Oil produced during the first 24 months of production from a horizontal well drilled and completed after March 31, 1995. The exemption is subject to the "trigger" provisions described below.

- Oil produced during the first 60 months of production from either a vertical new well or a horizontal new well drilled and completed on tribal trust land after July 31, 1997.

- Oil produced from a horizontal reentry well for a period of 9 months beginning on the date the well is recompleted as a horizontal well. The exemption is subject to the "trigger provisions" described below.

- Oil produced from a two-year inactive well for a period of ten years beginning the first day of the month in which the Industrial Commission's certification is received by the Tax Commissioner. The exemption is subject to the "trigger provisions" described below.

- Oil produced from a qualifying well that has been worked over. The exemption is for a 12-month period starting with the first day of the third month after completion of the workover project. A qualifying well is a well that has produced less than 50 barrels per day during the last six months of continuous production before workover. The well operator must notify the Industrial Commission before beginning the project. Project cost must exceed $65,000 or production must increase 50% or more in the first two months after project completion. The exemption is subject to the "trigger" provisions described below.

- Incremental oil from a qualifying secondary or tertiary recovery project. The exemption is 5 years for secondary recovery projects and 10 years for tertiary recovery projects from the date the incremental production begins.

"Trigger" Provisions

The reduced rate provisions and/or exemptions for new wells, horizontal wells, horizontal reentry wells, two-year inactive wells, and workover wells are ineffective if the average price of a barrel of crude oil for any consecutive 5-month period is $33 or more. The reduced rate and the exemptions are reinstated if the average price falls below $33 a barrel.

Distribution of Revenue

Revenue from the oil extraction tax is distributed as follows:

- 60% to the State General Fund.
- 20% divided equally between the Common Schools Trust Fund and Foundation Aid Stabilization Fund.
- 20% to the Southwest Water Pipeline Sinking Fund and to a Resources Trust Fund. Principal and income from the Resources Trust Fund may be expended only pursuant to legislative appropriation and are available for water and certain energy related projects.

Reference: North Dakota Century Code ch. 57-51.1.

HISTORICAL OVERVIEW

OIL AND GAS GROSS PRODUCTION TAX

Significant Changes In Law

1953 Session. The legislature enacted the gross production tax at a rate of 4¼% of gross value at the well and created a revenue distribution formula.

1957 Session. The rate was increased from 4¼% to 5% and the revenue distribution formula was adjusted (see chart on page 55).

1981 Session. The legislature amended the revenue distribution formula (see chart on page 55).

1983 Session. The legislature required monthly rather than quarterly remittance, and raised the maximum distributions to the counties (see chart on page 55).

1985 Session. The legislature specified that oil reclaimed from tank bottoms and pit oil material has value for tax purposes only if a cash price is paid by the oil reclaimer.

1989 Session. The law was changed to specifically state that the gross production tax is a real property tax. The revenue distribution formula was amended, effective July 1, 1991, to allocate 33 1/3 % of the first one-fifth portion to the Oil and Gas Impact Grant Fund.

1991 Session. The tax on gas was changed from 5% of gross value to an annually adjusted flat rate per mcf. Procedures were provided for determining gross value at the well of oil under arm's length and non-arm's length contracts. The legislature approved administrative changes recommended by a special Taxpayer Bill of Rights project involving the private sector and the North Dakota Office of State Tax Commissioner, including a 10% per annum interest rate on refunds and reducing the assessment and refund period from six to three years.

1993 Session. The interest accrual period was changed on tax refunds for periods after June 30, 1993. Interest begins to accrue 60 days after the due date of the return, after the return was filed, or after the tax was fully paid, whichever occurs later. The legislature also specified that tax from undetermined sources will be allocated between the State General Fund and the county that received the least amount of revenue during the fiscal year.

1997 Session. The legislature has clarified that the periods for assessment or refund run from the later of the due date of the original return or the date the original return was filed. The legislature also specified that the North Dakota Office of State Tax Commissioner has two years after an amended return is filed to audit that return and assess any additional tax that is due. The legislature has provided the North Dakota Office of State Tax Commissioner the authority to require purchasers to file monthly reports by electronic data interchange or other form of electronic media and to waive the producer's requirement to file a monthly return. The legislature authorized the use of alternative methods for signing, subscribing, or verifying a return filed by electronic means, including telecommunications. A permanent oil tax trust fund was established for the deposit of oil extraction and gross production tax revenues which exceed specific amounts in a biennium.

OIL EXTRACTION TAX

Significant Changes in Law

1980 Initiated Measure. The 6½% oil extraction tax was created through an initiated measure passed by the voters in the 1980 General Election. The revenue distribution formula was: 45% to the State General Fund, 45% to schools, and 10% to the trust fund. The measure also included an individual income tax energy cost relief credit.

1981 Session. The legislature amended the distribution formula (see chart on page 55).

1983 Session. The distribution formula was changed (see chart on page 55). Filing requirements were changed from a quarterly to a monthly basis.

1987 Session. The legislature provided an exemption for the first 15 months of production from a new well (drilled and completed after April 27, 1987). The rate was reduced from 6½% to 4% for a new well after the 15-month exemption and for production from a qualifying secondary or tertiary recovery project well. These incentives would be eliminated if the average crude oil price is $33 or more per barrel. The legislature repealed the exemption for private royalty interest and expanded the stripper well definition to allow more marginal wells to qualify for an exemption.

1989 Session. The legislature provided a 12-month exemption for production from a qualifying well after completion of a workover project. This incentive is subject to the "trigger."

1991 Session. An exemption was created for incremental oil from a qualifying secondary or tertiary recovery project. A June 30, 1995 sunset was placed on certification of secondary projects. After the expiration of the exempt period, the incremental oil would be eligible for the 4% reduced rate. The reduced rate incentive is subject to the "trigger." The "trigger" was amended to reinstate the reduced rates and exemptions if the average crude oil price falls below $33 per barrel.

1993 Session. The workover exemption was amended to eliminate the $30,000 minimum project cost requirement and a 4% reduced rate was adopted for oil produced from wells which receive the workover exemption after June 30, 1993.

1995 Session. The stripper well definition was broadened from 20 to 30 barrels per day for wells over 10,000 feet deep. The exemption for a horizontal new well was increased from 15 to 24 months and a 9-month exemption was created for a horizontal reentry well. A 10-year exemption was created for oil from a two-year inactive well. To get the full benefit of an exemption or the 4% reduced rate, producers were given an 18-month period to file the Industrial Commission's certification of well status with the Office of State Tax Commissioner. For secondary recovery projects, the sunset for certification was removed. The revenue distribution formula was changed as shown in the chart below.

1997 Session. A 60-month exemption was created for production from a well drilled and completed on an Indian reservation or on tribal trust land after July 31, 1997. The legislature amended previous legislation to keep the current distribution factors at the current percentages (see chart on following page).

Distribution of Gross Production Tax Revenue

Fiscal Year	Total Distributions	State General Fund	County Fund	Impact Grant Fund
1986	54,129,624	36,208,124	17,921,500	
1987	34,410,003	22,033,315	12,376,688	
1988	35,260,547	22,736,519	12,524,028	
1989	29,434,368	17,923,334	11,511,034	
1990	33,972,649	20,738,906	13,233,743	
1991	47,612,332	31,127,810	16,484,522	
1992	32,536,334	17,993,251	12,612,291	1,930,792
1993	29,802,080	16,075,676	11,791,588	1,934,816
1994	22,093,783	11,541,422	9,116,849	1,435,512
1995	23,798,926	12,019,079	10,209,527	1,570,321
1996	26,548,326	13,550,184	11,228,254	1,769,888
1997	34,505,108	19,054,995	13,149,772	2,300,341
1998	28,610,476	15,156,083	11,547,020	1,907,364
1999 (estimate)	25,843,000	12,727,000	11,417,000	1,699,000

SOURCE: North Dakota Office of State Tax Commissioner, Comparative Statement of Collections; State Treasurer's Office, and estimates prepared with the Office of Management and Budget.

Distribution of Oil Extraction Tax Revenue

Fiscal Year	Total Distributions	State General Fund	Education Funds*	Resources Trust Fund
1986	57,148,758	51,493,652		5,655,106
1987	35,391,141	31,877,584		3,513,557
1988	36,954,125	33,282,631		3,671,494
1989	27,455,827	24,680,068		2,775,759
1990	31,156,324	27,768,967		3,387,357
1991	38,140,609	34,370,173		3,770,436
1992	26,699,694	24,044,310		2,655,384
1993	26,717,760	24,113,200		2,604,560
1994	16,152,813	14,586,537		1,566,276
1995	16,379,609	14,741,648		1,637,961
1996	16,811,677	11,168,763	2,640,498	3,002,416
1997	18,964,317	11,398,059	3,763,686	3,802,573
1998	15,204,014	9,295,710	2,937,272	2,971,032
1999 (estimate)	12,860,000	7,876,000	2,492,000	2,492,000

* Distribution is split evenly between the Common School Trust Fund and the Foundation Aid Stabilization Fund.

SOURCE: North Dakota Office of State Tax Commissioner, Comparative Statement of Collections; State Treasurer's Office and estimates prepared with the Office of Management and Budget.

OIL EXTRACTION TAX

1981	$ 23,651,815
1982	89,141,246
1983	86,952,446
1984	91,472,873
1985	77,799,141
1986	62,565,514
1987	34,988,979
1988	36,954,125
1989	27,398,372
1990	30,847,416
1991	38,274,835
1992	26,677,270
1993	26,606,259
1994	16,218,450
1995	16,354,433
1996	18,063,813
1997	20,204,863
1998	17,509,572
CUMULATIVE TOTAL	$ 741,631,422