2013 HOUSE FINANCE AND TAXATION

HB 1234

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
February 4, 2013
Job #18219

☐ 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.

Minutes: *Attached testimony #1, 2*

Chairman Belter: Opened hearing on HB 1234.

Representative Streyle: Introduced bill. See attached testimony booklet #1 and #2.

Representative Froseth: Your bill removes all exemptions with the exception on page 11 starting on line 4 the exemption for non-tribal properties inside the Fort Berthold reservation that has a 60 month exemption from the extraction tax. Was there any reason why you didn't remove that one?

Representative Streyle: No, that was in the last bill and I wouldn't have any problem changing that.

Representative Kelsh: You listed a number of challenges that the industry is facing; housing, infrastructure, and workforce so out of all those challenges where do you rate the tax structure as being in order of importance to the industry?

Representative Streyle: I would put it in the top three. The leases will mostly be covered within the next 9-12 months in theory and once that's done there is nothing. If I was sitting in a board room making a decision about these companies that do business out of state I would strongly look at moving my capital just because the rate of return is better and then you've covered all your leases. To me it is very critical that we do this soon because some of these decisions can leave a billion dollars here or there and that's a lot of jobs and a lot of economic activity.

Representative Drovdal: Would you explain a bit better in detail about eliminating the exemption on stripper wells? Are you completely taking them off or are you putting on more restrictions or redefining it?

Representative Streyle: It gets rid of it.

Representative Drovdal: Totally?

Representative Streyle: Yes.

Representative Marie Strinden: I know Texas charges some taxes that we don't. Is it possible to get a list of all the taxes that the other states charge?

Representative Streyle: Yes, I could put together some information on that.

Vice Chairman Headland: Do you have any idea of how much of the area and the minerals in these other shale plays have not been leased?

Representative Streyle: I would guess in some of the more mature basins that there are pretty much leased up for the most part. I could try to find that information for you.

Chairman Belter: Further testimony in support of 1234?

Ron Ness, President of the North Dakota Petroleum Counsel: We stand in support of this bill. The concept of a broad discussion about what is the proper rate of taxation in North Dakota and what is a proper structure for oil taxes we have brought before this body for the past several years. Now is the time to address the tax structure and go to work on a bill that will provide the certainty and the predictability not for only the counties and the cities but also for the and the water community and the school funding. The extraction tax goes away on any new well fi the price of oil is below $52.50 for more than five months in North Dakota. All existing production drops to 9% and all wells drilled within the past 24 months drop back to 5% for the remainder of their 24 months and all new wells drop to 5% so that's 130% swing in the rate of taxation including dropping 800,000 barrels of oil from 11 ½ to 9% overnight. This is estimated to be somewhere to be $2.1 billion in this coming biennium. That's the question the state and interested parties should look at if the price drops that rapidly. If you wait until then to address it then you're addressing it in somewhat of a panic mode because I think that five month trigger is broken because by the time I get to that price level and it's actually below $52.50 for five months you probably sustained a decrease in oil price for maybe eight months and by then I think operators would have made their decisions. Once you begin to see that decline curve of Bakken wells and stop the drilling decreasing production the tax revenues are going to go down. This bill is a tradeoff. We are trading off 30 plus years of incentives, triggers, and all of those mechanisms recognizing that when that tax rate went up 130% in November 1980 it chased industry out of North Dakota along with a price decline. The oil operator and that board room wants to make a long term commitment to the Bakken but they want to understand they have a fair and fixed tax rate going forward so they can plug that into their formula. They can't predict the price of oil no more than any of us can but they can predict all those other formulas. All those things you can put into that formula and eliminate that uncertainty it would make your decision making process better. Under this bill the tradeoff only comes if the oil production goes up which means more revenues are coming in. This is a significant issue for North Dakota. If the price drops below $52.50 for five months I suspect that is one of four things in North Dakota that could bring you back in special session because it is a tremendous impact on your budget. Anything you can do as policy makers in North Dakota to provide some predictability in the amount of revenues coming

forward and provide that certainty back to a major industry in the state we support. If this bill was enacted North Dakota would have a pretty simple tax structure.

Representative Froseth: This bill eliminates the exemption for stripper wells. I think that would be devastating for some counties and even though those counties don't bring in as much tax revenue they employ a lot of people who service those stripper wells.

Ron Ness: I believe this bill only removes the stripper property provisions for Bakken and Three Forks wells. I believe Mr. Walstad may be able to address that for me.

Vice Chairman Headland: It's on page six.

Ron Ness: I believe this is prospective only and it eliminates the stripper property designation which I believe we talked about a week or so ago for Bakken and Three Forks wells only. We would agree with you completely with the concerns you raised.

Vice Chairman Headland: Can you give the committee and idea of how much it costs to disassemble a rig and move it across the country?

Ron Ness: I think it's just like moving any other piece of equipment. Board rooms make decisions on where you can get the best return on your capital so you tear that rig down in McKenzie County and you'll pay the freight to move that truck or that series of 18 wheelers anywhere in the country. In North Dakota you'd probably pay a tax moving in but it's a fraction of a percent on what it would cost to drill an additional Bakken well.

Representative Klein: You probably have some idea of the rigs that got moved from Alaska to the Bakken area. Do you have any idea how much that cost?

Ron Ness: We have seen incredible movement of not only rigs but companies from Alaska to North Dakota and I think Alaska is something this committee should look at. Alaska has issues with federal land but when you look at what Alaska did with their tax rate about 6-8 years ago they have eventually taken shale play type activity for the independent oil and gas industry off the table and they are now struggling to keep the Alaskan pipeline full of oil. Subsequently we are now shipping Bakken oil via train to the west coast to satisfy the needs of the refineries out there. The governor of Alaska is trying hard to provide a fairer and competitive tax rate to get industry there.

Representative Haak: This burden of a tax on the industry, is this something the legislature put on the industry or is this something that was voted on by the people of North Dakota?

Ron Ness: The 5% gross production tax was in place and is intended to go back to the local communities. The 6 ½% extraction tax excluding any provisions in the stripper wells was voted by the people in 1980. In 1987 the legislature realized that was creating an incredible disincentive. In every legislative session since then there has always been a discussion on the appropriate rate of taxation. There has also been discussion on the people's tax and this was never really enacted because those triggers that went into affect in 1987 were in place on any new or old production until October 2004. After seven years

the legislature has the ability to make substantial change to initiated measures so that tax was dormant in its fullest version. The recognition was there but it was a discouragement to exploration in North Dakota.

Representative Kelsh: If the price of oil were to hit $52.50 for a five month period wouldn't that mean that the world economy is pretty much tanked and we would be dealing with a lot of other issues other than the loss of revenue from oil?

Ron Ness: I would say quite contraire to that because the economy may thrive under extremely low oil prices in certain situations. You may see an economic increase in other areas of the country. This tax structure takes too long, the system created was under a very different time and it's dating back to 1987 with tweaks throughout.

John Olson, Continental Resources Inc.: We are here to support the bill but just as importantly we ask that you continue this discussion on tax policy and the oil and gas industry in North Dakota. The majority of our resources are in North Dakota and they want to stay. There are challenges and have been recognized. In Alaska and California tax policy has a role to play in production and investment in those states.

Chairman Belter: Further testimony in support of 1234? If not, is there any opposition to 1234? Any neutral testimony?

Ryan Rauschenberger, Tax Department: In the red book there was a question on other states tax rates and on page 77 we have the top 14 oil producing states listed with their local taxes and the state range of tax rates. You can add those together and get your starting point for analyzing the different taxes. All the tax structures are different throughout the states as some have a separate property tax on royalties and reserves that we try to throw in the mix.

Chairman Belter: Are there any questions? Any other neutral testimony? If not we will close the hearing on HB 1234.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
February 12, 2013
Job #18843

☐ 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.

Minutes: *Attached bill and amendments #1, 2*

Representative Drovdal: Distributed marked up bill and amendments. See attached #1 and 2. Explained the amendments.

Representative Hatlestad: At no time will the rate fall below 10 percent?

Representative Drovdal: Not for a regular well but for a stripper well it will.

Representative Hatlestad: I'm not sure you answered my question. If all the triggers and all that stuff are gone the tax rate will never fall below 10% except for the stripper wells?

Representative Drovdal: That is correct.

Representative Kelsh: On section 5, is the recertification a one time after that first twelve months or is that every twelve months?

Representative Drovdal: I guess I didn't ask that direct question. Mr. Walstad said that if it drops down to 50 barrels it would fall under there. It would have to be recertified on a regular basis.

Representative Kelsh: Do you know what the effective tax rate is right now on all oil in North Dakota?

Representative Drovdal: I heard it was just under 10% but I don't have the exact figure. That would include stripper well and regular production well.

Chairman Belter: Have you asked for a new fiscal note?

Representative Drovdal: I have not requested one. I talked to Kathy Strombeck and she indicated it would be pretty revenue neutral.

Representative Drovdal: Made a motion to move the amendments 1005.

Representative Klein: Seconded.

VOICE VOTE: MOTION CARRIED.

Representative Drovdal: Made a motion for a Do Pass as Amended.

Representative Hatlestad: Seconded.

ROLL CALL VOTE: 10 YES 3 NO 1 ABSENT

Representative Drovdal will carry this bill.

FISCAL NOTE
Requested by Legislative Council
01/15/2013

Bill/Resolution No.: HB 1234

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				$(156,000,000)		
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 1234 reduces the oil extraction tax rate on a graduated basis if specified production levels are met. The bill also removes an exemption for higher producing wells in stripper properties within the Bakken and Three Forks formation.

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.*

Section 2 of HB 1234 reduces the oil extraction tax rate from 6.5% to 4.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of HB 1234 removes the automatic exemption for high producing wells drilled in stripper properties and requires these wells to individually produce at stripper levels before receiving the oil extraction tax exemption. This automatic exemption is removed for wells drilled in the Bakken and Three Forks formation.

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, HB 1234 is expected to result in a reduction in the oil extraction tax rate of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $240 million in the 2013-15 biennium. The closing of the stripper loophole for Bakken and Three Forks formation stripper properties is expected to increase oil extraction tax revenues by an estimated $84 million in the 2013-15 biennium. Therefore, HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $156 million in the 2013-15 biennium. The funds affected include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust, and Strategic Investment and Improvements 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: 02/01/2013

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1 of 2

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Title.02000

Prepared by the Legislative Council staff for
Representative Drovdal
February 12, 2013

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1234

Page 1, line 1, after "reenact" insert "section 15-05-10, subsection 4 of section 38-08-04, and"

Page 1, after line 4, insert:

"**SECTION 1. AMENDMENT.** Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property <u>or individual stripper wells</u> as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations."

Page 3, line 27, after "<u>8.</u>" insert ""<u>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.</u>

<u>9.</u>"

Page 3, line 27, after ""property"" insert "<u>outside the Bakken and Three Forks formations</u>"

Page 4, line 26, remove the overstrike over "~~is~~"

Page 5, line 16, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 16, after "on" insert "or after"

Page 5, line 18, remove ", which must remain the rate unless a"

Page 5, line 19, remove "lower rate is determined under subsections 2 through 5"

Page 5, line 20, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 20, after "on" insert "or after"

Page 5, line 22, remove ", which must remain"

Page 5, line 23, remove "the rate unless a lower rate is determined under subsections 3 through 5"

Page 5, line 24, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 24, after "on" insert "or after"

Page 5, line 26, remove "one hundred thousand"

Page 5, line 26, remove "which must remain the"

Page 5, line 27, replace "rate unless a lower rate is determined under subsection 4 or 5" with "or for production from wells drilled and completed on or after the first day of July 2015, whichever event occurs first"

Page 5, remove lines 28 through 31

Page 6, remove lines 1 through 3

Page 6, line 10, after "property" insert "or individual stripper well"

Page 6, line 10, remove "On or"

Page 6, replace lines 11 through 16 with "A well in the Bakken or Three Forks formation which was certified as a stripper well or as part of a stripper well property at the time it is reentered or reworked retains its stripper well or stripper well property exempt status for the first twelve months of production from that well after completion of the reentry or reworking project. After that period, the stripper well or stripper well property exempt status is lost after the average daily production of the well exceeds one hundred barrels per day for a calendar month and the well is then subject to a reduced tax rate of two percent under this chapter until production from that well individually meets the requirements of the definition of stripper well under section 57-51.1-01."

Page 17, line 6, remove the overstrike over "~~**or rate reduction**~~"

Page 17, line 10, after "exemption" insert "or rate reduction"

Page 17, line 11, after "property" insert "or individual stripper well"

Page 17, line 13, after "property's" insert "or individual stripper well's"

Renumber accordingly

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

2013 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1234

House Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment 1005

☐ 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) _____ 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. 1234

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. Hatlestad

Representatives	Yes	No	Representatives	Yes	No
Chairman Wesley Belter	✓		Rep. Scot Kelsh		✓
Vice Chairman Craig Headland	✓		Rep. Steve Zaiser	AB	
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) 10 No 3

Absent 1

Floor Assignment Rep. Drovdal

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

REPORT OF STANDING COMMITTEE

HB 1234: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (10 YEAS, 3 NAYS, 1 ABSENT AND NOT VOTING). HB 1234 was placed on the Sixth order on the calendar.

Page 1, line 1, after "reenact" insert "section 15-05-10, subsection 4 of section 38-08-04, and"

Page 1, after line 4, insert:

"**SECTION 1. AMENDMENT.** Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

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4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property <u>or individual stripper wells</u> as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations."

Page 3, line 27, after "<u>8.</u>" insert ""<u>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.</u>

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Page 6, remove lines 1 through 3

Page 6, line 10, after "property" insert "or individual stripper well"

Page 6, line 10, remove "On or"

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Page 17, line 11, after "property" insert "or individual stripper well"

Page 17, line 13, after "property's" insert "or individual stripper well's"

Renumber accordingly

2013 SENATE FINANCE AND TAXATION

HB 1234

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
3/11/2013
Job Number 19693

☐ Conference Committee

Committee Clerk Signature	Angela Rittenmiller

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes: Testimony Attached

Chairman Cook opened the hearing on HB 1234.

Representative Streyle introduced HB 1234 (attachment 1) and offered an amendment (attachment 2).

Vice Chairman Campbell - As far as the trigger price, explain that, so you're eliminating the trigger price at $52.00 per barrel?

Representative Streyle - Yes the trigger will go away.

Vice Chairman Campbell - Grand Forks Mayor and the League of Cities are in town and I spent 15 minutes trying to convince, you know what our opposing people are saying, don't worry these oil guys are going nowhere, you are being bought off etc. How do you tell these people that in a nutshell because there are a lot of people who are against all of this and it concerns me. Do we compromise this, taxes or not?

Representative Streyle -It's a thing where what makes good public policy might not make good political policy at the time but I think we have to take it when we come here, we shouldn't just look the next year or 6 months out. For our kids and grandkids, and I think having a competitive, simple to understand, where everyone can figure it out in 30 seconds, I don't think there is anybody in this state that understands the oil tax at this point.

Senator Miller - Do you think that this type of breakdown of tax policy with the reductions as a per day as we go forward, do you think that could cause some sort of inadvertent competitive advantage for a particular company that might be well positioned going forward. They hold a lot of leases out there. Do you understand what I'm getting at?

Representative Streyle - If I understand you are asking about the current bill as it stands on new production only basically.

Senator Miller - Maybe I'm misunderstanding your amendments that instead this would be across the board then?

Representative Streyle - Yes

Senator Burckhard - How does this bill compare to SB 2336?

Representative Streyle - I have not looked through the details on that.

Senator Triplett - You reference rig count along the way in your presentation. Do you consider a decline in rig count as a bad omen for production in North Dakota?

Representative Streyle - The high was 218 now we are at 187. I think most in the industry will pop back up a little bit with the efficiencies and the drilling. Any time you are reducing rigs I look at that as a negative I guess.

Senator Triplett - With all due respect, I think you have that backwards. It won't pop back up because of the efficiencies. My understanding from presentations that Mr. Helms has made to us is that the declining rig count has more to do with efficiencies in drilling than it does with anybody planning to walk away or actually walking away from the oil play in North Dakota.

Representative Streyle - I'm not disputing that. My concern is not right now. Its 10 years from now down the road. I think we need to incent them to invest here long term and with the popup of many of the shale plays worldwide and then the United States. We are not the only dog in this game anymore.

Senator Triplett - There have been a couple of companies who have reduced their holdings in North Dakota or have even sold their North Dakota assets to other companies. Are you aware of any single instance of a company abandoning its assets in North Dakota?

Representative Streyle - I don't sit in the board rooms. I don't know what their reasons are.

Representative Drovdal - The stripper well part of it came from a bill that had it introduced into the House. Stripper well definition was put into place when to oil boom started to slow down and in order to encourage the developing companies to go in and get that last barrel of crude out of the ground. (23:44)

Chairman Cook - Representative Streyle's testimony indicated that in 2011, 43% of oil producing wells in North Dakota was qualified as stripper wells. 43% of the wells in North Dakota are paying on the 5% production tax. That seemed a little high to me but I know there is a lot of them out there that do not pay the extraction tax. Are you familiar with that number, and my question is wouldn't you put this stripper property fix on the bill that you have, how many wells in North Dakota go from paying 5% tax to 11.5%.

Representative Drovdal - Under this bill it does not affect any current wells. This is only for new production. It will not change any tax structure of any wells that are currently out there. The percentage that you quoted I am not familiar with that percentage.

Chairman Cook - But if we don't pass it there are a whole lot of wells that will go to 0% extraction tax.

Representative Drovdal - The tax department said they expect another 140 wells would qualify for the stripper well that may be a new Bakken production.

Senator Triplett - You know the history of the stripper well property exemption in the state of North Dakota, right?

Representative Drovdal - I'm somewhat familiar with it.

Senator Triplett - It was intended for and initiated at a time when virtually all, maybe all wells, were vertical wells. Is that correct?

Representative Drovdal - Yes, there were no horizontal wells even thought of when this definition was put in place.

Senator Triplett - And it was intended as a way of offsetting the risk of exploration and drilling of new wells when there wasn't so much of a guarantee of getting oil. Would that be a fair statement?

Representative Drovdal - That is my belief and that is why I think we need to change it to individual wells.

Senator Triplett - Why not just remove the notion of stripper properties all together? Why this mish mash of properties somewhere and not properties elsewhere?

Representative Drovdal - I'm not catching the question, that we need to have a definition of some kind of well that's a low producer.

Senator Triplett - If you go to page 4 of the bill, number 9, stripper well property, you are defining it now to mean a property outside of the Bakken and Three Forks. So you are saying that you are getting rid of stripper well properties for new production within the Bakken and Three Forks but you're still leaving the idea of stripper well properties for everything outside the Bakken. I'm saying why not just be clean about it if we are trying to simplify and get rid of the concept of stripper well properties and you could still have the individual wells.

Representative Drovdal - I guess I didn't bother with the rest of them.

Senator Triplett - Are you familiar with the concept of maximum efficient rate relative to production from an existing oil well?

Representative Drovdal - I am not.

Vice Chairman Campbell - To sum this up; compare it to the Senate version of this. The first year that this stripper reformation of the bills would be how many dollars, what would be the dollars that we would gain back from that revenue?

Representative Drovdal - The best I can answer that question is that the last time we had a fiscal note on just a stripper part of it itself it was about $84 million. That was before we added the 2% so it's really a figure that's just a guess out of the air.

Senator Dotzenrod - Does the bill include annual recertification of the stripper wells?

Representative Drovdal - I've heard that we should have them recertify. The only time it's required is when they go in and move or can re-drill it.

Chairman Cook - The bill as introduced is for the first day of July 2015, the rig would go in to effect, the amendments that Representative Streyle now change that to July 2016 just so you are aware.

Senator Oehlke - Could you refresh my memory as to why we go from, I know we went from 30 to 40 barrels a day on the stripper well status, now we are looking at maybe going to 50. What is the reason for that?

Representative Drovdal - That figure came from me and it was just a guess.

Chairman Cook - That 50 barrel a day is that only the Bakken and Three Forks?

Representative Drovdal - Yes

Senator Triplett - Are you aware of any single oil company who has laid their rigs down in North Dakota and driven away without selling off their assets to some other company who then picked up the drilling?

Representative Drovdal - During the last oil boom almost every major oil company laid down their stuff and left because of price, taxes, etc.

Senator Triplett - Your talking in the 1980's.

Representative Drovdal - Yes

Senator Triplett - My question was about the current oil boom.

Representative Drovdal - Oil companies are here to make a profit and they are making a profit. Not on every single well but they are making a profit and they are going to stay here as long as they can successfully drill. (39:10)

Senator Triplett - My question was really specific and maybe not well enough stated but relative to the current Bakken play, horizontal drilling with fracking, are you aware of any single company that has laid down it's rigs and driven away without selling its assets to some other company who stayed behind to work the development. Yes or no.

Representative Drovdal - Off the top of my head I couldn't mention anyone.

Chairman Cook - If the president gets the way with the current tax policy that is sitting there and pass some of the tax increases on the oil industry and 50% of the capital leaves do you think that you will see some oil companies laying down their rigs because they don't have the capital to keep them running?

Representative Drovdal - If the taxes keep going up they will not be profitable because they are only producing, they start out with production at very low levels and they drop off 50% in 12 months and 50% after that. They will not do it at a loss and they will lay them down and move out of state. (41:22)

Chairman Cook - Do you think it would be wise for the legislature to wait until they have left the state and then try to change policy to bring them back or do we want to do some things that might make it easier for them just to stay here.

Representative Drovdal - Foresight is really hard. I would rather look into the future instead of afterwards. (42:04)

Senator Triplett - Do you have any estimation of the possibility that the EPA would actually cut off fracking entirely as opposed to maybe regulating it a little around the edges if they get their hooks into it.

Representative Drovdal - I do feel that with all the action going on in Pennsylvania and New York that there certainly is a possibility that we are going to see restrictions on fracking. (43:06)

Senator Triplett - If the restrictions are that maybe somebody shouldn't do fracking in shale plays in New York where they are associated with ground water where the shall is producing both gas and ground water as opposed to here where we have 5,000 feet of impermeable clays. Don't you think that scientists at the federal level are smart enough to make the distinction that maybe they should be regulating fracking in New York but not regulating fracking here? Do you really have so little trust in science that you think they can't make that call?

Representative Drovdal - I have faith in the science, I don't always have faith in some of the policies that come out of Washington D.C. and like us they pass an umbrella law in more cases than not. (43:59)

Senator Triplett - If the fear mongering that is going around about the EPA in this building were accurate, and the EPA outlawed fracking, do you really think this little tax policy would make any difference at all in the run for the borders?

Representative Drovdal - No it would not make any difference. (44:57)

Ron Ness, North Dakota Petroleum Council - The Petroleum Council, in its current form stands in opposition to HB 1234. We have been observing and monitoring the amendments as they come through each of the committees and the discussions and when you look at

where we are at today on this particular bill, when it came in it was pretty simple. Essentially step down the oil tax rate in lieu of eliminating the price sensitive triggers, all 10 of them and it lowered the rate on all new production to 9%. In its current form the top total rate would be 10% so it is migrated up 1%. In addition, if you look at really how this will work as those triggers would be reached you would have varying rates at leach level so you would drill wells at 11.5%, if you drilled them later you would be at 11%, those wells would stick I think at that percent and then you would have them at 10.5% and then 10%.

Ron Ness went on to discuss the provisions of the bill and that he thinks it is moving in the wrong direction. (48:36)

Senator Oehlke - How many rigs are out there drilling right now?

Ron Ness - I believe there are 182 drilling rigs give or take a few.

Senator Oehlke - Are any of them drilling outside of a stripper well property?

Ron Ness - I think 98% of those rigs would be drilling outside the stripper well property.

Senator Oehlke - Let's pretend you got your dream and we changed it to a flat 9.5% period, that's it. Stripper well any well doesn't matter if oil is coming out of the ground its 9.5%. You happy with that?

Ron Ness - No we would not be happy with that.

Senator Oehlke - A minute ago you said you liked 9.5%.

Ron Ness - I do like 9.5% but you are talking about marginal well production at 5%. There's a big difference between; that is why you've got 3 thresholds, less than 10, less than 20 and less 30. (57:40)

Senator Oehlke - So the answer is that we can't simplify it.

Ron Ness - I think you can simplify very easily by having a fair rate for new production and a fair rate for stripper production.

Senator Oehlke - What are those rates?

Ron Ness - I would say we would probably be happy at 9.5% and if you wanted to provide something maybe 6.5%.

Senator Oehlke - 6.5% at what production level?

Ron Ness - I think there is an opportunity just to make all stripper wells 6.5%.

Senator Oehlke - When you say stripper well I hear a well, I don't hear 1,280 acres or a quarter, I hear a well. To me that is a stripper well. I don't hear properties, what are you saying, the property or what?

Ron Ness - You can get to the eliminations, you could provide a fair rate, you also get a return for the water people and the education people if you provide a little bit above the 5% which is a zero extraction tax. I would want to do that math on whether that... Its different ownership but I would think somewhere in that... We had a bill in 2009 that passed the Senate, Representative Onstad and I had the bill and it was 7% and 9% tax, plain and simple. (1:00:00)

Senator Oehlke - You mentioned that your previous bill that the Senate looked at in 2009 said 7% and 9%. Now are saying 9.5% and 6.5% so we went up on one end and down on the other. Is there a reason for that?

Ron Ness - Call it what you want but the desire for additional tax revenues continues to be present no matter how much, at that point we were probably collecting $1-2.5 million a biennium in oil tax revenues. Today we are talking about $5 billion. (1:01:17)

Senator Triplett - People who had actually done drilling, would have been in there with drilling rigs and produced wells and then laid down their rigs without selling their assets. I'm not aware of any.

Ron Ness - It has happened. (1:07:18)

Chairman Cook - We left here 2 years ago knowing full well that we had a little stripper property issue that we had to resolve this session. Today we have 2 pieces of legislation that try to do that. You testified in support of the Senate bill, and an oil company testified opposed to the oil bill. You are opposed to this one. Somehow I would hope that we do not have as an option going home without fixing it. Somehow I hope that we all decide we are going to fix it and find the best manner and I would hope we could do it in a way that is a win win for all. Are you suggesting we kill this bill, or are you suggesting that we've got to work on this bill to make it better?

Ron Ness - I would suggest all of the above. I think this committee has the best grasp of this issue. (1:08:57)

Senator Triplett - Maximum efficient rate relative to analysis of stripper wells. Can you describe what that means?

Ron Ness - As an operator if you want to seek a certification under a stripper classification you need to make request to the Industrial Commission, you need to have a hearing, provide the engineering data and reservoir data and efficiency data that you are producing that well at maximum efficient rate in order to receive that. In industry terms you can't throttle back your well. (1:10:45)

Senator Triplett - I was looking for a little more detail of the engineering piece of it. The reason I am bringing this up is because I worked on a stripper well bill last session and Lynn Helms recommended to us on that bill that we put that phase which he referred to as a term of art within the industry, put that phrase actually into the stripper well bill and we did that. I'm wondering if you could describe in slightly more detail what the engineering and

the reservoir data is that allows our regulatory folks to understand and believe that a well is being produced at the maximum efficient rate.

Ron Ness - I cannot provide that. We would not object to that language being in these stripper positions.

Jean Schaffer, North Dakota Water Coalition - Mr. Ness said it correctly; the current oil boom has given us the funding and resources larger than we have ever seen. While we have those significant resources, our needs are equivalent if not greater because of the whim of mother nature. Western area water supply is looking at about a $240 million coming down the road, Southwest Pipeline another $150 million, both communities trying to deal with oil impact needs for water development in their areas. Fargo-Moorhead flood control is about $1.8 billion project at a 25% cost share. Most river flood control and river valley water supply are close to a billion dollars each so while we are currently working on our water infrastructure as we are able we are facing a scenario where federal funding is all going to but dry up for us so we are having to fix these problems on our own. I just wanted to give you a brief statement on that.

Chairman Cook - We all understand this oil tax funds the water world.

Senator Triplett - If you could just summarize for us from the Tax Departments perspective what you know in terms of the number of Bakken wells that are on stripper status versus the number of other wells on stripper status. Can you verify or add to that?

Kevin Schatz, Oil Supervisor, Tax Department - I do not know off the top of my head but it would be real easy to run those for you and get it to the committee.

Chairman Cook closed the hearing on HB 1234.

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
4/2/2013
Job Number 20749

☐ Conference Committee

Committee Clerk Signature Angela Rittenmiller

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes:

Chairman Cook opened discussion on HB 1234.

Senator Dotzenrod - The amendments that I have offered (attachment 3), it is a hog house amendment that takes the bill and makes it into a bill that just does one thing and that is to fix the stripper property loophole. It deletes references to stripper property and I went through the amendments and looked through the sections and it looked like they would do that. They put in the annual recertification of wells and John Walstad thought too that these amendments would take care of basically closing the stripper property loophole.

Chairman Cook - You are closing all stripper properties and all formations?

Senator Dotzenrod - Yes

Chairman Cook - Do you have an idea of the fiscal note?

Senator Dotzenrod - No

Chairman Cook - I would guess this is very similar if not almost identical to the bill that was introduced in the House by Representative Drovdal and I think the fiscal note of that was $104 million. Would it be your intent then with these amendments to pass the bill and go home with a $104 million tax increase on the oil industry?

Senator Dotzenrod - I think the way the stripper property loophole has been used has been to exempt fairly large producing wells from the oil extraction tax in a way that was not intended at the time that these sections were passed there were no horizontal wells and so I think what we have is probably almost a stereotypical or classic example of what a loophole is. (2:36)

Chairman Cook - Well it will have a $104 million fiscal note to it. Don't you think that you refer to this as a loophole, but don't you think that maybe the stripper property incentive that was put in place for the old vertical wells actually accomplished exactly what it wanted to do and that maybe with the evolution of the Bakken and the Three Forks and the different type of economies that existed with those wells probably created an unintended consequence?

Senator Dotzenrod - I don't know the history of how the horizontal wells got to be used but I think, my understanding of it is that it was sort of an accounting discovery in the process of going through their accountants reviewing the laws and getting in compliance with their states and the various states they operate in and they found this provision and started saying why not take this provision and apply it to these horizontal wells we've got. I wish I knew the history better of how it developed but I think for the companies that are using it when they found it was there they probably thought, well this is something we didn't expect and we might as well use it.

Chairman Cook - I would argue that in the old formations that the incentive was offered to entice the oil companies to go in there and make a large investment. The carrot was that they were going to have no extraction tax applied to that if they made that large investment and assume the risk that came along with it. I think we found that maybe not to be as true in the Bakken and Three Forks which is why the original bill just eliminated for them formations. I'm comfortable going ahead with this, to a certain degree. I'm not comfortable with raising the taxes on the oil industry $104 million. I think it's imperative that if we are going to fix this we try our best to move towards a bill that is more revenue neutral. The only other question I have then is with the recertification, wells in other formations that have taken advantage of the incentive and made the investment and may be over 30 barrels of oil per day, you would claw back and change the tax rate of them, is that correct?

Senator Dotzenrod - I'm not sure how that would work. It seems to me that once the well is qualified, when they are doing annual certifications now, my understanding with annual certifications is that in the course of finding that a well is over 30 that is no longer a stripper well. If you were continuing to be certified every year and finding that you are 30 or below then I think you are exempt from the oil extraction tax.

Senator Triplett - I don't think that Senator Dotzenrod's amendment has a claw back provision. That was in my amendment to your bill that moved it back 2 years but it's not in here.

Chairman Cook - Maybe I used the work claw back, I think the recertification could change the status of an existing well.

Senator Triplett - Yes, going forward but I think the term claw back I think refers to going back in time. I think the chairman is right regarding the reason for which stripper wells were given the tax exemption in terms of the stripper well property piece and it was about encouraging investment and I think it was specifically about encouraging reinvestment in places where the oil companies had been unsuccessful in the old vertical drilling where they came up with dry holes in an area and the state as a policy matter wanted them to keep looking for oil in places where they had not yet found it. I think that is the fundamental reason that it is so inappropriate as a tax policy for the Bakken where the risk is gone as we

heard from the chief lobbyist for the petroleum industry, the only failures are in the folks who are looking to define the edges. Certainly we all know the Bakken feathers out at some point on the landscape and it's not in a really straight line and so they have to work their way around and figure out where it's feathering out. So there is some slight risk of a dry hole or a less producing hole on the very edges but what we have learned from experience and the testimony of Lynn Helms is that within the confines of the Bakken, it's virtually 100% so there is no longer any risk of not finding oil. I think that is the main reason to say that it does not belong in in our tax code in the situation that we have with the Bakken and the Three Forks and I don't hear of anyone planning to go back to drilling vertical wells. No one ever talks about that, I think that is just old history at this point.

Chairman Cook - The bill we had before us in SB 2336 had this provision fix only for the Bakken and Three Forks and that is why I'm asking the question is because, now you are bringing up a policy change that offers it across. Is that a policy change that you are going to hold firm to or would you be open to just making it to the Bakken and Three Forks?

Senator Dotzenrod - I don't see any reason to go into the state and fence off certain perimeters and say this policy applies within the fence, the other policies outside the fence. It seems to me that I would be very inclined toward saying that we will have a policy that applies across the state and this is it.

Chairman Cook - I would be happy to put forth as much effort as we could to find something where all of us could agree on a compromise on this issue. I'm happy to go home and do nothing with this issue if it stays as controversial. Are you amenable to any efforts on this amendment that you offer to make it revenue neutral?

Senator Dotzenrod - To make it revenue neutral implies that we are going to have sort of a permanent, to use this loophole as a means to create a permanent reduction in rates that it seems to me to make sense to be about where they are today. The idea that we would fix a loophole which is an unintended sort of way of avoiding 100% of the extraction tax, to trade that off for some lowering of a tax that's about where it should be, I can't see... I guess you should never say never but my inclination would be there is no state policy objective here.

Chairman Cook - We use the word loophole rather freely I think. I'm not necessarily talking about a rate reduction. Let's take that off the table. We have the 11.5% rate reduction, or the 2% rate reduction off, we've got the triggered incentives off, there are things we could do right here with this piece of legislation. You do not have the withholding requirement, we could put that on. You do not have the incentive for the non-Bakken, Three Forks on, that had quite a positive fiscal note. I think there is merit for that. There are other things I think we could do with this, would you be amenable to any of them?

Senator Dotzenrod - The things you have mentioned sound like pretty reasonable things to do. (12:20)

Senator Triplett - I'm fine with the withholding, I have always been fine with that. In terms of suggesting that we need to do incentives for something outside the Bakken when there has been no proof that we need to do incentives. The fact that people aren't drilling outside

the Bakken is because the Bakken area is the area that was leased up where the large reservoir of oil was defined and identified and thoroughly studied so they have been racing to secure their leases in the Bakken. The oil companies have not had the time or the inclination to drill outside the confines of the Bakken because that is where their leases have been and they had the 100% guarantee that they were going to find oil. You give an incentive when you have to give an incentive or when there is a reason to give an incentive. When there is somebody saying, okay we've got the Bakken finished now and gosh we are just going to go somewhere else next because you haven't given us a good enough tax reason to stay. There is no indication of that. These oil companies are booked up with their drilling rigs for the next 20-25 years if Lynn Helms is telling to us correctly in just doing infill drilling in the Bakken. I think there is no justification at this point for providing additional incentives. To suggest that we have to do anything to make it right with anyone, this is a loophole and I don't think it's being free with the language to suggest it. It was not anything that anyone from the 1980's would ever have imagined giving as an exemption in this kind of an environment. They were giving an exemption to encourage drilling in places where the oil company was unsuccessful. (14:44)

Chairman Cook - Don't you think that there are oil companies that have leased land, secured, outside the Bakken who do not have leased land inside the Bakken, who because of the economies of drilling in the Bakken can no longer afford to drill on their own lands?

Senator Triplett - They haven't been here telling us they need an incentive. We have not heard from a single one of them.

Senator Burckhard - Wasn't it Representative Streyle that said 43% of our wells are stripper wells, is that possible?

Chairman Cook - I don't know. I would go to Lynn Helms with that question.

Senator Oehlke - Could you see the value in, one of the pieces of testimony we had when we were hearing the oil folks was the huge need for roads and of course that is no mystery. Everybody understands that and the state's pouring a lot of money into roads right now, but could you see any wisdom in doing a stripper fix like this and designating the dollars, whatever they are, could you see designating that money possibly toward roads and as those roads get better, adjusting the stripper well tax down?

Senator Dotzenrod - The stripper well taxes right now, many of these are 5%. I can't really understand why we would want to try to find a taxing system that would put us down below that 5% level.

Senator Oehlke - I was just thinking of the excise extraction tax.

Senator Dotzenrod - On your first point about roads, I think that one of the real objectives of having a meaningful tax on oil production is for the roads is for infrastructure. The impacts that have gone along with the industry have been largely seen in roads. They are affecting many other things and we may not even have a good handle on all the impacts that are going on in the oil country, but infrastructure if there was some thought that we could, because it's a high priority, to try to get a fairly straightforward tax policy on oil that to

me we've lost some of that by having this loophole here. The idea that we are now going in to properties and having wells that are putting out a 1,000 barrels a day and they are getting a complete exemption from the extraction tax because of this loophole, to me is a tax policy gone haywire to see something like that happening. It doesn't make any sense. It's a high priority to get this stripper property loophole fixed. (19:33)

Senator Oehlke - I think from my perspective and though in this process would be that right now the need is so great. It's hard to argue that fixing the stripper well situation is maybe not a bad idea. On the other hand we also know that these roads are getting built better and able to withstand, the number for load now is 105,500 on everything, so now let's fast-forward 6 years, and now we have a pretty good road system out there that's very substantial and now it's handling all the traffic, the roads are going to be better and the demand for the high level of building new roads and that heavy maintenance is not going to be as great. That is why I thought maybe designating these extra dollars that come in from this toward that road effort helping the oil companies get their job done better and safer and quicker would be better for everybody and then add a point 4 or 6 years from now perhaps even reducing the overall extraction tax a bit.

Senator Triplett - Senator Oehlke as the chair of the Transportation Committee knows better than the rest of us exactly what the road needs are out there going unmet. I will point out that we've done an extraordinary thing already this year by authorizing the bidding and construction of $620 million in advance of the beginning of the biennium and then we have a lot more in the regular Department of Transportation appropriations bill. If the perception is that we are still not meeting the immediate needs or the needs for the next 2 years that can be accomplished by the level of contractors we have available and such, I wouldn't have any problem at all with saying that the additional money that comes in from this tax should be specifically allocated toward infrastructure in the west. That wouldn't bother me at all if we are thinking we are still coming up short. I do think it would be too soon to say that then because of that we should at some point in the future reduce the extraction tax. I don't think they are really all that much related. I think that what the oil companies have gotten from the stripper well exemption really can be perceived as a gift to them that now we are saying we are taking away the gift and just because they have gotten a gift in the past doesn't mean we have to give them something when we say we aren't giving them a gift any longer. In terms of saying to the people of western North Dakota, we are going to start collecting the tax that we should have been collecting all along and we will focus it directly on your needs in western North Dakota. That I think is a good idea.

Senator Miller - Regardless of what you want to call it, a loophole or a tax increase, the simple fact is if we passed these amendments there will be more tax revenue coming in to the state because of what oil companies do. I will never support a tax and spend policy that takes new revenues in and simply spends more. We have enough revenue in the state to fund our priorities, repair the roads, we need to put more money back in the hands of taxpayers and oil companies are taxpayers too and they do good things for this country.

Senator Triplett - No one suggests that oil companies aren't doing good things for this country. What is happening in North Dakota is truly game changing for this entire nation and I think we all understand that. That the technology that has been developed by the oil companies working in North Dakota is of worldwide significance and we are all grateful.

That doesn't mean that we give up our own tax policy and the long term net effect of not fixing the stripper well property problem is that every well in the Bakken will over time become a stripper well if it's left to its own decline. The oil companies having secured their lease could choose not to do their infill drilling until their first well has become a stripper well and then everything else that they drill for the rest of time will be a stripper property well and the effective tax rate in this state will be 5% and there will be no money for our water development projects, no money for our education funding, there will be only half the amount of money for our legacy fund, and so certainly I'm not advocating this as a tax and spend either, it all goes into the balance that we have and our appropriations folks in the end will decide how much to spend and how much to give back in tax relief in other forms or how much to save. That is beyond our pay grade here in this committee, but this isn't about increasing the actual revenues to the state, it's about having fair and consistent tax policy that everyone can understand and live with and leaving this problem in place means virtually an ever changing tax policy company by company and property by property. I don't think that's good policy and wouldn't expect the oil companies would think it was good policy either.

Chairman Cook - I think we have all agreed, 141 legislators, that it is a goal to get home and fix this little thing called stripper property tax. Senator Miller made a point, which goes back to my original question, is there a way we can make this revenue neutral? 141 legislators, there are legislators here who are not going to vote for a bill that has a tax increase on the oil industry. We are sitting here with a fair amount of money and it's no time to raise the taxes on anybody. That is something we need to set politically that if we are going to look for something where we can all be happy, we need to take that into consideration which goes back to my original question of what can we do to this to make it less of an issue for people like Senator Miller and even myself to vote for it.

Senator Triplett - Maybe I can make a suggestion that we suspend our conversation and actually ask the tax department and the legislative council folks to produce a fiscal note for us so we have a clearer understanding.

Chairman Cook - One more question, I think our budget has in there I think $5.2 billion in oil tax revenue for the next biennium, isn't it?

Senator Dotzenrod - That sounds familiar.

Chairman Cook - I consider this oil revenue to be the most volatile source of revenue our state has. We've had plenty of conversations about past history, boom and bust nature of it. When I introduced SB 2336 I started with a slide that spoke to all of the situations and conditions that exist out there regarding fracking and oil taxes that could affect this industry. Let's put on our most rosy had and say that everything continues to run on all 8 cylinders in regard to oil drilling in North Dakota. We could get a lot more than $5.2 billion, don't you think?

Senator Dotzenrod - I think we could.

Brief discussion followed.

Chairman Cook closed discussion on HB 1234.

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
4/3/2013
Job Number 20820

☐ Conference Committee

Committee Clerk Signature

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes:

Chairman Cook opened discussion on HB 1234.

Chairman Cook - Are you interested at all in a discussion to reduce that impact amount?

Senator Dotzenrod - I guess I'm interested in any discussion about some way to try to get some of the stripper property loophole closed. I think this look back, we are talking about, it's not like a claw back. It's basically a reestablishing of, at the time a well is recertified it makes a judgment about whether or not that well is a stripper well at that time and then imposed the consequences would take place from that day forward. I don't know just how the term look back, it's not asking for a recovery of taxes that might have been due in the past, it only imposes...

Chairman Cook - That is what I would call a claw back. This is just a look back, but you still have companies out there I would guess that have made a decision to make a capital investment looking at what the rules were and what their potential returns are and you are going to change the rules in which they made that investment. So the question is, if you want to reduce the amount and I think in order to get what your trying to do even considered, is you are going to have to reduce the fiscal note.

Senator Dotzenrod - I guess I would consider that. I don't know I would have to think about it a little bit. A well that has been a stripper well, the old rule, once a stripper always a stripper would apply for those in the past but from the time that this act became effective that rule wouldn't apply any longer because we'd have recertification. (4:03)

Chairman Cook - We all know the importance of the issue, we all know what we've got to do I think to go home with this issue resolved or home with it unresolved. (4:45)

Senator Triplett - Yesterday we had a pretty good discussion around the table and I was struggling some to make my point about this issue and I certainly heard from some committee members that they would never vote for what they perceived as to be a tax increase and last night when I thinking about this I thought of a different way to discuss it. I want to give you credit for that Mr. Chairman, you have consistently through my time on this committee talked about the importance of tax policy being fair. We have talked about sales tax a great deal in this committee and based on your work on the streamline sales tax project nationwide. We have talked about the fact that internet sales are not taxed and how unfair that is to main street America. That retailers with a fixed position on the ground have to collect sales tax and remit it to the state, and the folks who do internet sales do not and therefore they have an advantage and how unfair that is and that we should work to get everybody playing on a level playing field and to do that we would have to get internet sales taxed. I think you would agree that you would not consider that to be a tax increase even though it would be making those people who had not previously paid a tax, pay a tax. It would just be leveling the playing field and making everyone play be the same rules. That is how I see the stripper property exemption. Not everybody is ever going to be able to get a well on stripper property status, but for those who do, it's a huge advantage and by getting rid of the stripper property exemption all we are doing is putting everyone on a level playing field. I absolutely do not see this as a tax increase. Despite the fact that it will have an significant positive fiscal impact, the result will be that it will put everyone on the same playing field paying the same tax for producing the same product, and I think that gets to your first point, which you lecture us on correctly at the beginning of every session, that the most important thing that we can do with tax policy is to make sure that it's fair. Is there anything wrong with my analogy?

Chairman Cook - It's an excellent analogy but yes it is wrong, it's flawed. I will make this argument. We do not have to pass any legislation in our tax imposition laws to increase the tax revenue based on streamline sales tax. All that needs to happen is we get collection authority, but we don't have to change any tax laws. The taxes are already imposed. That is the difference in your analogy, is to do this we have to change tax imposition laws.

Senator Triplett - I would call that a technical difference. I would agree with you if the legislature had consciously put the stripper property exemption in place as a meaningful exemption as they did relative to the old vertical wells. Then I would agree with you. I do think we all agree here, and not just in this room here, but everyone in the legislature understands the history. That it was put on relative to vertical wells as an incentive in places where oil is not consistently found. It really was just an oversight in drafting because at the time it was drafted horizontal drilling did not exist and fracking didn't exist and nobody knew about source rocks and the fact that you could find the Bakken in a place the way it is with oil the way it is. So in that sense it is a technical defect in our law, not tax policy. We all agree it's not good tax policy, it's a technical defect. I see correcting the technical defect to be the same as getting the taxation authority on the internet sales. The basic premise of my argument is that we need to be getting toward tax fairness which means treating all oil companies the same across the board. I think the only way we get to that is to get rid of the stripper property.

Chairman Cook - I commend you on your effort. Again we have to change the impositions. I think to argue that it is a technical correction, there may be some who, it's exactly the way the wanted it. I don't know, but we still have to change tax imposition code.

Senator Dotzenrod - My thought about this is that we should fix the stripper property problem and that we don't need to make any other adjustments other than to fix the stripper property problem. We do have a basic ideological divide here that maybe it's not possible to bridge. (Senator Dotzenrod provided his own analogy - 12:38)

Chairman Cook closed discussion on HB 1250.

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
4/3/2013
Job Number 20836

☐ Conference Committee

Committee Clerk Signature Angela Rittenmiller

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes:

Chairman Cook opened discussion on HB 1234.

Lynn Helms, Department of Mineral Resources - See attachment 4.

Senator Triplett - If we were to draw a line and say we are going to move forward but we aren't going to look back, that would help you from an administrative standpoint of not having to do that, and it's a problem that will resolve itself over a period of years I guess is my question.

Lynn Helms - It will. (16:08)

Senator Oehlke - You mentioned these 2560's and they have to have 4 wells on them within a 3 year period or so. If they don't actually get the 4 wells put in in the time period that's allotted to them do they lose, does that 2560 lose its stripper well status?

Lynn Helms - What we do is bring the spacing unit back and we break it up and turn it in to a 1280 or something smaller. The well might continue to have its stripper well status, but its property would be reduced to half or a fourth of what it was.

Senator Oehlke - I think you mentioned something about this stripper property; it could fall below combined production status. Explain how that works if I've got 3 wells out there do they all have to, the whole total production has to go below 30 barrels or how does that work?

Lynn Helms - It is per well rate. It's a mathematical average production per well. (18:13)

Senator Oehlke - So then the measured depth, is it how far down or how far over or is it how far the pipe actually went, because I remember someone talking about how sometimes these wells aren't drilled all that straight and it might take 3 miles of pipe to go 2 miles deep.

Lynn Helms - It actually is the total length of pipe. (20:12)

Senator Dotzenrod - The estimate that we have heard in the committee for the stripper well property losses over the biennium we are in now is around $50 million projected that in the next biennium we are talking about $84 - $105 million depending on whether or not you include or exclude just those wells in the Bakken or you make it statewide. We anticipate that will grow from there if we do nothing about it. Can I assume that these 123 wells that you have identified, that is where these numbers are coming from, the 50 and 84?

Lynn Helms - The growth in the numbers is additional Bakken and Three Forks wells qualifying for stripper well property status. That's what is causing the growth in the numbers. (22:05)

Senator Dotzenrod - Then can we assume that when those 200 come on there in 2017 that at that point when that well and that property become stripper well property then in a fairly short order there will be some drilling going on in some more wells on that property that will be drilled with the idea that they won't have to pay any oil extraction tax.

Lynn Helms - That would be my expectation. (24:57)

Lynn Helms went through the certification process.

Chairman Cook - How long would it take if you had to recertify 2,974 wells?

Lynn Helms - I don't think we could get it done in a year. (31:54)

Chairman Cook - How about having an annual recertification on all new stripper wells?

Lynn Helms - You mean prospective, going forward, it would be somewhat burdensome but it would be do-able. (33:11)

Chairman Cook - What do you think we would gain by doing it? How many wells are going to lose their stripper status?

Lynn Helms - I think if you look at the numbers its maybe around 5%.

Senator Triplett - If you have a well on stripper status and you would always do the analysis for maximum efficient production in the initial certification, is that a true statement?

Lynn Helms - Correct

Senator Triplett - If it achieves stripper status then and nothing was done to it, just the laws of physics would say that it would continue to decline, so you are saying that annual certification is not necessary and would be of no benefit unless there is something done to

it, a work over of some sort and the whole idea of stripper status is to encourage them to do something, so if we got rid of the notion of annual certification but instead said when some event happened like a work over that then they would be required to be recertified 12 or 18 months after that event happened, giving them some time to get their benefit from it, but if it really did enhance the well to extent that it was producing at a large amount that then there would be some end to it. Does that make sense to you?

Lynn Helms - In my opinion stripper well status is intended to encourage people to take risks on that well. I would like to reward them for taking risks on that well. My real concern with stripper wells is stripper well properties. I think that's the elephant in the room that we have to address. The business of recertification and that is investing a great deal of time and effort into a small set of wells that have over performed everybody's expectations. (38:39)

Senator Dotzenrod - You mentioned that the real big problem is in the stripper property designation and I've always heard when this topic has come up that in order to fix the stripper well property problem you have to have a certification. You have to have annual certification to make it work. I'm not sure if I misunderstood that, or is there such a thing as biennial? Am I wrong about that?

Lynn Helms - I don't think they are linked unless you are trying to do something retroactively with the 111 that shave already qualified their properties. Going forward there is no link there. (44:27)

Chairman Cook closed discussion on HB 1234.

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
4/4/2013
Job Number 20853

☐ Conference Committee

Committee Clerk Signature Angela Rittenmiller

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes:

Chairman Cook opened discussion on HB 1234.

John Walstad, Legislative Council went through amendments 13.0225.02007 (attachment 5).

Senator Wardner handed out attachment 6.

Chairman Cook - It looks to me then that the protected tax increase that the oil industry is going to have pay for this next biennium is $87 million. There is $81 million for the tribe, $6 million for the state.

Senator Wardner - That is correct.

Chairman Cook - Anything in the discussion regarding the fees that are being charged to the oil industry?

Senator Wardner - Any time we brought up those other fees, and I know that was discussed in the initial agreement, they get really upset. They really feel that they are a sovereign nation and that is their business. When it comes to the fees for trucks coming on to the reservation the SPUD fee, and by the way the $100,000 SPUD fee that was negotiated by Governor Hoven and the tribes afterwards, that was a legitimate thing. We did want them to report and say that we are using some of this new money on roads. Roads are a real issue up there. A lot of push back on that.

Senator Triplett - Can you tell us what involvement the industry has had in these negotiations or has it mostly been between your office and the governor's office and the tribal representatives?

Senator Wardner - They haven't been active in it, no.

Chairman Cook closed discussion on HB 1234.

2013 SENATE STANDING COMMITTEE MINUTES

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

HB 1234
4/4/2013
Job Number 20898

☐ Conference Committee

Committee Clerk Signature Angela Pittenger

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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.

Minutes:

Chairman Cook opened discussion on HB 1234.

Chairman Cook handed out amendments 13.0225.02008.

Senator Oehlke - I'll move the amendment 13.0225.02008.

Seconded by **Senator Burckhard**.

Senator Dotzenrod - We put in 40 barrels a day to qualify as a stripper well in the Bakken and Three Forks. Current law is 30. I would like that to stay 30. What is the reason we are going to 40?

Chairman Cook - To try to reduce the amount of tax increase on the oil industry by $13.6 million.

Brief discussion followed on the revenue numbers and the extraction decline curve.

Senator Dotzenrod moved to amend the amendment changing 40 barrels back to 30 barrels.

Motion failed due to lack of second.

Roll Call Vote on the Amendment 6-0-1

Senator Oehlke - I'll move **Do Pass as Amended and re-refer to Appropriations**.

Seconded by **Vice Chairman Campbell**.

Senator Miller - For the record I just want to state that I will probably vote for this but I have many misgivings about several parts of this bill and the last part especially.

Chairman Cook - You aren't alone. It's got a ways to go.

Roll Call Vote 7-0-0

Carried by **Chairman Cook**.

FISCAL NOTE
Requested by Legislative Council
02/22/2013

Revised
Amendment to: HB 1234

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				$(42,900,000)		
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).*

Engrossed HB 1234 reduces the oil extraction tax rate on new production on a graduated basis if specified production levels are met. The bill also expands the definition of stripper wells, and eliminates stripper properties in the Bakken and Three Forks formations.

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.*

Section 4 of engrossed HB 1234 reduces the oil extraction tax rate on new production from 6.5% to 5.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of engrossed HB 1234 expands the definition of stripper well for wells drilled in the Bakken and Three Forks formation to 50 barrels of oil produced each day. It also closes the stripper property loophole for wells drilled in the Bakken and Three Forks formations. Section 5 of engrossed HB 1234 creates a new category of re-worked stripper wells and authorizes special tax treatment.

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, engrossed HB 1234 is expected to result in a reduction in the oil extraction tax rate for new production in the biennium of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $100.4 million in the 2013-15 biennium. The expansion of the stripper exemption to 50 BOPD for qualifying wells within the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $26.7 million in the 2013-15 biennium. The stripper property "fix" is expected to increase revenues by an estimated $84.2 million in the 2013-15 biennium. The re-worked stripper provisions contained in Section 5 may have a slight positive impact, but it cannot be estimated because the number of wells in stripper properties and might be re-worked is unknown. Except for the provisions contained in Section 5, engrossed HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $42.9 million in the 2013-15 biennium. The funds affected by this revenue reduction include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools

Trust, and Strategic Investment and Improvements Funds. (Note: The 2/26/2013 version of this fiscal note did not include the positive revenue associated with the "stripper fix".)

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: 03/18/2013

FISCAL NOTE
Requested by Legislative Council
01/15/2013

Bill/Resolution No.: HB 1234

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				$(156,000,000)		
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 1234 reduces the oil extraction tax rate on a graduated basis if specified production levels are met. The bill also removes an exemption for higher producing wells in stripper properties within the Bakken and Three Forks formation.

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.*

Section 2 of HB 1234 reduces the oil extraction tax rate from 6.5% to 4.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of HB 1234 removes the automatic exemption for high producing wells drilled in stripper properties and requires these wells to individually produce at stripper levels before receiving the oil extraction tax exemption. This automatic exemption is removed for wells drilled in the Bakken and Three Forks formation.

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, HB 1234 is expected to result in a reduction in the oil extraction tax rate of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $240 million in the 2013-15 biennium. The closing of the stripper loophole for Bakken and Three Forks formation stripper properties is expected to increase oil extraction tax revenues by an estimated $84 million in the 2013-15 biennium. Therefore, HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $156 million in the 2013-15 biennium. The funds affected include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust, and Strategic Investment and Improvements 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: 02/01/2013

13.0225.02008
Title.03000

Prepared by the Legislative Council staff for
Senator Cook
April 3, 2013

3/4/13
TD

1 of 15

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01 and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

<u>Withholding requirement for oil and gas royalty payments to nonresidents.</u>

<u>1. For purposes of this section:</u>

a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

b. "Remitter" means any person who distributes royalty payments to royalty owners.

c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed

by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.

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. "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 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. "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 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.

8. "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.

9. "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. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, after June 30, 2013, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and forty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

11. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before July 1, 2013, on 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.~~12. "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.~~13. "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 5. 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, 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 or individual stripper well.

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:

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(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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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, and before July 1, 2015, 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.

10. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed

outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 6. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 7. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

SECTION 8. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

Date: 4-4-13
Roll Call Vote #: 1

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1234

Senate Finance & Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 13.0225.02008

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

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Senator Oehlke Seconded By Senator Burckhard

Senators	Yes	No	Senator	Yes	No
Chariman Dwight Cook	X		Senator Jim Dotzenrod	X	
Vice Chairman Tom Campbell	X		Senator Connie Triplett		
Senator Joe Miller	X				
Senator Dave Oehlke	X				
Senator Randy Burckhard	X				

Total (Yes) 6 No 0

Absent 1

Floor Assignment

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

Date: 4-4-13
Roll Call Vote #: 2

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1234

Senate Finance & 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 Dotzenrod Seconded By

Senators	Yes	No	Senator	Yes	No
Chariman Dwight Cook			Senator Jim Dotzenrod		
Vice Chairman Tom Campbell			Senator Connie Triplett		
Senator Joe Miller					
Senator Dave Oehlke					
Senator Randy Burckhard					

Total (Yes) No

Absent

Floor Assignment

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

motion to amend the amendment changing 40 barrels to 30 barrels.

Motion failed due to lack of Second

Date: 4-4-13
Roll Call Vote #: 3

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1234

Senate Finance & 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 Oehlke Seconded By Senator Campbell

Senators	Yes	No	Senator	Yes	No
Chariman Dwight Cook	X		Senator Jim Dotzenrod	X	
Vice Chairman Tom Campbell	X		Senator Connie Triplett	X	
Senator Joe Miller	X				
Senator Dave Oehlke	X				
Senator Randy Burckhard	X				

Total (Yes) 7 No 0

Absent 0

Floor Assignment Senator Cook

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

REPORT OF STANDING COMMITTEE

HB 1234, as engrossed: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** and **BE REREFERRED** to the **Appropriations Committee** (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1234 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 create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01 and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

<u>Withholding requirement for oil and gas royalty payments to nonresidents.</u>

<u>1.</u> <u>For purposes of this section:</u>

<u>a.</u> <u>"Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.</u>

b. "Remitter" means any person who distributes royalty payments to royalty owners.

c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.

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. "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 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. "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 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.

8. "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.

9. "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. <u>"Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, after June 30, 2013, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and forty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.</u>

11. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before July 1, 2013, on 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.~~12. "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.~~13. "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 5. 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, 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 or individual stripper well.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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, and before July 1, 2015, 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.

10. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 6. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property <u>or individual stripper well</u> 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 or stripper well's qualification period.

SECTION 7. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

SECTION 8. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

2013 SENATE APPROPRIATIONS

HB 1234

2013 SENATE STANDING COMMITTEE MINUTES

Senate Appropriations Committee
Harvest Room, State Capitol

HB 1234
04-10-2013
Job # 21060

☐ Conference Committee

Committee Clerk Signature	Alice Delzer

Explanation or reason for introduction of bill/resolution:

A BILL relating to oil extraction tax rates and exemptions

Minutes: See attached testimony.

Chairman Holmberg called the committee to order on Wednesday, April 10, 2013 at 9:00 am in regards to HB 1234. Roll call was taken. All committee members were present.

Becky J. Keller - Legislative Council
Sheila Peterson - OMB

Chairman Holmberg we have our final bill of the session. The committee members are familiar with the bill. We are going to ask for a brief description of the bill what it does in regards to the stripper wells.

Fred Fox, Vice Chairman of the Three Affiliated Tribes testified in favor of HB 1234 and provided Testimony attached # 1 with attachment entitled "Summary of Tax Revenues and Disbursements July 1, 2008 through March 31, 2013" He is asking for passing of this bill concerning the Three Affiliated Tribes, an amendment where both the state and tribe share equally in the oil and gas revenues generated on the fort Berthold Reservation. Further we support the suspension of the current extraction tax holiday that applies to reservation lands. Finally we support a stable and consistent tax structure to encourage the further development of our intertwined economies and our individual governments. (9.03)

Ron Ness, President of the ND Petroleum Council: Provided Testimony attached # 2. Here today representing our own gas industry but in addition specifically the ten oil and gas companies that do business in the Baaken on the reservation. We stand in support of the Tribal amendment provisions. By the way, the legislative leaders, all 4 of them, the governor's office and the leaders of the Tribal Council and tribal chairman have been working on essentially since the middle of January. In 2007, when this body passed the bill that really brought this agreement in play late in the session. Prior to that it had been 27 years since an oil well had been drilled on tribal lands. Today, the Three Affiliated Tribes represents about 20% of North Dakota's Baaken production. If you take 20% out of those 40,000 jobs that are directly impacted by the industry, directly working for the industry that's

8000 jobs. It is a substantial economic driver to the state of ND and has been a tremendous economic benefit. I think the question before you today is Why should we do this? What's in this for us? The issue really is that there has been substantial benefits not only to our friends on the Three Affiliated Tribes, the creation of jobs, the economic development that wasn't there before 2007. We negotiated this deal to insure that we create a stable business climate which would attract activity and today is the day we come with a new proposal for you to create a fair playing field going forward. What you have before you is a bill that increases the tax on industry, by this particular part, it increases the tax by eliminating the oil tax extraction tax exemption of 5 years or 60 months on fee lands, generates $87M over the next two years. If you look at what industry is here asking you to do today is to essentially, increase the tax on the industry, and split it in all of the revenues going forward. We are not particularly thrilled with HB 1234 in it's current form. We have come to accept the bill that was agreed upon in the Senate Finance and Tax committee, but this is an important element in this bill. The 10 companies that I talk about and the reason we are willing to do this today, is because they estimate, they are spending between $75 and $100M a year on additional costs, fees, road work, all those costs that they are having to support those tribal roads, those tribal communities. The same things you heard about yesterday in House Bill 13 apply on the reservation. If you look at the Great Plains Transportation Institute and you talk to Denver Toliver, he would tell you the worst roads in the oil patch are on the Three Affiliated Tribes. The tribes have essentially got no help from the BIA, they have relied heavily on the industry to maintain and help support those roads and the additional costs and fees are in jeopardy of driving industry off the reservation. If the tribal council determines that this agreement is not fair and they impose their own tax, the State of ND will likely lose. We are debating over about $720M today. If you look at senator Wardner's spread sheet, if you don't drill the wells you're just fighting over less money. So this is not a big cost for the state of ND. This is a win/win because the tribe wants to see the continued activity, it's good for their economy but it comes with challenges, we all know that. And the same challenges apply on the reservation as they do across the rest of the Baaken community and we strongly support this. We have spent the last two years meeting with the tribal council, this is the solution, they have wanted us to pony up substantial amount of money into their road funds. We have provided equipment, we have done road work, but the answer is making sure they are satisfied with the agreement and I am hopeful that the Senate will see it that way as well. We feel so strongly about this that we're willing to make changes to the tax code, and have you split 50/50 split on tribal lands and fee lands. I think going forward is fair. It helps address those needs as needed. (14.10)

Senator Warner: Do you have a sense that where you had prior agreements with the tribe you can back off some of the fees if this goes through?

Mr. Ness: There was a version of a bill I worked on last fall that said essentially trying to back you off some of those additional fees but I think through the spirit of the agreement and finding something that we can agree with the tribal leaders on that we certainly hope that will be the case. And you come back every two years, if that's not the case, that's something we will look at in the future. (14.51)

Senator Warner: I think we both agree that tribes are sovereign entities and it's not the business of the legislature to dictate tribal policy. We would hope they would see that this act of good will to be moved in that direction.

Mr. Ness: Fred Fox has been absolutely a key part of this since day one, before the first bill passed and his run with the Tribal Energy Council, he can share that message back to the tribal leaders. (15.26)

Joshua Ruffo, Enerplus Resources, a Canadian Oil and Gas Company, testified in favor of HB 1234. We have 74,000 acres on Fort Berthold, currently producing 79 wells. We've been producing since 2010. About 14% of the overall Enerplus production company wide comes from ft. Berthold. Nearly half of our capital investment for 2013 will be dedicated to all Fort Berthold projects. We have 2 rigs running now we expect to drill 22 new wells this year on trust lands. We employ a growing work force of employees, many of whom are both members of Fort Berthold and the surrounding areas. Enerplus is an active supporter in the community of Mandaree and we feel Fort Berthold is an important part to Enerplus for 2013 and beyond as our company grows. We recognize the impact development has had on Fort Berthold, especially on roads. We were the first company to agree to terms with the Three Affiliated Tribes on BI30. We actually adopted the road and we have spent our own money to enhance it and put dust control down, Enerplus is leaning upward to provide an alternate route around the town of Mandaree to take traffic off of certain roads. That's currently in the environmental process. We will help maintain gravel roads, dust control efforts, working that right now with all the other operators. However, road maintenance, the operators is not a long term solution, but an equitable share of the tax revenue for the tribe is. Enerplus shares the concerns in the industry and the tribe over the tax policy that is very uncertain right now. (17.40)

Jim Glenn, HALCON Resources, out of Denver, here to support the bill. We are a new entry into the reservation and Affiliated Tribes. I worked the Williston basin for 35 years, and have never worked on the reservation before HALCON is currently operating 6 rigs on the reservation, that's essentially $50M a month that we are spending on the reservation. We see that stability is the question here and we have to have stability to continue that kind of operation. We are going in front of the Industrial Commission to get approval for drilling 12 wells so this activity, we plan, will continue if stability is determined here by this passing of tax bills. We are here in support of this bill. We see instability with the BIA and the BIM the EPA, Air, Water, everyplace else and you have the control to stabilize the tax situation by passing this bill. With this kind of investment we are in strong support of the tribe and this tax effort to stabilize and continue our development on the reservation. (19.32)

Chairman Holmberg: Anyone else to testify? Seeing none we will close the hearing on 1234.

2013 SENATE STANDING COMMITTEE MINUTES

Senate Appropriations Committee
Harvest Room, State Capitol

HB 1234
April 11, 2013
Job # 21119

☐ Conference Committee

Committee Clerk Signature Rose Laning

Explanation or reason for introduction of bill/resolution:

A bill relating to income tax withholding for oil and gas royalties

Minutes:

Legislative Council - Sheila M. Sandness
OMB - Laney Herauf

Chairman Holmberg opened the discussion on HB 1234. All committee members were present. The date of the fiscal note is 4-5-13.

Senator Wardner offered and explained amendment 13.0225.02010. This amendment is a statement on reporting and what the money is going to be used for on the reservation. The 3 affiliated tribes must report annually to the budget section of the legislative management and must inform the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry. I think it's a good opportunity for legislators and members of Fort Berthold to get together and talk about the issues out there. I think this is a good amendment.

Senator Carlisle: Are you comfortable with annually or should it be biannually,

Senator Wardner: I was not involved in the crafting of this language but it was agreed on by the two parties. All we are doing is providing the parameters.

Senator Mathern: Who of the three affiliated tribes approved this amendment?

Senator Wardner: There are at least 5 council members here that were involved. Fred Fox is in the room and could answer that question.

Senator Mathern: I'd like to be assured that the tribe has seen and has approved this amendment.

Fred Fox, Councilman, Three Affiliated Tribe: There are 7 council members, 5 members have approved of this measure. We passed it 6-1 in council.

Senator Carlisle moved amendment 13.0225.02010.

Senator Krebsbach seconded

Voice vote carried.

Vice Chairman Bowman moved **Do Pass as Amended** on HB 1234.

Senator Robinson seconded

A roll call vote: Yea: 13 Nay: 0 Absent: 0

The bill goes to Finance & Tax and Senator Cook will carry the bill on the floor.

13.0225.03000

FISCAL NOTE
Requested by Legislative Council
04/05/2013

Amendment to: HB 1234

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			$4,200,000	$61,900,000		
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).*

Bill expands the prod. level for qual. stripper wells, eliminates stripper properties, allows withhold. on nonres. royalty pymts, creates incent. for wells outside the Bakken, repeals holiday. for drilling on Ind. lands, and modifies the revenue sharing agreement.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 40 BOPD and closes another loophole by eliminating stripper tax treatment for new wells drilled in existing stripper properties. Section 5 creates an incentive for wells drilled outside the Bakken and Three Forks formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 7 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, engrossed HB 1234 with Senate Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 40 BOPD is expected to reduce oil extraction tax revenues a modest $14 million in the 2013-15 biennium, growing significantly in future biennia as the wave of Bakken wells reach 40 BOPD and achieve stripper exemption status years earlier than current law. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $35.4 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 7 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil extraction tax "buckets". Section 7 also authorizes the redistribution of

an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribe under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net additional oil extraction tax revenue which is distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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: 04/09/2013

FISCAL NOTE
Requested by Legislative Council
02/22/2013

Revised
Amendment to: HB 1234

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				$(42,900,000)		
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).*

Engrossed HB 1234 reduces the oil extraction tax rate on new production on a graduated basis if specified production levels are met. The bill also expands the definition of stripper wells, and eliminates stripper properties in the Bakken and Three Forks formations.

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.*

Section 4 of engrossed HB 1234 reduces the oil extraction tax rate on new production from 6.5% to 5.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of engrossed HB 1234 expands the definition of stripper well for wells drilled in the Bakken and Three Forks formation to 50 barrels of oil produced each day. It also closes the stripper property loophole for wells drilled in the Bakken and Three Forks formations. Section 5 of engrossed HB 1234 creates a new category of re-worked stripper wells and authorizes special tax treatment.

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, engrossed HB 1234 is expected to result in a reduction in the oil extraction tax rate for new production in the biennium of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $100.4 million in the 2013-15 biennium. The expansion of the stripper exemption to 50 BOPD for qualifying wells within the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $26.7 million in the 2013-15 biennium. The stripper property "fix" is expected to increase revenues by an estimated $84.2 million in the 2013-15 biennium. The re-worked stripper provisions contained in Section 5 may have a slight positive impact, but it cannot be estimated because the number of wells in stripper properties and might be re-worked is unknown. Except for the provisions contained in Section 5, engrossed HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $42.9 million in the 2013-15 biennium. The funds affected by this revenue reduction include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools

Trust, and Strategic Investment and Improvements Funds. (Note: The 2/26/2013 version of this fiscal note did not include the positive revenue associated with the "stripper fix".)

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: 03/18/2013

FISCAL NOTE
Requested by Legislative Council
01/15/2013

Bill/Resolution No.: HB 1234

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				$(156,000,000)		
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 1234 reduces the oil extraction tax rate on a graduated basis if specified production levels are met. The bill also removes an exemption for higher producing wells in stripper properties within the Bakken and Three Forks formation.

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.*

Section 2 of HB 1234 reduces the oil extraction tax rate from 6.5% to 4.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of HB 1234 removes the automatic exemption for high producing wells drilled in stripper properties and requires these wells to individually produce at stripper levels before receiving the oil extraction tax exemption. This automatic exemption is removed for wells drilled in the Bakken and Three Forks formation.

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, HB 1234 is expected to result in a reduction in the oil extraction tax rate of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $240 million in the 2013-15 biennium. The closing of the stripper loophole for Bakken and Three Forks formation stripper properties is expected to increase oil extraction tax revenues by an estimated $84 million in the 2013-15 biennium. Therefore, HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $156 million in the 2013-15 biennium. The funds affected include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust, and Strategic Investment and Improvements 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: 02/01/2013

13.0225.02010
Title.04000

Prepared by the Legislative Council staff for
Senator Wardner
April 10, 2013

4/11/13
TD

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the amendments adopted by the Senate to Engrossed House Bill No. 1234 as printed on pages 1119-1131 of the Senate Journal be amended as follows:

Page 1131, after line 35, insert:

"12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report, at a minimum, informs the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry."

Renumber accordingly

Date: 4-11-13

Roll Call Vote # 1

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES

BILL/RESOLUTION NO. 1234

Senate Appropriations Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 13.0225.02010

Action Taken ☑ Adopt Amendment ☐ Do Pass as Amended ☐ Do Pass ☐ Do Not Pass

Motion Made By Carlisle Seconded By Krebsbach

Senators	Yes	No	Senator	Yes	No
Chariman Ray Holmberg			Senator Tim Mathern		
Co-Vice Chairman Bill Bowman			Senator David O'Connell		
Co-Vice Chair Tony Grindberg			Senator Larry Robinson		
Senator Ralph Kilzer			Senator John Warner		
Senator Karen Krebsbach					
Senator Robert Erbele					
Senator Terry Wanzek					
Senator Ron Carlisle					
Senator Gary Lee					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

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

Voice Vote. carried

Date: 4-11-13

Roll Call Vote # 2

2013 SENATE STANDING COMMITTEE
ROLL CALL VOTES

BILL/RESOLUTION NO. 1234

Senate Appropriations Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken ☐ Adopt Amendment ☑ Do Pass as Amended ☐ Do Pass ☐ Do Not Pass

Motion Made By Bowman Seconded By Robinson

Senators	Yes	No	Senator	Yes	No
Chariman Ray Holmberg	✓		Senator Tim Mathern	✓	
Co-Vice Chairman Bill Bowman	✓		Senator David O'Connell	✓	
Co-Vice Chair Tony Grindberg	✓		Senator Larry Robinson	✓	
Senator Ralph Kilzer	✓		Senator John Warner	✓	
Senator Karen Krebsbach	✓				
Senator Robert Erbele	✓				
Senator Terry Wanzek	✓				
Senator Ron Carlisle	✓				
Senator Gary Lee	✓				

Total (Yes) 13 No 0

Absent 0

Floor Assignment F+T Cook

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

REPORT OF STANDING COMMITTEE

HB 1234, as engrossed and amended: Appropriations Committee (Sen. Holmberg, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (13 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1234, as amended, was placed on the Sixth order on the calendar.

That the amendments adopted by the Senate to Engrossed House Bill No. 1234 as printed on pages 1119-1131 of the Senate Journal be amended as follows:

Page 1131, after line 35, insert:

"12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report, at a minimum, informs the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry."

Renumber accordingly

2013 CONFERENCE COMMITTEE

HB 1234

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 19, 2013
Job #21313

☒ Conference Committee

Minutes:

Chairman Headland: The bill has changed quite a bit since the House has last seen it. Is there someone from the Senate who would like to explain the changes?

Senator Cook: Reviewed the changes to the bill.

Chairman Headland: You also changed the allowable of daily production to increase to 40 barrels.

Senator Cook: The threshold on the deeper wells went from 30 to 40.

Representative Drovdal: We've addressed about three different stripper well languages; one for Bakken, one for all oil drilling, and one was a look-back. Which stripper provision did you include in the bill? What kind of dollars?

Senator Cook: $104M.

Representative Drovdal: That would be the stripper provision without the look-back?

Senator Cook: Without the look back.

Representative Drovdal: The House did include in this bill taxes based on production levels. We had passed a tax reduction bill, as you did. We need to clarify to make sure we have the correct language. How does the tribal agreement affect the counties and cities on the oil and gas distribution formula?

Senator Cook: I don't believe it does.

Representative Drovdal: The counties will continue to receive the same amount of dollars?

Senator Cook: I believe so.

Representative Drovdal: How does it affect the Legacy Fund?

Senator Cook: That money is not going to be subject to the 30%. We will verify that information on the counties.

Chairman Headland: Would it not be proper that state collected tax run through the proper distribution as it would with any other political subdivision? Wouldn't it be proper that state collected tax dollars flow into the Legacy Fund as well?

Senator Cook: We didn't make any changes. The only thing we changed in the tribal agreement was to eliminate the five year holiday on extraction tax and we changed the formula of how it is distributed. It is now distributed 50/50 between the state and the tribes. I don't believe that money was subject to Legacy Fund deposits in the past and we didn't change that.

Senator Triplett: Maybe you should clarify your question. Are you asking what happens to the money that goes to the tribes? Or is it about what goes to the state?

Chairman Headland: For clarification, I'm asking about the tribes 50% allocation. I'm not clear as to whether the counties receive their allocation or if the 30% goes into the Legacy Fund?

Senator Triplett: I believe, to the extent that it's allocated to the tribe, that it does not flow through the process. There is a difference in quantity, but not in how the process flows the money through. The dollars that the tribes get will be applied to the landscape, which is also part of the counties.

Chairman Headland: If that's the current way it's being done, then that's one thing. But I think in new negotiations, something else could occur. I just want to be clear on how it's occurring today.

Representative Drovdal: The voters of North Dakota put the Legacy Fund in and required 30%. Would you tell me what incentives are in this bill and which have been removed?

Senator Cook: We are creating one new incentive for non-Bakken. The five year holiday that exists today for extraction tax for non-trust land is being eliminated. We have another incentive that is set to expire this June. That's where the extraction tax is reduced if oil hits $55 a barrel. It goes back on if it hits to 70. We're taking that sunset off. It will stay in place.

Representative Drovdal: The trigger for all oil production is still on, but the trigger for the Bakken incentive is off?

Senator Cook: We haven't done any changes with the triggered incentives.

Representative Drovdal: You went from 30 to 40 barrels. Can you tell me the effect that will have in the future of the stripper well classifications?

Senator Cook: You can read that in the fiscal note. I think we will get them to stripper well status probably three to four years sooner. As we worked on this bill, there are things in

here that none of us like. If ever there was an effort to fix a problem with an understanding that we all have to compromise, we did it here.

Representative Drovdal: There is some concern on the House side that we have put a Band-Aid on the stripper problem because we haven't fixed all of the stripper well definitions. By increasing the number of wells going on the stripper status, there is going to be a substantial fiscal note in the future caused by this triple effect. Also, we're talking about a significant tax increase on the industry that's contributing considerably. We've given tax breaks to just about everybody except the industry that's doing us the most good. I would like to see us work on making this close to revenue neutral.

Senator Cook: Going down to 30 would increase the tax on them. I don't like the tax increase either.

Senator Triplett: The tribal piece is an increase on the oil industry. The industry came into the hearing and said they were in agreement with this because they understood the need for additional revenues to get the infrastructure up to speed. The stripper tax reform, I think, is a matter of how you think about it. I don't perceive that as a tax increase because it's closing a loophole.

Representative Drovdal: On the tribal part of it, we are going to split 50/50 with them to help them take care of their needs. I understand there is a $38.5M increase to the tribe on the 50/50 agreement. There's also a change in the incentive of $87M increase, half of that going to the tribes.

Representative Kelsh: One of the things I don't like in this is that there is no annual certification of the stripper wells. I would like to see that at some point down the road.

Senator Cook: We addressed the annual recertification. I think we could talk about that at a future point. We shot for a goal of being revenue neutral. We fell a little short, but the compromise was there and we achieved what we wanted to.

Chairman Headland: I was the bill carrier and one of the things the House needs is a revenue neutral bill. There's a lot in the Senate bill that we like and we need. We will be bringing amendments to further clarify the House's position. Recessed the committee.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 19, 2013
Job #21332

☒ Conference Committee

Committee Clerk Signature

Minutes:

No attachments.

Meeting called to order. Roll taken.

Chairman Headland: The House has indicated to the Senate that any legislation we move forward should go revenue neutral. We are looking at preparing amendments. We're wondering if the Senate has anything they'd want to bring to the table.

Senator Cook: No, we don't. I'm interested to see your amendments. There was conversation made about recertification.

Representative Drovdal: I would like to hear discussion on recertification. Are we talking about recertification of all the wells or just those asking for rework?

Senator Cook: Lynn Helms gave a presentation on the number of stripper wells, where they are, how many are active, etcetera. His comment was that with recertification, he would need FTEs. He said that recertification on all new wells would disqualify about 5% of them. He made a strong point to the committee that recertification is not a big deal, that not a lot of wells would lose stripper status, and it would be a lot of work for his office.

Representative Drovdal: With the 5%, were those wells that had been reworked in order to get the production back up?

Senator Cook: Possibly some were. That led to our discussion where we talked about the re-entry and another horizontal well. That's why we put that amendment on the bill.

Representative Kelsh: The bill the Senate sent to us had an annual recertification clause in there. I'm wondering what the language was on that and if that's what Mr. Helms referred to.

Senator Cook: That was before we had the conversation with Mr. Helms. As we did our due diligence on the bill, we came to the conclusion jointly that recertification was not a necessary policy. You would want to have a conversation with Mr. Helms, not with me.

Representative Drovdal: We are working with Mr. Walstad on an amendment. Before we start writing all these amendments, we'd like to come to more of an understanding. If I bring an amendment in that says that we give the 50% to the tribe and also all other oil and gas producing counties, would you support that amendment?

Senator Cook: No response.

Chairman Headland: Since we don't really have anything new to talk about, and I understand that the process of getting these amendments can be cumbersome and lengthy, why don't we adjourn...

Senator Cook: I would hope that any amendments will be related to 1234 only.

Chairman Headland: I assure you that will be the case.

Senator Cook: If you want to save time drafting amendments, the only way would be if you'd tell us what your amendments are going to do. I don't assume that what you just said will be what your amendments to 1234 are going to do. If you want to have a discussion on it, feel free to explain what it is you're thinking of doing.

Chairman Headland: We are waiting on some information before wanting to share that. I apologize that we haven't gotten it yet. We'll stand adjourned, and we'll try to reschedule as soon as we have an idea, and hopefully we'll bring an amendment.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 20, 2013
Job #21352

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Chairman Headland: Is there any information you would like to talk about?

Senator Cook: The beauty of the bill. I'd make a motion but I don't think it's going to go anywhere.

Chairman Headland: We are working on some amendments but unfortunately they are not ready. I'm not sure what there is for us to discuss. We could talk about some of the principles behind it but we probably wouldn't be able to fully talk about the amendments so we will adjourn until further notice.

Senator Triplett: You kept us in town for this?

Chairman Headland: Unfortunately it happened that way. It wasn't my decision.

Senator Triplett: With all due respect I thought you said yesterday that if it didn't appear the amendments would be ready we wouldn't meet today. Maybe we are owed an explanation anyway?

Chairman Headland: It was indicated to me that when I made that statement the amendments would be ready. However, we viewed them and there were parts missing. I apologize for that.

Senator Triplett: Thank you for the explanation.

Chairman Headland: Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 22, 2013
Job #21377

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Marked up bill 13.0225.02012 (#1) and amendments #2

Chairman Headland: The amendments we were waiting for have arrived.

Representative Drovdal: Distributed a marked up bill and proposed amendments 13.0225.02012. See attachment #1 and 2. We've been working on this bill and the amendments and the weekend has provided more headaches and criticism of where we are at right now. I am deeply concerned this bill in its current form would not get through the House right now. One reason is because it hasn't had a hearing and the representatives haven't heard this. Another concern is there is no money going into the legacy fund off this share we are giving away. There is a concern over the 30-40 barrel which is addressed in this. It is a tax increase from $66M to $80M. I have a couple questions; if this is approved on the reservation does the tax go away and whatever fees the oil companies are going to start paying for are they still going to be paying tariffs? There are 307.75 miles on Fort Berthold Indian Reservation and of those miles 285 are maintained and paid for by Mountrail County and 22.5 miles maintained by BIA. This marked up version of the bill with the amendments eliminates the stripper well and use it at 30 barrels to qualify for a stripper well. It removes all the incentives including the one for the Bakken and the Three Affiliated Tribes. It puts in an incentive for new wildcats or horizontal wells outside the Bakken. It removes triggers. It has the 50-50 split on all taxes on the reservation. It has the reporting requirements the Senate put on. It reduces the extraction tax from 6 ½% to 6% and includes withholding for the non-residents on royalties across the state of North Dakota. I would move the adoption of the amendments if appropriate.

Chairman Headland: Maybe we should go through the bill section by section before we make any motions. In fairness of the Senate we should take a few minutes to review it before we do anything. I think Mr. Walstad should go through this if he is willing.

John Walstad, Legislative Council: Reviewed amendments on the Christmas tree version. The first couple sections in the bill as it came from the House have no changes. Section 3 is new and is the withholding requirement for oil and gas royalties for nonresidents. Section 4 changes the definition of "average price" to "average statewide production" because in the original version there was a need to know the average

statewide production number with regard to rates changes. That is eliminated because there is no triggering of rate changes in here anymore. The next significant change is on page 6 relating to a stripper well and stripper well property definitions. It's important to understand what these would do in this version. The production in the deepest wells has a limit of 30 barrels a day and that returns the 10,000 foot wells to a 30 barrel per day status to attain stripper well treatment. The definition for stripper wells is all new. Initially this related to wells in the Bakken or Three Forks formation and now this distinction is eliminated so that any stripper well to qualify has to meet those per barrel requirements and includes a well that was drilled and completed before July 1, 2013 and which was part of a stripper well property on June 30. This is the grandfathering for stripper wells. After June 30, if those wells are re-drilled or repaired that status can change. In the definition of stripper well property there is new language meaning after July 1, 2013 no more stripper well properties will be added to the list of properties that exist on June 30; it will be individual well basis from that point forward.

Senator Cook: That's not a change, is it?

John Walstad: Not really. We've had different language before when we did that same kind of this and this provides that no more certification of new stripper well properties after June 30.

Senator Cook: Isn't that the way 1234 is right now?

John Walstad: On lines 21-23 the black lettering is in the House version but now that sentence has been added with the additional requirement of re-drill or repair after June 30 to lose that status. Certification of properties was not in the House version. At the end of that definition is new language but not a new discussion point.

Senator Cook: It's not a change in policy.

John Walstad: True. At the bottom of page 7 the oil extraction tax rate section becomes a lot shorter with this change. Line 27 is the end of the section now and would say the rate of the tax is six percent and that would begin to apply for production July 1 and after. The rest of that section is eliminated and that stepladder rate change is eliminated. On page 9 on the exemption provisions the stripper well exemption is re-written somewhat. A well exempt as part of a stripper well property at the time it is re-drilled or repaired retains exempt status as a stripper well or property for the first 12 months of production from that well after completion and after that period that exemption status is lost as of the first day of the next calendar quarter. It is one year plus whatever remains of the calendar quarter at the end of that one year. At that point the stripper well exemption would be lost unless the operator requests and receives recertification from the Industrial Commission that the well's production is not in excess of 30 barrels a day.

Senator Cook: 1234 eliminates stripper well properties and now we are keeping stripper well properties for the sole purpose of this section so if they go into a stripper well property and drill another well it gets stripper well status for one year, regardless of what the production is.

John Walstad: Correct. At that point the exemption would automatically disappear. It was written this way so the Industrial Commission would not have to look at every one of those wells if the operator knows they are getting 600 barrels a day or so they won't apply for recertification at 30 barrels. I think it cuts some paperwork that way. On page 14 this is the oil extraction exemption that applies under current law for wells drilled in the boundaries of an Indian reservation or on property owned by a tribe prior to August 1997. Current law provides a five year exemption but this provision would eliminate that five year exemption under state law but wouldn't eliminate it for wells in place that have qualified for the exemption by June 30. It grandfathers in wells in place or drilled as of June 30 and thereafter a five year exemption would not apply. On top of page 15 it refers to the wildcat provision which is an exemption of 75,000 barrels during the first 18 months for wells outside the Bakken and Three Forks formations and the rate would be 2% instead of 6 percent.

Senator Miller: Do you have any idea what the fiscal change would be in this provision?

Representative Drovdal: This is the bill sent over from the Senate so I'm sure you already have that but I will find it.

Senator Miller: I'm talking about the grandfather for the reservation.

Representative Drovdal: I was under the impression it is what you proposed to us but I will refer back to John Walstad.

John Walstad: This does have a fiscal impact but I don't recall the number.

Senator Miller: I would say it would have a major fiscal effect.

John Walstad: The tax department has completed an analysis of each of the changes so they could run through those numbers for you. Let's go to page 21, this is the provision that relates to the state tribal agreement for oil taxes. The current production agreement and law is required to apply to all wells but this would add the oil extraction to also apply to all wells within a reservation. Currently the extraction tax by agreement will not exceed 6 ½% but this now would not exceed the maximum rate of 6% and the tribal agreement rate is not to exceed that but may be reduced between the governor and the tribes. The most significant change in revenue sharing is on lines 20-26. Production from fee lands is 20% of gross production tax but this would require that the fee land share for the state and the tribes would be based on production tax and extraction tax then the combined tax would be divided evenly between the tribes and the state. That has a fiscal effect which can be reviewed.

Senator Triplett: That language is identical to what was in the Senate version.

John Walstad: It's not new. On page 23 there is a new subsection 12 and the agreement must require that the Three Affiliated Tribes are to report annually to the budget section and that would identify projects totally investment at least 10% of tribal oil and gas gross production and oil extraction tax receipts of the tribe for that year in essential infrastructure.

Senator Triplett: The last one you mentioned is a substantial change from the tribal agreement that the governor and the leadership worked out because it was just a reporting before and now it's a reporting with a substantive requirement in the report.

John Walstad: That is pretty new.

Senator Triplett: It appears there is a substantive change in the tribal agreement.

Representative Drovdal: The request I had was that the language be the same as the senate version so somewhere this has been changed.

Chairman Headland: This is the change that you and I had requested. Mr. Walstad, in the agreement with the tribes on the revenue sharing it's been indicated to us that the current agreement of 80-20 the tribe's portion doesn't contribute to the legacy fund. Our thoughts are that if we are going to give us some of the state's revenue that currently flows into the legacy fund we should have a discussion of adjusting the language so that it would still flow to the legacy fund prior to being distributed to the tribe. That is something still being discussed and could be added to this bill.

John Walstad: That's true. There's nothing in here that would require funds from some state source to be contributed to the legacy fund to reflect the tax revenue collected and allocated to the tribe. The language wouldn't be hard to draft but I think you need to find out from the tax department on the cost because I think it would be very substantial.

Chairman Headland: We will make sure to address that with the tax department.

Representative Drovdal: When I was giving that road report those are the miles on what Mountrail County shows on their part of the reservation. There may be additional roads. McKenzie County wasn't reporting.

Chairman Headland: Meeting adjourned due to time constraints. Next meeting scheduled at 4:00pm this afternoon.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 22, 2013
Job #21409

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes: *Attachment #1.*

Fort Berthold Indian Reservation Boundaries within Mountrail County attachment #1.

Chairman Headland: Again I have to apologize to the committee and attendants. There was a misinterpretation of the amendment and it would change the fiscal impact in a direction that the House would not be interested in. We will have new language drafted.

Senator Miller: Where did this sheet of paper originate from?

Representative Drovdal: That was included in a booklet from the Mountrail County Commission.

Senator Cook: Do you have any idea what you're going to change in the amendments?

Chairman Headland: Yes, I think it will be relative to the rate reduction.

Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 23, 2013
Job #21447

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes: *Attachments #1,2,3*

Representative Drovdal: Distributed amendments 13.0225.02015 and marked up version of the bill. See attachments #1 and 2. Explained amendments. The individual stripper wells are still listed as well as the stripper properties. In section 2 we put the definition of individual stripper wells back in. Section 3 is the withholding on nonresidents which is the same as it came over from the senate. On page 4 there was language taken out of there because of the definition. On page 6 lines 10 the change in the stripper definition in all categories, not just the Bakken and Three Forks formations. On the bottom of page 6 and top of page 7 it defines the stripper well or the well to be drilled included after June 30, 2013 so we're going forward with the stripper well property and saying what a stripper well does to qualify. On page 7 line 18 there is a new effective date of September 30, 2014. On page 8 there is a tax reduction from 6 ½% to 6% on extraction tax and that is effective on all wells on September 30, 2014. Page 9 section 6 starting with line 12 there is an exemption for a re-drilled or repaired stripper well. If they go in and re-work a well that has qualified as a stripper well and on stripper property they will have twelve months production then the Industrial Commission will re-certify it as either stripper or regular well. If it recertifies as a stripper well it will qualify for the 6% exemptions but if it is not it will pay the 11% tax overall. Page 14 and 15 subsection 6 is the incentive drilling for outside the Bakken or the wildcat wells. It is the same that we had for the Bakken earlier. The triggers are taken out of this amendment. On the bottom of page 21 and top of 22 is the agreement between the State of North Dakota and the Three Affiliated Tribes. We left the change as proposed by the senate; 50-50 split on all taxes of revenue from the fees and trust lands in the reservation. On page 23 lines 14-17 there is an agreement of a reporting process that requires they notify us that at least 10% of the money is going to infrastructure.

Chairman Headland: The only change between this amendment and the last amendment you brought forward was the timing of the rate change to make the bill revenue neutral?

Representative Drovdal: The intent was to have a half percent on new production and that turned out to be a half percent on oil production so we changed the date of it going into effect to September 30, 2014.

Chairman Headland: The amendment Mr. Walstad presented to the committee was on all production and this is on all production but it starts at a date that would give the bill a revenue neutral impact?

Representative Drovdal: Yes. It will have a zero impact fiscally by starting September 30.

Senator Triplett: On page 4 you pointed out language was crossed out but didn't explain the reason for it so can you explain that?

Chairman Headland: The average price and all that language is stripped off because that is based on language that would count barrels instead of a time certain. We don't need to look at daily production; it will be on all production which is why that language was struck.

Senator Triplett: On page 6 and 9 there were about three places where drills are re-drilled or repaired. Are you defining anywhere in here what you mean by repaired and how much of a repair would be necessary for it to mean anything?

Representative Drovdal: The language of re-drilled and repaired came from the Industrial Commission.

Senator Triplett: I'm not familiar with the definition so can you tell me what it is?

Representative Drovdal: I don't know exactly what it is but it is reworking the well.

Senator Triplett: When you say re-drill or repair the "or" makes it stand on its own so I think we need to know what we're meaning.

Chairman Headland: We will have that defined by someone for us.

Senator Cook: As I listen to the comments I keep hearing a desire to make this revenue neutral and that is supposed to be the intent of these amendments?

Chairman Headland: I think the House all along has looked at legislation and comments have been made on the floor that we would desire any changes to the oil tax be seen as revenue neutral.

Senator Cook: I see three things done in this legislation that would increase taxes on the oil industry and one thing done that would decrease them. You have a half percent rate reduction on the extraction tax on all oil?

Chairman Headland: That's correct.

Senator Cook: That's worth what?

Chairman Headland: I think Mr. Rauschenberger has that information to present to the committee.

Ryan Rauschenberger, Office of State Tax Commissioner: Distributed a revised fiscal effect. See attachment #3. In front of you is a rough fiscal overview to the amendment. Some of the numbers you've seen before in other bills and some of these numbers are new. The stripper well change is to the positive of $105M and that is for both Bakken and non-Bakken stripper properties and stripper wells extraction tax. The next number is the incentive for outside of the Bakken and that is negative $35.4M oil extraction tax. The tribal sharing change is negative $37.5M and that is a mix of production tax and extraction tax. $35M of that reduction is due to the change in share of the fee production. Currently, 20% goes to the tribe and 80% to the state and that shift to the 50-50 is a negative $35M to gross production tax. Another $2.5M comes from those wells currently benefiting from the 60 month tribal exemption on extraction tax on fee land. When those start coming off this biennium instead of 100% going to the state that will now be split 50-50 based on this amendment and that is $2.5M. Most of the wells aren't five years old so there are only a few that fall into that. The removal of the five year holiday is the prospective change on new wells drilled on fee lands and this is an oil extraction tax with a positive $43.5M. The income tax withholding is a general fund positive of $4.2M. The half percent tax reduction on all production starting October 2014 so everything before is under current law and after would be an $80M negative on oil extraction tax. That comes to a zero amount if you include that general fund amount so the entire bill would have a zero net fiscal note.

Senator Cook: That $80M reflects nine months?

Ryan Rauschenberger: 8 months.

Senator Cook: For a full fiscal year we are looking at $240M?

Ryan Rauschenberger: For a full biennium it's $240M.

Senator Cook: The first five numbers you just reviewed are all in 1234 as it came to us. The only thing that is changed is the $80M. You made three other changes in the bill that would have a tax increase on the oil industry. You've changed 40 barrels to 30 barrels so that is going to be a tax increase. You added a recertification on wells that are re-worked that wasn't in the bill when it came here. You're taking away all the exemptions and we had a $2B fiscal note on that so that is a tremendous tax increase. I don't know how you can call this revenue neutral. It looks like a great big tax increase to me.

Chairman Headland: That's the way it was explained to us but I understand your point.

Ryan Rauschenberger: The reason the 30 barrels isn't taken into account here is because it is current law so we wouldn't score that against another bill or amendment.

Senator Cook: The bill came here at 40 barrels and when we moved the fiscal note from 30-40 it was listed at $14M in this biennium growing significantly in future biennia. It certainly has a fiscal impact.

Ryan Rauschenberger: I can ask Kathy how she scored that and will get back to you. As far as this analysis goes it is from current law.

Chairman Headland: We asked the tax department to provide us with a revenue neutral scenario and that's what we thought we had gotten.

Senator Cook: The recertification of re-worked stripper wells is a change. Can someone give me an idea of the fiscal cost on that?

Ryan Rauschenberger: It all depends on how many are re-worked because it takes an action by a taxpayer. We have no way of knowing the impact.

Senator Cook: It's a tax increase and you can't measure it.

Ryan Rauschenberger: That's correct.

Senator Triplett: We normally request a fiscal impact for the upcoming biennium and the following one also. Has anyone been requested to do a fiscal analysis for the full biennium of 2015-17?

Chairman Headland: We have not made that request.

Senator Triplett: If I make that request can we get that by tomorrow?

Ryan Rauschenberger: We can do our best. There are a lot of moving parts in this.

Representative Drovdal: All fiscal notes are based on current law, not on proposed changes.

Senator Triplett: Senator Cook believes this is a big tax increase to him but I say this looks like a big tax decrease to me.

Chairman Headland: We will let the senate think about the information we gave them and I'm sure they will come with suggestions. Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 24, 2013
Job #21473

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes: *Attachment #1*

Chairman Headland: In our last meeting the tax department was asked to provide a fiscal note that showed the impact of the house amendments into the next biennium.

Ryan Rauschenberger, Office of State Tax Commissioner: Distributed Major Provisions of HB 1234 Amendment, attachment #1. We did some additional analysis you can see on the right side of this handout and made some assumptions with growth in production. With the stripper well property elimination we increased that to $220M for the next biennium because you carry forward the existing $105M for the 2013-15 biennium and you assume there are more wells drilled within that property. The incentive outside the Bakken and Three Forks has somewhat of a carryover effect with the $35.4M from the 2013-15 because some of those wells are drilled later in the biennium and receive the incentive that carries through to the next biennium as well and we assume more wells will be drilled outside the Bakken and Three Forks. Tribal tax sharing change was negative $37.5M and grossed it up to $119.9M including both gross production tax and extraction tax due to the shift from 20% to 50% in the tribe's favor. The removal of the five year holiday on the reservation also increases the next biennium giving our assumptions to be $78M change. We didn't include anything for the $4.2M from the income tax withholding for royalties because that's more of a timing issue and by that biennia it's in the base already and is more of just speeding up the revenues. Finally, the ½% tax reduction on all production goes to $264M in the 2015-17 assuming we go from 830,000 barrels to 850,000 barrels from the 2013-15 biennium and it grows by 10 percent. That brings the whole fiscal note for the bill to negative $142.5M which includes the tribal shift as well.

Senator Cook: The assumptions for the 2013-15 biennium is $80 a barrel oil?

Ryan Rauschenberger: That's correct; $80 a barrel oil and production ranging from 830,000 barrels to 850,000 barrels.

Senator Cook: For the next biennium you left it at $80 barrel oil?

Ryan Rauschenberger: That's correct. We wanted to change as few variables as possible.

Senator Cook: Your production levels are 10% increase?

Ryan Rauschenberger: Ten percent so I think we're looking at 930,000 barrels give or take a couple thousand.

Senator Cook: Isn't it true there are a lot of unknown assumptions that could be made that dials up any number we want down here from a large tax decrease to a large tax increase?

Ryan Rauschenberger: Given all the variables in the bill and actions it will take to make something an increase or a decrease it could go either way. Depending on how much production on the tribal piece occurs on or off the reservation given the 182 rigs that are occurring it could have a shift either way in reality.

Senator Cook: The trigger incentives are what drives our effective tax rate down and when you remove them, depending on the price of oil in the future, that could be up to a $2B tax increase.

Ryan Rauschenberger: Given certain circumstances and if the triggers didn't kick in, given the lower price of oil, it would lock that in and those triggers would not kick in.

Senator Cook: Only four years ago we were an hour away from that happening.

Ryan Rauschenberger: In April of 2009 we were one day away from the triggers kicking in.

Chairman Headland: If we did nothing we could face that same possibility and have quite a dramatic impact on oil tax revenues.

Ryan Rauschenberger: It goes both ways.

Representative Drovdal: Could you tell how much additional revenue will come in to North Dakota in that biennium for that 10% growth in production?

Ryan Rauschenberger: The current biennium forecast is $5.2B so we would assume with everything else constant we are talking about another half billion holding at 11 1/2 percent.

Representative Drovdal: Is that ½ billion dollars $500M more if we leave the tax at 11 ½% or if we leave it at 11 percent?

Ryan Rauschenberger: That would be the 11 ½% so we would add another $520M onto that and that would be holding price constant but growing production.

Representative Drovdal: If we do the half percent reduction our gross additional income from the new production is going to be around $250M.

Ryan Rauschenberger: I would say roughly in that area.

Representative Drovdal: We are splitting with the tribe $37.5M but with reducing the holiday we are also giving $43.5M for a total of $81M. Is that true in the next biennium it would be $119.9M plus $78M for a total of around $200M that the tribe will be able to use for infrastructure needs?

Ryan Rauschenberger: I believe that to be correct. We calculated those numbers earlier in the session when scenarios were being discussed with the tribal shift numbers.

Chairman Headland: With the tribal agreement and the revenue the state already collects a certain percentage of that is deposited to the legacy fund so when the state is going to give up a portion of that revenue it's my understanding that the legacy fund deposit goes away. Have you figured out what that number would be?

Ryan Rauschenberger: Right now we estimate in the 2013-15 biennium the current agreement would be $319M with no law change. With the legacy 30% of that it would be around that plus another $100M.

Chairman Headland: We are at the point where we need to decide what we agree on in the house amendments if there is anything and I believe there are.

Senator Cook: What do you believe there are?

Chairman Headland: To agree on?

Senator Cook: Yes.

Chairman Headland: I believe we agree on the provision to eliminate the stripper status as it currently works and move to the direction of the house with some possible discussion on what that number should be. We have it at 30 barrels and you have it at 40 barrels so I think that is a place to start.

Senator Cook: I don't know if there is anything here that we agree on yet. I think 1234 as it passed the senate dealt with two issues; the stripper property fix and tribal agreement. The position the house brings with the amendments is the third big issue which is the rate reduction along with the removal of the trigger incentives. That is the issue that's been on the table early in the session and was taken off and as far as I'm concerned it is off. I don't know why we would want to go down and have that discussion again over the rate reduction versus the trigger incentives and to what degree the rate reduction should be to make it a fair bill to all that pay the taxes. I would hope that we focus our attention on the two issues that were in 1234 as it left the senate and that is the stripper property fix and the tribal agreement.

Representative Drovdal: When 1234 left the house it had those things in it. Just because the senate decides something doesn't mean that we are automatically on board with it and vice versa too when we get your bills. You may have determined it's off the table but the house had not. I want to review the bill you sent to us. You sent a stripper well over with $105M tax increase which we don't agree with. You sent along a tribal agreement which we had never heard before was split $37.5M with the rest of the state with a tax increase of

$4M which we hadn't seen before. You took off incentives which was another tax increase to oil companies for $87M which we get half of and that's just about $200M increase to an industry that is providing just about 50% of the revenue of the state of North Dakota right now. You remove some incentives because you said they were loopholes but you put an incentive on that is apparently a loophole too because it is worth $35M negative figure. You raised the barrels which was $14M. I've asked why you voted for it and I haven't ever received an answer. I recognize there was a good faith effort on the Three Affiliated Tribes, the governor, and the senator to get together on an agreement but there is something missing there. The house didn't know anything about this and wasn't any part of this agreement but we are part of the legislative body; we are a second branch of the senate. We are asking you to tell us how we can sell this to our people with all the objections on this. I need some answers.

Senator Cook: There were 46 people who voted green for this bill and nobody voted against the bill so that's pretty good information about why we voted for it. We worked very hard on the oil portion of this bill and the stripper fix and we found consensus in the committee. The tribal agreement was added to the bill by the majority leader of the senate. We listened to the arguments and we know there is an issue that we have to deal with and that's the tribal agreement. We can do nothing with the tribal agreement and we can let all the industry that is on the tribe probably pull off. If you want to get the tribal agreement out of here then let's have that discussion on how to get it off if that's the discussion you want to have.

Representative Drovdal: I don't believe I ever mentioned anything about taking the tribal agreement off I just want to understand it. It is quite a hunk of money that is going to the tribe that would have been used by the state. I need to explain that to my floor.

Senator Cook: I can't give you why the agreement ended up the way it did. I didn't negotiate the agreement. There's no use of negotiating with me, you might as well renegotiate with the tribal people that made the agreement. If you want to change the agreement you can offer the changes to it but now you have to renegotiate the agreement.

Chairman Headland: I'm not sure this debate is getting us anywhere. One of the principles the house has indicated they want on any bill on oil tax is to make it somewhere close to revenue neutral. We may need to have a conversation with leadership and see if that is something we want to discuss. We are not really getting anywhere right now.

Representative Drovdal: I haven't seen any amendments from the senate at all to try and move us in any direction. I would invite some suggestions from them in areas we can agree on but it should be at the next meeting or we will have to give up on the whole thing.

Chairman Headland: I think Senator Cook clearly indicated he is not interested in looking at anything we presented. That tells me they are not interested. If I am misreading that statement now is the time to let me know.

Senator Cook: I think I made myself pretty clear in the areas we are not interested in which is the discussion of the rate reduction and the removal of the triggered incentives. If

you want to take that off the table then we can sit here and talk about what is left in the bill and then I think we could find some consensus.

Chairman Headland: Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 24, 2013
Job #21490

☒ Conference Committee

Committee Clerk Signature	Mary Brucker

Minutes:

No attachments.

Senator Cook: There have been a lot of conversations and I think that there is one thing we can all agree on and that is to make this revenue neutral and that should be our goal. So far we have disagreement on what is actually going to make it revenue neutral. I have some ideas to make it revenue neutral but they are not ready yet at this time. I would ask that we adjourn so that I can get this done.

Chairman Headland: Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 25, 2013
Job #21522

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Attachments #1 and amendments #2 and 3

Senator Cook: The amendments I'm working on are not yet done but Senator Triplett has some that we should discuss.

Senator Triplett: Neither of my amendments is in the form I want but we can discuss them and get them in better form. Senator distributed a map of the Bakken formation (#1) and proposed amendments 13.0225.02018 (#2) and explained. If we are talking about doing a non-Bakken incentive that would incentivize work in other counties of the state then we need to define this more tightly and that was my effort.

Senator Cook: My first effort in defining the area that was going to be eligible for this non-Bakken incentive was to find it in counties. We looked at the counties that don't have a lot of Bakken play in it and it is all of them but four. The original definition I had was an incentive for all oil producing counties excluding the largest four oil producing counties. The reason we walked away from that is because it was possible that certain counties would want to get out of it. I understand what you're getting at and I tend to agree with you. It's an issue that we probably need to be very clear at and one way to be clear is to identify it by county boundaries.

Senator Triplett: I'm actually fond of actual facts so the county boundaries are more of a determining factor than where the drilling is already taking place. The idea is we don't want to do anything that is going to further incentivize drilling in the communities that are already overwhelmed.

Chairman Headland: I believe that we would agree to be willing to further and better define what would constitute for this exemption. Do you have another amendment?

Senator Triplett: Offered another amendment 13.0225.02017. See attachment #3. This is a long term study proposal on the theory that Senator Cook has been preaching and that one of his major concerns is the possibility of the triggers going back on and causing a serious loss to the state.

Senator Cook: Like the changes to oil industry practices you are insinuating new technology?

Senator Triplett: Yes. I guess I don't know what I am insinuating entirely; I'm just saying we should get some help in thinking about this because I think inside the legislature there is adequate expertise to get a grip on this. This is to try and find out the old and ineffective in our tax policy. We just do these things without serious understanding of what the implications are.

Representative Drovdal: Oil industry is a big industry in North Dakota so I think the study is probably a good idea. On the language "shall" mean they have to or does it just recommend that they do.

Senator Triplett: In my vocabulary I was trying to tell them to do it. It is all negotiable.

Chairman Headland: Was it your intent to further define this language as well.

Senator Triplett: Yes. This is all I had right now.

Chairman Headland: Senator Cook, do you anticipate your amendments will be ready today or tomorrow?

Senator Cook: I was surprised they weren't ready at the start of this meeting. Mr. Walstad is under a lot of pressure to get amendments done but I'm sure they will be done tomorrow. Eventually we are going to have to get comfortable with the language and combine them.

Representative Kelsh: I have a suggestion on the study and that is to define a process for selecting the consulting firm and whether it would be a bidding process or an interviewing process.

Senator Triplett: Good idea.

Chairman Headland: Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 26, 2013
Job #21540

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes: *Attachment #1*

Chairman Headland: Senators, how are the amendments progressing?

Senator Cook: I just came from John Walstad's office and they are going through the system now.

Senator Triplett: Mr. Walstad is working on my amendments also. Ron Ness came up with the suggestion using both concepts from yesterday in a way that would be easier for people to follow. On the map I handed out yesterday the medium brown colors define existing fields that have been defined by the industrial commission. Mr. Ness recommended using the notion of a defined field then went x number of miles away from that which would be a hard crisp line yet it would be more nuanced than using the county line.

Chairman Headland: I think that would be reasonable.

Representative Drovdal: Have you visited with Lynn Helms about the definition of the Bakken and Three Forks? They are a geographical location so if we have a wildcat it could be below or above the Bakken and Three Forks which could be existing fields because they are horizontal.

Senator Triplett: I understand that perfectly but I think the point of the new non-Bakken exemption is to encourage activity physically away from where the activity is. There is no rational argument anyone could make that we as a state should be incentivizing more activity where our communities are already overwhelmed. If we are going to do an incentive it is to say to try the other roads in the state where there isn't much activity right now.

Representative Kelsh: In looking at this map it looks like a hard defined boundary. I'm not sure where that came from; is it a physical land description or is it a meats and bounds survey that could be used to define it?

Senator Triplett: No apparently not. It's from a geologist's view. It is between the dark lines and the lighter brown that are the actual definitions of fields that have been developed

by the industrial commission. That is why it made sense to me from a legally defensible position.

Chairman Headland: I also crafted an amendment on the language involved in the agreement with the tribe on the ten percent but it is not quite what I had asked for. Distributed proposed amendments 13.0225.02020 (attachment #1). I wanted the word "recommends" but council put the word "encourage" the tribes to put the 10% investment. I also asked for the reporting that may occur to be bi-annual but it was changed from time to time. I don't know if that is something we can work with here and just change some words or if I need to take it back to council. This would be the direction I would go with the language.

Senator Triplett: As it was presented to us in the senate by the majority leader it was presented as a complete package that had been negotiated between the governor's office, leadership of the legislature and leadership of the three affiliated tribes. Has this been vetted past those people?

Chairman Headland: I tried to present it to the leaders in that area but I don't think they've been able to show it to some of the council to see if it would be something agreeable. Hopefully by this afternoon they will.

Representative Drovdal: Have you considered changing the "shall" to "may" in the study.

Senator Triplett: I was counting on you to tell me if I needed to do that or not.

Representative Drovdal: I would like to see "may" on it.

Senator Triplett: If you're not going to do it maybe I will go talk to your leader and ask if I can get some kind of commitment that legislative management will take it really seriously even if I put "may" on it.

Representative Drovdal: As important as oil industry is to us I am pretty sure that it would be selected but if you feel comfortable doing that then that would be fine.

Senator Triplett: I thought you would do that but I can certainly do it before this afternoon's meeting.

Senator Cook: I don't know if it makes a difference but I will be on the study. If you put "shall" it is a reason for somebody to be mad and upset. I think "may" is the right thing but you can do whatever.

Chairman Headland: We will adjourn and hopefully at our next meeting this afternoon we can get some work done.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 26, 2013
Job #21560

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

No attachments.

Chairman Headland: Senator Triplett, have you made any progress?

Senator Triplett: I have. I don't have anything to pass out but we are making progress. I got the proposed changes to Mr. Walstad and he consulted with Lynn Helms and Bruce Hicks at the oil and gas division and they advised him that my understanding of the field was not entirely accurate. Some of the stray wells, individual wells, are named as a field so they suggested that while the idea was good the 20 miles was too much because it would be drawing a 40 mile circle around a single well and that was really the idea. They suggested 10 miles as a more reasonable number so he is working on that. Someone had authorized him to incorporate my amendments in with the group that is being done.

Senator Cook: The final amendments have to be all together. I would suggest that since we are going to be here tomorrow then we can work on amendments and meet on Monday morning and kick this thing out.

Chairman Headland: I agree.

Senator Triplett: Do we have anything to report on the tribal agreement?

Chairman Headland: I haven't had a chance to speak with my leader. I think we are going to try and convince him that it won't work in this bill.

Senator Triplett: Okay.

Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 29, 2013
Job #21596

☐ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes: *Attachments #1, 2*

Chairman Headland: Senator Cook handed out an amendment and I've asked John Walstad to explain the amendments.

John Walstad, Legislative Council: Explained amendments 13.0225.02021. See attachment #1. The triggering of various exemptions and new well rate reductions and such will continue under this bill to remain in place subject to the old trigger. There will be no new stripper well properties created after June 30, 2013. Wells drilled after that date only individual wells can become stripper wells, no more property treatment. However, existing stripper well properties will continue in that status with the exception of it is for a well re-entered and re-completed as a horizontal well and those wells will be allowed a one year grandfather of stripper well status but will then have to be re-certified. If the production from those wells is not less than $35 a barrel they will not be stripper wells, they will then not be subject to the stripper well exemption.

Chairman Headland: Would you clarify that last statement? $35 a barrel or 35 barrels a day?

John Walstad: Thirty-five barrels a day assuming they are Bakken wells 10,000 feet or more in depth. Continued reviewing amendments. Trigger price is set at $55.

Senator Cook: Do you know what the trigger price is today?

John Walstad: $52.40.

Senator Cook: Maybe we should look at changing that to $52.50. We can come back to that.

John Walstad: There is a sentence at the end of section 10, the effective date clause; it says it is not effective unless on July 1, 2013 section 6 of this act becomes effective.

Chairman Headland: Do you want to clarify?

John Walstad: Do you want me to say what it means?

Chairman Headland: I think we all know what that means so let's move on.

John Walstad: Continued reviewing the amendments. The oil extraction tax rate in section 6 of the bill is 6 ½% of gross value for wells drilled and completed before July 1, 2013 then it becomes 6% for wells drilled and completed after June 30, 2013. We have some language about stripper well property where the well is re-entered and recompleted and that has to re-qualify as stripper well, those wells even after recompletion would be subject to the 6 ½% tax permanently because they were originally drilled and completed before July 1, 2013. Section 7 is the exemptions from the oil extraction tax. On page 10 are some changes and is an exemption that has existed for many years and was intended to stimulate drilling on the reservation but in here it is changed to provide that for wells drilled on a reservation that were drilled and completed before July 1, 2013 and qualified for the existing provision of law allowing a five year exemption from the extraction tax that exemption would continue for the balance of the five years that are applicable to that well. However, any well drilled and completed after June 30, 2013 on the reservation is not eligible for this exemption. The wildcat incentive provides rate reduction for the first 75,000 barrels in the first 18 months for a well drilled and completed 10 miles or more outside the Bakken or Three Forks formation.

Chairman Headland: When I'm reading this language now I can see that I've misinterpreted this section. I thought it was a 2% reduction from the 6 ½% but the way I read it now I think it's just setting the rate for this exempt area at 2%, is that correct?

John Walstad: Yes, I believe that is correct.

Senator Cook: That was the intention. It's the same since it was first in here.

John Walstad: Yes, that is what it was patterned after.

Chairman Headland: It may become something different than it is.

John Walstad: Continued reviewing the amendments.

Representative Drovdal: In section 7 am I correct in assuming we are eliminating two incentives; on the reservation and the Bakken/Three Forks formation?

John Walstad: Yes. Continued reviewing the amendments. The tribal agreement is changed to provide the oil production and extraction tax would come into play on fee lands and it would be divided evenly between the state and the tribes.

Senator Cook: On the part of the tribal agreement it had some reporting requirements and I would hope that it was identical to what was passed out in the senate.

John Walstad: I thought was to just be eliminated.

Senator Cook: No, I just wanted to eliminate changes to it.

John Walstad: Oh.

Representative Drovdal: Could you say that again?

Senator Cook: When the tribal agreement portion left the senate there was a reporting requirement and that should stay in.

Chairman Headland: Yes, that needs to stay in. Could the tax department help us through some of the impacts of revenues?

Representative Drovdal: On the wells that are re-entered and recompleted is there a recertification before they qualify on the newer wells?

John Walstad: A well that is on stripper well property that is re-entered and recompleted they would have to be recertified.

Representative Drovdal: No.

John Walstad: They would have to be recertified. The 6 ½% to 6% rate reduction and how it relates to reservation production, if you look at page 15 there is a provision that the state's oil and gas production tax and oil extraction tax must apply to all wells. However in subsection 3 the state's extraction tax may not exceed 6 ½% but may be reduced through a negotiation between the governor and the Three Affiliated Tribes. The agreement that is entered could provide that same 6 ½% or 6% or a provision could be added here to make it clear that would be the rate for reservation production and the same change would apply. In this version that is not there so make a mark on that section if you want an additional change.

Ryan Rauschenberger, Office of State Tax Commissioner: Distributed Major Provisions of HB 1234 (Senate) Amendment attachment #2. The prospective stripper well property provision keeps that $105M. Raising the Bakken/Three Forks stripper barrels per day to 35 barrels was $14M but now is $7M.

Representative Drovdal: In the previous fiscal note I thought it was a negative $14M.

Ryan Rauschenberger: That is a typo and it should be a negative $7M as opposed to $14M. We kept the same numbers for the tribal shifts in production tax and the elimination of the extraction tax and then the splitting of that tax.

Representative Drovdal: This estimate is on the 6 ½% tax?

Ryan Rauschenberger: Yes. Because it is an unknown we base it on the 6 ½ percent. The withholdings on royalties is unchanged. The half percent reduction on new wells drilled after June 30, 2013 would be $10.4M based on prospective rate of drilling 1,800 wells for the next biennium.

Chairman Headland: That would also assume the rate reduction carried through on the reservation land and that would be reduced to 11% overall.

Ryan Rauschenberger: In that provision I would say that is more than likely because so much production is coming from 21 rigs. We look at it as a statewide number but that would also assume across the entire state.

Senator Triplett: You mentioned your assumptions were on 1,800 wells. You meant per year instead of biennium?

Ryan Rauschenberger: That is correct.

Senator Triplett: Can you tell us what number you're using in terms of estimated dollar value per barrel of oil?

Ryan Rauschenberger: It's an $80 North Dakota price. That's the actual value received minus the discounts. I am missing one line which is the wildcat number. We will redo the sheet and make the necessary changes. The original non-Bakken number was based on 2-3 rigs per month and we scored that at $35.4M. Now there are probably 9 or 10 rigs that would fall on this provision which could be a number around $1M.

Chairman Headland: You can email this information out to us as quickly as you can.

Senator Cook: If our goal is to make this revenue neutral then we should look at a January 1, 2014 effective date for sections 5 and 6? I'm looking at the state tax policy and excluding the tribal agreement.

Ryan Rauschenberger: We can get you the right date too because of the delay in the tax month. There is a provision that adds $2.50 to the trigger price that isn't in the bill but is in current law and that would bring it up to $55.00. Under the definition of the price of oil it adds $2.50.

Senator Cook: The other thing we should include is if we want the study that Senator Triplett recommended. Another thing is the definition of the non-Bakken. We need to have a discussion on whether we want to have that incentive available for this new formation that is getting a lot of attention in Bottineau.

Chairman Headland: I believe so. We are going to have a discussion with Lynn Helms and I believe Representative Drovdal has already made that inquiry.

Representative Kelsh: When you revise the fiscal note can you get us for the next biennium as well?

Ryan Rauschenberger: I would be happy too.

Senator Triplett: On the senate side we took out the annual recertification idea and Representative Drovdal's amendment had it back in again. The reason for taking it out was because Lynn Helms told us that it would be an administrative nightmare and would require an extra fte to make it work. The tax department has the software to do it and it wouldn't

add anything to their costs. All they would need from the oil and gas are their sundry reports.

Chairman Headland: Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 29, 2013
Job #21606

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Attachment #1

Senator Cook: I have some proposed changes to the amendments we discussed this morning. The changes are in section 5 with the change of $52.50. I think that if we change the effective date for the reduction in the extraction tax to January 1, 2014 we will have this bill very close to revenue neutral. We are making changes to remove the confusion of the definition of the non-Bakken and Three Forks incentive and hopefully to alleviate concerns on the cost. The way these amendments are the fiscal note of $35M should have been reduced but we have to verify that yet. The other change is on page 15 on the state oil extraction tax and it must apply to oil and gas production on the Fort Berthold reservation. And the study and reporting is going in there just as it was as it passed the senate.

Chairman Headland: It appears that the house can probably agree to this but it is pending on seeing the fiscal implication and making sure the proper language is adhered to in the non-Bakken exemption.

Representative Drovdal: Ryan might have some additional information.

Ryan Rauschenberger, Office of State Tax Office: Distributed attachment Major Provision of HB 1234 (Senate) Amendment. See attachment #1. The wildcat incentive may be half or depending on how restrictive that provision possible could not able to determine because of geographic restrictions as opposed to just pool specific. To make the current biennium revenue neutral you would want to have a January 2014 date but if that was reduced to half that would be sped up a quarter so then you could do the October date. That is more restrictive because you couldn't drill through the Bakken if you have a Bakken field drill a Madison well within a field that already has a Bakken pool definition. It is reasonable not to lower that.

Representative Kelsh: On your previous fiscal note from last week the 2015-17 biennium impact on the half percent reduction was $264M. I'm wondering why it's now $180.6M.

Ryan Rauschenberger: The last time I provided 2015-17 information was on all production and this is still just new. Carry forward the 2013-15 wells that were drilled and have a new reduced rate of 11% and they are still producing but decline in the next biennium and you have new wells coming on so there are a few moving parts there.

Reducing the rate on all production would include the 8,000 wells that are already drilled so this fiscal note doesn't assume there is any rate reduction on the existing 8,500 wells.

Representative Drovdal: The stripper well provision is going to raise $105M, raising the barrel from 30 to 35 will be a loss of $7M, income tax withholding is going to be $7.2 gain, ½% reduction on all production is going to be $100.4M, the wildcat incentive is $35.4M, but the incentive we are removing on the reservation is going to raise $40,100,000 for the state of North Dakota.

Ryan Rauschenberger: In this amendment it would be just a rate reduction on new wells after a date certain, after June 30 in the current version.

Representative Drovdal: You don't have the additional income the state will be getting off eliminating incentives on the reservation on new production.

Ryan Rauschenberger: That's correct.

Representative Drovdal: That is part of the agreement straight for the state. The tribal agreement is separate.

Senator Cook: If you get a fiscal note it will be included and it's also included on the bottom of this report. It's just broken down into parts.

Senator Triplett: We are expecting amendments by 5:30pm?

Chairman Headland: There's not much more to discuss until the amendments are here.

Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 29, 2013
Job #21616

☐ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Chairman Headland: There are no amendments ready.

Senator Cook: They are in the process but they aren't done yet.

Chairman Headland: See you back tomorrow morning.

Meeting adjourned.

2013 HOUSE STANDING COMMITTEE MINUTES

House Finance and Taxation Committee
Fort Totten Room, State Capitol

HB 1234
April 30, 2013
Job #21635

☒ Conference Committee

Committee Clerk Signature Mary Brucker

Minutes:

Attached amendments #1

Representative Drovdal: Distributed amendments 13.0225.02024. See attachment #1.

Chairman Headland: Is this the amendment we looked at before?

Senator Cook: I think that policy is the same with the important policy change is on page 11 which is a four year sunset on the non-Bakken incentive to be completed before July 1, 2017. There is a 6% rate in the stripper well definition. I'm happy with the bill.

Representative Drovdal: Made a motion for Senate to Recede from Senate Amendments and Further Amend.

Senator Cook: Seconded.

Chairman Headland: Any discussion?

Senator Triplett: I wasn't involved in the amendments so could John Walstad explain them to us?

John Walstad, Legislative Council: Reviewed the attached amendments 13.0225.02024. On page 5 on the stripper well and stripper well property definitions language is added that these provisions applied during the time the rate of tax for new wells is six percent. Trigger price is set without the inflator at $52.40 for a full calendar month and it would trigger those dormant reductions and exemptions that are in law but not currently in effect. The definition section has the sunset date on the new wells on reservation lands. The wildcat exemption has a date of July 1, 2017. Anything drilled after that date would not qualify for this exemption but if drilled before that date would continue to have the 75,000 barrels or 18 months. The tribal agreement language is on the last page.

Senator Triplett: Is the language on page 16 the last page of the tribal agreement the same as it left the senate?

John Walstad: It is the same.

Senator Triplett: In an earlier version on page 10 subsection 8 that had been deleted as being superseded by the tribal agreement but it's still in this one so was that intentional?

John Walstad: There's a sunset here. This allows the exemption for wells in place that have qualified prior to this date to keep the five year exemption after that date.

Representative Kelsh: What is the revised fiscal note with this amendment for this biennium and next biennium?

Ryan Rauschenberger, Office of State Tax Commissioner: Right now this current bill with the effective dates in it would be a negative 9.6.

Representative Kelsh: I would like to see that in paper form before we vote.

Chairman Headland: Any of these proposed amendments that have been added to this bill don't change that what you received yesterday.

Representative Kelsh: It would be $27M this biennium and $73M next biennium?

Ryan Rauschenberger: That would be correct.

Senator Triplett: On page 16 section 9 for the study proposal you had all advised me earlier that it should be changed to a "shall consider" but I see that it was not changed so are you comfortable with that language now?

Representative Drovdal: I'm not real comfortable with it but I've had enough and I'm ready to vote. If we go back again I would have it changed.

Senator Triplett: It was just an oversight?

Representative Drovdal: Yes.

Senator Cook: That is an oversight. I recommend changing the two "shall consider" to "may." Then the legislative management "may" obtain the services of an independent consultant.

Chairman Headland: Let's reconsider our actions.

Senator Cook: Withdrew his second.

Representative Drovdal: Withdrew his motion.

Senator Cook: Made a motion for the Senate to Recede from Senate Amendments and Further Amend per .02024 with change on page 16 section 9 changing the "shall consider" to "may consider" and "shall" to "may."

Representative Drovdal: Seconded.

Senator Triplett: On page 15 with the tribal agreement I see in sub 3 of section 8 we're saying the rate must be applied at the rate established under our oil extraction tax chapter. Has the tribe been consulted and do we know if they accept the 6% as opposed to the 6 ½% which they negotiated?

Chairman Headland: They are certainly aware of it and I didn't ask for their approval.

Representative Drovdal: I mentioned it to them but I don't recall if I got an answer or not. I think they had to go back to the tribal council.

Chairman Headland: I thought they would accept state policy.

Senator Triplett: I don't agree with the overall tone of this bill of reducing the oil extraction tax by half percent basically in exchange for the stripper property. The stripper property was a loophole and we are closing a loophole on an existing tax. If we're going to reduce the top rate from 11 ½ down to 11% then it seems to be there should be something else we are exchanging out in terms of more of these triggers going away or more of these exemptions going away. I don't think it's there. The tribal piece needs to be considered on the side separately because it's primarily for the benefit of a different jurisdiction. I will be voting no on this bill and I have other amendments prepared that would have the study and some other pieces but not the tax rate change.

Chairman Headland: You offered an amendment on the floor of the senate chamber that would have reduced the extraction tax by half percent but there's not enough in this version of the bill for you to support that?

Senator Triplett: That's correct.

Representative Drovdal: When we came down here we had $1.6M more revenue than we expected and I don't remember anyone telling me to start raising taxes. The stripper provisions are $105M, the half percent on new production is $100M, plus we are freezing the trigger which could be a gigantic thing and we're taking the incentive away on the Three Affiliated Tribes and the Bakken. I think oil companies are giving up quite a bit in order to get this passed. I think it's a good bill and I'm ready to vote for it.

Senator Triplett: We will agree to disagree on the increase tax piece. I think reasonable people can look at this differently.

Senator Cook: Main street fairness does not touch tax code. It doesn't change one tax; it is simply a collection issue. Here we are actually changing tax code.

Senator Miller: I disagree that this stripper tax is being exploited as a loophole. I think it's largely been used in the intent it was designed and that was to incent new drilling and employ new technologies and extract more oil. I don't believe we have a major abuse problem going on in this state. I don't think we have an abuse problem at all. I'm going to support this but what Senator Triplett said and what I said are not in agreement and I don't follow that logic at all.

Chairman Headland: I am going to support this bill.

ROLL CALL VOTE: 4 YES 2 NO 0 ABSENT

MOTION CARRIED.

Meeting adjourned.

13.0225.05000

FISCAL NOTE
Requested by Legislative Council
05/01/2013

Amendment to: Engrossed HB 1234

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			$4,200,000	$(14,100,000)		
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 1234 First Engrossment with Conference Committee Amendments makes changes to the oil taxes, modifies the revenue sharing agreement with the Three Affiliated Tribes, and imposes withholding on nonresidents royalty payments.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 35 BOPD and eliminates the stripper tax reduction for new wells drilled in existing stripper properties. Section 5 reduces the oil extraction tax rate on new wells to 6%. Section 6 creates a wildcat incentive for new wells drilled outside existing formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 8 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, HB 1234 First Engrossment with Conference Committee Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 35 BOPD is expected to reduce oil extraction tax revenues by an estimated $7 million in the 2013-15 biennium. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The oil extraction tax rate reduction for new wells drilled after July 1, 2013 is expected to reduce oil extraction tax by an estimated $100.4 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $17.7 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 8 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil

extraction tax "buckets". Section 8 also authorizes the redistribution of an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribes under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net reduction in oil extraction tax revenue which reduces revenues distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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: 05/01/2013

13.0225.03000

FISCAL NOTE
Requested by Legislative Council
04/05/2013

Amendment to: HB 1234

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			$4,200,000	$61,900,000		
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).*

Bill expands the prod. level for qual. stripper wells, eliminates stripper properties, allows withhold. on nonres. royalty pymts, creates incent. for wells outside the Bakken, repeals holiday. for drilling on Ind. lands, and modifies the revenue sharing agreement.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 40 BOPD and closes another loophole by eliminating stripper tax treatment for new wells drilled in existing stripper properties. Section 5 creates an incentive for wells drilled outside the Bakken and Three Forks formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 7 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, engrossed HB 1234 with Senate Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 40 BOPD is expected to reduce oil extraction tax revenues a modest $14 million in the 2013-15 biennium, growing significantly in future biennia as the wave of Bakken wells reach 40 BOPD and achieve stripper exemption status years earlier than current law. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $35.4 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 7 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil extraction tax "buckets". Section 7 also authorizes the redistribution of

an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribe under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net additional oil extraction tax revenue which is distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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.*

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Date Prepared: 04/09/2013

FISCAL NOTE
Requested by Legislative Council
02/22/2013

Revised
Amendment to: HB 1234

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				$(42,900,000)		
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).*

Engrossed HB 1234 reduces the oil extraction tax rate on new production on a graduated basis if specified production levels are met. The bill also expands the definition of stripper wells, and eliminates stripper properties in the Bakken and Three Forks formations.

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.*

Section 4 of engrossed HB 1234 reduces the oil extraction tax rate on new production from 6.5% to 5.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of engrossed HB 1234 expands the definition of stripper well for wells drilled in the Bakken and Three Forks formation to 50 barrels of oil produced each day. It also closes the stripper property loophole for wells drilled in the Bakken and Three Forks formations. Section 5 of engrossed HB 1234 creates a new category of re-worked stripper wells and authorizes special tax treatment.

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, engrossed HB 1234 is expected to result in a reduction in the oil extraction tax rate for new production in the biennium of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $100.4 million in the 2013-15 biennium. The expansion of the stripper exemption to 50 BOPD for qualifying wells within the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $26.7 million in the 2013-15 biennium. The stripper property "fix" is expected to increase revenues by an estimated $84.2 million in the 2013-15 biennium. The re-worked stripper provisions contained in Section 5 may have a slight positive impact, but it cannot be estimated because the number of wells in stripper properties and might be re-worked is unknown. Except for the provisions contained in Section 5, engrossed HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $42.9 million in the 2013-15 biennium. The funds affected by this revenue reduction include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools

Trust, and Strategic Investment and Improvements Funds. (Note: The 2/26/2013 version of this fiscal note did not include the positive revenue associated with the "stripper fix".)

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.*

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Date Prepared: 03/18/2013

FISCAL NOTE
Requested by Legislative Council
01/15/2013

Bill/Resolution No.: HB 1234

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				$(156,000,000)		
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 1234 reduces the oil extraction tax rate on a graduated basis if specified production levels are met. The bill also removes an exemption for higher producing wells in stripper properties within the Bakken and Three Forks formation.

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.*

Section 2 of HB 1234 reduces the oil extraction tax rate from 6.5% to 4.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of HB 1234 removes the automatic exemption for high producing wells drilled in stripper properties and requires these wells to individually produce at stripper levels before receiving the oil extraction tax exemption. This automatic exemption is removed for wells drilled in the Bakken and Three Forks formation.

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, HB 1234 is expected to result in a reduction in the oil extraction tax rate of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $240 million in the 2013-15 biennium. The closing of the stripper loophole for Bakken and Three Forks formation stripper properties is expected to increase oil extraction tax revenues by an estimated $84 million in the 2013-15 biennium. Therefore, HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $156 million in the 2013-15 biennium. The funds affected include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust, and Strategic Investment and Improvements 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.*

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Date Prepared: 02/01/2013

Adopted by the Conference Committee

April 30, 2013

YR
4/30/13
1 of 17

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on page 1510 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01, 57-51.1-02, and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions, rates, and exemptions and the state-tribal oil tax agreement; to provide for a study; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

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SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

   c. The United States as trustee for individual Indians;

   d. A publicly traded partnership;

   e. An organization that is exempt from the tax under this chapter; or

   f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

   b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each

partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.~~

~~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.~~3. "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.~~4. "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.~~5. "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 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.~~6. "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 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.

~~8.~~7. "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.

~~9.~~8. "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.~~9. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, during the time the rate of tax for new wells is six percent under section 57-51.1-02, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and thirty-five barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

10. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before the time the rate of tax for new wells is six percent under section 57-51.1-02, on 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~~an average price per barrel for crude oil of less than fifty-two dollars and ~~fifty~~forty cents~~, as indexed for inflation~~for a full calendar month. ~~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~~ The trigger price definition in this subsection is effective only during the time the rate of tax for new wells is six percent under section 57-51.1-02.

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

57-51.1-02. Imposition of oil extraction tax.

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

The rate of tax is six and one-half percent of the gross value at the well of the oil extracted for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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;

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 for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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 6. AMENDMENT. Section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

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57-51.1-03. ~~(Effective through June 30, 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 <u>or individual stripper well</u>.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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~~

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~~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.~~ The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed before July 1, 2017, outside the Bakken and Three Forks formations and ten miles or more outside an established field in which the industrial commission has defined the pool to include the Bakken or Three Forks formation, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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.~~

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(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 7. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 8. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation ~~may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes~~must be applied at the rate established under chapter 57-51.1.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production and oil extraction taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes'

fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report, at a minimum, informs the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry.

SECTION 9. LEGISLATIVE MANAGEMENT STUDY - ANALYSIS OF FUTURE OIL INDUSTRY CHANGES - CONSULTANT ASSISTANCE. The legislative management shall consider studying the likely changes to oil industry practices, production, impacts, and tax policy within the forseeable future. To assist with this study, the legislative management may obtain the services of an independent consultant with demonstrated insight into current and future production advances, including use of carbon dioxide and water or other means of enhancing production; effects of mature production areas on state and local tax policy; future infrastructure needs; and environmental considerations. The objective of the study is development of a legislative vision of appropriate long-term policy issues and revenue and expenditure expectations. The legislative management shall report its findings and recommendations, together with any legislation to implement the recommendations, to the sixty-fourth legislative assembly.

SECTION 10. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

13.0225.05000

FISCAL NOTE
Requested by Legislative Council
05/01/2013

Amendment to: Engrossed HB 1234

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			$4,200,000	$(14,100,000)		
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 1234 First Engrossment with Conference Committee Amendments makes changes to the oil taxes, modifies the revenue sharing agreement with the Three Affiliated Tribes, and imposes withholding on nonresidents royalty payments.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 35 BOPD and eliminates the stripper tax reduction for new wells drilled in existing stripper properties. Section 5 reduces the oil extraction tax rate on new wells to 6%. Section 6 creates a wildcat incentive for new wells drilled outside existing formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 8 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, HB 1234 First Engrossment with Conference Committee Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 35 BOPD is expected to reduce oil extraction tax revenues by an estimated $7 million in the 2013-15 biennium. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The oil extraction tax rate reduction for new wells drilled after July 1, 2013 is expected to reduce oil extraction tax by an estimated $100.4 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $17.7 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 8 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil

extraction tax "buckets". Section 8 also authorizes the redistribution of an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribes under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net reduction in oil extraction tax revenue which reduces revenues distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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: 05/01/2013

13.0225.04000

FISCAL NOTE
Requested by Legislative Council
04/05/2013

Amendment to: HB 1234

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			$4,200,000	$61,900,000		
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).*

Bill expands the prod. level for qual. stripper wells, eliminates stripper properties, allows withhold. on nonres. royalty pymts, creates incent. for wells outside the Bakken, repeals holiday. for drilling on Ind. lands, and modifies the revenue sharing agreement.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 40 BOPD and closes another loophole by eliminating stripper tax treatment for new wells drilled in existing stripper properties. Section 5 creates an incentive for wells drilled outside the Bakken and Three Forks formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 7 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, engrossed HB 1234 with Senate Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 40 BOPD is expected to reduce oil extraction tax revenues a modest $14 million in the 2013-15 biennium, growing significantly in future biennia as the wave of Bakken wells reach 40 BOPD and achieve stripper exemption status years earlier than current law. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $35.4 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 7 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil extraction tax "buckets". Section 7 also authorizes the redistribution of

an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribe under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net additional oil extraction tax revenue which is distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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: 04/09/2013

13.0225.03000

FISCAL NOTE
Requested by Legislative Council
04/05/2013

Amendment to: HB 1234

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			$4,200,000	$61,900,000		
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).*

Bill expands the prod. level for qual. stripper wells, eliminates stripper properties, allows withhold. on nonres. royalty pymts, creates incent. for wells outside the Bakken, repeals holiday. for drilling on Ind. lands, and modifies the revenue sharing agreement.

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.*

Section 3 authorizes income tax withholding on nonresident royalty payments. Section 4 increases the stripper incentive for Bakken wells producing 40 BOPD and closes another loophole by eliminating stripper tax treatment for new wells drilled in existing stripper properties. Section 5 creates an incentive for wells drilled outside the Bakken and Three Forks formations and repeals the existing 60-month oil extraction tax holiday for wells drilled on Indian nontrust lands. Section 7 makes changes to the oil and gas revenue sharing agreement with the Three Affiliated Tribes.

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, engrossed HB 1234 with Senate Amendments is expected to increase state general fund revenues by $4.2 million during the 2013-15 biennium due to a speed-up in individual income tax collections from the withholding on royalty provisions. The expanding of the stripper tax incentive to Bakken wells producing 40 BOPD is expected to reduce oil extraction tax revenues a modest $14 million in the 2013-15 biennium, growing significantly in future biennia as the wave of Bakken wells reach 40 BOPD and achieve stripper exemption status years earlier than current law. The closing of the stripper property loophole is expected to increase oil extraction tax revenues an estimated $105.3 million in the 2013-15 biennium. The incentive for new wells drilled outside the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $35.4 million in the 2013-15 biennium. The repeal of the 60-month Indian lands incentive is expected to increase oil extraction tax revenues by an estimated $87 million in the 2013-15 biennium. Section 7 authorizes the redistribution this additional $87 million 50% to the Tribe, and 50% to the state's oil extraction tax "buckets". Section 7 also authorizes the redistribution of

an additional estimated $37.5 million from the state's "buckets" to the Three Affiliated Tribe under the provisions that change the split to 50% Tribe 50% State. The amount shown as "other funds" in IA is the net additional oil extraction tax revenue which is distributed to Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust and Strategic Investments and Improvement 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: 04/09/2013

FISCAL NOTE
Requested by Legislative Council
02/22/2013

Revised
Amendment to: HB 1234

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				$(42,900,000)		
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).*

Engrossed HB 1234 reduces the oil extraction tax rate on new production on a graduated basis if specified production levels are met. The bill also expands the definition of stripper wells, and eliminates stripper properties in the Bakken and Three Forks formations.

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.*

Section 4 of engrossed HB 1234 reduces the oil extraction tax rate on new production from 6.5% to 5.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of engrossed HB 1234 expands the definition of stripper well for wells drilled in the Bakken and Three Forks formation to 50 barrels of oil produced each day. It also closes the stripper property loophole for wells drilled in the Bakken and Three Forks formations. Section 5 of engrossed HB 1234 creates a new category of re-worked stripper wells and authorizes special tax treatment.

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, engrossed HB 1234 is expected to result in a reduction in the oil extraction tax rate for new production in the biennium of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $100.4 million in the 2013-15 biennium. The expansion of the stripper exemption to 50 BOPD for qualifying wells within the Bakken and Three Forks formations is expected to reduce oil extraction tax revenues by an estimated $26.7 million in the 2013-15 biennium. The stripper property "fix" is expected to increase revenues by an estimated $84.2 million in the 2013-15 biennium. The re-worked stripper provisions contained in Section 5 may have a slight positive impact, but it cannot be estimated because the number of wells in stripper properties and might be re-worked is unknown. Except for the provisions contained in Section 5, engrossed HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $42.9 million in the 2013-15 biennium. The funds affected by this revenue reduction include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools

Trust, and Strategic Investment and Improvements Funds. (Note: The 2/26/2013 version of this fiscal note did not include the positive revenue associated with the "stripper fix".)

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: 03/18/2013

FISCAL NOTE
Requested by Legislative Council
01/15/2013

Bill/Resolution No.: HB 1234

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				$(156,000,000)		
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 1234 reduces the oil extraction tax rate on a graduated basis if specified production levels are met. The bill also removes an exemption for higher producing wells in stripper properties within the Bakken and Three Forks formation.

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.*

Section 2 of HB 1234 reduces the oil extraction tax rate from 6.5% to 4.0% in increments as certain specified production targets are met. According to the official revenue forecast, the oil production level in the 2013-15 biennium would be sufficient to meet the first incremental rate reduction -- from 6.5% to 6%. Section 3 of HB 1234 removes the automatic exemption for high producing wells drilled in stripper properties and requires these wells to individually produce at stripper levels before receiving the oil extraction tax exemption. This automatic exemption is removed for wells drilled in the Bakken and Three Forks formation.

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, HB 1234 is expected to result in a reduction in the oil extraction tax rate of one-half of one percent, from 6.5% to 6.0%. This is expected to reduce oil extraction tax revenues by an estimated $240 million in the 2013-15 biennium. The closing of the stripper loophole for Bakken and Three Forks formation stripper properties is expected to increase oil extraction tax revenues by an estimated $84 million in the 2013-15 biennium. Therefore, HB 1234, if enacted, is expected to reduce oil extraction tax revenues by an estimated $156 million in the 2013-15 biennium. The funds affected include Legacy, Resources Trust, Foundation Aid Stabilization, Common Schools Trust, and Strategic Investment and Improvements 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: 02/01/2013

2013 HOUSE CONFERENCE COMMITTEE ROLL CALL VOTES

Committee: Finance + Tax

Bill/Resolution No. 1234 as (re) engrossed

Date: 4-30-13

Roll Call Vote #: 1

Action Taken

- ☐ HOUSE accede to Senate amendments
- ☐ HOUSE accede to Senate amendments and further amend
- ☐ SENATE recede from Senate amendments
- ☒ SENATE recede from Senate amendments and amend as follows

House/Senate Amendments on HJ/SJ page(s) 1510 --

☐ Unable to agree, recommends that the committee be discharged and a new committee be appointed

((Re) Engrossed) WITHDRAWN was placed on the Seventh order of business on the calendar

Motion Made by: Rep. Drovdal Seconded by: Senator Cook

Representatives	4-29 am	4-29 pm #2	4-30	Yes	No		Senators	4-29 am	4-29 pm #2	4-30	Yes	No
Chairman Headland	✓	✓	✓				Senator Cook	✓	✓	✓		
Rep Drovdal	✓	✓	✓				Senator Miller	✓	✓	✓		
Rep Kelsh	✓	✓	✓				Senator Triplett	✓	✓	✓		

Vote Count Yes: 15th mtg No: Absent:

House Carrier Senate Carrier

LC Number . of amendment

LC Number . of engrossment

Emergency clause added or deleted

Statement of purpose of amendment

2013 HOUSE CONFERENCE COMMITTEE ROLL CALL VOTES

Committee: Finance + Tax

Bill/Resolution No. 1234 as (re) engrossed

Date: 4-30-13

Roll Call Vote #: 1

Action Taken

- ☐ HOUSE accede to Senate amendments
- ☐ HOUSE accede to Senate amendments and further amend
- ☐ SENATE recede from Senate amendments
- ☒ SENATE recede from Senate amendments and amend as follows

House/Senate Amendments on HJ/SJ page(s) 1510 -

☐ Unable to agree, recommends that the committee be discharged and a new committee be appointed

((Re) Engrossed) _____ was placed on the Seventh order of business on the calendar

Motion Made by: Sen. Cook Seconded by: Rep. Drovdal

Representatives	4-30			Yes	No		Senators	4-30			Yes	No
Chair Headland	✓			✓			Senator Cook	✓			✓	
Rep. Drovdal	✓			✓			Sen. Miller	✓			✓	
Rep. Kelsh	✓				✓		Sen. Triplett	✓				✓

Vote Count Yes: 4 No: 2 Absent: 0

House Carrier Rep. Drovdal Senate Carrier _____

LC Number _____ . _____ of amendment

LC Number _____ . _____ of engrossment

Emergency clause added or deleted

Statement of purpose of amendment

amendments .02024
+ amend pg. 16 "shall" changed to "may"

REPORT OF CONFERENCE COMMITTEE

HB 1234, as engrossed: Your conference committee (Sens. Cook, Miller, Triplett and Reps. Headland, Drovdal, S. Kelsh) recommends that the **SENATE RECEDE** from the Senate amendments as printed on HJ page 1510, adopt amendments as follows, and place HB 1234 on the Seventh order:

That the Senate recede from its amendments as printed on page 1510 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01, 57-51.1-02, and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions, rates, and exemptions and the state-tribal oil tax agreement; to provide for a study; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

<u>Withholding requirement for oil and gas royalty payments to nonresidents.</u>

<u>1. For purposes of this section:</u>

a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

b. "Remitter" means any person who distributes royalty payments to royalty owners.

c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to

establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.~~

~~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.~~3. "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.~~4. "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.~~5. "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 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.~~6. "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 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.

~~8.~~7. "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.

~~9.~~8. "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.~~9. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, during the time the rate of tax for new wells is six percent under section 57-51.1-02, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and thirty-five barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

10. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before the time the rate of tax for new wells is six percent under section 57-51.1-02, on 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~~an average price per barrel for crude oil of less than fifty-two dollars and ~~fifty~~forty cents~~, as indexed for inflation~~for a full calendar month. ~~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~~ The trigger price definition in this subsection is effective only during the time the rate of tax for new wells is six percent under section 57-51.1-02.

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

57-51.1-02. Imposition of oil extraction tax.

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

The rate of tax is six and one-half percent of the gross value at the well of the oil extracted for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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;

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 for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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 6. 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, 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 or individual stripper well.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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.~~The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed before July 1, 2017, outside the Bakken and Three Forks formations and ten miles or more outside an established field in which the industrial commission has defined the pool to include the Bakken or Three Forks formation, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 7. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property <u>or individual stripper well</u> 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 <u>or stripper well's</u> qualification period.

SECTION 8. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation ~~may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes~~must be applied at the rate established under chapter 57-51.1.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production and oil extraction taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report, at a minimum, informs the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry.

SECTION 9. LEGISLATIVE MANAGEMENT STUDY - ANALYSIS OF FUTURE OIL INDUSTRY CHANGES - CONSULTANT ASSISTANCE. The legislative management shall consider studying the likely changes to oil industry practices, production, impacts, and tax policy within the forseeable future. To assist with this study, the legislative management may obtain the services of an independent consultant with demonstrated insight into current and future production advances, including use of carbon dioxide and water or other means of enhancing production; effects of mature production areas on state and local tax policy; future infrastructure needs; and environmental considerations. The objective of the study is development of a legislative vision of appropriate long-term policy issues and revenue and expenditure expectations. The legislative management shall report its findings and recommendations, together with any legislation to implement the recommendations, to the sixty-fourth legislative assembly.

SECTION 10. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

Engrossed HB 1234 was placed on the Seventh order of business on the calendar.

2013 TESTIMONY

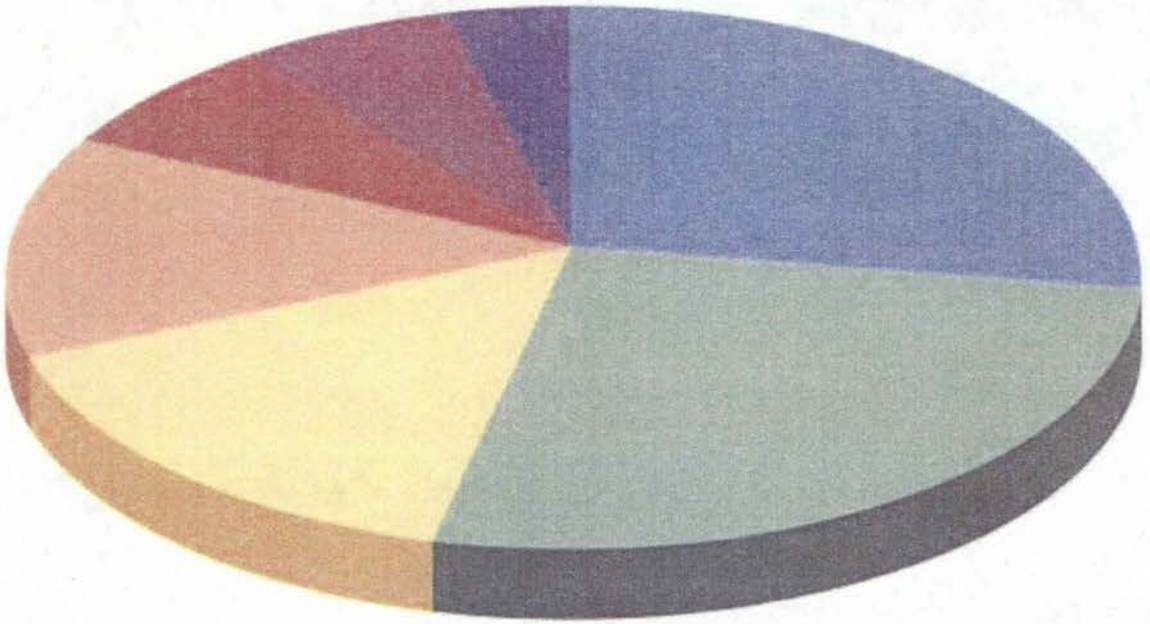
HB 1234

Source: U.S. Energy Information Administration based on data from various published studies. Canada and Mexico plays from ARI.
Updated: May 9, 2011

14

Fig. 1: Oilfield services expenditures in top US shales – 2012

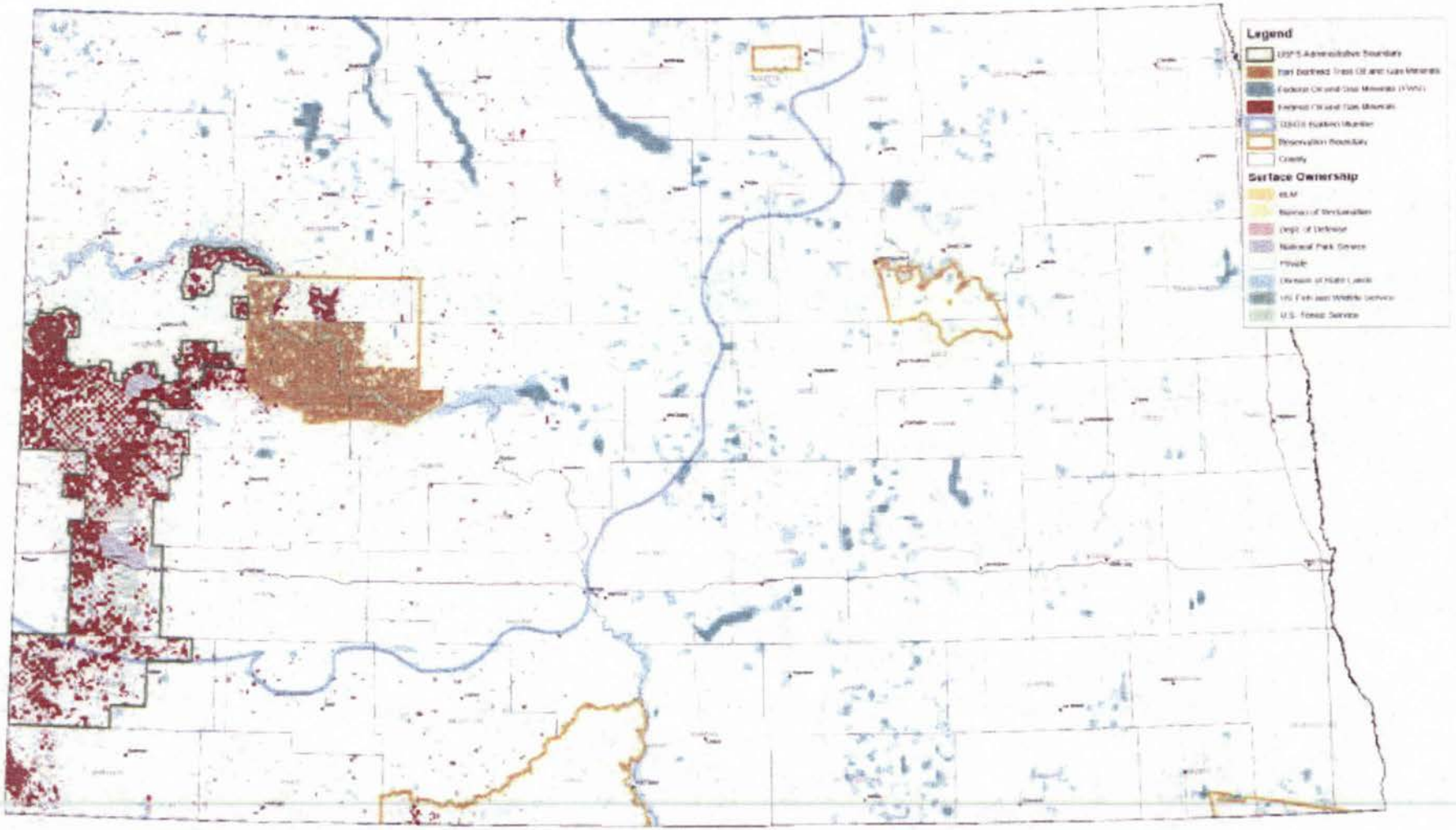
Total - $54.3 billion



- Bakken
- Eagle Ford
- Permian
- Marcellus
- Anadarko-Woodford
- Granite Wash
- Niobrara

OIL&GAS FINANCIAL JOURNAL

e.g. 1#



83% of Bakken spacing units contain some federal minerals

A federal permit is required for a well bore to penetrate those tracts

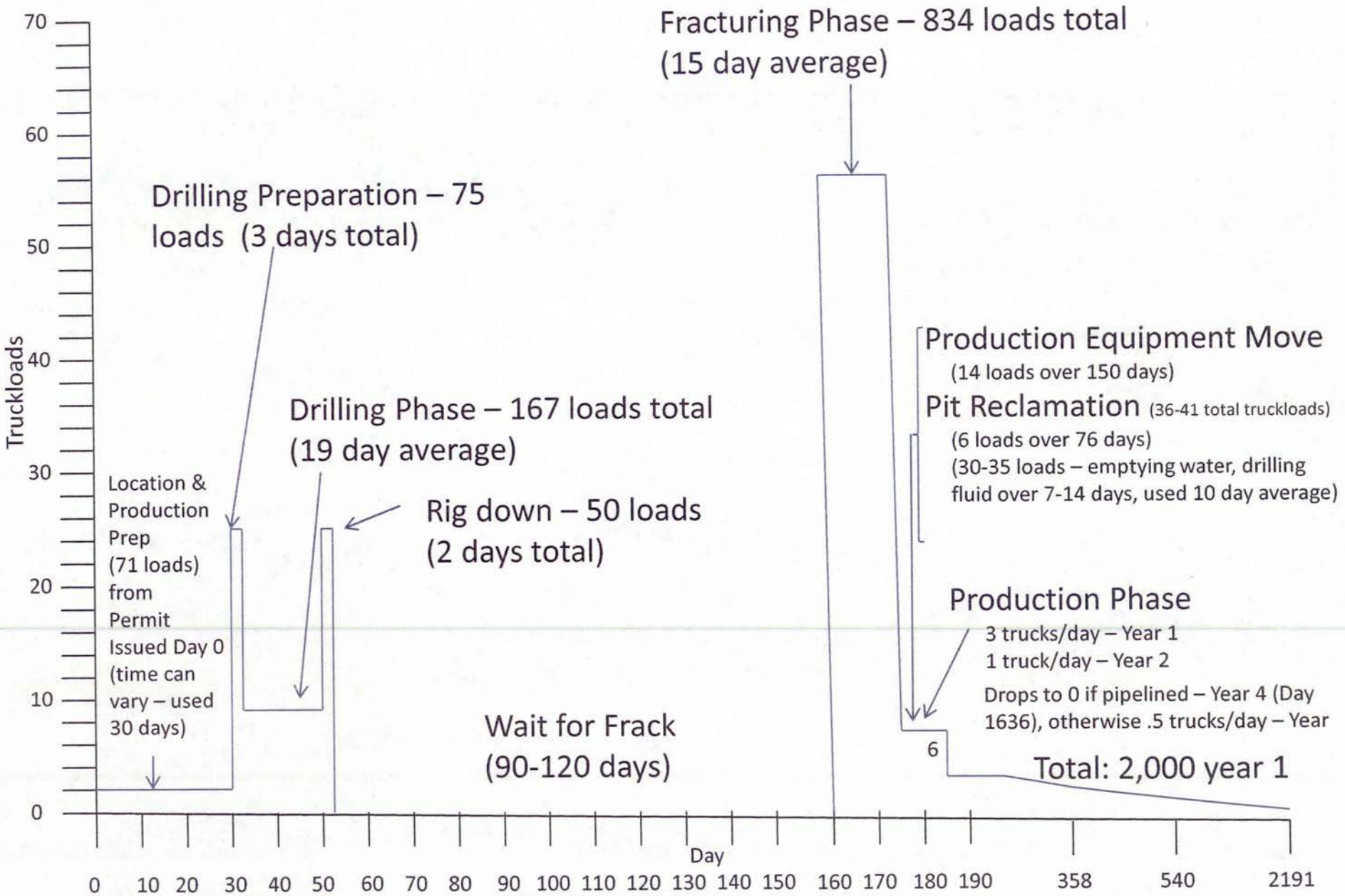
43% of the spacing units contain federal ownership of <25% or 320 acres

50% of the spacing units contain federal ownership of <32%

#1 p.3

New Bakken Well – Truckload Timeline

NDDOT
North Dakota Department of Transportation



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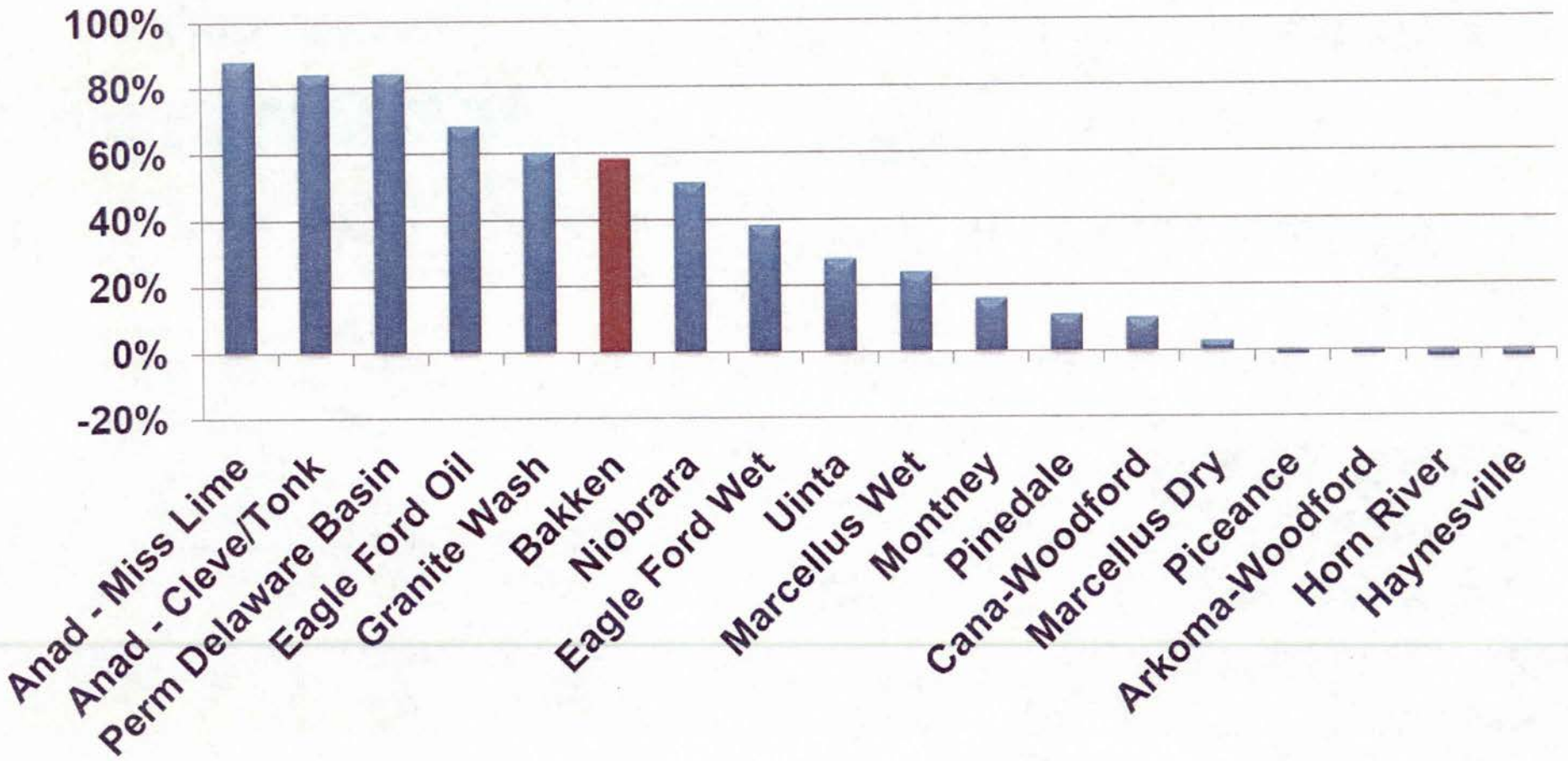
BENTEK Energy LLC

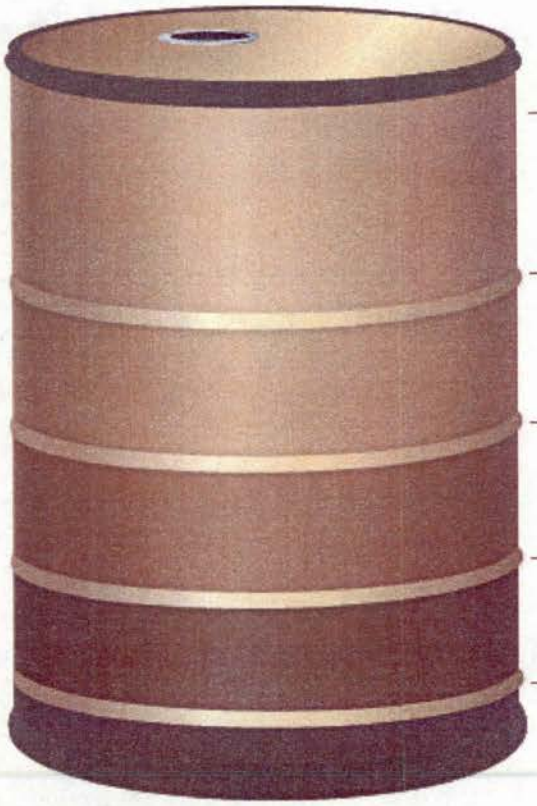
Bakken Earns Above Average Returns



Price Assumptions: *Gas = 12 month forward average curve for each regional pricing point as of June, 2012 (price range $2.45-$2.86/Mcf)*
Oil = 6 month average WTI +/- differential as of June, 2012 (price range $84.40-$100.43/barrel)
NGLs = weighted average $/barrel based on current Mt. Belvieu prices and the typical composition in each region (range $23.79-$45.22/barrel)

Sid #1 p.5

OIL & GAS TAX ALLOCATION



Legacy Fund 33.5%

Statutory Fund 21.4%

Strategic Investments & Improvements Fund; Property Tax Relief Fund; State Disaster Fund; ND Outdoor Heritage Fund; Oil & Gas Research Fund; Energy Conservation Fund; Renewable Energy Development Fund

Constitutional Funds 21.2%

Resources Trust Fund; Common Schools Trust Fund; Foundation Aid Stabilization Fund

Political Subdivisions and Tribes 18%

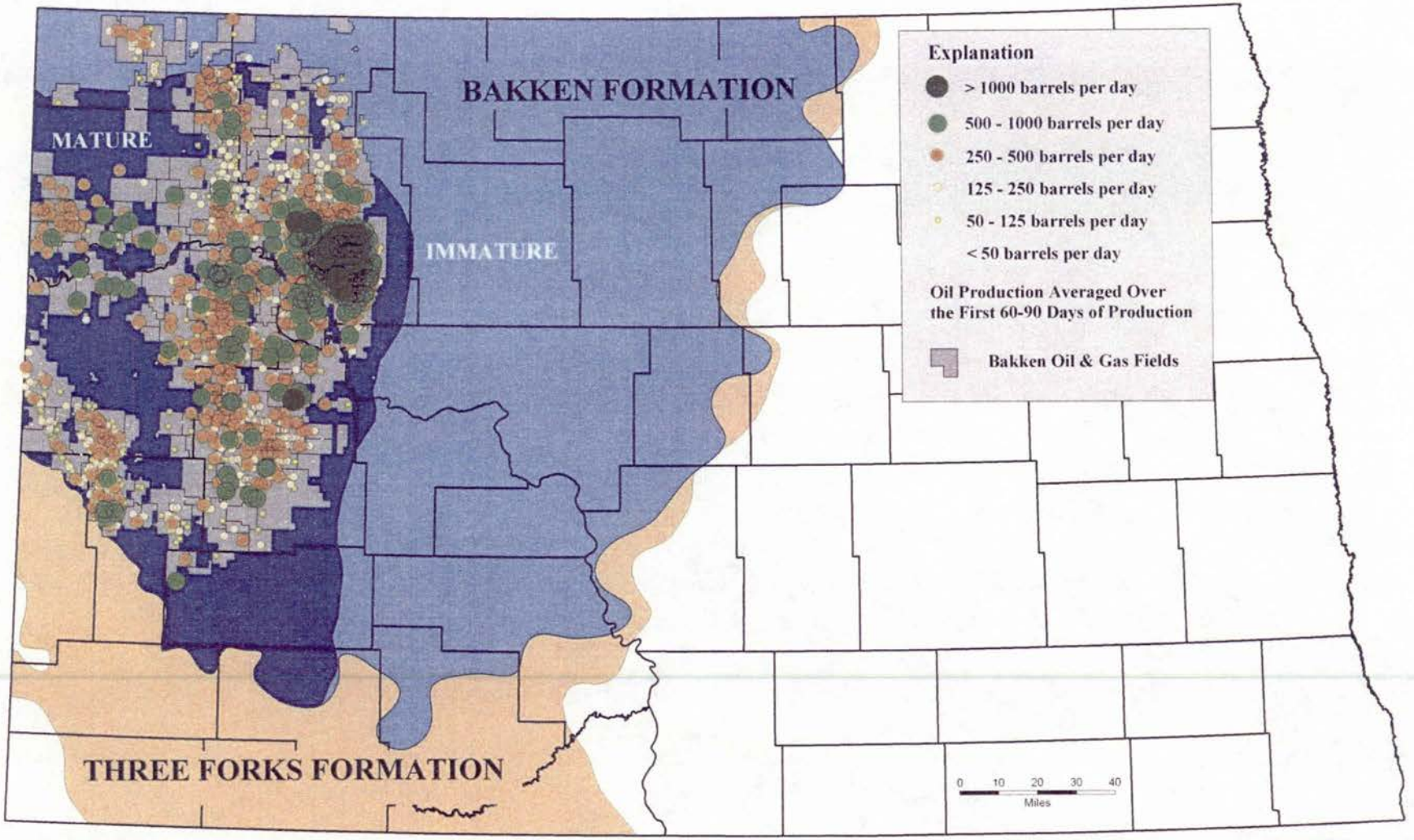
Distributions to Cities & Counties; Oil & Gas Impact Grant Fund; Tribal Allocations

General Fund 5.9%

- **Industry Paid $205 million in production taxes in September 2012**
- **$1.3 billion fiscal year 2011.**

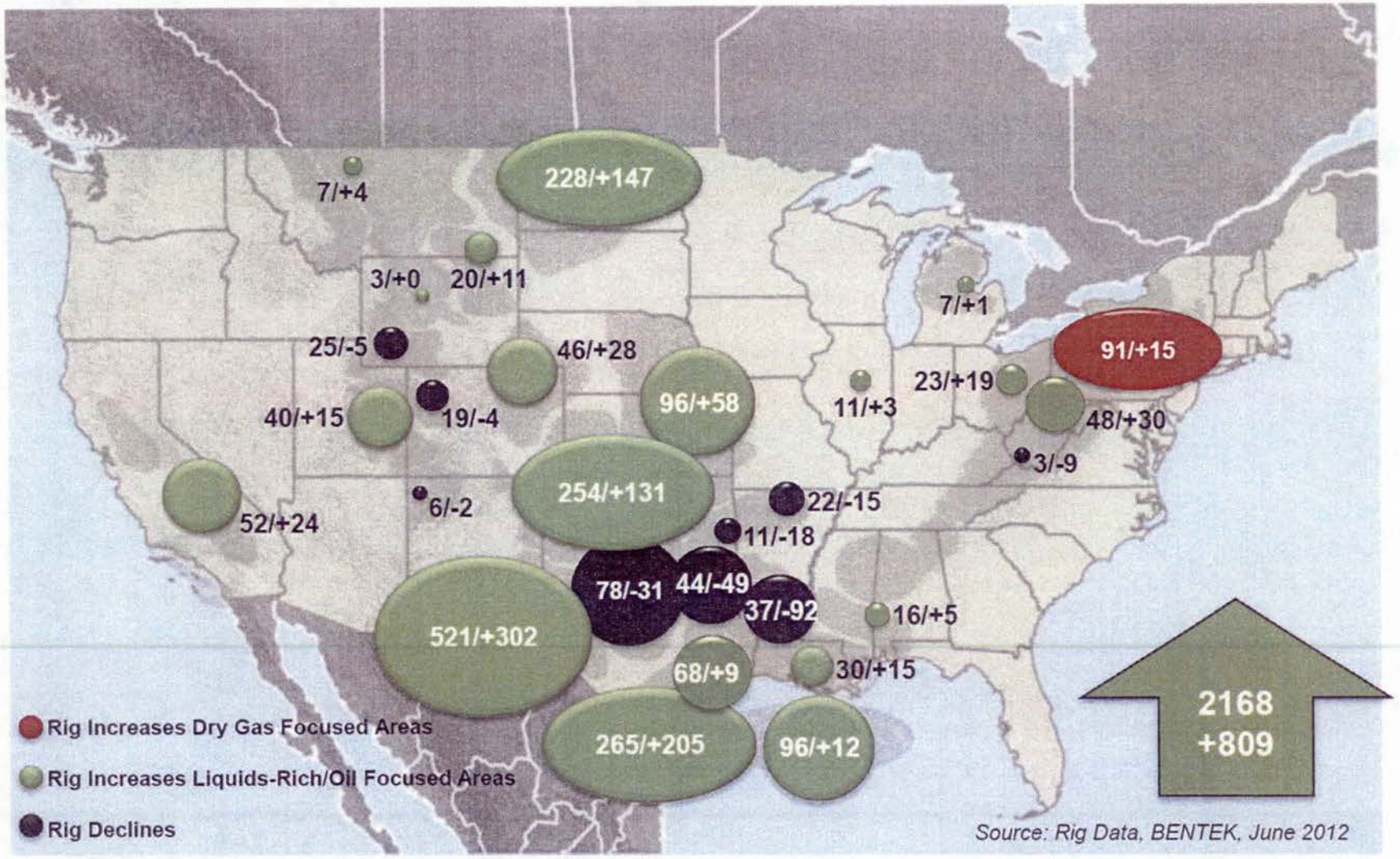
9.d
1#

First 60 - 90 Day Average Bakken Pool Production by Well



BENTEK Energy LLC

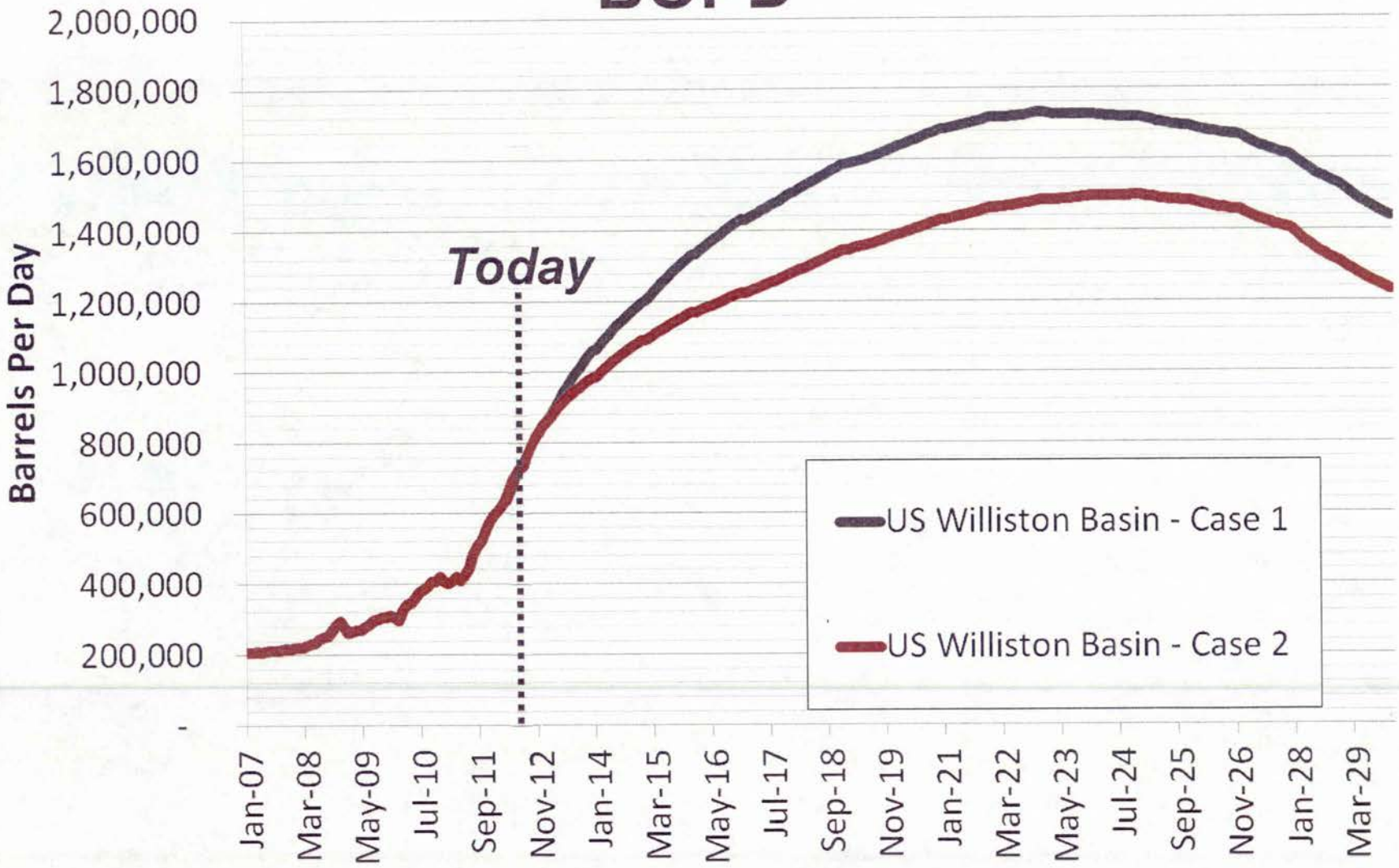
Plays With High Returns Attract Drilling Rigs



Active rig count: June 15, 2012 / Change in rig count from Jan. 1, 2010

8.d 1#

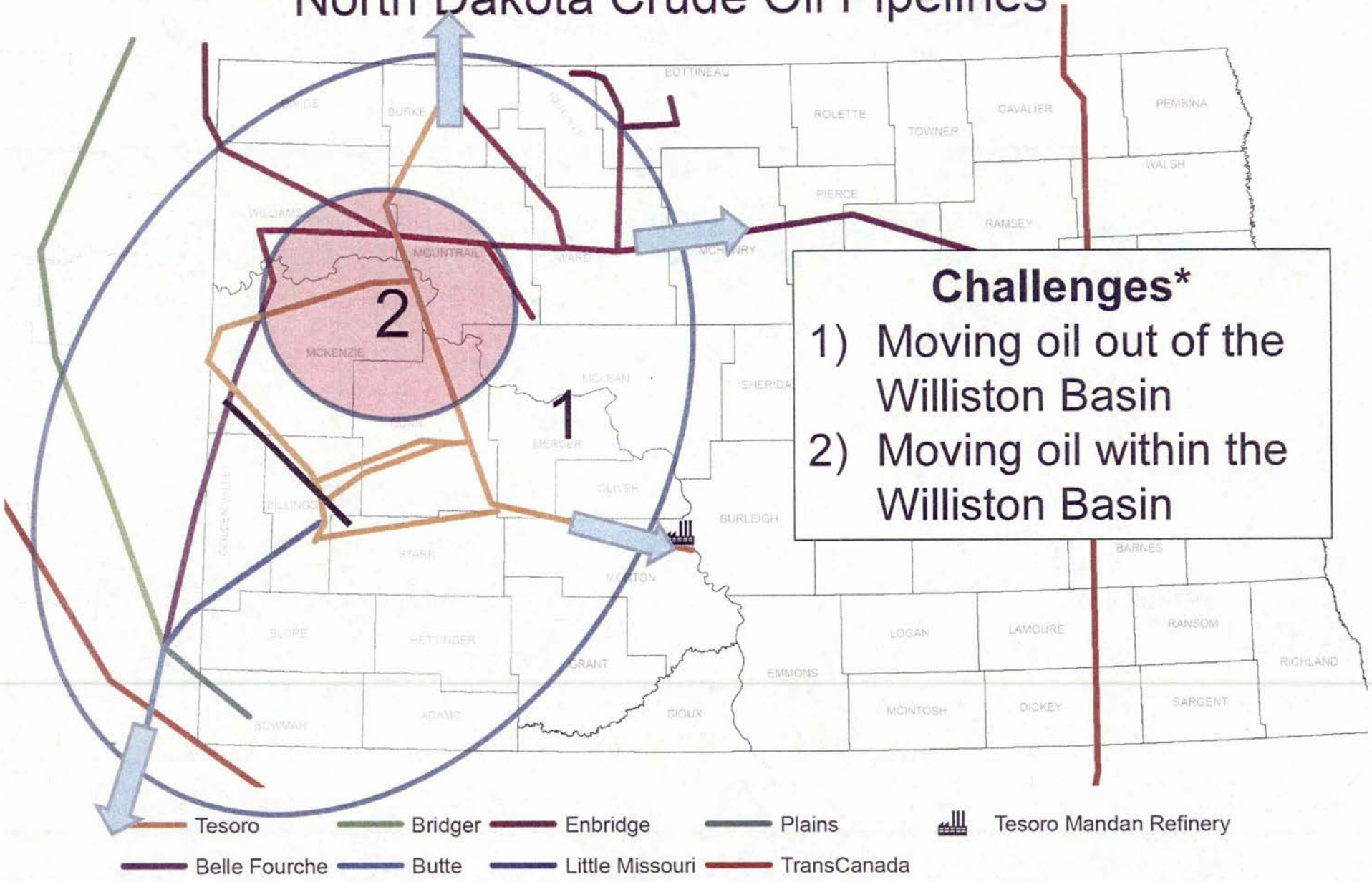
Forecasting Williston Basin Oil Production, BOPD



Production forecast is for visual demonstration purposes only and should not be considered accurate for any near or long term planning.

p.9 #1

North Dakota Crude Oil Pipelines

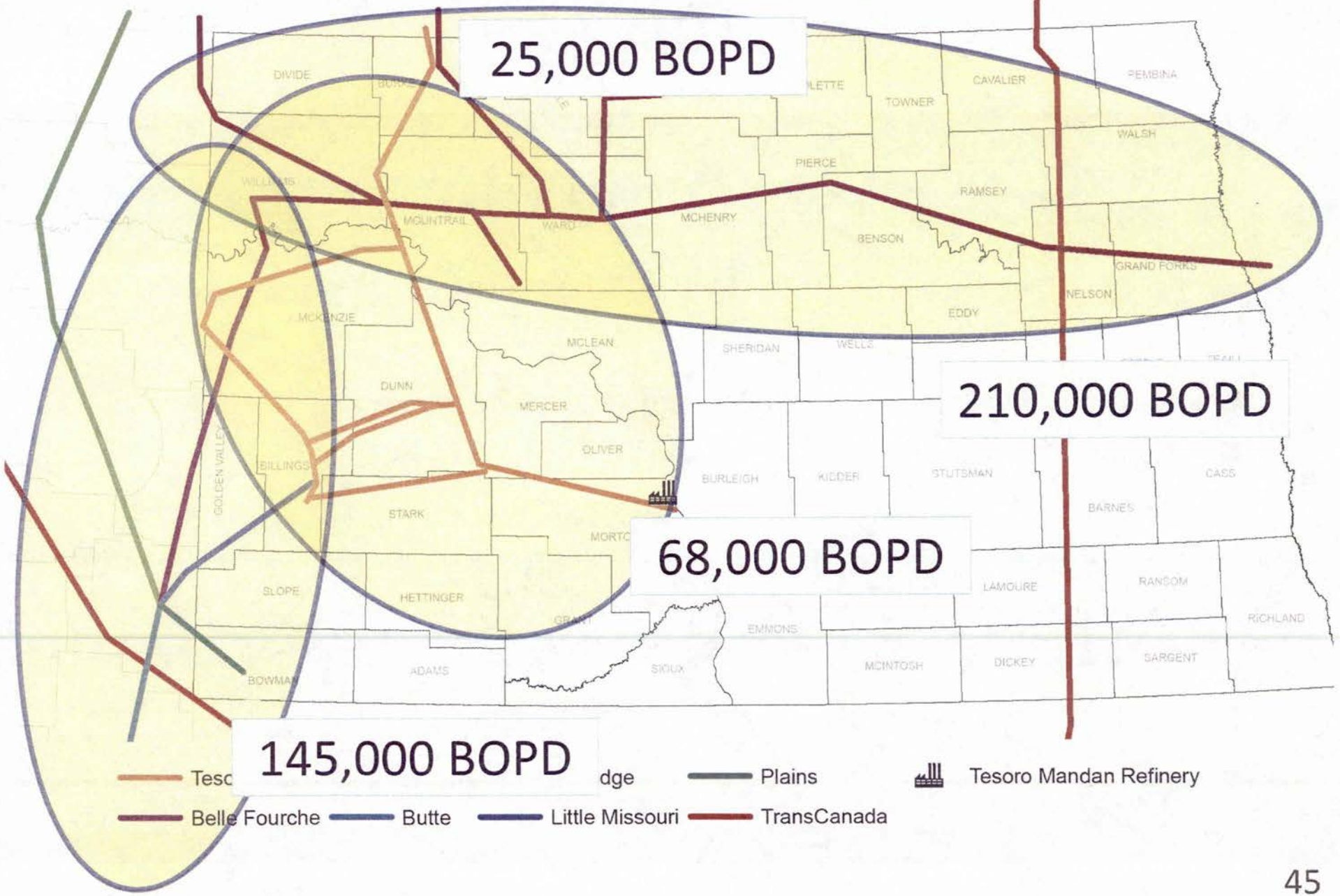


Challenges*

1) Moving oil out of the Williston Basin
2) Moving oil within the Williston Basin

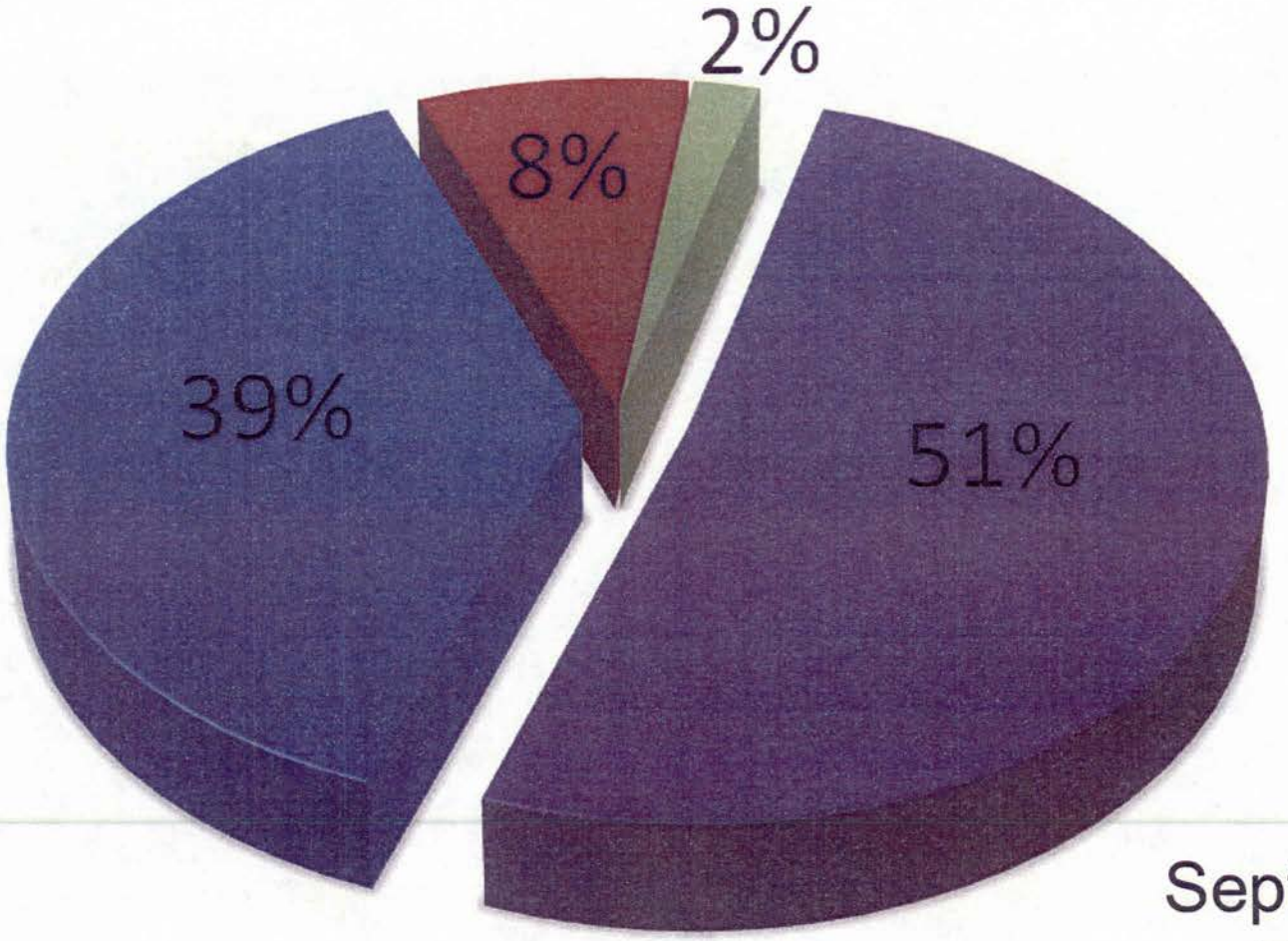
*Modified from Bridger and Belle Fourche Pipelines

North Dakota Crude Oil Pipelines



p.11 #1

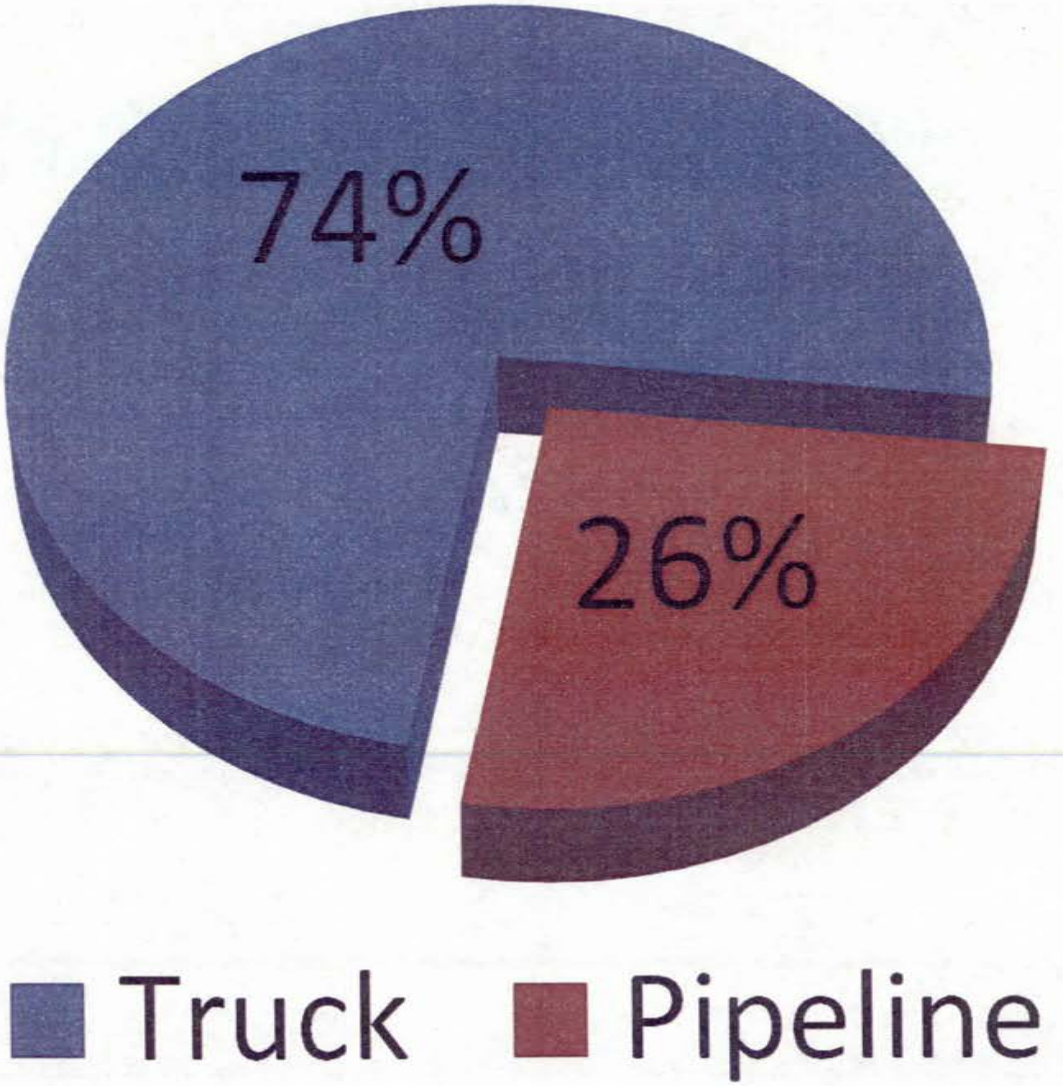
Williston Basin Oil Transportation



September 2012

- Pipeline Export
- Tesoro Refinery
- Truck to Canadian Pipelines
- Estimated Rail

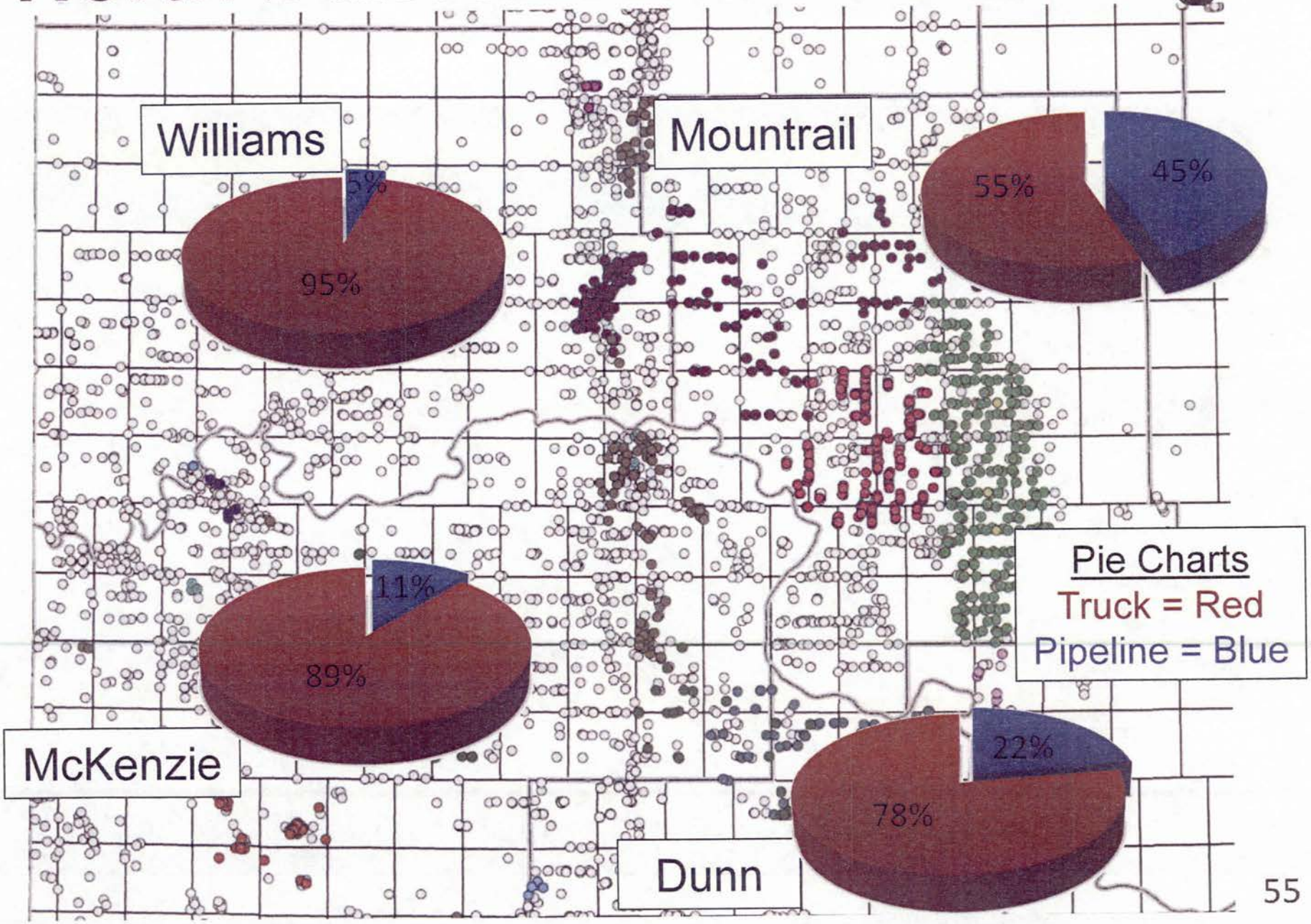
North Dakota Crude Gathering



February 2012 Data

#1 p.13

North Dakota Crude Gathering



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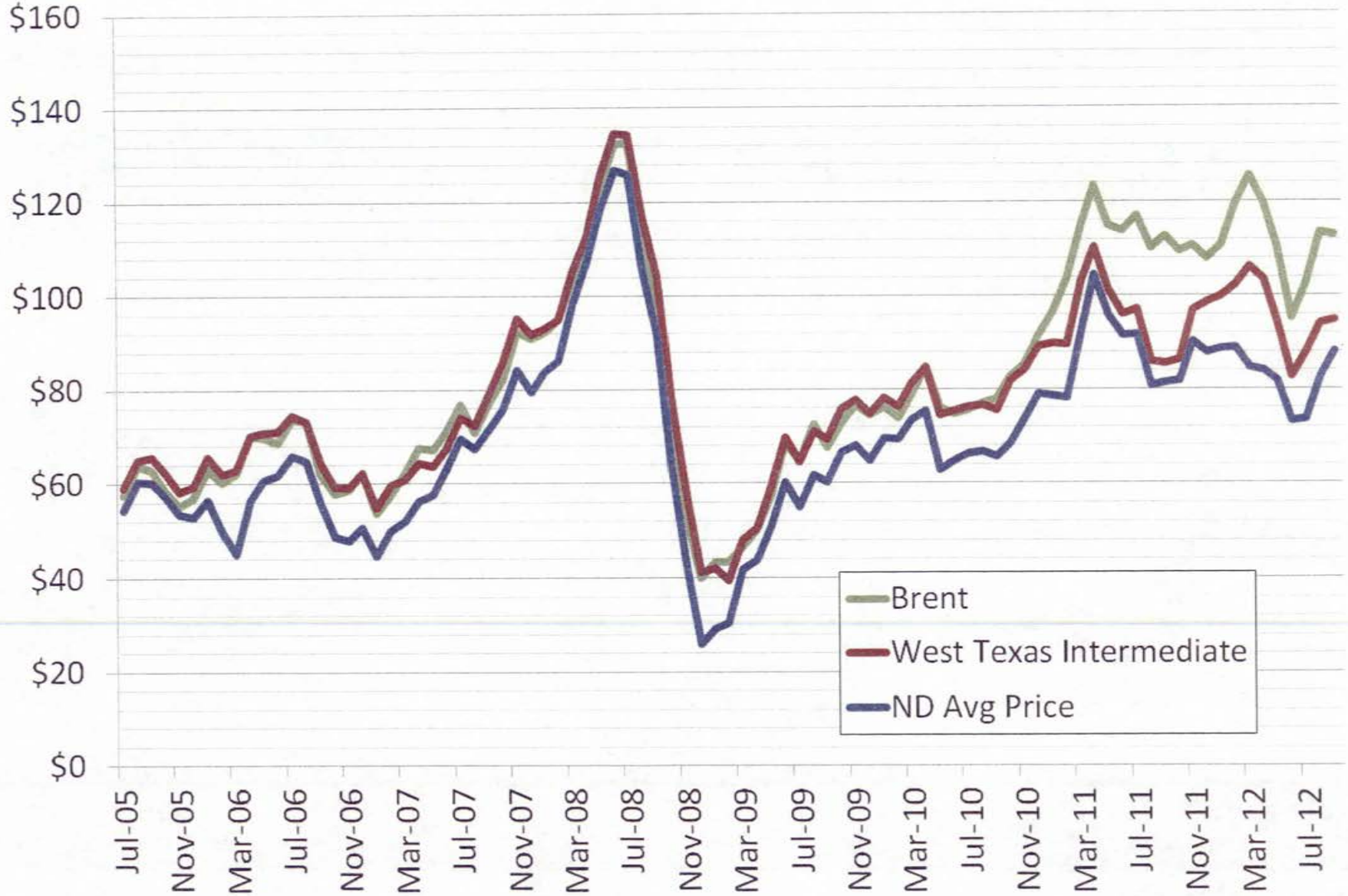
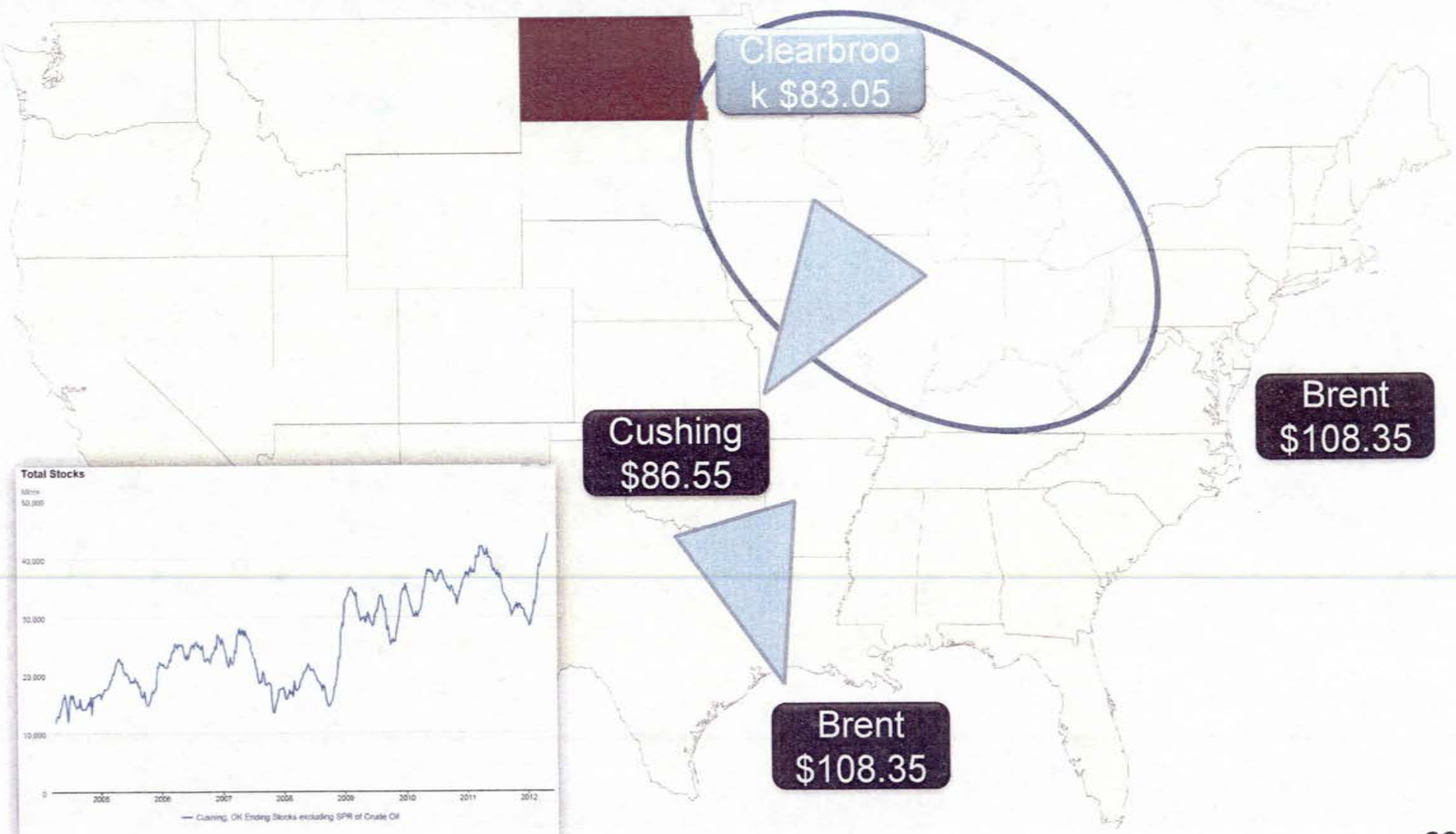
Crude Oil Prices

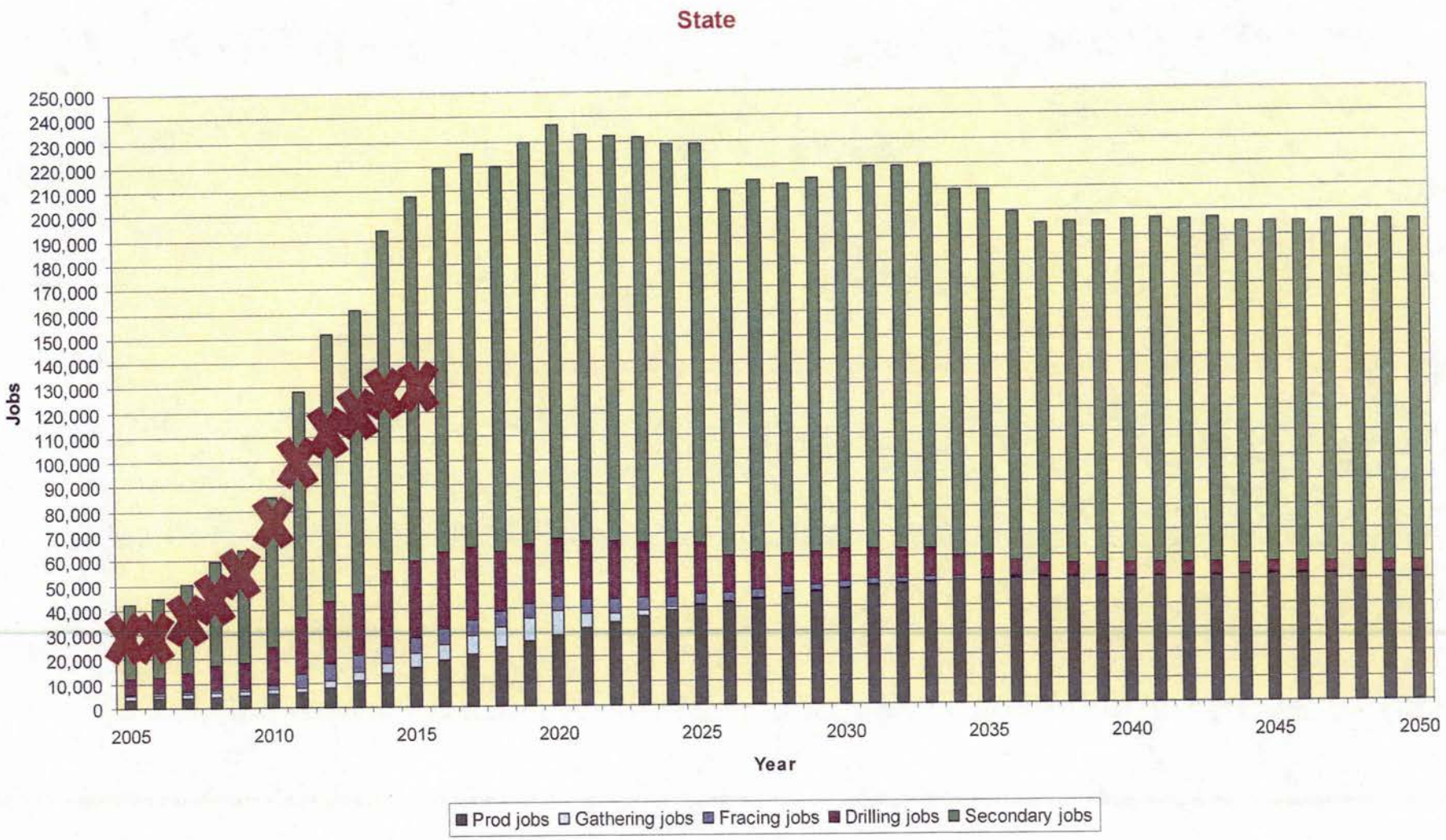


#1 p.15

Crude Pricing – Dec 10, 2012



Expected Case



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Colorado study shows Mineral Industries >> Government & Recreation

Industry	Jobs Multiplier	Earnings Multiplier
Information	4.25	2.73
Utilities	3.82	2.24
Mining	3.44	2.08
Manufacturing	3.32	2.85
Management of Companies	2.70	1.64
Real Estate, Rental & Leasing	2.42	3.27
Finance	2.30	1.93
Wholesale trade	2.17	1.69
Professional & Technical Services	1.95	1.58
Construction	1.81	1.57
Government	1.79	1.63
Transportation and Warehousing	1.73	1.65
Health Care & Social Assistance	1.61	1.53
Other Services	1.50	1.66
Administrative & Waste Services	1.48	1.63
Education	1.41	1.59
Retail	1.41	1.66
Arts, Entertainment & Recreation	1.37	1.61
Accomodation & Food Service	1.35	1.76

Shale Play Competition

- Leases are held
  - Bakken operators now have options on where to put their capital
  - Competition is Real
    - » Eagle Ford in South Texas – 285 Rigs
    - » Permian Basin, Texas – 500 Rigs
    - » Utica, Niobrara, Scoop & many others across the country
- Bakken costs are high – operators are trying to lower costs
- Maintaining a business friendly climate
  - Tax issues
  - Regulatory issues
  - Federal permitting & regulatory issues
  - 23 New Rules in 2012 – increased costs

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Bakken – The Bakken shale play is one of the biggest oil discoveries in recent history. Long known since the early days of drilling in the Williston basin, the Bakken shale was largely ignored until technology came along to make it economic to develop. Since then, it has become a huge success.

Seven E&P companies will account for about 65% of Bakken drilling this year. In rank order they are: Continental Resources, Hess, Whiting Petroleum, Statoil/Brigham, Oasis Petroleum, Marathon, and EOG Resources.

Each is developing ways to become more efficient and reduce drilling days/well to somewhere in the mid-20s.

These wells will be around 10,000-foot TVD and cost over $9 million each.

Eagle Ford – About 400 miles in length and stretching from Southwest Texas into East Texas, the Eagle Ford shale is a very interesting play with oil, liquids, and dry gas windows with 60% to 70% carbonate content and a more brittle geology that's good for fracturing.

Four companies account for around 45% of all drilling here: Chesapeake Energy, EOG, Conoco Phillips, and Marathon. But there are other very aggressive players including Pioneer, Anadarko, Talisman/Statoil, and BHP (which paid $12 billion for Petrohawk and gained significant Eagle Ford holdings).

Most are drilling $6.5 million to $7 million wells with focus on the Eagle Ford's oil and liquids windows.

Western North Dakota

- 1,100 to 2,700 wells/year = 2,000 expected
  - 100-225 rigs = 12,000 – 27,000 jobs
  - Another 10,000-15,000 jobs building infrastructure
  - 200 rigs can drill the wells needed to secure leases in 1 year
  - 200 rigs can drill the wells needed to develop spacing units in 18 years
  - 35,000-40,000 new wells = 45,000-50,000 long term jobs

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SUMMARY OF PROPOSED 2012 RULES

NDAC	RULES	PROPOSED CHANGE
43-02-03 GENERAL RULES		
43-02-03-05	Enforcement of Laws and Rules	Move language to 43-02-03-28 (Safety Regulation)
43-02-03-15	Bonds	Increase $20,000 bond to $50,000
		Commercial SWD bond increased from $20,000 bond to $50,000
		Eliminates $50,000 10-well blanket bond
43-02-03-16	Permit to Drill	Consider csg imbrittlement due to H_2S when considering recompletions
43-02-03-16.3	Recovery of a Risk Penalty	Clarify that "approximate" well loc is to be included in the invitation to participate
		Requires the drilling or spacing unit be included in the invitation to participate
43-02-03-18	Drilling Units	Allows temporary spacing order effective for up to 3 yrs, not 1-1/2 yrs
43-02-03-19	Site Construction	Amends rule to address only initial well site construction
		Soil stabilization additives and materials require approval from Director
		Must reduce size of well site after completion if not used f/well operations
43-02-03-19.1	Fencing, Screening, and Netting of Pits	Amended to also address "drilling" pits which were newly created
43-02-03-19.2	Disposal of Waste Material	Requires all waste material from undesirable events to be immediately disposed
43-02-03-19.3	Earthen Pits and Open Receptacles	Requires flare pits to be at least 150 feet from wells and tanks
		Allows lined fresh wtr pit for frack water f/1yr in cut w/only drinking wtr chemicals
43-02-03-19.4	Drilling Pits	Creates new section addressing pits allowing cuttings, but no fluids
		Must reclaim pit w/in 30 days after drilling well; Director may grant exceptions
		Allows small lined pit f/trench water and rig wash, but reclaim before MORT
		Must dike pit to keep surface water from entering
43-02-03-19.5	Reserve Pits	Creates new section allowing reserve pits only for wells < 5000' deep or SWD
		Must reclaim pit w/in one yr after completing well
		Must slope surface to promote surface drainage away from reclaimed area
43-02-03-21	Casing, Tubing, and Cementing	Requires remedial work f/inadequate sur csg job to be approved by Director
		Requires surface casing pressure test after cementing
43-02-03-25	Deviation Tests and Directional Surveys	Requires directional surveys to be in reference to true north
43-02-03-27.1	Hydraulic Fracture Stimulation	Creates new section addressing hydraulic fracture stimulation
		Must use popoff valves, rupture disk, remote valve
		Use frack string: no chem disclosure if > 350psi on annulus after frack
		Frack down csg: run csg evaluation f/thickness of csg and cmt w/chem disclosure
43-02-03-28	Safety Regulation	Incorporated language removed from 43-02-03-05 on well shut in f/public safety
		Requires automatic shut-down equip if well is threat to public health or safety
		Prohibits injection equipment from being installed < 500' from occupied dwelling
43-02-03-30.1	Leak and Spill Cleanup	Creates new section and incorporates language from 43-02-03-49&53
		Requires operators to respond w/appropriate resources to contain & clean up spills
43-02-03-31	Well Log, Completion and Workover Reports	Run CBL prior to completion
		File two digital copies of logs, instead of one digital and one paper
43-02-03-34.1	Reclamation of Surface	Creates new section to address final restoration after well is plugged
		No additional requirements: Language taken from 43-02-03-19
43-02-03-49	Oil ~~Spills,~~ Prod Equip, Dikes, and Seals	Amend rule--move spill reference to 43-02-03-30.1
		Must remove "unused" equip rather than "unusable"
43-02-03-51	Treating Plant	Increases minimum bond from $20,000 to $50,000 for treating plants
43-02-03-53	Saltwater Handling Facilities	Amend rule--move spill reference to 43-02-03-30.1
		Requires oil recovered from saltwater handling facilities to be reported to Director
		Must remove "unused" equip rather than "unusable"
43-02-03-54	Investigative Powers	Director can timely (instead of "immediately") reply to a complaint
		Allows Director to decline to investigate--can appeal to IC
43-02-03-55	Abandonment of Wells-Suspension of Drilling	Abandonment will now include water source wells and stratigraphic tests
43-02-03-88.1	Special Procedures Administrative Hearings	Allows applications for additional wells on a spacing unit without live testimony
		Comments and objections to hearings must be rec'd prior business day by 5pm
43-02-03-90.2	Official Notice	Comments and objections to hearings must be rec'd prior business day by 5pm
43-02-12 GEOPHYSICAL EXPLORATION REQUIREMENTS		
43-02-12-06	Notification of Work Performed	Director may require progress reports prior to completion of a project

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#2

HB 1234 Testimony Outline - Rep. Roscoe Streyle, District 3

1) Explain Bill

a) 800,000, 900,000, 1,000,000, 1,250,000, 1,500,000 (-.50%)

b) All exemptions gone (Amendment to keep Wildcat Exemption on first 75,000 barrels)

c) Closes the stripper well exemption

1) The statute that defines stripper wells and stripper well properties has three categories to qualify: Over a 12-month consecutive period – wells at a depth of 6,000 feet or less that did not exceed 10 barrels of oil per day; wells at a depth between 6,000 and 10,000 that did not exceed 15 barrels per day; and wells more than 10,000 feet that did not exceed 30 barrels per day. Bakken wells generally are at a depth of roughly 10,000 to 11,000 feet.

2) 2011, 43 percent of oil-producing wells in ND were qualified as stripper wells.

3) 5% vs. 11.50% - Stripper wells don't pay extraction tax

4) Only Bakken/Three Forks wells - Old wells keep exemption (Renville/Bottineau/Etc.)

d) Overstruck language makes the point on the complexity of ND tax structure

1) Reduced rates and/or exemptions apply for new vertical and horizontal wells, new wells drilled on Indian land, work over wells, stripper wells, two-year inactive wells, horizontal reentry wells, enhanced recovery wells, and qualifying Bakken wells.

2) Production 5% and the oil extraction 6.5%; 4% if the well qualifies for a reduced rate; 2% from qualifying wells in the Bakken formation; and 0% if the well qualifies for an exemption.

2) Explain Fiscal Note

a) $156M reduction - Minor compared to revenue raised (3.05% of $5.1B) (-$240M, +$84M)

b) Budget for 2013-2015 built on 800,000-850,000/bpd

d) Consider amendment for Wildcat Exemption 75,000 barrels (Tax Exemption) = $25-35M/year

3) Reasons for Introduction

a) One of Highest tax rate in nation (ND-11.50%, TX-9.20%, WY-6%, OK-7%)

b) Complex tax structure (6.50% Extraction, 5% Production), many exemptions, etc.

c) Paying hundreds of millions in sales tax, corporate/personal/property tax - Fairness Issue

d) Simplify tax structure - Easy to budget and understand

e) Removes trigger for budget certainty - $52.50 (5 Months of Average Price Below)

4) Risks to ND/Oil Industry

a) EPA Fracking - Stop/Slow down permits and fracking

b) BLM Fracking - Stop/Slow down permits and fracking

c) Global economy concerns- Oil price collapse

d) Administration budget contains tax changes - Reduce drilling capital 30-50%

e) US Fish & Wildlife - Trying to have final say in permitting process

f) Global competition - Explain (ND 185 Rigs-Been Dropping)

1) Eagle Ford South Texas - 285 Rigs

2) Permian Basin Texas - 500 Rigs

3) Better pricing on coasts and gulf (Texas advantage) - Brent Pricing

g) Bakken costs are high compared to Eagle Ford and others, $9M+ vs. $6.5-7M

1) EOG, Marathon, Statoil - In Both Bakken and Eagle Ford (3 of top 7 in ND)

h) Challenges - Climate, Workforce shortage, Housing, Infrastructure, Water

i) Counties/Cities issues with Road Weight and Crew Camps/Housing Restrictions

j) Oil to Market Issues (Truck/Rail/Pipe) - Handouts ($1 in discount costs $29M Taxes)

k) ND regulations - 23 new one in 2012

l) FEDERAL GOVERNMENT AND FEDERAL TAXES

5) Economic Impact

a) 35,000+ more well to drills

b) Population of ND at all time high

c) Lowest unemployment rate in the nation

d) Lower taxes = more economic growth in the long term

e) $5.1B in taxes (2013-2015) - $212.5M/month

#1

Sixty-third
Legislative Assembly
of North Dakota

HOUSE BILL NO. 1234

Introduced by

Representatives Streyle, Owens, Thoreson

Senator Armstrong

A BILL for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and 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 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties or individual stripper wells and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property or individual stripper wells as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve

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secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. 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 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.

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~~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~~, certified as qualifying by the industrial commission, and from which the project operator ~~must have~~has 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.

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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" 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.

9. "Stripper well property" means a "property" outside the Bakken and 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

#1 p.5

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 4. 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;~~

~~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.~~

1. Six percent ~~beginning~~for production from wells drilled and completed 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 eight hundred 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~~for production from wells drilled and completed 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 nine 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~~for production from wells drilled and completed 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 one million~~ one hundred thousand~~ barrels per day, ~~which must remain the rate unless a lower rate is~~

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~~determined under subsection 4 or 5~~ or for production from wells drilled and completed on or after the first day of July 2015, whichever event occurs first.

~~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 one million two 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 one million five hundred thousand barrels per day.~~

SECTION 5. 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, 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 or individual stripper well. ~~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 seven hundred twenty-five thousand barrels per day, a well drilled and completed in the Bakken or Three Forks formation and which is within a stripper well property is not exempt under this subsection until production from that well individually meets the requirements of the definition for stripper well status under section 57-51.1-01.~~ A well in the Bakken or Three Forks formation which was certified as a stripper well or as part of a stripper well property at the time it is reentered or reworked retains its stripper well or stripper well property exempt status for the first twelve months of production from that well after completion of the reentry or reworking project. After that period, the stripper well or stripper well property exempt status is lost after the average daily production of the well exceeds one hundred barrels per day for a calendar month and the well is then subject to a reduced tax rate of two percent under this chapter until production from that well individually meets the requirements of the definition of stripper well under section 57-51.1-01.

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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.

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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~~

#1 p.10

~~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.~~

#1 p. 11

~~(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.~~

#1 p.12

~~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~~

#1 p. 13

~~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, 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~~

#1 p.14

~~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~~

#1 p. 15

~~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~~

#1 p. 16

~~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.~~

#1 p.17

~~(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~~

#1 p.18

~~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 6. 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 or rate reduction on production from a stripper well property or individual stripper well 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 or individual stripper well'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~~

#1
P.19

~~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 7. EFFECTIVE DATE. This Act is effective for taxable events occurring after June 30, 2013.

13.0225.01005
Title.

Prepared by the Legislative Council staff for
Representative Drovdal
February 12, 2013

#2

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1234

Page 1, line 1, after "reenact" insert "section 15-05-10, subsection 4 of section 38-08-04, and"

Page 1, after line 4, insert:

"**SECTION 1. AMENDMENT.** Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property <u>or individual stripper wells</u> as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations."

Page 3, line 27, after "<u>8.</u>" insert ""<u>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.</u>

<u>9.</u>"

Page 3, line 27, after ""property"" insert "<u>outside the Bakken and Three Forks formations</u>"

Page 4, line 26, remove the overstrike over "~~is~~"

Page 5, line 16, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 16, after "on" insert "or after"

Page 5, line 18, remove ", which must remain the rate unless a"

Page 5, line 19, remove "lower rate is determined under subsections 2 through 5"

Page 5, line 20, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 20, after "on" insert "or after"

Page 5, line 22, remove ", which must remain"

Page 5, line 23, remove "the rate unless a lower rate is determined under subsections 3 through 5"

Page 5, line 24, replace "beginning" with "for production from wells drilled and completed"

Page 5, line 24, after "on" insert "or after"

Page 5, line 26, remove "one hundred thousand"

Page 5, line 26, remove "which must remain the"

Page 5, line 27, replace "rate unless a lower rate is determined under subsection 4 or 5" with "or for production from wells drilled and completed on or after the first day of July 2015, whichever event occurs first"

Page 5, remove lines 28 through 31

Page 6, remove lines 1 through 3

Page 6, line 10, after "property" insert "or individual stripper well"

Page 6, line 10, remove "On or"

Page 6, replace lines 11 through 16 with "A well in the Bakken or Three Forks formation which was certified as a stripper well or as part of a stripper well property at the time it is reentered or reworked retains its stripper well or stripper well property exempt status for the first twelve months of production from that well after completion of the reentry or reworking project. After that period, the stripper well or stripper well property exempt status is lost after the average daily production of the well exceeds one hundred barrels per day for a calendar month and the well is then subject to a reduced tax rate of two percent under this chapter until production from that well individually meets the requirements of the definition of stripper well under section 57-51.1-01."

Page 17, line 6, remove the overstrike over "**~~or rate reduction~~**"

Page 17, line 10, after "exemption" insert "or rate reduction"

Page 17, line 11, after "property" insert "or individual stripper well"

Page 17, line 13, after "property's" insert "or individual stripper well's"

Renumber accordingly

HB 1234 Testimony Outline - Rep. Roscoe Streyle, District 3

1) Explain Bill

a) New production only - 800,000, 900,000, 1,000,000 (-.50%)

Proposed Amendment 900,000, 1,000,000, 1,100,000, 1,250,000 (-.50) - All production

b) All exemptions gone

c) Closes stripper well exemption - Rep. Drovdal will explain tax committee changes in the bill.

1) The statute that defines stripper wells and stripper well properties has three categories to qualify: Over a 12-month consecutive period – wells at a depth of 6,000 feet or less that did not exceed 10 barrels of oil per day; wells at a depth between 6,000 and 10,000 that did not exceed 15 barrels per day; and wells more than 10,000 feet that did not exceed 30 barrels per day. Bakken wells generally are at a depth of roughly 10,000 to 11,000 feet.

2) 2011, 43% of oil-producing wells in ND were qualified as stripper wells. (5% tax)

d) Fixes stripper well property issue when reentering stripper well or property

e) Overstruck language makes the point on the complexity of ND tax structure

1) Reduced rates and/or exemptions apply for new vertical and horizontal wells, new wells drilled on Indian land, work over wells, stripper wells, two-year inactive wells, horizontal reentry wells, enhanced recovery wells, and qualifying Bakken wells.

2) Production 5% and the oil extraction 6.5%; 4% if the well qualifies for a reduced rate; 2% from qualifying wells in the Bakken formation; and 0% if the well qualifies for an exemption.

2) Fiscal Note

a) Governors Budget for 2013-2015 built on 800,000-850,000/bpd

3) Reasons for Introduction

a) One of Highest tax rate in nation (ND-11.50%, TX-9.20%, WY-6%, OK-7%)

b) Complex tax structure (6.50% Extraction, 5% Production), many exemptions, etc.

c) Paying hundreds of millions in sales tax, corporate/personal/property tax - Fairness Issue

d) Simplify tax structure - Easy to budget and understand

e) Removes trigger for budget certainty - $52.50 (5 Months of Average Price Below)

4) Risks to ND/Oil Industry

a) EPA Regulation on Fracking - Stop or Slow down permits and fracking

b) BLM Regulation on Fracking - Stop or Slow down permits and fracking

c) Global economy concerns- Oil price drop

d) Administration budget contains tax changes - Reduce drilling capital 30-50%

e) US Fish & Wildlife - Trying to have final say in permitting process

f) Global competition - ND 187 Rigs - Down from 218

1) Eagle Ford South Texas - 285 Rigs

2) Permian Basin Texas - 500 Rigs

3) Better pricing on coasts and gulf (TX/OK advantage) - Brent Pricing

g) Bakken costs are high compared to Eagle Ford and others, $9M+ vs. $6.5-7M

1) EOG, Marathon, Statoil - In Both Bakken and Eagle Ford (3 of top 7 in ND)

h) Other Challenges - Climate, Workforce shortage, Housing, Infrastructure, Water

i) Counties/Cities issues with Road Weight and Crew Camps/Housing Restrictions

j) Oil to Market Issues (Truck/Rail/Pipe) - $1 in discount costs $29M Taxes

k) ND regulations - 23 new one in 2012

l) FEDERAL GOVERNMENT AND FEDERAL TAXES

5) Economic Impact

a) 35,000+ more well to drills

b) Population of ND at all time high

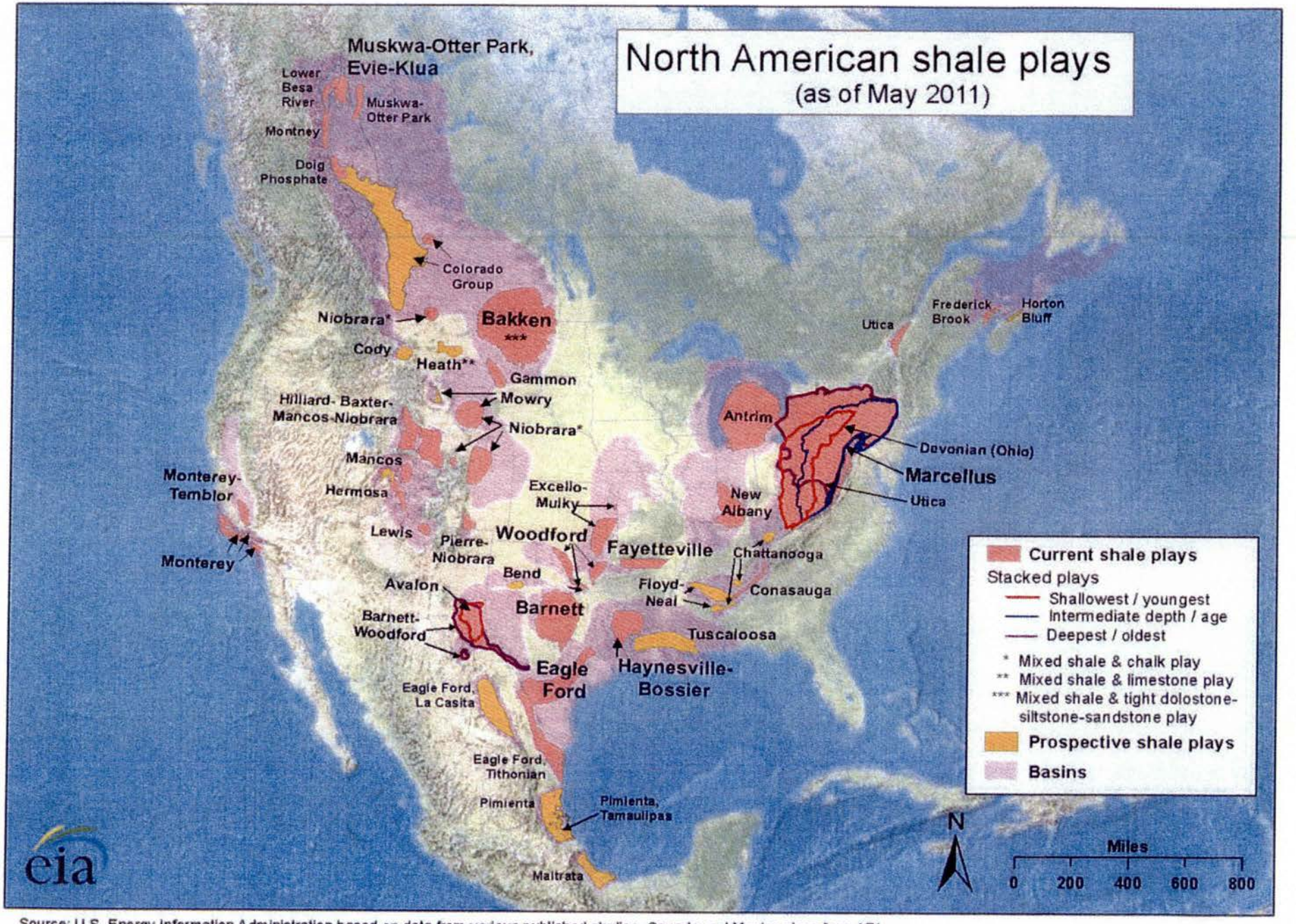
c) Lowest unemployment rate in the nation

d) Lower taxes = more economic growth in the long term

e) 90 wells per month needed to maintain production

f) December numbers - 8,224 wells, 768,853/bpd

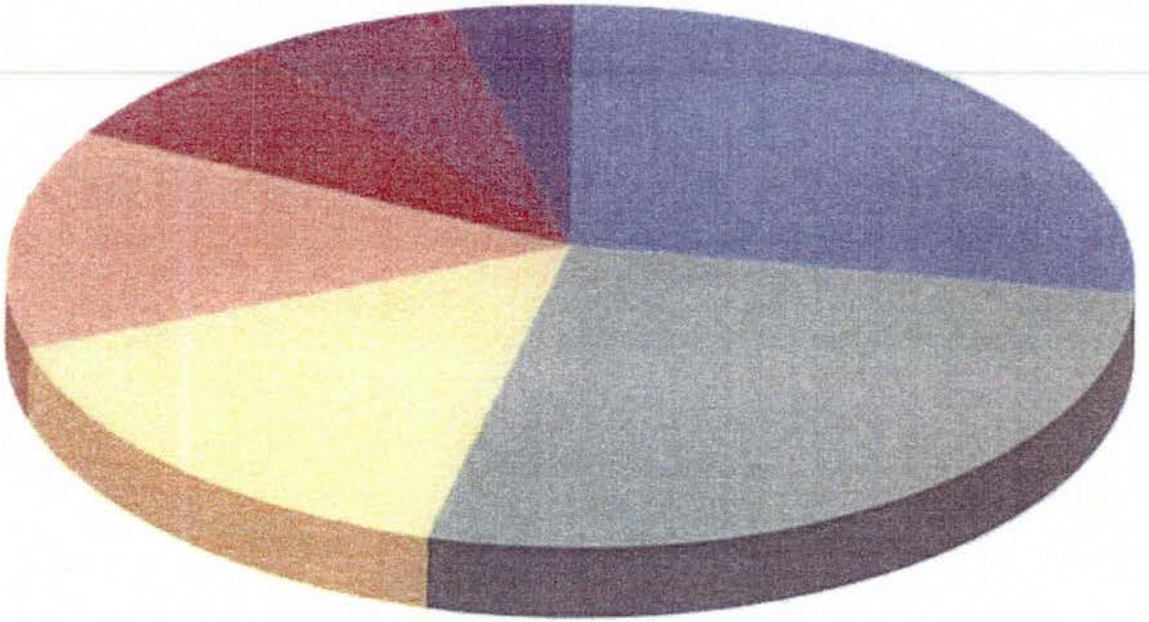
g) $5.1B in taxes (2013-2015) - $212.5M/month = 43% of total budget



Source: U.S. Energy Information Administration based on data from various published studies. Canada and Mexico plays from ARI.
Updated: [illegible] 2011

Fig. 1: Oilfield services expenditures in top US shales – 2012

Total - $54.3 billion



- Bakken
- Eagle Ford
- Permian
- Marcellus
- Anadarko-Woodford
- Granite Wash
- Niobrara

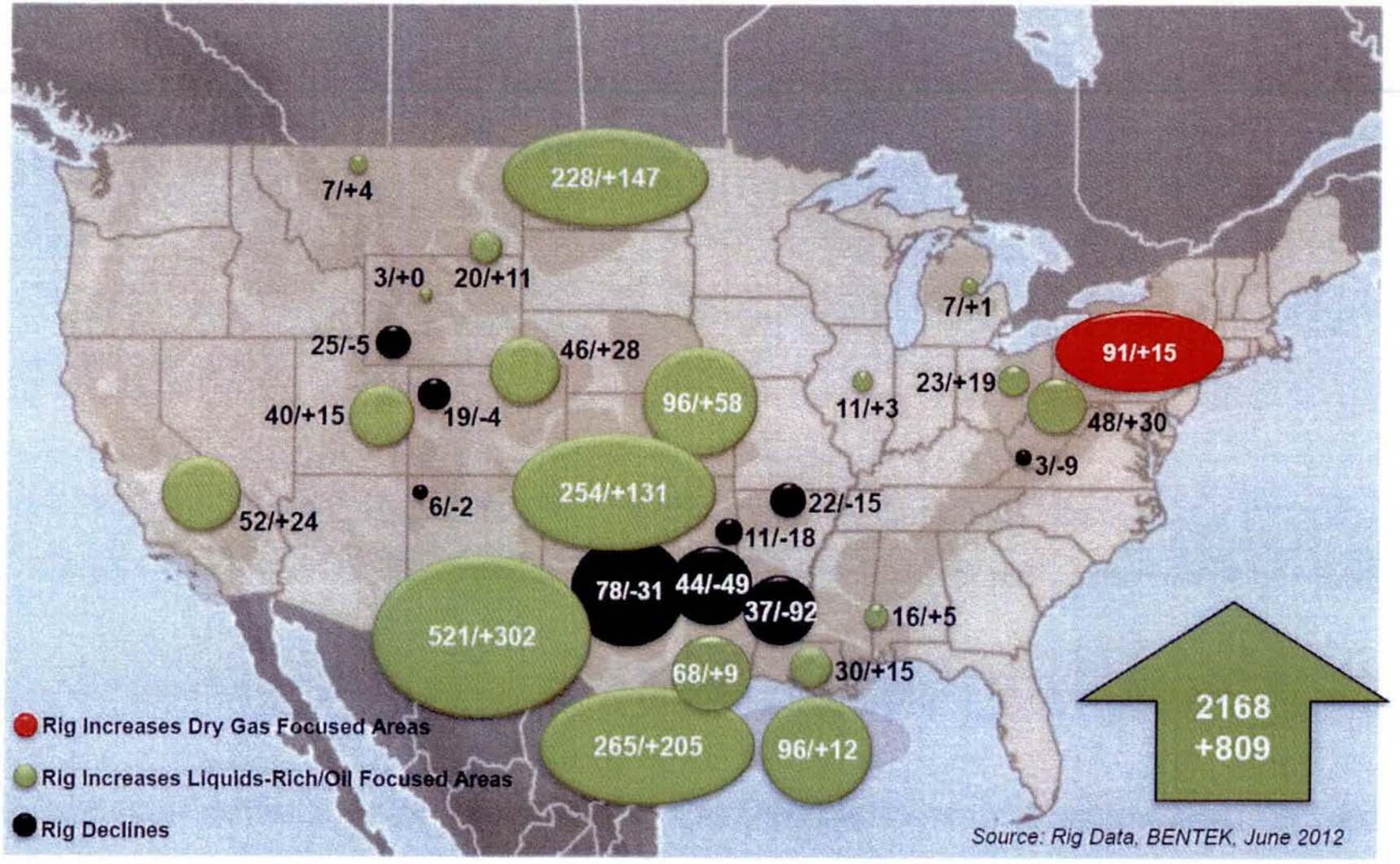
OIL&GAS FINANCIAL JOURNAL

Shale Play Competition

- Leases are held
  - Bakken operators now have options on where to put their capital
  - Competition is Real
    - » Eagle Ford in South Texas – 285 Rigs
    - » Permian Basin, Texas – 500 Rigs
    - » Utica, Niobrara, Scoop & many others across the country
- Bakken costs are high – operators are trying to lower costs
- Maintaining a business friendly climate
  - Tax issues
  - Regulatory issues
  - Federal permitting & regulatory issues
  - 23 New Rules in 2012 – increased costs

BENTEK Energy LLC

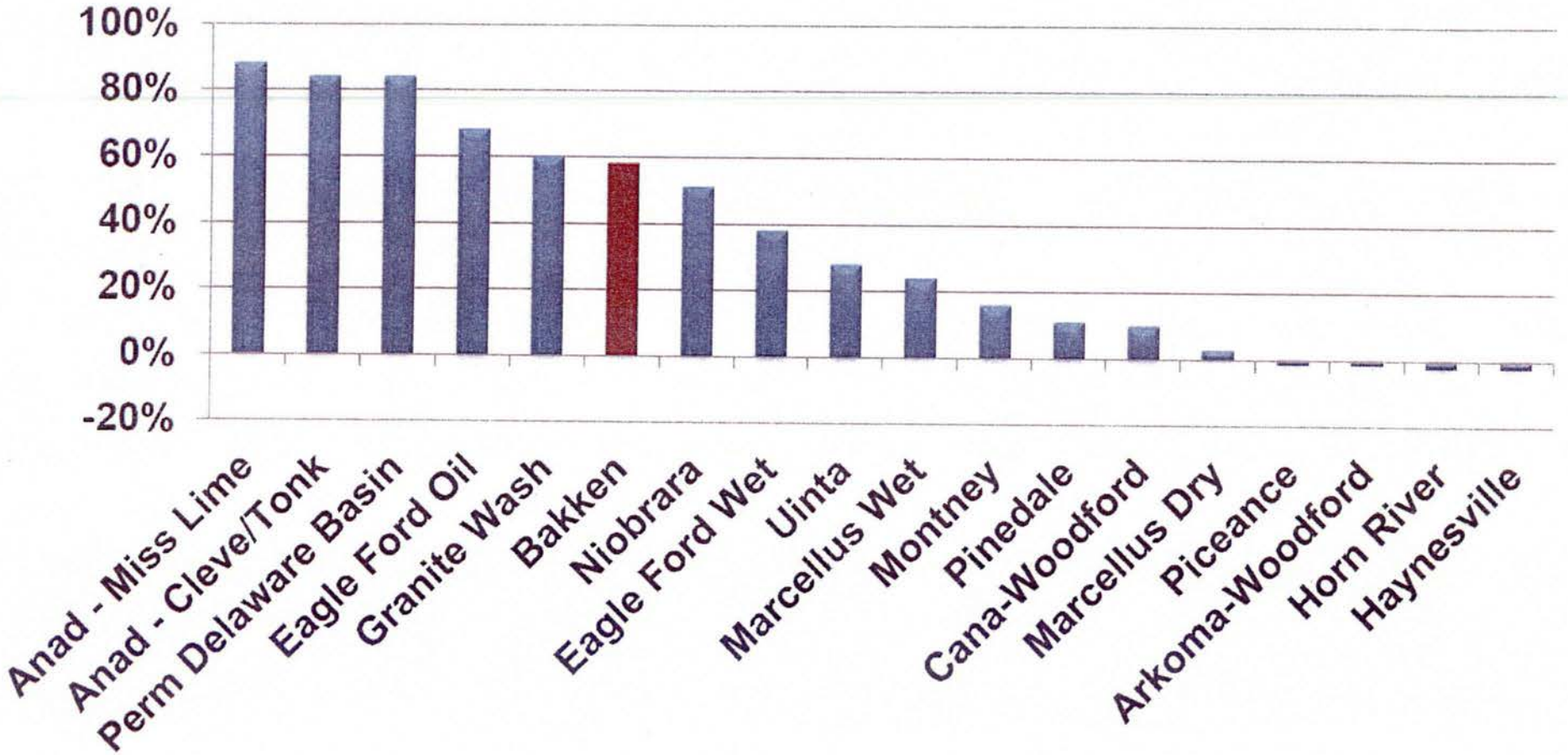
Plays With High Returns Attract Drilling Rigs



Active rig count: June 15, 2012 / Change in rig count from Jan. 1, 2010

BENTEK Energy LLC

Bakken Earns Above Average Returns



Price Assumptions: *Gas = 12 month forward average curve for each regional pricing point as of June, 2012 (price range $2.45-$2.86/Mcf)*
Oil = 6 month average WTI +/- differential as of June, 2012 (price range $84.40-$100.43/barrel)
NGLs = weighted average $/barrel based on current Mt. Belvieu prices and the typical composition in each region (range $23.79-$45.22/barrel)

Bakken – The Bakken shale play is one of the biggest oil discoveries in recent history. Long known since the early days of drilling in the Williston basin, the Bakken shale was largely ignored until technology came along to make it economic to develop. Since then, it has become a huge success.

Seven E&P companies will account for about 65% of Bakken drilling this year. In rank order they are: Continental Resources, Hess, Whiting Petroleum, Statoil/Brigham, Oasis Petroleum, Marathon, and EOG Resources.

Each is developing ways to become more efficient and reduce drilling days/well to somewhere in the mid-20s.

These wells will be around 10,000-foot TVD and cost over $9 million each.

Eagle Ford – About 400 miles in length and stretching from Southwest Texas into East Texas, the Eagle Ford shale is a very interesting play with oil, liquids, and dry gas windows with 60% to 70% carbonate content and a more brittle geology that's good for fracturing.

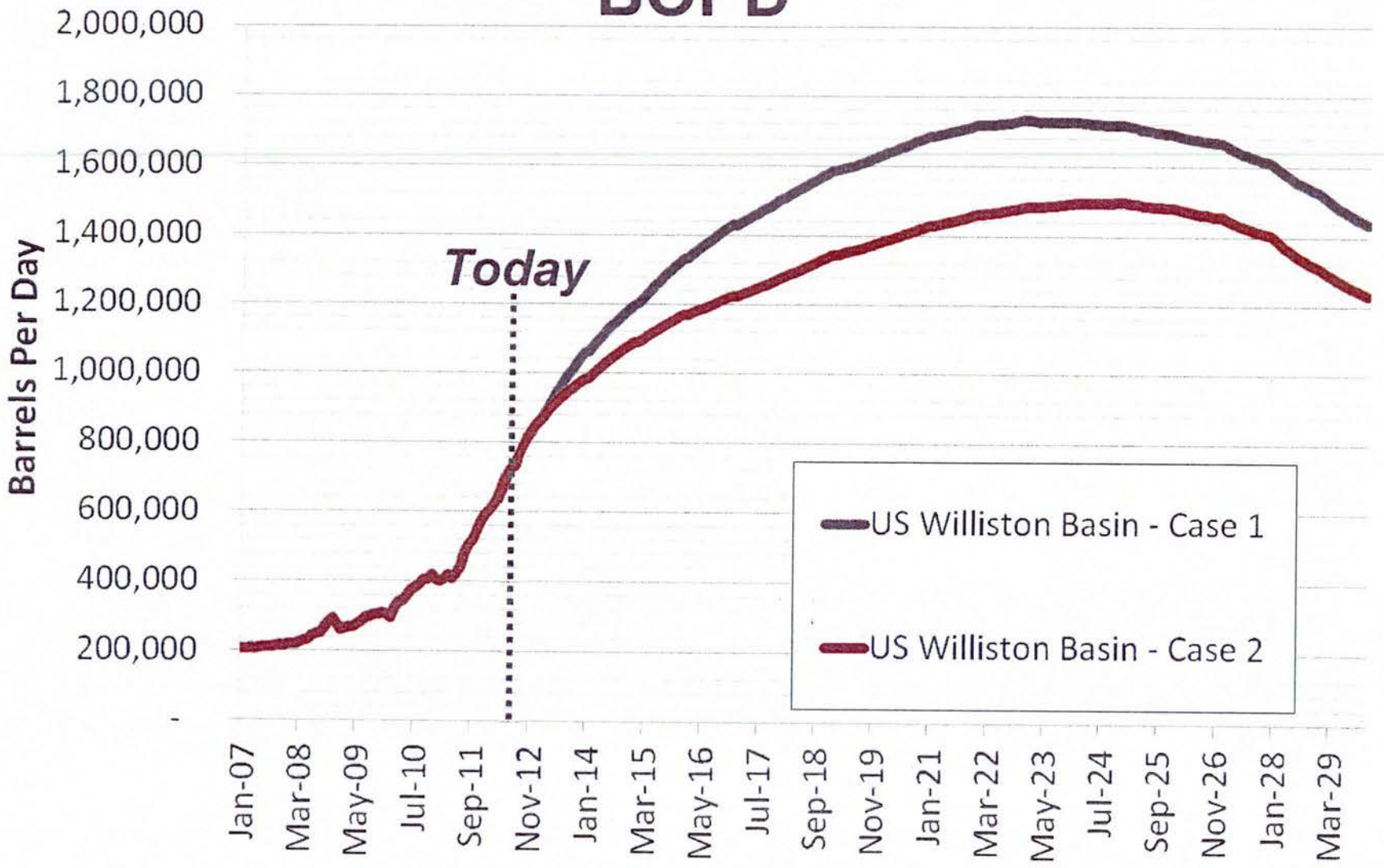
Four companies account for around 45% of all drilling here: Chesapeake Energy, EOG, Conoco Phillips, and Marathon. But there are other very aggressive players including Pioneer, Anadarko, Talisman/Statoil, and BHP (which paid $12 billion for Petrohawk and gained significant Eagle Ford holdings).

Most are drilling $6.5 million to $7 million wells with focus on the Eagle Ford's oil and liquids windows.

Permian – Several exciting shales now overlay an historic conventional oil basin where drilling began in the 1920s. They include the Avalon, Leonard, Wolfcamp, Bone Spring Field, Spraberry Field, and Yeso Oil Play. Also included is the Wolfberry Trend which refers to the Wolfcamp Shale and the Spraberry Field.

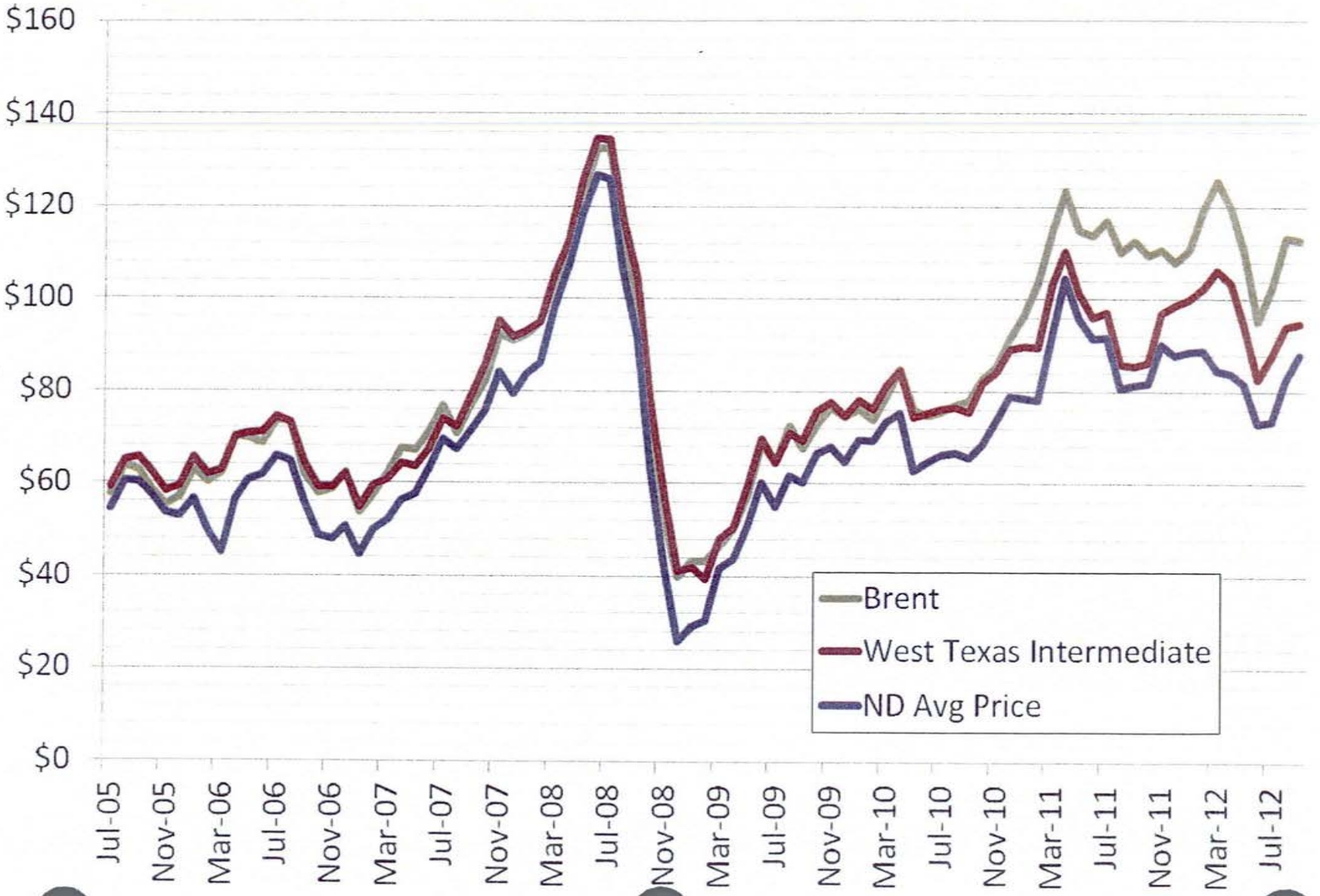
There are plenty of operators of record here, but just eight account for around 70% of shale drilling today in the Permian. The top three: Pioneer Natural Resources, Concho Resources (which just spent over $1 billion to acquire Three Rivers Operating), and Apache. Oxy follows close behind, then comes Energen, Sandridge, Cimarex, and EOG.

Forecasting Williston Basin Oil Production, BOPD

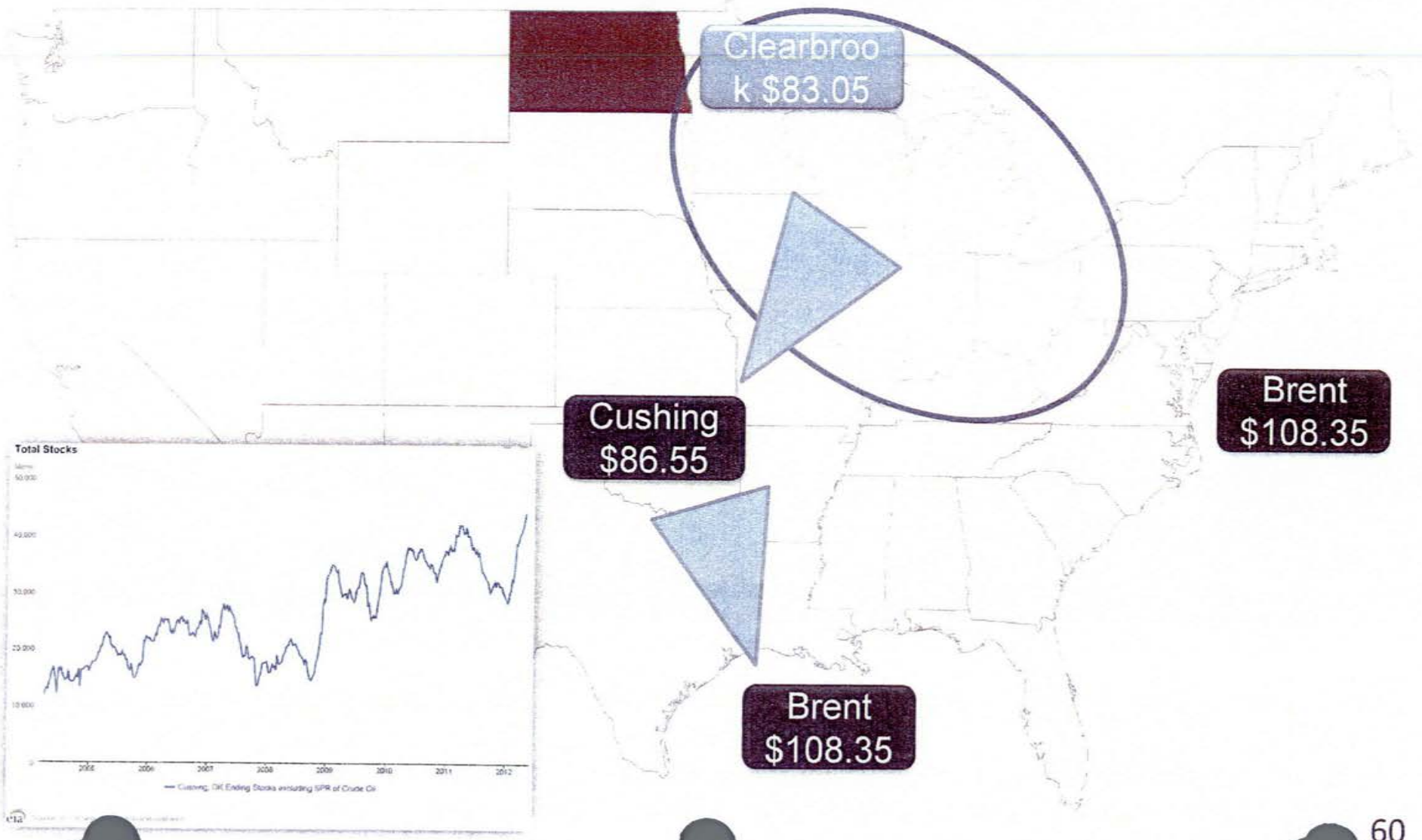


Production forecast is for visual demonstration purposes only and should not be considered accurate for any near or long term planning.

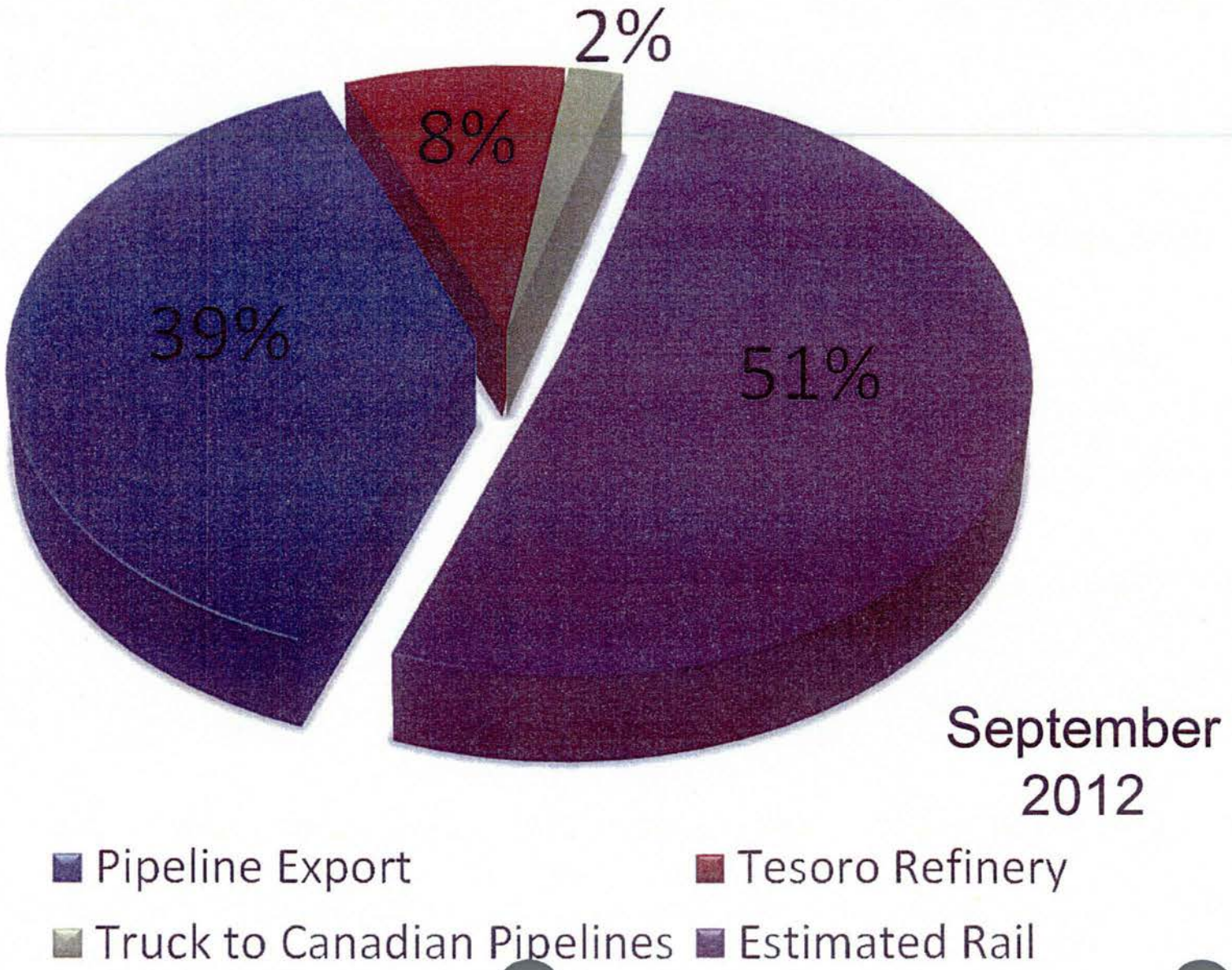
Crude Oil Prices



Crude Pricing – Dec 10, 2012



Williston Basin Oil Transportation



Western North Dakota

- 1,100 to 2,700 wells/year = 2,000 expected
  - 100-225 rigs = 12,000 – 27,000 jobs
  - Another 10,000-15,000 jobs building infrastructure
  - 200 rigs can drill the wells needed to secure leases in 1 year
  - 200 rigs can drill the wells needed to develop spacing units in 18 years
  - 35,000-40,000 new wells = 45,000-50,000 long term jobs

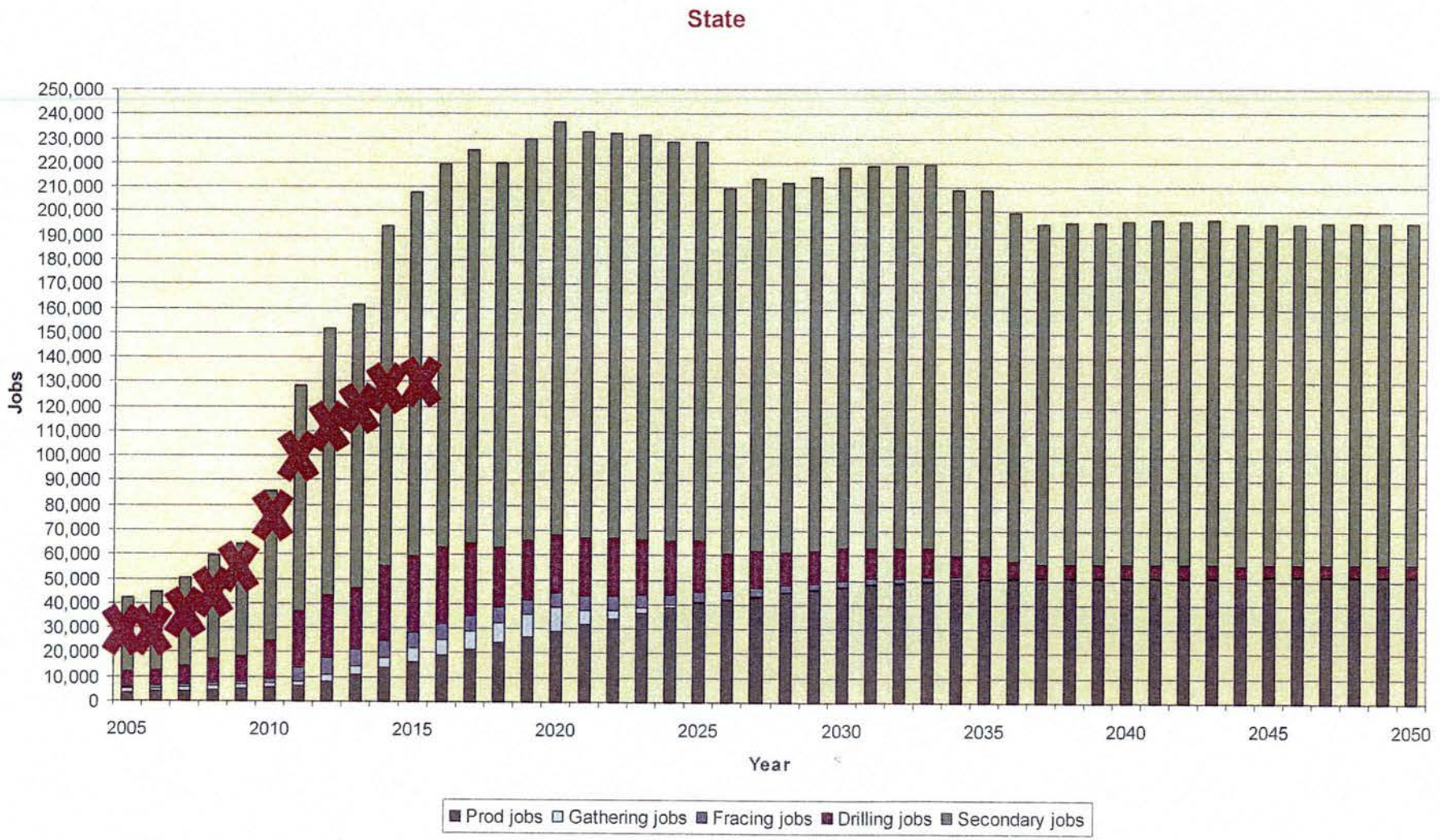
North Dakota Oil Jobs

Workforce Growth:

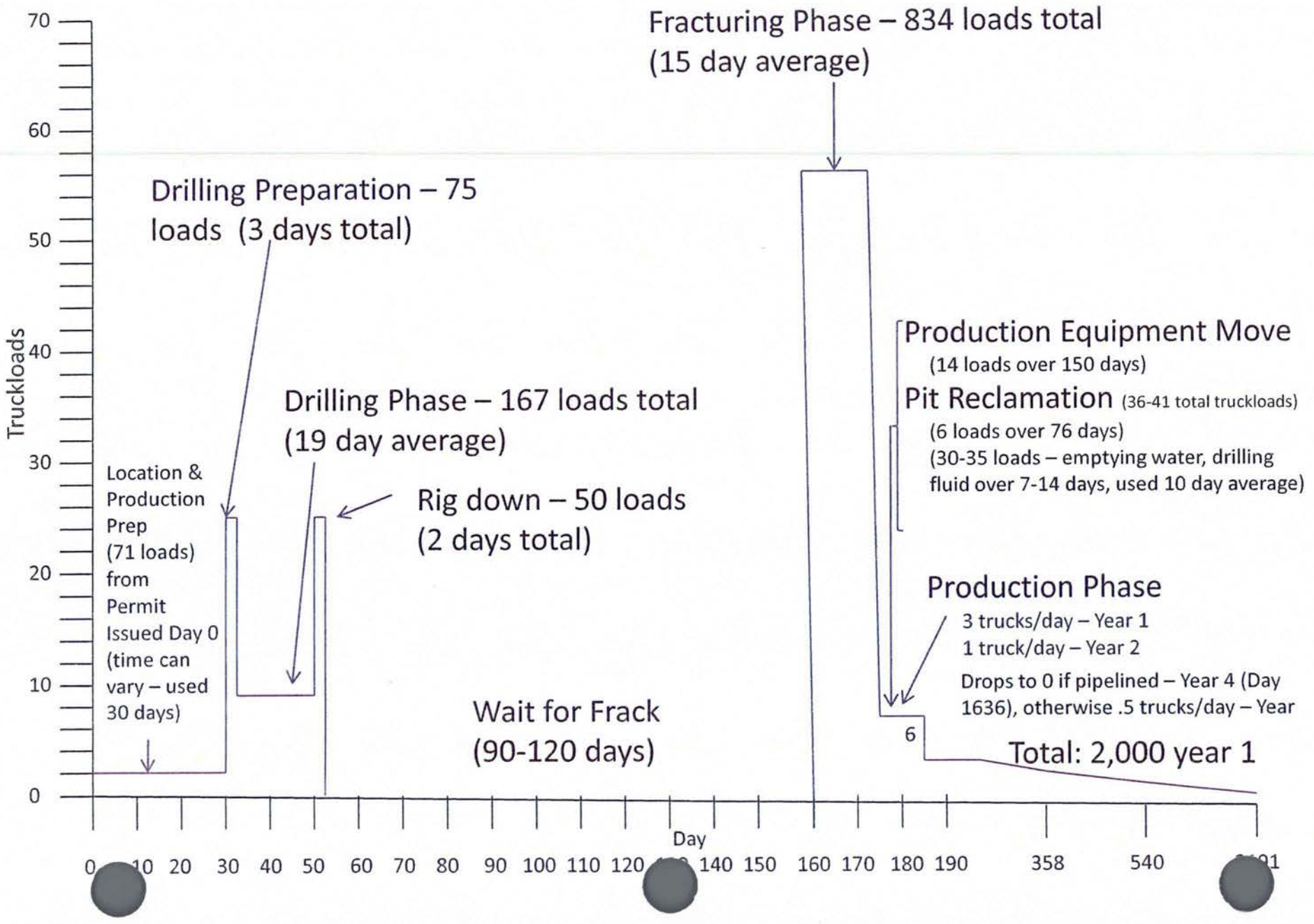
2005 -	**4,500 direct jobs**
2009 -	**18,000 direct jobs**
2012 -	**35-40,000 direct jobs**

Estimates in the future could double or triple the workforce.

Expected Case



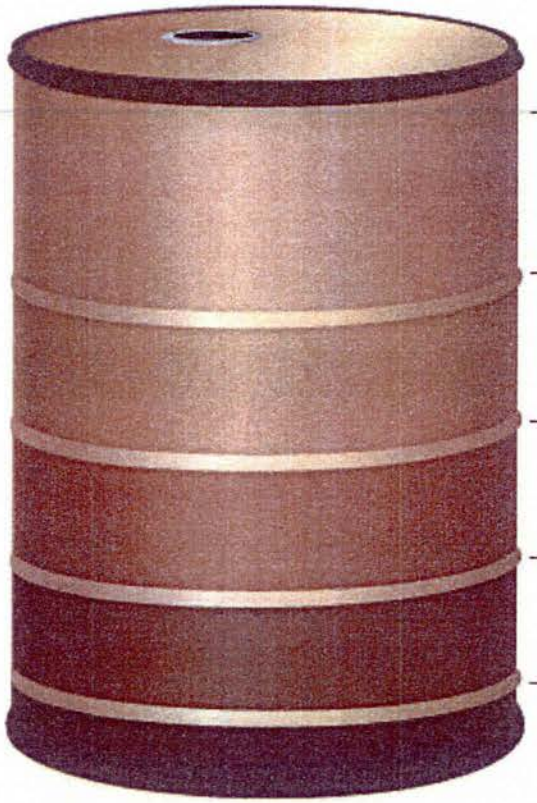
New Bakken Well – Truckload Timeline



SUMMARY OF PROPOSED 2012 RULES

NDAC	RULES	PROPOSED CHANGE
43-02-03 GENERAL RULES		
43-02-03-05	Enforcement of Laws and Rules	Move language to 43-02-03-28 (Safety Regulation)
43-02-03-15	Bonds	Increase $20,000 bond to $50,000
		Commercial SWD bond increased from $20,000 bond to $50,000
		Eliminates $50,000 10-well blanket bond
43-02-03-16	Permit to Drill	Consider csg imbrittlement due to H_2S when considering recompletions
43-02-03-16.3	Recovery of a Risk Penalty	Clarify that "approximate" well loc is to be included in the invitation to participate
		Requires the drilling or spacing unit be included in the invitation to participate
43-02-03-18	Drilling Units	Allows temporary spacing order effective for up to 3 yrs, not 1-1/2 yrs
43-02-03-19	Site Construction	Amends rule to address only initial well site construction
		Soil stabilization additives and materials require approval from Director
		Must reduce size of well site after completion if not used f/well operations
43-02-03-19.1	Fencing, Screening, and Netting of Pits	Amended to also address "drilling" pits which were newly created
43-02-03-19.2	Disposal of Waste Material	Requires all waste material from undesirable events to be immediately disposed
43-02-03-19.3	Earthen Pits and Open Receptacles	Requires flare pits to be at least 150 feet from wells and tanks
		Allows lined fresh wtr pit for frack water f/1yr in cut w/only drinking wtr chemicals
43-02-03-19.4	Drilling Pits	Creates new section addressing pits allowing cuttings, but no fluids
		Must reclaim pit w/in 30 days after drilling well; Director may grant exceptions
		Allows small lined pit f/trench water and rig wash, but reclaim before MORT
		Must dike pit to keep surface water from entering
43-02-03-19.5	Reserve Pits	Creates new section allowing reserve pits only for wells < 5000' deep or SWD
		Must reclaim pit w/in one yr after completing well
		Must slope surface to promote surface drainage away from reclaimed area
43-02-03-21	Casing, Tubing, and Cementing	Requires remedial work f/inadequate sur csg job to be approved by Director
		Requires surface casing pressure test after cementing
43-02-03-25	Deviation Tests and Directional Surveys	Requires directional surveys to be in reference to true north
43-02-03-27.1	Hydraulic Fracture Stimulation	Creates new section addressing hydraulic fracture stimulation
		Must use popoff valves, rupture disk, remote valve
		Use frack string: no chem disclosure if > 350psi on annulus after frack
		Frack down csg: run csg evaluation f/thickness of csg and cmt w/chem disclosure
43-02-03-28	Safety Regulation	Incorporated language removed from 43-02-03-05 on well shut in f/public safety
		Requires automatic shut-down equip if well is threat to public health or safety
		Prohibits injection equipment from being installed < 500' from occupied dwelling
43-02-03-30.1	Leak and Spill Cleanup	Creates new section and incorporates language from 43-02-03-49&53
		Requires operators to respond w/appropriate resources to contain & clean up spills
43-02-03-31	Well Log, Completion and Workover Reports	Run CBL prior to completion
		File two digital copies of logs, instead of one digital and one paper
43-02-03-34.1	Reclamation of Surface	Creates new section to address final restoration after well is plugged
		No additional requirements: Language taken from 43-02-03-19
43-02-03-49	Oil ~~Spills,~~ Prod Equip, Dikes, and Seals	Amend rule--move spill reference to 43-02-03-30.1
		Must remove "unused" equip rather than "unusable"
43-02-03-51	Treating Plant	Increases minimum bond from $20,000 to $50,000 for treating plants
43-02-03-53	Saltwater Handling Facilities	Amend rule--move spill reference to 43-02-03-30.1
		Requires oil recovered from saltwater handling facilities to be reported to Director
		Must remove "unused" equip rather than "unusable"
43-02-03-54	Investigative Powers	Director can timely (instead of "immediately") reply to a complaint
		Allows Director to decline to investigate--can appeal to IC
43-02-03-55	Abandonment of Wells-Suspension of Drilling	Abandonment will now include water source wells and stratigraphic tests
43-02-03-88.1	Special Procedures Administrative Hearings	Allows applications for additional wells on a spacing unit without live testimony
		Comments and objections to hearings must be rec'd prior business day by 5pm
43-02-03-90.2	Official Notice	Comments and objections to hearings must be rec'd prior business day by 5pm
43-02-12 GEOPHYSICAL EXPLORATION REQUIREMENTS		
43-02-12-06	Notification of Work Performed	Direc[illegible] require progress reports prior to completion of a project

OIL & GAS TAX ALLOCATION



Legacy Fund 33.5%

Statutory Fund 21.4%

Strategic Investments & Improvements Fund; Property Tax Relief Fund; State Disaster Fund; ND Outdoor Heritage Fund; Oil & Gas Research Fund; Energy Conservation Fund; Renewable Energy Development Fund

Constitutional Funds 21.2%

Resources Trust Fund; Common Schools Trust Fund; Foundation Aid Stabilization Fund

Political Subdivisions and Tribes 18%

Distributions to Cities & Counties; Oil & Gas Impact Grant Fund; Tribal Allocations

General Fund 5.9%

- **Industry Paid $205 million in production taxes in September 2012**
- **$1.3 billion fiscal year 2011.**

Amendment to HB 1234 - Representative Streyle

1) Six percent for production wells 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 nine hundred thousand barrels per day.
    a. *-.50% reduction in production tax at 900,000bpd*

2) Five and one-half percent for production wells 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 one million barrels per day.
    a. *-.50% reduction in production tax at 1,000,000bpd*

3) Five percent for production wells 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 one million one hundred thousand barrels per day.
    a. *-.50% reduction in production tax at 1,100,000bpd*

4) Four and one-half percent for production wells 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 one million two hundred fifty thousand barrels per day or for production on wells on or after the first day of July 2016, whichever event occurs first.
    a. *-.50% reduction in production tax at 1,250,000bpd*

13.0225.02001
Title.

Prepared by the Legislative Council staff for
Senator Dotzenrod
March 22, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, subsection 10 of section 57-51.1-01, subsection 2 of section 57-51.1-03, and subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code, relating to the oil extraction tax exemption for stripper wells; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper ~~well properties~~wells and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to annually classify and determine the status and depth and average daily production of wells that are stripper ~~well property~~wells as defined in ~~subsection 8 of~~ section 57-51.1-01, to annually certify to the tax commissioner which wells are stripper wells and the depth and average daily production of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. AMENDMENT. Subsection 10 of section 57-51.1-01 of the North Dakota Century Code is amended and reenacted as follows:

10. "Stripper well ~~property~~" means a ~~"property"~~well 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.~~

SECTION 4. AMENDMENT. Subsection 2 of section 57-51.1-03 of the North Dakota Century Code is amended and reenacted as follows:

2. The activity of extracting from the earth any oil from a stripper well ~~property~~.

SECTION 5. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted 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~~well's qualification period.

SECTION 6. EFFECTIVE DATE. This Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

Miller, Joe T.

From: Helms, Lynn D.
Sent: Wednesday, April 03, 2013 10:25 AM
To: Miller, Joe T.
Subject: RE: Oil producing wells

Good morning,

Yesterday turned into a whirlwind around here.

We have 9,150 wells capable of production and 8,224 wells actually producing at the end of January 2013 (the latest month data is available).

There are 2,974 active stripper wells as follows:
1,622 have single well status
562 are in enhanced oil recovery units
789 have spacing unit stripper well property status
123 are Bakken / Three Forks
111 have qualified a 1280 spacing unit for stripper well property status
5 are producing significantly above the 30 barrel per day current stripper well qualifying rate
1 new well on a 1280 acre Bakken stripper well property with IP rate of 508 barrels oil per day / January 2013 production 203 barrels oil per day
Original well had initial production of 73 barrels oil per day / January 2013 production 5 barrels oil per day
1 new drill well on a 1280 acre Bakken stripper well property no production reported yet
Original well now plugged had initial production of 40 barrels oil per day
5 pending applications
12 have qualified a 640 acre spacing unit
none are producing significantly above the 30 barrel per day current stripper well qualifying rate
no new wells on a 640 acre Bakken stripper well property as of January 2013

There are 187 inactive stripper wells as follows:
26 temporarily shut in
146 temporarily abandoned to retain the well bore
15 temporarily abandoned for observation

-----Original Message-----
From: Miller, Joe T.
Sent: Tuesday, April 02, 2013 9:50 AM
To: Helms, Lynn D.
Subject: Oil producing wells

Lynn,

How many oil producing wells do we have and how many are stripper wells?

Joe

13.0225.02007
Title.

Prepared by the Legislative Council staff for
Senator Cook

April 3, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

Page 1, line 1, after "A BILL" replace the remainder of the bill with "to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01, 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

<u>Withholding requirement for oil and gas royalty payments to nonresidents.</u>

<u>1. For purposes of this section:</u>

a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

b. "Remitter" means any person who distributes royalty payments to royalty owners.

c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed

by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.

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. "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 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. "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 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.

8. "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.

9. "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. "Stripper well" means a well drilled and completed after June 30, 2013, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and forty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

11. "Stripper well property" means wells drilled and completed before July 1, 2013, on 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.~~12. "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.~~13. "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 5. 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, 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 or individual stripper well.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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, and before July 1, 2015, 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.

10. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed

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outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 6. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 7. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~ All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

SECTION 8. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

FORT BERTHOLD

Year or Biennium	Current Agreement Tax Dept. Estimate		Production Fee Land 20%-50% Increase		Extraction 60 Month Exemption Eliminated		Extraction Existing Wells Coming Off 60 Month Exemption		New Proposed Total	Change
2009	2.4 M									
2010	10.9 M									
2011	33.8 M									
2012	74.7 M									
2013 (1ST 6 mo.)	65.0 M - (Estimate)									
Proposal										
2013-15	319.2 M	+	34.8 M	+	43.5 M	+	2.7 M	=	400.2 M	81.0 M
2015-17	528.1 M	+	119.9 M	+	78.0 M	+	33.7 M	=	759.7 M	231.6 M

STATE - NORTH DAKOTA

Year or Biennium	Current Agreement Tax Dept. Estimate		Production Fee Land 80%-50% Increase		Extraction 60 Month Exemption Eliminated		Extraction Existing Wells Coming Off 60 Month Exemption		New Proposed Total	Charge
2009	7.2 M									
2010	25.3 M									
2011	61.2 M									
2012	113.5 M									
2013 (1st 6 mo.)	90.0 M - (Estimate)									
Proposal										
2013-15	388.8 M	+	-34.8 M	+	43.5 M	+	-2.7 M	=	394.8 M	6.0 M
2015-17	767.9 M	+	-119.9 M	+	78.0 M	+	-33.7 M	=	692.3 M	-75.6 M

Prepared by the Legislative Council staff for
Senator Cook

April 3, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01 and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

<u>Withholding requirement for oil and gas royalty payments to nonresidents.</u>

<u>1. For purposes of this section:</u>

a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

b. "Remitter" means any person who distributes royalty payments to royalty owners.

c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed

by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.

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. "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 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. "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 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.

8. "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.

9. "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. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, after June 30, 2013, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and forty barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

11. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before July 1, 2013, on 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.~~12. "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.~~13. "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 5. 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, 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 or individual stripper well.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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, and before July 1, 2015, 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.

10. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed

outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 6. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 7. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

SECTION 8. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly

#1
HB 1234
4-10-13

NORTH DAKOTA HOUSE OF REPRESENTATIVES

APPROPRIATIONS COMMITTEE

TESIMONY OF THREE AFFILIATED TRIBES

VICE CHAIRMAN FREDERICK W. FOX

APRIL 10, 2013

CHAIRMAN HOLMBERG AND DISTINGUISHED COMMITTEE MEMBERS, MY NAME IS FRED FOX AND I SERVE AS THE VICE CHAIRMAN OF THE THREE AFFILIATED TRIBES – THE MANDAN HIDATSA ARIKARA NATION. I AM HERE TODAY TO PROVIDE TESTIMONY ON HOUSE BILL 1234 THAT CONCERNS THE PROPOSED AMENDMENT TO THE CURRENT OIL AND GAS TAX AGREEMENT BETWEEN THE STATE OF NORTH DAKOTA AND THE THREE AFFILIATED TRIBES.

IN 2008, THE THREE AFFILIATED TRIBES AND THE GOVERNOR'S OFFICE NEGOTIATED THE CURRENT TAX AGREEMENT BETWEEN OUR TWO GOVERNMENTS. AT THAT TIME, I SERVED AS THE ENERGY DIRECTOR FOR THE TRIBES AND WAS INVOLVED IN ALMOST ALL OIL & GAS ISSUES INVOLVING OUR TRIBE. BOTH THE TRIBE AND THE STATE BOTH UNDERSTOOD THAT WE NEEDED TO FIND COMMON GROUND TO PROVIDE A STABLE TAX STRUCTURE IN A LEGAL ENVIRONMENT WHERE BOTH THE STATE AND THE TRIBE HAVE THE AUTHORITY TO ASSESS TAXES ON OIL AND GAS ACTIVITY ON THE FORT BERTHOLD RESERVATION.

THE TRIBE WORKED VERY CLOSELY WITH THE GOVERNOR'S OFFICE, BOTH SIDES REALIZING THAT EACH GOVERNMENT HAD A SERIOUS STAKE IN THE

DEVELOPMENT OF RESERVATION. WHILE WE WERE NOT COMPLETELY SATISFIED WITH THE TERMS, THE TRIBE VIEWED AS NECESSARY STARTING POINT TO STIMULATE OIL & GAS EXPLORATION AND PRODUCTION ON FORT BERTHOLD. IN FACT, THE FIRST BAKKEN OIL WELL ON TRUST LAND WAS DRILLED SOON AFTER THE TRIBE AND THE STATE ENTERED INTO THIS AGREEMENT. HOWEVER, WE HAVE ALWAYS MAINTAINED THE POSITION THAT WE WOULD BOTH COME BACK TO THE TABLE IN THE FUTURE TO REVIEW AND UPDATE THAT AGREEMENT. THAT IS WHY WE ARE ALL HERE TODAY, TO REVIEW AND DISCUSS HOUSE BILL 1234.

IN 2008 AND AGAIN IN 2010 WHEN WE RENEWED THAT INITIAL AGREEMENT, NO ONE IN THE TRIBE OR THE STATE KNEW WHAT IMPACTS OIL AND GAS ACTIVITY WOULD HAVE. NO ONE COULD HAVE PREDICTED THE COSTS OF INCREASED HEAVY MOTOR VEHICLE TRAFFIC, AN INCREASED POPULATION AND THE SHEER AMOUNT OF INCREASED INDUSTRIAL ACTIVITY IN OUR COMMUNITIES. AT THAT TIME, WE WERE JUST SEEKING TO INCREASE THE OIL AND GAS ACTIVITY WITHIN OUR RESPECTIVE LANDS IN THE HOPES OF IMPROVING THE LIVES OF THE PEOPLE WHO LIVE AND WORK THERE.

NOW IN 2013, THE TRIBE IS FACING THE TRUE COSTS OF OIL EXPLORATION ON THE FORT BERTHOLD RESERVATION, BOTH FINANCIALLY AND IN TERMS OF HUMAN IMPACTS. WHILE MUCH HAS BEEN SAID ABOUT THE REVENUES THE TRIBE RECEIVES AND I MIGHT ADD, AS THE STATE ALSO RECEIVES TO A MUCH LARGER DEGREE, MOST OF OUR TRIBAL INCOME GOES DIRECTLY TO HISTORICALLY UNDERFUNDED TRIBAL GOVERNMENTAL SERVICES.

WE ARE NOT TALKING ABOUT EXCESSIVE OR EXTRAVAGANT SERVICES, WE ARE TALKING ABOUT BASIC HEALTHCARE, AFFORDABLE HOUSING, POTABLE WATER TO ALL RESIDENTS OF THE RESERVATION, LAW ENFORCEMENT, ELDERLY SERVICES, SOCIAL SERVICES AND OF COURSE ROAD MAINTENANCE AND IMPROVEMENT.

IN FISCAL YEAR 2013, WE HAVE ALREADY EXPENDED $5 MILLION ON ROADS, ALLOCATED $18 MILLION TO AFFORDABLE HOUSING, AN ADDITIONAL $9 MILLION TO PROVIDE STAFF HOUSING FOR OUR ELBOWOODS HEALTH CARE FACILITY AND $6.5 MILLION TO THE OPERATIONS OF THE TRIBAL HEALTH FACILITY. WE HAVE FUNDED OUR TRIBAL PROGRAMS, PROVIDED NEW EMPLOYMENT OPPORTUNITIES, WORKED TO REDUCE OUR OVERALL GOVERNMENTAL DEBT....MUCH AS THE STATE OF NORTH DAKOTA HAS DONE WITH ITS TAX REVENUES. AS WE DO NOT HAVE MANY OF THE ADDITIONAL TAX REVENUE STREAMS AS THE STATE DOES, THE TRIBE MUST UTILIZE AND MAXIMIZE EVERY DOLLAR WE RECEIVE TO ACHIEVE THOSE BASIC GOVERNMENTAL GOALS.

AN IMPORTANT ELEMENT WE MUST NOT LOSE FOCUS AS WE DISCUSS AND WORK TOWARD AMENDING THE ORIGINAL TAX AGREEMENT, THE TRIBE AND THE STATE OF NORTH DAKOTA ARE BOTH SOVEREIGN GOVERNMENTS. WE MUST WORK TOGETHER WITHIN A GOVERNMENT-TO-GOVERNMENT BASIS THROUGH THE ACKNOWLEDGEMENT THAT EACH OF US ARE WORKING TO ACHIEVE BOTH COMMON AND INVIDUAL GOALS AS WE SERVE AND PROTECT OUR LANDS, OUR IDENTITIES AND OUR MANY CONSTIUENTS.

IN CLOSING, I AM HERE TO REINFORCE THE TRIBAL BUSINESS COUNCIL'S OFFICIAL POSITION AS APPROVED IN OUR MARCH 28, 2013 MEETING WHERE WE PASSED OUR OFFICIAL SUPPORT OF THE CURRENT LANGUAGE OF HOUSE BILL 1234 BEFORE US TODAY. AN AMENDMENT WHERE BOTH THE STATE AND TRIBE SHARE EQUALLY IN THE OIL & GAS REVENUES GENERATED ON THE FORT BERTHOLD RESERVATION, REGARDLESS OF THE WHETHER THAT LAND IS IN FEE OR TRUST. FURTHER, WE SUPPORT THE SUSPENSION OF THE CURRENT EXTRACTION TAX HOLIDAY THAT APPLIES TO RESERVATION LANDS. FINALLY, WE SUPPORT A STABLE AND CONSISTENT TAX STRUCTURE TO ENCOURAGE THE FURTHER DEVELOPMENT OF OUR INTERWINED ECONOMIES AND OUR INDIVIDUAL GOVERNMENTS.

THANK YOU FOR THE OPPORTUNITY TO SPEAK TO THE COMMITTEE TODAY

Summary of Tax Revenues and Disbursements
July1, 2008 Through March 31, 2013

	Trust	Non-Trust
Source of Tax Revenues	$327,868,072 (64%)	$188,443,401 (36%)

	Tribe	State
Disbursements Of Tax Revenues	$201,541,970 (39%)	$314,769,503 (61%)

64% of the total tax dollars collected on the agreement were from Trust lands. However the Tribe only received 39% of the total tax revenues collected within the boundaries of the Fort Berthold Reservation.

Note: Trust lands as defined in the State-Tribe Tax Agreement includes land held in Trust by the United States for both the Government of the Three Affiliated Tribes and its individual tribal members. Non-Trust is defined as all acres in a spacing unit not classified as trust lands.

Note: The information does not exactly match the actual distribution from the State Treasurer Office because the disbursements include refunds, interest and penalties, etc. not included in the State Tax Commission spreadsheet.

Note: The tax agreement calls for a 50/50 split on Trust lands for both production and extraction taxes, a 20/80 split for production taxes on fee land a 0/100 split for extraction tax on fee lands (after the five year exemption) for the tribe/state

Sources: Information presented herein was generated from data received from the North Dakota Office of the State Tax Commission.

#2

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

Testimony of Ron Ness
House Bill 1234
Senate Appropriations Committee
April 10, 2013

Chairman Holmberg and members of the Senate Appropriations Committee, my name is Ron Ness, president of the North Dakota Petroleum Council. The North Dakota Petroleum Council represents more than 400 companies in all aspects of the oil and gas industry, including oil and gas production, refining, pipeline, transportation, mineral leasing, consulting, legal work, and oilfield service activities in North Dakota. I appear before you today in support of the Tribal tax provisions included in House Bill 1234.

Just like in the counties across the oil patch, rapid oil and gas development has impacted Fort Berthold. The same challenges facing our oil impacted counties, like housing shortages, inadequate emergency, health and social services, and growing maintenance needs for roads and infrastructure, are facing the Reservation. In fact, the community needs on the Reservation may be greater given they were lacking services and infrastructure prior to the rapid growth of oil and gas development.

Road maintenance and repair is an ongoing concern on the Reservation. Most oil and gas activity on the Reservation requires travel on BIA or tribal roads. Companies operating on the Reservation have dedicated significant resources to help maintain Reservation roads and manage dust control efforts, but this is not a sustainable, long-term solution. The added costs associated with road work and other fees continue to be a significant concern for our operators. If operators do not drill the projected wells as a result of increased costs and fees on the reservation, the state will see a much larger deduction in revenues.

By increasing the share of tax dollars going back to the Tribe, HB 1234 will help address these issues, increase the stability of our operations on Tribal lands, and improve essential infrastructure and services on Fort Berthold. A lack of fiscal and regulatory certainty make it very difficult to continue operating at such a high cost. Unless we can pass an agreement, that uncertainty will continue, putting oil and gas development on Fort Berthold in serious jeopardy. We feel North Dakota's current tax revenue projections and budget surplus make increasing the share of oil and gas tax revenue returned to the Three Affiliate Tribes a timely and reasonable request. I would be happy to answer any questions.

13.0225.02012

Sixty-third
Legislative Assembly
of North Dakota

FIRST ENGROSSMENT

ENGROSSED HOUSE BILL NO. 1234

Introduced by

Representatives Streyle, Owens, Thoreson

Senator Armstrong

A BILL for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and sections 57-51.1-01, 57-51.1-02, 57-51.1-03, ~~and~~ 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax rates and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties or individual stripper wells and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells

that are stripper well property or individual stripper wells as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:
   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.
   b. "Remitter" means any person who distributes royalty payments to royalty owners.
   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.
2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.
3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:
   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;
   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];
   c. The United States as trustee for individual Indians;
   d. A publicly traded partnership;

1 e. An organization that is exempt from the tax under this chapter; or
2 f. The same person or entity as the remitter.
3 4. a. This section does not apply to a remitter that produced less than three hundred
4 fifty thousand barrels of oil or less than five hundred million cubic feet of gas in
5 the preceding calendar year as certified to the tax commissioner in the manner
6 and on forms prescribed by the tax commissioner.
7 b. Each remitter that is exempt from withholding under this subsection shall make
8 an annual return to report royalty payments that exceed the dollar amounts in
9 subsection 6 and must be reported in the same manner as provided in section
10 57-38-60.
11 5. a. Each year, a publicly traded partnership that is exempt from withholding under
12 subsection 3 shall transmit to the tax commissioner, in an electronic format
13 approved by the tax commissioner, each partner's United States department of
14 the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed
15 electronically for the year with the United States internal revenue service.
16 b. A royalty owner that is a publicly traded partnership, or an organization exempt
17 from taxation under section 57-38-09, shall report to the remitter and tax
18 commissioner under oath, on a form prescribed by the tax commissioner, all
19 information necessary to establish that the remitter is not required under
20 subsection 2 to withhold royalty payments made to the partnership or
21 organization.
22 6. If the royalty payment made to a royalty owner under this section is less than six
23 hundred dollars for the current withholding period, or is less than one thousand dollars
24 if the payment is annualized, the tax commissioner may grant a remitter's request to
25 forego withholding the tax from the royalty payment made to that royalty owner for the
26 current withholding period or, if applicable, the royalty payments for the annual period.

27 **SECTION 4. AMENDMENT.** Section 57-51.1-01 of the North Dakota Century Code is
28 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 closedstatewide 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.~~3. "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.~~5.4. "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~~, certified as qualifying by the industrial commission, and from which the project operator ~~must have~~has obtained incremental production as defined in ~~subsection 5 of section 57-51.1-03~~rules of the industrial commission.

~~8.6.~~5. "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.~~7.6. "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~~9.7. "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~~thirty 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~~which was considered part of a stripper well property for purposes of this chapter on June 30, 2013, and which has not been redrilled or repaired after June 30, 2013.

~~9.~~8. "Stripper well property" means a "property" ~~outside the Bakken and Three Forks formations~~ certified by the industrial commission before July 1, 2013, 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~~A well drilled and completed after June 30, 2013, on a stripper well property is not a stripper well and is not exempt under subsection 2 of section 57-51.1-03 until production from that well individually qualifies it as a stripper well under subsection 7.

~~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 5. 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;~~

~~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.~~

~~1. Six percent for production from wells drilled and completed 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 eight hundred thousand barrels per day.~~

~~2. Five and one-half percent for production from wells drilled and completed 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 nine hundred thousand barrels per day.~~

~~3. Five percent for production from wells drilled and completed 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 one million barrels per day, or for production from wells drilled and completed on or after the first day of July 2015, whichever event occurs first.~~

SECTION 5. 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, 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 or individual stripper well. A well ~~in the Bakken or Three Forks formation which was certified as a stripper well or as~~that is exempt as part of a stripper well property at the time it is ~~reentered or reworked~~redrilled or repaired retains its stripper well or stripper well property exempt status for the first twelve months of production from that well after completion of the ~~reentry or reworking~~redrilling or repairing project. After that period, the stripper well or stripper well property exempt status is lost ~~after the average daily production of the well exceeds one hundred barrels per day for a calendar month and the well is then subject to a reduced tax rate of two percent under this chapter until production from that well individually meets the requirements of the definition of stripper well under section 57-51.1-01~~as of the first day of the next calendar quarter if the industrial commission has not recertified that well as a stripper well.
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 drilled and completed before July 1, 2013, and located within the boundaries of an Indian reservation;

b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

c. The well is drilled and completed before July 1, 2013, on lands held by an Indian tribe if the tribe's 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.~~

5. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 6. 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 <u>or rate reduction</u> on production from a stripper well property <u>or individual stripper well</u> 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 <u>or individual stripper well's</u> 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 7. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.
2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.
3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed ~~six and one-half percent~~the maximum rate under chapter 57-51.1 but may be reduced through negotiation between the governor and the Three Affiliated Tribes.
4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.
5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:
   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.
   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~
   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.
6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.
8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.
9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.
10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.
11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.
12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report identifies projects totaling investment of at least ten percent of tribal oil and gas gross production and oil extraction tax receipts of the tribe for that year in essential infrastructure.

SECTION 8. EFFECTIVE DATE. ~~This~~Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013.

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

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on pages 1508-1511 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "Act" insert "to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties;"

Page 1, line 2, remove "and"

Page 1, line 2, after "57-51.1-03.1" insert ", and 57-51.2-02"

Page 1, line 3, after "exemptions" insert "and the state-tribal oil tax agreement"

Page 2, after line 3, insert:

"**SECTION 3.** A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period."

Page 2, line 15, overstrike ""Average"

Page 2, line 20, remove "statewide production" means the number of barrels of oil produced from wells"

Page 2, remove line 21

Page 2, line 22, remove "that month, as determined by the industrial commission"

Page 2, line 22, overstrike the period

Page 2, line 23, overstrike "3."

Page 3, line 1, replace "4." with "3."

Page 3, line 7, replace "5." with "4."

Page 3, line 18, replace "6." with "5."

Page 4, line 15, replace "7." with "6."

Page 4, line 18, replace "8." with "7."

Page 4, line 18, remove "inside the Bakken or Three Forks formations"

Page 4, line 23, replace "fifty" with "thirty"

Page 4, line 25, remove "inside the Bakken or Three Forks formations which was"

Page 4, line 26, replace the second "and" with "which"

Page 4, line 27, after "2013" insert ", and which has not been redrilled or repaired after June 30, 2013"

Page 4, line 28, replace "9." with "8."

Page 4, line 28, remove "outside the Bakken and Three Forks"

Page 4, line 29, replace "formations" with "certified by the industrial commission before July 1, 2013."

Page 5, line 4, overstrike "Wells which did not actually yield or produce oil during the qualifying"

Page 5, overstrike lines 5 through 7 and insert immediately thereafter "A well drilled and completed after June 30, 2013, on a stripper well property is not a stripper well and is not exempt under subsection 2 of section 57-51.1-03 until production from that well individually qualifies it as a stripper well under subsection 7"

Page 5, line 27, overstrike "and one-half"

Page 5, line 27, overstrike the comma

Page 5, line 28, overstrike "except that the rate of tax is"

Page 6, line 11, remove the overstrike over the overstruck period

Page 6, remove lines 18 through 30

Page 7, line 8, remove "in the Bakken or Three Forks formation which was"

Page 7, line 9, replace "certified as a stripper well or as" with "that is exempt as"

Page 7, line 10, replace "reentered or reworked" with "redrilled or repaired"

Page 7, line 11, remove "reentry"

Page 7, line 12, replace "or reworking" with "redrilling or repairing"

Page 7, line 13, remove "after the average daily production of the well exceeds one hundred"

Page 7, replace lines 14 through 16 with "as of the first day of the next calendar quarter if the industrial commission has not recertified that well as a stripper well."

Page 12, line 6, after "is" insert "drilled and completed before July 1, 2013, and"

Page 12, line 7, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "the" insert "tribe's"

Page 12, after line 27, insert:

"5. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion."

Page 19, after line 15, insert:

"**SECTION 7. AMENDMENT.** Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed ~~six and one-half percent~~the maximum rate under chapter 57-51.1 but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report identifies projects totaling investment of at least ten percent of tribal oil and gas gross production and oil extraction tax receipts of the tribe for that year in essential infrastructure."

Page 19, line 16, replace "This" with "Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this"

Renumber accordingly

#1

FORT BERTHOLD INDIAN RESERVATION (F.B.I.R.)

BOUNDARIES WITHIN MOUNTRAIL COUNTY

TOTAL MILES OF ROAD

307.75	TOTAL ROADS ON THE F.B.I.R.

RESERVATION ROADS MAINTAINED BY MOUNTRAIL COUNTY =

221.50	TOWNSHIP GRAVELED ROADS
47.25	COUNTY GRAVELED ROADS
16.50	COUNTY PAVED ROADS
285.25	ALL ROADS MAINTAINED BY MOUNTRAIL COUNTY

RESERVATION ROADS MAINTAINED BY BUREAU OF INDIAN AFFAIRS =

10.00	GRAVELED ROADS
12.50	PAVED ROADS
22.50	ALL ROADS MAINTAINED BY B.I.A. (TO THE BEST OF OUR KNOWLEDGE)

FACT :

COUNTY / TOWNSHIPS MAINTAINS 93% OF THE ROADS ON THE RESERVATION

B.I.A MAINTAINS 7% OF THE ROADS ON THE RESERVATION

13.0225.02015
Title.

Prepared by the Legislative Council staff for
Representative Drovdal
April 23, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on pages 1508-1511 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "Act" insert "to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties;"

Page 1, line 2, remove "and"

Page 1, line 2, after "57-51.1-03.1" insert ", and 57-51.2-02"

Page 1, line 3, after "exemptions" insert "and the state-tribal oil tax agreement"

Page 2, after line 3, insert:

"**SECTION 3.** A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period."

Page 2, line 15, overstrike ""Average"

Page 2, line 20, remove "statewide production" means the number of barrels of oil produced from wells"

Page 2, remove line 21

Page 2, line 22, remove "that month, as determined by the industrial commission"

Page 2, line 22, overstrike the period

Page 2, line 23, overstrike "3."

Page 3, line 1, replace "4." with "3."

Page 3, line 7, replace "5." with "4."

Page 3, line 18, replace "6." with "5."

Page 4, line 15, replace "7." with "6."

Page 4, line 18, replace "8." with "7."

Page 4, line 18, remove "inside the Bakken or Three Forks formations"

Page 4, line 23, replace "fifty" with "thirty"

Page 4, line 25, remove "inside the Bakken or Three Forks formations which was"

Page 4, line 26, replace the second "and" with "which"

Page 4, line 27, after "2013" insert ", and which has not been redrilled or repaired after June 30, 2013"

Page 4, line 28, replace "9." with "8."

Page 4, line 28, remove "outside the Bakken and Three Forks"

Page 4, line 29, replace "formations" with "certified by the industrial commission before July 1, 2013,"

Page 5, line 4, overstrike "Wells which did not actually yield or produce oil during the qualifying"

Page 5, overstrike lines 5 through 7 and insert immediately thereafter "A well drilled and completed after June 30, 2013, on a stripper well property is not a stripper well and is not exempt under subsection 2 of section 57-51.1-03 until production from that well individually qualifies it as a stripper well under subsection 7."

Page 5, line 22, after the first boldfaced period insert "**(Effective through September 30, 2014)**"

Page 5, line 27, overstrike the comma

Page 5, line 28, overstrike "except that the rate of tax is"

Page 6, line 11, remove the overstrike over the overstruck period

Page 6, replace lines 18 through 30 with:

"**(Effective after September 30, 2014) 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."

Page 7, line 8, remove "in the Bakken or Three Forks formation which was"

Page 7, line 9, replace "certified as a stripper well or as" with "that is exempt as"

Page 7, line 10, replace "reentered or reworked" with "redrilled or repaired"

Page 7, line 11, remove "reentry"

Page 7, line 12, replace "or reworking" with "redrilling or repairing"

Page 7, line 13, remove "after the average daily production of the well exceeds one hundred"

Page 7, replace lines 14 through 16 with "as of the first day of the next calendar month if the industrial commission has not recertified that well as a stripper well."

Page 12, line 6, after "is" insert "drilled and completed before July 1, 2013, and"

Page 12, line 7, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "the" insert "tribe's"

Page 12, after line 27, insert:

"5. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion."

Page 19, after line 15, insert:

"**SECTION 8. AMENDMENT.** Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed ~~six and one-half percent~~the maximum rate under chapter 57-51.1 but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report identifies projects totaling investment of at least ten percent of tribal oil and gas gross production and oil extraction tax receipts of the tribe for that year in essential infrastructure."

Page 19, line 16, replace "This" with "Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this"

Renumber accordingly

13.0225.02015

Sixty-third
Legislative Assembly
of North Dakota

FIRST ENGROSSMENT

ENGROSSED HOUSE BILL NO. 1234

Introduced by

Representatives Streyle, Owens, Thoreson

Senator Armstrong

A BILL for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, and sections 57-51.1-01, 57-51.1-02, 57-51.1-03, ~~and~~ 57-51.1-03.1, and 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax rates and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties or individual stripper wells and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells

that are stripper well property or individual stripper wells as defined in ~~subsection 8 of~~ section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:
   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.
   b. "Remitter" means any person who distributes royalty payments to royalty owners.
   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.
2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.
3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:
   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;
   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];
   c. The United States as trustee for individual Indians;
   d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 closedstatewide 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.~~4.3. "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.~~5.4. "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,~~ certified as qualifying by the industrial commission, and from which the project operator ~~must have~~has obtained incremental production as defined in ~~subsection 5 of section 57-51.1-03~~rules of the industrial commission.

~~8.~~6.5. "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.~~7.6. "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~~8.7. "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~~thirty 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~~which was considered part of a stripper well property for purposes of this chapter on June 30, 2013, and which has not been redrilled or repaired after June 30, 2013.

~~9.~~8. "Stripper well property" means a "property" ~~outside the Bakken and Three Forks formations~~certified by the industrial commission before July 1, 2013, 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.~~A well

drilled and completed after June 30, 2013, on a stripper well property is not a stripper well and is not exempt under subsection 2 of section 57-51.1-03 until production from that well individually qualifies it as a stripper well under subsection 7.

~~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 5. AMENDMENT. Section 57-51.1-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-02. (Effective through September 30, 2014) ~~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;~~

~~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.~~

~~1. Six percent for production from wells drilled and completed 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 eight hundred thousand barrels per day.~~

~~2. Five and one-half percent for production from wells drilled and completed 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 nine hundred thousand barrels per day.~~

~~3. Five percent for production from wells drilled and completed 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 one million barrels per day, or for production from wells drilled and completed on or after the first day of July 2015, whichever event occurs first.~~

(Effective after September 30, 2014) 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.

SECTION 6. 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, 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 or individual stripper well. A well ~~in the Bakken or Three Forks formation which was certified as a stripper well or as~~that is exempt as part of a stripper well property at the time it is ~~reentered or reworked~~redrilled or repaired retains its stripper well or stripper well property exempt status for the first twelve months of production from that well after completion of the ~~reentry or reworking~~redrilling or repairing project. After that period, the stripper well or stripper well property exempt status is lost ~~after the average daily production of the well exceeds one hundred barrels per day for a calendar month and the well is then subject to a reduced tax rate of two percent under this chapter until production from that well individually meets the requirements of the definition of stripper well under section 57-51.1-01.~~as of the first day of the next calendar month if the industrial commission has not recertified that well as a stripper well.
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 drilled and completed before July 1, 2013, and located within the boundaries of an Indian reservation;

b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

c. The well is drilled and completed before July 1, 2013, on lands held by an Indian tribe if the tribe's 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.~~

5. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 7. 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 <u>or rate reduction</u> on production from a stripper well property <u>or individual stripper well</u> 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 <u>or individual stripper well's</u> 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 8. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.
2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.
3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed ~~six and one-half percent~~the maximum rate under chapter 57-51.1 but may be reduced through negotiation between the governor and the Three Affiliated Tribes.
4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.
5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:
   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.
   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~
   c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.
6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.
8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.
9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.
10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.
11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.
12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report identifies projects totaling investment of at least ten percent of tribal oil and gas gross production and oil extraction tax receipts of the tribe for that year in essential infrastructure.

SECTION 9. EFFECTIVE DATE. ~~This~~Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013.

#3

HB 1234 Amendment – Revised Fiscal Effect

Stripper well change	**+105 million**
Incentive outside the Bakken/Three Forks	**-$35.4 million**
Tribal tax sharing change (GPT and OET)	**-$37.5 million**
Remove 5-year holiday on reservation	**+43.5 million**
Income tax withholding on royalties	**+4.2 million**
½% tax reduction on all production October 2014	**$-80 million**
Total state fiscal impact =	**$0**

Major Provisions of HB 1234 Amendment

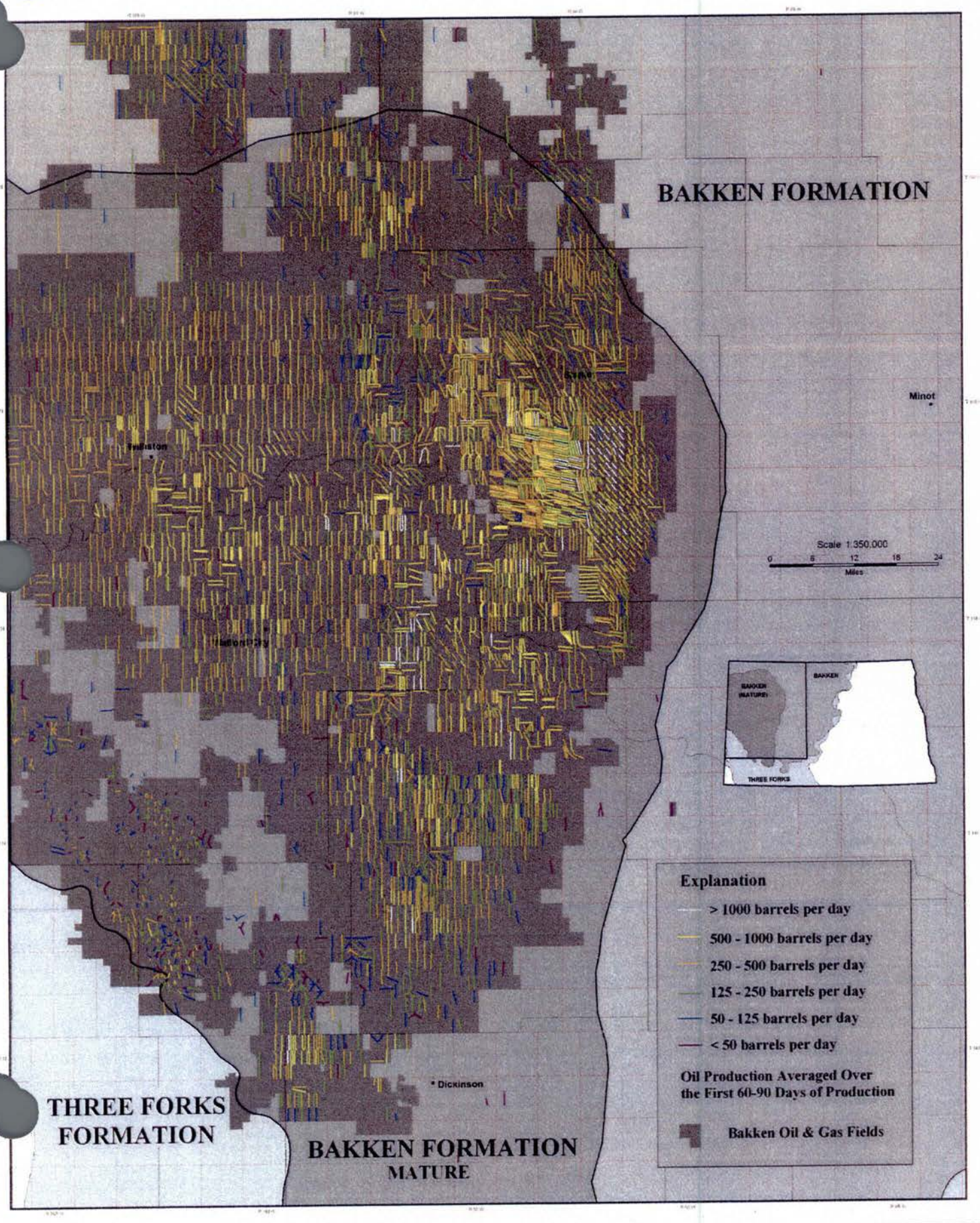
And Rough Estimate of 2015-17 Impact

	2013-15 Biennium	2015-17 Biennium/1
Stripper well property elimination	$ 105,000,000	$ 220,000,000 /2
Incentive outside the Bakken/Three Forks	(35,400,000)	(56,600,000) /3
Tribal tax sharing change (GPT and OET)	(37,500,000)	(119,900,000) /4
Remove 5-year holiday on reservation	43,500,000	78,000,000 /4
Income tax withholding on royalties	4,200,000	One-time Speed-up Only
½% tax reduction on all production October 2014	(80,000,000)	(264,000,000) /5
Total	$ (200,000)	$ (142,500,000)

/1 There is no official forecast for the 2015-17 biennium. Assumptions for a rough estimate are below:
/2 Revenue increase is compounded with 10% growth assumed in 2015-17 biennium
/3 Cost of incentive repeats in next biennium plus the last 6 months of incentive from 2013-15 biennium
/4 Estimate provided to Tribe that continues a trend
/5 Assumes 10% growth in oil extraction tax

First 60 - 90 Day Average Bakken Horizontal Production by Well

April 2013



Prepared by the Legislative Council staff for
Senator Triplett
April 24, 2013

#2

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

10. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the mature area of the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

13.0225.02017
Title.

Prepared by the Legislative Council staff for
Senator Triplett
April 25, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

Page 1, line 3, after the semicolon insert "to provide for a study;"

Page 19, after line 15, insert:

"**SECTION 7. LEGISLATIVE MANAGEMENT STUDY - ANALYSIS OF FUTURE OIL INDUSTRY CHANGES - CONSULTANT ASSISTANCE.** The legislative management shall study the likely changes to oil industry practices, production, impacts, and tax policy within a range ten years to thirty years in the future. To assist with this study, the legislative management shall obtain the services of an independent consultant with demonstrated insight into current and future production advances, including use of carbon dioxide and water or other means of enhancing production; effects of mature production areas on state and local tax policy; future infrastructure needs; and environmental considerations. The objective of the study is development of a legislative vision of appropriate long-term policy issues and revenue and expenditure expectations. The legislative management shall report its findings and recommendations, together with any legislation to implement the recommendations, to the sixty-fourth legislative assembly."

Renumber accordingly

Prepared by the Legislative Council staff for
Representative Headland
April 26, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on pages 1508-1511 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "Act" insert "to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties;"

Page 1, line 2, remove "and"

Page 1, line 2, after "57-51.1-03.1" insert ", and 57-51.2-02"

Page 1, line 3, after "exemptions" insert "and the state-tribal oil tax agreement"

Page 2, after line 3, insert:

"**SECTION 3.** A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

c. The United States as trustee for individual Indians;

d. A publicly traded partnership;

e. An organization that is exempt from the tax under this chapter; or

f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period."

Page 2, line 15, overstrike ""Average"

Page 2, line 20, remove "statewide production" means the number of barrels of oil produced from wells"

Page 2, remove line 21

Page 2, line 22, remove "that month, as determined by the industrial commission"

Page 2, line 22, overstrike the period

Page 2, line 23, overstrike "3."

Page 3, line 1, replace "4." with "3."

Page 3, line 7, replace "5." with "4."

Page 3, line 18, replace "6." with "5."

Page 4, line 15, replace "7." with "6."

Page 4, line 18, replace "8." with "7."

Page 4, line 18, remove "inside the Bakken or Three Forks formations"

Page 4, line 23, replace "fifty" with "thirty"

Page 4, line 25, remove "inside the Bakken or Three Forks formations which was"

Page 4, line 26, replace the second "and" with "which"

Page 4, line 27, after "2013" insert ", and which has not been redrilled or repaired after June 30, 2013"

Page 4, line 28, replace "9." with "8."

Page 4, line 28, remove "outside the Bakken and Three Forks"

Page 4, line 29, replace "formations" with "certified by the industrial commission before July 1, 2013,"

Page 5, line 4, overstrike "Wells which did not actually yield or produce oil during the qualifying"

Page 5, overstrike lines 5 through 7 and insert immediately thereafter "A well drilled and completed after June 30, 2013, on a stripper well property is not a stripper well and is not exempt under subsection 2 of section 57-51.1-03 until production from that well individually qualifies it as a stripper well under subsection 7."

Page 5, line 22, after the first boldfaced period insert "**(Effective through September 30, 2014)**"

Page 5, line 27, overstrike the comma

Page 5, line 28, overstrike "except that the rate of tax is"

Page 6, line 11, remove the overstrike over the overstruck period

Page 6, replace lines 18 through 30 with:

"**(Effective after September 30, 2014) 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."

Page 7, line 8, remove "in the Bakken or Three Forks formation which was"

Page 7, line 9, replace "certified as a stripper well or as" with "that is exempt as"

Page 7, line 10, replace "reentered or reworked" with "redrilled or repaired"

Page 7, line 11, remove "reentry"

Page 7, line 12, replace "or reworking" with "redrilling or repairing"

Page 7, line 13, remove "after the average daily production of the well exceeds one hundred"

Page 7, replace lines 14 through 16 with "as of the first day of the next calendar month if the industrial commission has not recertified that well as a stripper well."

Page 12, line 6, after "is" insert "drilled and completed before July 1, 2013, and"

Page 12, line 7, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "completed" insert "before July 1, 2013,"

Page 12, line 9, after "the" insert "tribe's"

Page 12, after line 27, insert:

"5. The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed outside the Bakken and Three Forks formations, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion."

Page 19, after line 15, insert:

"**SECTION 8. AMENDMENT.** Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed ~~six and one-half percent~~the maximum rate under chapter 57-51.1 but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The legislative assembly encourages the Three Affiliated Tribes to provide for investment of ten percent or more of tribal oil and gas gross production and oil extraction tax receipts in essential infrastructure. The Three Affiliated Tribes may report from time to time to the budget section of the legislative management on the tribe's success in essential infrastructure improvements."

Page 19, line 16, replace "This" with "Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this"

Renumber accordingly

13.0225.02021
Title.

Prepared by the Legislative Council staff for
Senator Cook
April 27, 2013

4-29-13 am

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on page 1510 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01, 57-51.1-02, and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions, rates, and exemptions and the state-tribal oil tax agreement; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

   c. The United States as trustee for individual Indians;

   d. A publicly traded partnership;

   e. An organization that is exempt from the tax under this chapter; or

   f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

   b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.

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. "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 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. "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 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.

8. "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.

9. "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. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, after June 30, 2013, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and thirty-five barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

11. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before July 1, 2013, on 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.~~12. "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.~~13. "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 5. AMENDMENT. Subsection 11 of section 57-51.1-01 of the North Dakota Century Code is amended and reenacted as follows:

11. "Trigger price" means ~~thirty-five~~fifty-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~~.

SECTION 6. AMENDMENT. Section 57-51.1-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.1-02. Imposition of oil extraction tax.

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

The rate of tax is six and one-half percent of the gross value at the well of the oil extracted for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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;

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 for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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 7. 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, 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 <u>or individual stripper well</u>.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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.~~The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed ten miles or more outside an established field in which the industrial commission has defined the pool to include the Bakken or Three Forks formation, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~**(Effective after June 30, 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 8. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 9. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production and oil extraction taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes' fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

SECTION 10. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013. Section 5 of this Act is not effective unless on July 1, 2013, section 6 of this Act becomes effective."

Renumber accordingly

#2

Major Provisions of HB 1234 (Senate) Amendment

		2013-15 Biennium
Stripper well property provision	$	105,000,000
Raising Bakken/Three Forks Stripper Barrels to 35	$	7,000,000
Tribal tax sharing change (GPT and OET)		(37,500,000)
Remove 5-year holiday on reservation		43,500,000
Income tax withholding on royalties		4,200,000
½% tax reduction new wells drilled after June 20, 2013		(100,400,000)
Total	$	21,800,000

#1 3-29-13 pm

Major Provisions of HB 1234 (Senate) Amendment

	2013-15 Biennium	2015-17 Biennium/1
Stripper well property provision	$ 105,000,000	$ 220,000,000 /2
Raising Bakken/Three Forks Stripper Barrels to 35 BOPD	$ (7,000,000)	(15,400,000) /3
Income tax withholding on royalties	4,200,000	One-time Speed-up Only
½% tax reduction new wells drilled after June 30, 2013	(100,400,000)	(180,600,000) /4
Wildcat Incentive	(35,400,000)	(56,600,000) /5
Total	$ (33,600,000)	$ (32,600,000)

/1 There is no official forecast for the 2015-17 biennium. Assumptions for a rough estimate are below:
/2 Revenue increase is compounded with 10% growth assumed in 2015-17 biennium
/3 Decrease is compounded due to revenue growth and addl well declines to 35 BOPD
/4 Assumes 6% OET rate effective for new wells drilled on/after July 1, 2013
/5 Cost of incentive includes carryover impact from the 2013-2015 biennium

(Tribal components shown below separated from the remainder of bill for analysis only)

Tribal tax sharing change (GPT and OET)	(37,500,000)	(119,900,000) /6
Remove 5-year holiday on reservation	43,500,000	78,000,000 /6
	6,000,000	(41,900,000)

/6 Estimate provided to Tribe that continues a trend

NOTE: If it is desired to make the fiscal note neutral for the 2013-2015 biennium, the 1/2% rate reduction should be made effective for production from new wells drilled January 2014

Prepared by the Legislative Council staff for
Representative Drovdal
April 30, 2013

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1234

That the Senate recede from its amendments as printed on page 1510 of the House Journal and pages 1119-1131 and 1329 of the Senate Journal and that Engrossed House Bill No. 1234 be amended as follows:

Page 1, line 1, after "A BILL" replace the remainder of the bill with "for an Act to create and enact a new section to chapter 57-38 of the North Dakota Century Code, relating to income tax withholding for oil and gas royalties; to amend and reenact section 15-05-10, subsection 4 of section 38-08-04, sections 57-51.1-01, 57-51.1-02, and 57-51.1-03, subsection 1 of section 57-51.1-03.1, and section 57-51.2-02 of the North Dakota Century Code, relating to oil extraction tax definitions, rates, and exemptions and the state-tribal oil tax agreement; to provide for a study; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Section 15-05-10 of the North Dakota Century Code is amended and reenacted as follows:

15-05-10. Royalties from oil leases - Rents from other leases - Rules.

Oil leases must be made by the board of university and school lands at such annual minimum payments as are determined by the board, but the royalty shall be not less than twelve and one-half percent of the gross output of oil from the lands leased. Oil leases made by the board may authorize a royalty of less than twelve and one-half percent for production from stripper well properties <u>or individual stripper wells</u> and qualifying secondary recovery and qualifying tertiary recovery projects as defined in section 57-51.1-01. Leases for gas, coal, cement materials, sodium sulfate, sand and gravel, road material, building stone, chemical substances, metallic ores, or colloidal or other clays must be made by the board in such annual payments as are determined by the board. The board may adopt rules regarding annual payments and royalties under this section.

SECTION 2. AMENDMENT. Subsection 4 of section 38-08-04 of the North Dakota Century Code is amended and reenacted as follows:

4. To classify wells as oil or gas wells for purposes material to the interpretation or enforcement of this chapter, to classify and determine the status and depth of wells that are stripper well property as defined in subsection 8 of section 57-51.1-01, to certify to the tax commissioner which wells are stripper wells and the depth of those wells, <u>to recertify stripper wells that are reentered and recompleted as horizontal wells,</u> and to certify to the tax commissioner which wells involve secondary or tertiary recovery operations under section 57-51.1-01, and the date of qualification for the reduced rate of oil extraction tax for secondary and tertiary recovery operations.

SECTION 3. A new section to chapter 57-38 of the North Dakota Century Code is created and enacted as follows:

Withholding requirement for oil and gas royalty payments to nonresidents.

1. For purposes of this section:

   a. "Publicly traded partnership" means a publicly traded partnership as defined in section 7704 of the Internal Revenue Code [26 U.S.C. 7704] which is not treated as a corporation.

   b. "Remitter" means any person who distributes royalty payments to royalty owners.

   c. "Royalty owner" means a person or entity entitled to receive periodic royalty payments for a nonworking interest in the production of oil or gas.

2. Except as provided in subsection 3, each remitter shall deduct and withhold from the net amount of the royalty payment made to each nonresident individual or business entity that does not have its commercial domicile in this state at the highest marginal rate provided in sections 57-38-30 and 57-38-30.3. Sections 57-38-59 and 57-38-60 apply to the filing of the returns and payment of the tax under this subsection.

3. This section does not apply to royalty payments made to a royalty owner if the royalty owner is:

   a. The United States or an agency of the federal government, this state or a political subdivision of this state, or another state or a political subdivision of another state;

   b. A federally recognized Indian tribe with respect to on-reservation oil and gas production pursuant to a lease entered under the Indian Mineral Leasing Act of 1938 [25 U.S.C. 396a through 396g];

   c. The United States as trustee for individual Indians;

   d. A publicly traded partnership;

   e. An organization that is exempt from the tax under this chapter; or

   f. The same person or entity as the remitter.

4. a. This section does not apply to a remitter that produced less than three hundred fifty thousand barrels of oil or less than five hundred million cubic feet of gas in the preceding calendar year as certified to the tax commissioner in the manner and on forms prescribed by the tax commissioner.

   b. Each remitter that is exempt from withholding under this subsection shall make an annual return to report royalty payments that exceed the dollar amounts in subsection 6 and must be reported in the same manner as provided in section 57-38-60.

5. a. Each year, a publicly traded partnership that is exempt from withholding under subsection 3 shall transmit to the tax commissioner, in an electronic format approved by the tax commissioner, each

partner's United States department of the treasury schedule K-1, form 1065, or form 1065-B, as applicable, filed electronically for the year with the United States internal revenue service.

b. A royalty owner that is a publicly traded partnership, or an organization exempt from taxation under section 57-38-09, shall report to the remitter and tax commissioner under oath, on a form prescribed by the tax commissioner, all information necessary to establish that the remitter is not required under subsection 2 to withhold royalty payments made to the partnership or organization.

6. If the royalty payment made to a royalty owner under this section is less than six hundred dollars for the current withholding period, or is less than one thousand dollars if the payment is annualized, the tax commissioner may grant a remitter's request to forego withholding the tax from the royalty payment made to that royalty owner for the current withholding period or, if applicable, the royalty payments for the annual period.

SECTION 4. 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 oil from the well during a calendar month period divided by the number of calendar days in that period, 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.~~

~~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.~~3. "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.~~4. "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.~~5. "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 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.~~6. "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 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.

~~8.~~7. "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.

~~9.~~8. "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.~~9. "Stripper well" means a well drilled and completed, or reentered and recompleted as a horizontal well, during the time the rate of tax for new wells is six percent under section 57-51.1-02, whose average daily production of oil during any preceding consecutive twelve-month period, 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] outside the Bakken and Three Forks formations, and thirty-five barrels per day for wells of a depth of more than ten thousand feet [3048 meters] in the Bakken or Three Forks formation.

10. "Stripper well property" means wells drilled and completed, or a well reentered and recompleted as a horizontal well, before the time the rate of tax for new wells is six percent under section 57-51.1-02, on 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~~an average price per barrel for crude oil of less than fifty-two dollars and ~~fifty~~forty cents~~, as indexed for inflation~~for a full calendar month. ~~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~~ The trigger price definition in this subsection is effective only during the time the rate of tax for new wells is six percent under section 57-51.1-02.

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

57-51.1-02. Imposition of oil extraction tax.

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

The rate of tax is six and one-half percent of the gross value at the well of the oil extracted for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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;

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 for wells drilled and completed before July 1, 2013, and six percent of the gross value at the well of the oil extracted for wells drilled and completed after June 30, 2013, 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 6. 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, 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 or individual stripper well.

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 drilled and completed before July 1, 2013, on nontrust lands located within the boundaries of an Indian reservation;

   b. The well is drilled and completed before July 1, 2013, on lands held in trust by the United States for an Indian tribe or individual Indian; or

   c. The well is drilled and completed before July 1, 2013, 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.~~The first seventy-five thousand barrels of oil produced during the first eighteen months after completion, from a well drilled and completed before July 1, 2017, outside the Bakken and Three Forks formations and ten miles or more outside an established field in which the industrial commission has defined the pool to include the Bakken or Three Forks formation, 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 under subsection 3, if the exemption under subsection 3 is effective during all or part of the first twenty-four months after completion.

~~(Effective after June 30, 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 7. AMENDMENT. Subsection 1 of section 57-51.1-03.1 of the North Dakota Century Code is amended and reenacted as follows:

1. To receive, from the first day of eligibility, a tax exemption on production from a stripper well property or individual stripper well 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 or stripper well's qualification period.

SECTION 8. AMENDMENT. Section 57-51.2-02 of the North Dakota Century Code is amended and reenacted as follows:

57-51.2-02. Agreement requirements.

An agreement under this chapter is subject to the following:

1. The only taxes subject to agreement are the state's oil and gas gross production and oil extraction taxes attributable to production from wells located within the exterior boundaries of the Fort Berthold Reservation.

2. The state's oil and gas gross production tax under chapter 57-51 and oil extraction tax under chapter 57-51.1 must apply to all wells located within the Fort Berthold Reservation.

3. The state's oil extraction tax under chapter 57-51.1 as applied to oil and gas production ~~attributable to trust lands~~ on the Fort Berthold Reservation ~~may not exceed six and one-half percent but may be reduced through negotiation between the governor and the Three Affiliated Tribes~~must be applied at the rate established under chapter 57-51.1.

4. Any exemptions for oil and gas production from trust lands under chapters 57-51 and 57-51.1 do not apply to production within the boundaries of the Fort Berthold Reservation except as otherwise provided in the agreement.

5. The allocation of revenue from oil and gas production and oil extraction taxes on the Fort Berthold Reservation must be as follows:

   a. Production attributable to trust lands. All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from trust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state.

   b. All other production. ~~The tribe must receive twenty percent of the total oil and gas gross production taxes collected from all production~~All revenues and exemptions from all oil and gas gross production and oil extraction taxes attributable to production from nontrust lands on the Fort Berthold Reservation must be evenly divided between the tribe and the state in lieu of the application of the Three Affiliated Tribes'

fees and taxes related to production on such lands. ~~The state must receive the remainder.~~

c. The state's share of the revenue as divided in subdivisions a and b is subject to distribution among political subdivisions as provided in chapters 57-51 and 57-51.1.

6. An oil or gas well that is drilled and completed during the time of an agreement under this chapter must be subject to the terms of the agreement for the life of the well.

7. The Three Affiliated Tribes must agree not to impose a tribal tax or any fee on future production of oil and gas on the Fort Berthold Reservation during the term of the agreement.

8. To address situations in which the tax commissioner refunds taxes to a taxpayer, the agreement must allow the tax commissioner to offset future distributions to the tribe.

9. The tax commissioner must retain authority to administer and enforce chapters 57-51 and 57-51.1 as applied to wells subject to any agreement authorized by this chapter.

10. An oil or gas well that is drilled and completed during the time an agreement under this chapter is in effect is subject to state regulatory provisions for the life of the well in addition to any other applicable regulatory provisions.

11. The federal district court for the western division of North Dakota is the venue for any dispute arising from a revenue-sharing agreement between the state and the Three Affiliated Tribes.

12. The agreement must require that the Three Affiliated Tribes report annually to the budget section of the legislative management and that the report, at a minimum, informs the budget section of tribal investments in essential infrastructure and fees, expenses, and charges the tribe imposes on the oil industry.

SECTION 9. LEGISLATIVE MANAGEMENT STUDY - ANALYSIS OF FUTURE OIL INDUSTRY CHANGES - CONSULTANT ASSISTANCE. The legislative management shall study the likely changes to oil industry practices, production, impacts, and tax policy within the forseeable future. To assist with this study, the legislative management shall obtain the services of an independent consultant with demonstrated insight into current and future production advances, including use of carbon dioxide and water or other means of enhancing production; effects of mature production areas on state and local tax policy; future infrastructure needs; and environmental considerations. The objective of the study is development of a legislative vision of appropriate long-term policy issues and revenue and expenditure expectations. The legislative management shall report its findings and recommendations, together with any legislation to implement the recommendations, to the sixty-fourth legislative assembly.

SECTION 10. EFFECTIVE DATE. Section 3 of this Act is effective for taxable years beginning after December 31, 2013, and the remainder of this Act is effective for taxable events occurring after June 30, 2013."

Renumber accordingly