



Investments in Energy Security

State Incentives to Maximize Oil and Gas Recovery

2004



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The viewpoints and recommendations contained in this publication do not necessarily represent those of the funding agency or the United States government.

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Introduction

This report is a supplement to the 2003 version of *Investments in Energy Security: State Incentives to Maximize Oil and Gas Recovery*, published by the Interstate Oil and Gas Compact Commission (IOGCC).

The IOGCC, with funding from the U.S. Department of Energy, compiles this annual catalogue of oil and gas incentive programs to assist government entities in developing and enhancing new and existing oil and natural gas incentives. The IOGCC is a 69-year-old organization representing the governors of 30 states that produce virtually all the domestic oil and natural gas in the United States.

Since the 2003 edition was published, several new incentives have been enacted or implemented. New or significantly altered incentive projects, as of the publication of this report, are listed at the right.

In this report, the IOGCC uses a somewhat broader definition of "incentive" than is traditional. The IOGCC's scope is not limited to tax incentives, but includes any program that assists oil and natural gas producers in the efficient recovery of petroleum resources while maintaining health and environmental protection.

State incentive programs are varied, including tax relief for low-volume, economically marginal wells or idle wells brought back into production; petroleum information services provided to the oil and gas industry; and incentives to develop and use new technologies that increase the efficiency of extraction. These programs vary in quantifiable effectiveness. While many have proven successful, over the years some incentives have been disappointments.

Please note that this supplement includes only the incentive catalogue portion of the IOGCC study. Not included is the well-received economic analysis of selected incentives, released in 2004 by the IOGCC. Readers should obtain a copy of the Spring 2004 *Making a Wise Investment* for a comprehensive look at the value of oil and gas incentive programs to the states. Due to data requirements for thorough evaluation, the economic analysis section includes only those incentives reported to the IOGCC prior to the 2003 legislative sessions.

It is important to note that even when a particular incentive program is not extensively used by industry or judged successful based on economic rewards to the state, its adoption can strengthen the interests of oil and natural gas producers considering expanding in that state. The attitude displayed by the state in adopting incentives is one of welcome, and business people prefer to operate where they are welcome.

In creating this report, the IOGCC worked with state, federal and international agencies and consulted with industry to compile and analyze information. Consistent with

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its mission of promoting the conservation and efficient recovery of petroleum resources while protecting health, safety and the environment, the IOGCC has created this publication to assist legislators and regulators who are crafting new incentives and to communicate states' actions with members of Congress, federal agency officials and the oil and gas industry.

A great deal of appreciation is due to the many individuals and organizations who provided information and guidance for this project. Many are recognized in the "Acknowledgments" portion of this publication, which also serves as a contact list for information regarding oil and gas incentive issues.

The Energy Council, an organization of elected and provincial legislators from 10 energy-producing states, the Canadian province of Alberta and Venezuela, has joined with the IOGCC to distribute this report. This collaborative effort will communicate findings to a wider audience.

Additional information about the IOGCC and an online version of this report can be accessed on the World Wide Web (www.iogcc.state.ok.us). For additional information about the Energy Council, call 972/243-7788.

State Incentive Programs

ALABAMA

Eastern Gulf Salt Tectonics Project, Geological Survey of Alabama

Investigators are conducting a research program called "Geometry and Evolution of Mesozoic-Cenozoic Salt Structures in the DeSoto Canyon and Eastern Mississippi Interior Salt Basins." This program is 50% supported by federal funds (Minerals Management Service) and 50% supported by the Geological Survey of Alabama.

Effective date: October 2001

Goal: To assess the structural geometry and hydrocarbon trapping mechanisms in onshore areas of the Mississippi interior salt basin in southwest Alabama and offshore areas of the DeSoto Canyon salt basin in state and federal waters adjacent to Alabama and Florida.

Impact: Results indicate that structural geometry in the study area is highly varied and includes peripheral faults, salt rollers, large salt pillows and salt diapirs. In onshore areas, hydrocarbons are produced mainly from Jurassic carbonate rocks in footwall uplifts with large salt pillows and salt diapirs. In offshore areas, by contrast, proven production comes from Jurassic eolian sandstone above salt rollers and above large salt pillows. The peripheral faults and salt diapirs of the DeSoto Canyon salt basin are largely unexplored, indicating that significant reservoir potential remains in the eastern Gulf of Mexico.

Severance Tax Reduction

The severance tax is defined as the privilege tax plus the production tax. The severance tax for oil and gas permitted on or after July 1, 1996, and before July 1, 1999, is reduced 50% from: production tax historically at 2% and the privilege tax historically as much as 8%. This bill gives a 50% tax break on both the privilege and the production tax from the commencement of production. The tax reduction now totals 1% production plus 3% privilege for the first five years of production.

Citation: Ala. Code § 40-20 (1975)

Effective dates: July 1, 1996, through July 1, 1999

Severance Tax Exemption

Extends the reduced rate of taxation to 1% for any well for which the initial permit issued by the Oil and Gas Board is dated on or after July 1, 1996, and before July 1, 2002, except a replacement well for which the initial permit is dated before July 1, 1996. This rate is in effect for a period of five years commencing with commercial production, after which the previous rate applies.

Citation: Ala. Code § 9-17-25(b) (1975)

Effective date: July 1, 1996; *End date:* July 1, 2002

Goal: Defray the expense connected with producing oil and gas.

New Wells

Oil and gas wells permitted on or after July 1, 1996, and before July 1, 2002, except a replacement well for a well for which the initial permit was issued before July 1, 1996, are eligible for a privilege tax reduction. The rate reduction of 4% is applicable for a period of

ALABAMA (continued)

five years commencing with commercial production, after which the 6% rate applies.

Citation: Act 96-277, House Bill No. 54; amends Ala. Code §§ 40-20-2(a) and 9-17-25 (1975)

Effective date: July 1, 1996

New Wells

Privilege tax is reduced from 8% to 6% for:

- Discovery wells;
- Development wells when drilling commenced within four years of the completion date of the discovery well and oil or gas is produced from a depth of 6,000 feet or greater;
- Development wells when drilling commenced within two years of the completion date of the discovery well, and oil or gas is produced from a depth of less than 6,000 feet.

This privilege tax reduction for New Wells applies only to wells permitted after July 1, 1984 and is to be applied for five years from the date production begins from these wells.

Citation: Ala. Code § 40-20-2(a)(4) (1975)

Effective date: July 1, 1984

Unit Operations

A reduction of the percentage required for ratification of a unit agreement was enacted by the legislation. This legislation reduces the percentage from three-fourths to two-thirds for ratification of a unit agreement under the terms of the allocation formula established by the State Oil and Gas Board and for ratification of an addition to the unit area. There has been no effectiveness study conducted.

Citation: 2000 Acts of Alabama 1714

Effective date: September 1, 2000

Goal: To encourage enhanced recovery.

Active supporters: State Oil and Gas Board.

Royalty Payment

Increases the minimum royalty payment threshold to \$100.

Citation: S.B. 92; Act 99-396

Marginal/Stripper Wells

Privilege tax is reduced from 8% to 4% of value on wells producing 25 barrels of oil or less per day, or 200 Mcf per day of natural gas.

Citation: Ala. Code §§ 40-20-1 and 2(a) (1975)

Effective date: 1985

Enhanced Recovery

Severance tax is reduced to 6% of value on any oil well produced or developed from a qualified enhanced recovery project. The State Oil and Gas Board of Alabama approves the projects and calculates "incremental production" by determining a base production rate.

ALABAMA (continued)

Incremental production for the project is production over that base rate. Incremental natural gas from a qualified enhanced recovery project is taxed at a reduced rate of 4%.

Citation: Ala. Code § 40-20-1 § 40-20-2(a)(2) (1975)

Effective date: May 1, 1985

Offshore Deep Wells

A privilege tax reduction to 4% for offshore wells permitted after July 1, 1998, and a borehole depth greater than 18,000 feet. A privilege tax reduction to 6% for offshore wells permitted before July 1, 1988, with a borehole depth greater than 18,000 feet. The wells must be drilled offshore in state waters. All new wells drilled after July 1, 1988, qualify for a privilege tax reduction to 6%.

Effective date: July 1, 1988; no sunset

Citation: Ala. Code § 40-20-2(a)(5)(1975)

Discovery Wells

Privilege tax reduction for discovery wells found after July 1, 1984. A tax reduction of 6% for qualifying discovery wells for up to five years from production date. Replacement wells for discovery wells also qualify for remainder of the five-year period. All new wells drilled after July 1, 1984, qualify for a privilege tax reduction to 6%.

Citation: Ala. Code § 40-20-2 (1975)

Effective dates: July 1, 1984; five years from production date.

Core and Sample Library, Geological Survey and State Oil and Gas Board

The Geological Survey of Alabama maintains a core and well sample library that includes cuttings from 4,000 oil and gas wells, core from 1,700 oil and gas wells, cuttings from 2,800 water and stratigraphic test wells and core from 350 industrial mineral core holes. Rules and regulations of the State Oil and Gas Board require that exploration companies submit cores and drill cuttings following the completion of wells. Rule 400-1-3-.10 of the Code of Alabama 1975 states in part that "a complete set of cuttings, correctly labeled and identified as to depth, shall be filed with the Board within 30 days from the time of completion of any well unless otherwise approved by the supervisor. If cores are taken, a complete set of cores, either whole or at least quarter slabs, correctly labeled and identified as to depth, shall be filed with the Board within six months from the time of completion of any well unless otherwise approved by the supervisor." The facility has four viewing rooms for use by operators and researchers.

Goals: To encourage oil and gas production by making useful data available to producers. Counteract the loss of infrastructure in the independent industry.

ALASKA

Acreage Limitation Increase

Aggregate state land acreage holding increased from 500,000 to 750,000 acres on all land other than tide and submerged land, of which not more than 500,000 acres may be located north of the Umiat baseline.

Citation: Alaska Stat. 38.05.140(c) as amended

Effective date: June 13, 2003; *End date:* Open end

ALASKA (continued)

Goal: To increase the opportunity of exploration companies to assemble acreage blocks outside of the primary North Slope producing area.

Active supporters: Gov. Frank Murkowski, Division of Oil & Gas, AOGCC and Legislators

Statewide Royalty Reduction

Gives Commissioner of Natural Resources right to determine royalty rates for uneconomical oil and natural gas resources - including never produced, shut in or about to be shut in.

Citation: Alaska Stat. 38.05.180 as amended

Effective date: June 12, 2003; *End date:* Open end

Goal: Bring known marginal resources into production and temporarily extend the life of production that is about to be abandoned.

Active supporters: Cook Inlet producers, Gov. Frank Murkowski and Legislators.

Gas Exploration and Development Tax Credit

Establishes a 10% exploration and development incentive tax credit for operators and working interest owners directly engaged in the exploration and production of natural gas south of the 68 degree North latitude.

Citation: Alaska Stat. 43.20 as amended

Effective date: May 20, 2003; *End date:* Ongoing

Goal: Promote exploration and development of natural gas resources for the in-state market.

Active supporters: Legislators.

Alaska Stranded Gas Development Act

Allows qualified groups to negotiate a fiscal regime for very large natural gas developments to maximize the benefit to the people of Alaska through the development of the state's stranded natural gas resources.

Citation: Alaska Stat. 43.82 as amended

Effective date: April 9, 2003; *End date:* March 5, 2005

Goal: Accelerate the marketing of North Slope natural gas resources to any major market which will generate revenue for the state of Alaska and jobs for Alaskans.

Active supporters: Gov. Frank Murkowski, Service Industry, Citizens and Legislators.

Oil and Gas Exploration Tax Credit

Creates a 20% tax credit for certain exploration drilling and geophysical costs for activities conducted more than three miles from an existing well or 25 miles beyond the boundary of an existing unit with an approval plan of development. Maximum tax credit is 40%.

Citation: Alaska Stat. 43.55.025

Effective date: September 9, 2003; *End date:* July 1, 2007

Goal: Stimulate exploration activity in areas near infrastructure.

Active supporters: Gov. Frank Murkowski and Legislators.

Land Access Incentives:

Areawide Lease Sales

Provide an established time each year that acreage within a geographical region will be available for lease. This will increase the number of lease sales conducted by the state to

ALASKA (continued)

four per year.

Effective date: January 1, 1997 *End date:* Ongoing

Impact: The first North Slope areawide lease sale brought \$52 million in bonus bids, making it the fourth-largest sale in state history. Two North Slope Foothills areawide sales have resulted in the largest amount of acreage ever leased in state sales - nearly 2 million acres. The state has held areawide lease sales every year since 1998. North Slope and Beaufort Sea areawide sales occur annually in October. Cook Inlet and North Slope Foothills areawide sales occur annually in May.

Goal: Allows companies to develop their exploration strategies and budgets.

Active Supporters: Industry, Former Gov. Tony Knowles, Legislature.

Shallow Gas Leasing

Over-the-counter leases are available specifically for the development of natural gas from coal seams and shallow gas sands from a field if a part of the field is within 3,000 ft. of the surface. There is an application fee of \$5,000 and annual rental payments are kept at \$1 per acre. A reduced royalty of 6.25%, rather than 12.5%, applies if the shallow gas is sold to a local utility. The royalty reduction applies only if the shallow gas is not in direct competition with higher royalty, deeper gas.

Citation: Alaska Stat. 38.05.177

Effective date: Adopted July 1996, no sunset

Goal: To locate local sources of gas that can be delivered to consumers in remote areas at less cost than alternative energy sources.

Impact: The state held its first noncompetitive Shallow Gas Lease Offering on February 29, 2000. The state has issued 107 Shallow Gas leases covering approximately 504,374 acres and has 2 applications for multiple leases pending.

Active Supporters: Industry, native corporations and rural utilities.

Exploration License Program

The Exploration License Program (ELP) offers large unexplored areas of Alaska for exploration. The license confers the exclusive right to explore, for up to 10 years, areas between 10,000 and 500,000 acres in size. Applicants bid on the license, and the applicant willing to spend the most on exploration wins the license fee. No licensee may hold more than 2 million acres under license at any given time.

Citation: Alaska Stat. 38.05.131-134

Effective date: 1996; no sunset

Goal: To encourage exploration in Alaska's interior and unexplored areas (not applicable to the Alaskan North Slope or Cook Inlet, which are known oil and gas provinces).

Impact: The state has issued two Exploration Licenses. One in the Copper River Basin and one in the Nenana Basin and currently has 2 licenses pending. Total land under license is 903,638 acres.

Economic Incentives:

Economic Limit Factor

The severance tax rates for oil and gas are reduced by a field's Economic Limit Factor (ELF). During the life of a field, production income diminishes while some operating costs remain fixed. At some point, total operating costs, royalties and production taxes, will

ALASKA (continued)

exceed gross revenue and the field may be shut in. This is called the economic limit. As production diminishes, the tax rate on the field also decreases. The ELF provides for lower tax rates based on daily per well production and the productivity of the field.

Citation: Alaska Stat. 43.55.012

Effective date: 1989; no sunset

Goals: To keep fields in production as they decline and encourage operators to drill development wells.

Impact: Severance tax rate is effectively zero for the smaller oil fields in Alaska.

Exploration Incentive Credits

Operators drilling on state lands may earn Exploration Incentive Credit (EIC) based on footage drilled and the region in which drilling takes place. Credits may be as high as 50% of eligible costs. Geophysical work qualifies for the EIC if that work is performed within two years prior to a lease sale. The geophysical data must be made public after the sale.

Citation: Alaska Stat. 38.05.180(i)

Effective date: November 9, 1979

Goal: To encourage exploration on state land.

Impact: Twenty exploratory wells qualifying for credit have been drilled on state leases; credits totaling \$54.7 million have been issued. The state has received no requests for the geophysical EIC.

The Commissioner of Natural Resources may grant an EIC for exploratory drilling, stratigraphic test well drilling, and for geophysical work on other lands within the state (this includes federal as well as private land owned by Native Alaskan regional corporations formed under the Alaska Native Claims Settlement Act). Wells must be drilled three or more miles from another well or within three miles of an oil or gas well when the commissioner finds that they are drilled in separate exploration targets. Credits may be as high as 50% for wells drilled on federal land, and 25% for wells on private land. The amount of drilling credits is based on feet drilled. Exploration data remains confidential for two years. The amount of credit may not exceed \$5 million per project, and the total of credits may not exceed \$30 million.

Citation: Alaska Stat. 41.09.010

Effective dates: July 7, 1994, through July 7, 2007

Goals: To encourage exploration in remote parts of the state and to provide a means for the state to obtain exploration data from state, federal and certain private lands.

Active Supporters: Industry.

Other Incentives:

Cook Inlet Discovery Royalty

Permits the granting of discovery royalty for wells in the Cook Inlet Sedimentary Basin that have discovered oil or natural gas in a previously undiscovered oil or natural gas pool, provided the wells are capable of producing in payable quantities. The discovery royalty is set at 5% for 10 years following the date of discovery.

Citation: Alaska Stat. 38.05.180(f)

Effective date: July 1996; *End date:* Ongoing

Goal: To encourage exploration for oil and natural gas in the Cook Inlet.

ALASKA (continued)

Active Supporters: Alaska Legislature, small Cook Inlet exploration and production firms.

Stranded Gas Pipeline Carriers

Former Gov. Knowles signed CSHB 290 into law, effective August 9, 2000. This law restricts common carrier status of a North Slope natural gas pipeline to intrastate transportation.

Citation: CSHB 290

Effective date: August 9, 2000

Goals: To free export shippers of North Slope natural gas from the common carrier requirement to accept all tendered volumes of natural gas.

Impact: The guarantee of pipeline capacity for an LNG export project is an incentive for developers of natural gas that is now stranded on the North Slope.

ARIZONA

Property Tax Reduction

The Property Tax Reform and Reduction Act, passed by the 42nd Legislature in July 1996, reduced the property tax assessment ratio for all real and personal property used by producing oil, gas and geothermal interests to 28% of full cash value from 100%. The tax rate will decrease an additional 1% per year until holding at 25% in 1999 and thereafter.

Citation: A.R.S. 42-15001

Effective date: 1996 tax year; no sunset

Goals: To provide tax equity for oil, gas and geothermal interests, and to encourage leasing and exploration activity.

Impact: The tax assessment ratio reduction is effective in achieving tax equity.

Active supporters: Paul Slayton, Mountain States Petroleum; John Somers, High Plains Petroleum; Arizona Oil and Gas Conservation Commission; Arizona Geological Survey.

ARKANSAS

Marginal Wells

Severance tax is reduced from 5% to 4% for marginal wells, which are defined by the state as wells which produce an average of less than 10 barrels of oil per day (BOPD) during any calendar month.

Effective date: February 25, 1983; no sunset

Act 1093 of 1995 provides severance tax relief to certain projects designed to increase oil production in Arkansas:

1. Idle Wells

Inactive oil wells (no production for 12 consecutive months) that are restored and reestablished as producing wells are exempted from severance taxes for 10 years from the date of renewed production.

Citation: Ark. Stat. 15-72-1002

2. Idle Fields

An inactive oil field that is later returned to production shall be exempted from

ARKANSAS (continued)

severance taxes for oil produced from all zones, horizons and formations that were once productive but have ceased to produce.

Citation: Ark. Stat. 15-72-1002

3. Enhanced Oil Recovery

Enhanced recovery projects approved by the Oil and Gas Commission are entitled to a 50% reduction in severance taxes for the incremental volume of oil attributable to the project.

Citation: Ark. Stat. 15-72-1001

4. New Technologies

Incremental production due to application of new research technologies approved by the Oil and Gas Commission is exempt from severance tax.

Citation: Ark. Stat. 15-72-1003

Effective date of Act 1093: April 10, 1995; no sunset

Goals: To provide an incentive to continue production from wells that have reached their economic limit, to encourage reestablishment of production from idle wells and to encourage initiation of enhanced recovery activities to maximize recovery of oil.

Impact: Because few operators have taken advantage of this program, it has been only moderately effective.

Discovery Gas Wells

The volume for discovery gas wells was increased from 50% to 75% of Absolute Open Flow. This change affects only newly discovered fields or zones discovered in existing fields that are deeper than any previous production in the field.

Citation: Arkansas Amendment to Rule D-16, Order Reference No. 74-94

Effective date: October 25, 1994; no sunset

Goal: To encourage exploration for and discovery of new gas sources in the Arkoma Basin.

Impact: No new discoveries have been made since the adoption of this rule change.

Active supporters: SEECO, Inc. (filed the petition for the amendment), Thomas C. Mueller, and Samson Resources Company.

Financial Responsibility

An amendment to an oil and gas rule reduces operator financial responsibility from \$15,000 to at least \$3,000 for each Intent to Drill or change of operator.

Citation: Amendment to Rule B-2, Order Reference 27-95

Effective date: June 21, 1995; no sunset

Goal: To increase exploration and drilling activity in Arkansas.

Impact: The lowering of this requirement is thought to have helped bring new oil and gas operators to Arkansas.

Active supporters: Oil and gas operators, Arkansas Oil and Gas Commission.

Services

Severance tax credit for saltwater disposal costs is available for production from wells that produce both oil or gas and saltwater. Costs include depreciation of cash investment, maintaining and improving the system, costs of services, labor, supplies, utilities and other

ARKANSAS (continued)

operating expenses.

Citation: Ark. Code Subchapter 2, 26-58-200 through 211

Effective date: June 11, 1969; no sunset

CALIFORNIA

Transfer of Pipeline Right of Way

This law allows a utility to transfer easements and right of ways associated with a section of gathering pipeline to an individual producer or a cooperative of producers.

Citation: AB 1234

Effective date: Signed into law, September 2002

Goals: To facilitate the transfer of gas gathering systems.

Active supporters: Assemblyman Anthony Peschetti, California Independent Petroleum Association, California Natural Gas Producers Association, and Industry.

Active, Idle, and Orphan Wells

In response to the growing number of idle and orphan wells, bonding levels for active and long-term idle wells and idle well fees were increased to provide more financial assurance and more funding to plug existing orphan wells. Such resources are needed to cover costs the Department of Conservation, Division of Oil, Gas and Geothermal Resources (Division) incurs for orphan well plugging and abandonment, and remediation of hazardous conditions. In addition, operators can provide idle well management options in lieu of the above bonding and fee requirements.

The Division's orphan well plugging fund doubled to \$1 million a year beginning July 1, 1999, before dropping back to \$500,000 per year commencing July 1, 2005. The additional funds will help eliminate the state's current orphan well inventory.

Citation: §§ 3008, 3202, 3204, 3205, 3205.5, 3206 and 3258. Public Resources Code

Effective date: January 1, 1999

Goals: To provide funding for the state to plug and abandon orphan wells, encourage idle well management and eliminate environmental and safety hazards.

Idle and Orphan Wells

California provides a 10-year abeyance of the assessment on oil and gas produced from orphan wells and wells that have been idle for five or more years when they are returned to productive status. Furthermore, the State Oil and Gas Supervisor may permit an operator to evaluate the economic viability of an orphan well for 90 days without having to provide bond coverage or assume plugging responsibility for the "adopted" orphan well.

Citation: § 3238, Public Resources Code

Effective date: January 1, 1997; no sunset

Goals: To resume production from idle and orphan wells, reduce the state's orphan well-plugging costs, increase the energy supply, eliminate environmental and safety hazards, create tax revenue, and produce jobs.

Impact: Positive response; nearly 1.2 million barrels of oil were exempted from the oil and gas assessment for 1999.

CALIFORNIA (continued)

Services

Natural gas used on-site for pressure-maintenance or other producing operations is exempt from assessment.

Used for repressuring or reinjection: 5,848,959 mcf

Natural Gas vented and flared: 3,940,154 mcf

Natural Gas used as fuel on lease: 63,365,665 mcf

COLORADO

Marginal/Stripper Wells

Oil and gas income from "stripper wells," i.e., wells that produce an average of 15 barrels or less of oil per producing day or 90,000 cubic feet of gas per producing day, is exempt from severance tax (stripper well threshold levels increased effective January 1, 2000).

A tax credit is available for 87.5% of ad valorem tax.

Citation: Colo. Rev. Stat. § 39-29-105

Effective date: January 1, 1985; no sunset

Active supporters: The Rocky Mountain Oil and Gas Association (RMOGA) drafted and supported this legislation. In addition, the Colorado Oil and Gas Association (COGA) supported the legislation to increase the stripper well threshold levels for purposes of severance tax exemption.

Levy Reduction and Fee Eliminations

In an effort to encourage more effective land and soil reclamation, rules were promulgated to address concerns related to permitting, surface owner notification, site preparation and interim and final reclamation. Elimination of 0.2 mills of environmental response fund levy, all drilling permit fees, recompletion permit fees, pit and other environmental permit fees, change of operator fees, hearing fees and reduction in conservation fund levy.

Citation: Reclamation Rules (300-Series, 800-Series, 1000-Series, 1100-Series)

Tax Offset

Severance taxes in Colorado are imposed on up to 5% of the gross income at the well-head, with a credit granted for a portion of ad valorem taxes paid. The net result is approximately a 1% tax rate on gross production. When the local property taxes (ad valorem taxes which are assessed based on 87.5% of the value of production) are above 5.7% they completely offset state severance tax obligation. Only five of the 30+ oil and gas producing counties in Colorado have property taxes below 5.7%, and consequently state severance tax is only effectively required to be paid in those five counties. There is effectively no state severance tax obligation in the other 25+ oil and gas producing counties.

Effective date: January 1, 1978; no sunset

Secondary/Tertiary Recovery

Oil and gas leasehold and lands employing secondary/tertiary recovery or recycling projects are assessed at 75% of the annual gross production value.

Citation: Colo. Rev. Stat. § 39-7-102(2)(a) and (b)

Effective date: January 1, 1978; no sunset

COLORADO (continued)

Goal: To conserve and avoid waste of oil and gas.

Impact: RMOGA believes this incentive has increased the efficiency of oil recovery through the application of secondary and tertiary recovery and recycling techniques.

Active supporters: RMOGA drafted and supported this program.

Prohibition Against Additional Taxes

Municipalities and counties may not consider oil and gas wells and their related facilities as a business or occupation for the purpose of imposing an occupational privilege tax.

Citation: H.B. 1045 (1996)

Effective date: April 17, 1996; no sunset

Impact: RMOGA's membership believes this legislation has been extremely effective.

Active supporters: RMOGA and Colorado Oil and Gas Association.

FLORIDA

Exemptions for New Fields, Old Wells and Shut-in Wells

This incentive encourages producers to drill wells in new fields, rework old wells and open shut-in wells by granting exemptions from tax on production from these type wells for a period of four to five years.

Citation: Fla. Stat. Title XIV, § 211.027

Effective dates: July 1, 1997; ends 48 months to 60 months after start date; repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

Deep Wells

Oil or gas produced after July 1, 1997, from wells at least 15,000 feet deep is exempt from production taxes for 60 months after completion date. No new exemptions will be granted after June 30, 2002.

Citation: Fla. Stat. Title XIV, § 211.02, and Chapter 86-178, Laws of 1986

Effective dates: July 1, 1996, repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

New Wells

Production from new oil or gas wells in an existing field established before July 1, 1997, is exempt from severance taxes for 48 months after completion. No new exemptions will be granted after June 30, 2002.

Citation: Fla. Stat. Title XIV, § 211.02, and Chapter 86-178 (1986)

Effective dates: July 1, 1996; repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

New Fields

Production from oil or gas wells drilled in a new field after July 1, 1997, is exempt from production taxes for 60 months after completion.

Citation: Fla. Stat. Title XIV, § 211.02, and Chapter 86-178 (1986)

FLORIDA (continued)

Effective dates: July 1, 1996; repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

Marginal/Stripper Wells

Severance tax is reduced from 8% to 5% for oil wells producing less than 100 BOPD. Stripper gas is taxed at \$0.12 Mcf.

Citation: Fla. Stat. Title XIV, § 211.02, and Chapter 86-178 (1986)

Effective date: July 1, 1986; no sunset

Horizontal Wells

Production from horizontal wells drilled after July 1, 1997 is exempt from severance taxes for 60 months after the completion date. No new exemptions granted after June 30, 2002.

Citation: Fla. Stat. Title XIV, § 211.027

Effective date: Repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

Tertiary Recovery

The severance tax rate is reduced from 8% to 5% for incremental production attributable to a tertiary recovery project.

Citation: Fla. Stat. Title XIV, § 211.02, and Chapter 86-178

Effective dates: July 1, 1996; repealed after June 30, 2007

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

Exemption for On-site Use of Production

Oil and gas produced and used on-site are exempt from severance taxes.

Citation: Fla. Stat. Title XIV, § 211.027 (1)

Effective date: July 1, 1996

Goal: To encourage and increase oil production.

Active supporters: Florida Independent Petroleum Producers Association.

ILLINOIS

Crude Oil Marketing and Education Act

This voluntary program is modeled after the Oklahoma Energy Resources Board. A tax of 1/10th of 1% of gross revenue of crude oil sales is collected into a fund. One-half of the fund is dedicated to abandoned oil field site cleanup and the remainder will fund energy education in public schools.

Effective date: July 1, 1998

Goal: To increase awareness of energy and oil issues among the general public, especially among school age children, and to clean up abandoned production sites.

Active supporters: IOGA.

ILLINOIS (continued)

Note: Illinois does not have a severance tax on oil or natural gas production.

INDIANA

Indiana Oil and Gas Association/Department of Natural Resources, Environmental Advisory Board

An oil and gas operator can apply to the Environmental Advisory Board through a written proposal to take over an orphan well(s) with the intent to produce, rework and produce or plug that well. If the proposal is accepted and the operator chooses to plug the well, costs for materials and supplies will be reimbursed from a Department of Natural Resources (DNR) grant awarded to the Indiana Oil and Gas Association (INOGA).

Effective date: January 15, 2002; no sunset

Goal: The goal is to increase production and reduce the number of orphan wells in Indiana.

Impact: The pilot project used to study the effectiveness of this incentive resulted in the elimination of over 50 wells from the Orphan Site Program. Of these, five wells were returned to production. The average cost of eliminating an orphan well was one-fifth the cost of the state contracted plugging. The actual increase in reserves has yet to be determined.

Active supporters: Former Gov. Frank O'Bannon, the INOGA, the Indiana DNR, and Industry.

KANSAS

NEW Unitization

HB 2652 was passed by the legislature and signed into law by the governor and thereby, changed the definition of "pool" as it relates to the underground accumulation of oil and gas. This statute change expanded the definition of a "pool" to include "one or more natural reservoirs that are pressure connected." This statutory change now allows for unitization in pools that have commingled production from more than one single reservoir due to pressure communication within the well bore. Additionally, this statute change provides that if at least 90% or more of the working interest owners approve, in writing, a contract for the unit operations of a pool or part of a pool, then the unit operations becomes effective without application to or order by the Kansas Corporation Commission. This statute is part of the supplement to the provisions of Article 13 of Chapter 55 of the Kansas Statutes Annotated and amendments thereto.

Citation: HB 2652 & HB 2907 Combined as it amends Article 13 of K.S.A. 55-1302

Effective date: April 21, 2004

Goal: To allow the right of unitization of certain commingled pressure communicated reservoir(s) within a common well bore. It also allows the establishment of voluntary unitization operations when at least 90% of the working interest owners, ratify in writing, establishing such unit operations without KCC application or order of approval.

Active supporters: Representatives of the State Energy Resource Coordination Council (SERCC); Kansas Corporation Commission (KCC); Kansas Independent Oil and Gas Association (KIOGA), and BP America Production Company.

Venting and Flaring of Gas

KANSAS (continued)

This statute change will allow venting or flaring of gas from natural gas wells (including gas from coal seams) when approved by the Kansas Corporation Commission (KCC). The venting or flaring of gas has always been associated with waste and, therefore, was not allowed except for associated casing head gas from oil wells.

Citation: Kansas Senate Substitute for HB 2043 as it amends K.S.A. 55-102

Effective date: June 13, 2002

Goal: To allow the limited venting or flaring of natural gas from both traditional and coal seam gas reservoirs for periods permitted by the KCC.

Active supporters: Kansas Independent Oil and Gas Association (KIOGA), Kansas Petroleum Council (KPC), and the Eastern Kansas Oil and Gas Association (EKOGA).

Tests of Gas Wells

This regulation change increases the daily minimum gas allowable in Kansas from 150 to 250 Mcfpd and exempts such minimum gas wells from the burden of annual gas well testing (including the required 72 hour shut-in period). Requires that the operator must apply for the exemption and annually report to the Kansas Corporation Commission (KCC) the well head shut-in pressure for such minimum wells that have been exempted. This includes all coal seam gas wells and conventional gas wells that produce less than 250 Mcfpd.

Citation: K.A.R. 82-3-304

Effective date: January 25, 2002

Goal: This incentive is designed to minimize the loss of gas production sales and associated expenses of the gas well test (pulling unit time, labor, etc.) for minimum wells.

Active supporters: KCC, Kansas Independent Oil and Gas Association (KIOGA), and the Kansas Petroleum Council (KPC).

Gas Allowables and Drilling Unit

This regulation change increases the daily allowable from 25% of the well's calculated absolute open-flow (AOF) to 50% of AOF. This amended rule also raises the minimum gas allowable from 150 Mcfpd to 250 Mcfpd.

Citation: K.A.R. 82-3-312

Effective date: January 25, 2002

Goal: To allow more gas to be produced from Kansas wells.

Active supporters: Kansas Corporation Commission (KCC), Kansas Independent Oil and Gas Association (KIOGA), and the Kansas Petroleum Council (KPC).

Temporarily Abandoned Wells; Penalty; Plugging

This regulation change allows operators more than 90 days of nonproduction before having to file a temporary abandonment (TA) application. It also provides a framework for non-producing wells that may be fully equipped and capable of production relief from filing for TA approval up to 364 days of nonproduction (perhaps due to low oil or gas prices, etc.) and extends the 90 day time requirement for plugging or returning a well back into service.

Citation: K.A.R. 82-3-111

Effective date: January 25, 2002

Goal: To allow operators more time to re-work, re-establish production for wells that may be non-producing for more than 90 days due to low product price or inability to obtain service equipment (pulling units, parts, etc.), without the formal filing of a TA application.

Active supporters: Kansas Corporation Commission (KCC), Kansas Independent Oil and Gas

KANSAS (continued)

Association (KIOGA), Kansas Petroleum Council (KPC), and the Eastern Kansas Oil and Gas Association (EKOGA).

Unitization

This act empowers the Kansas Corporation Commission (KCC) to unitize a pool upon request of a working interest owner under certain circumstances. First, the primary production from a pool has reached a low economic level and without introduction of artificial energy, abandonment of the well is imminent; or the unitized management sought is economically feasible and necessary to prevent waste. Second, the value of the estimated recovery is greater than the costs incident to conducting the recovery. Finally, the operation is fair and equitable. The act further establishes the rights of owners of oil and gas rights under unleased land as being a working interest to the extent of 7/8 interest and a royalty owner to the extent of 1/8 interest. The KCC can alter the extent of a royalty interest. Finally, the act states that it is the duty of the operator of the unit to file ad valorem taxes.

Citation: House Bill 2826 amending: K.S.A. 55-1304, K.S.A. 1999 Supp. 55-1305, K.S.A. 55-1308 and K.S.A. 55-1312

Effective date: March 30, 2000

Goals: Promote secondary operation/management standards for unitization.

Active supporters: Kansas Independent Oil and Gas Association (KIOGA), Kansas Petroleum Council (KPC), and the KCC.

Property Taxation

This act relates to the property tax valuation of oil and gas properties. Factors to be considered when assessing property taxes include the age of the well, quality of product produced, nearness to market, the cost of operation, the probable life of the well, character, extent and permanency of market, the quantity of product produced, the number of wells being operated and other factors affecting the value of the lease. The act also establishes the method for calculating the property taxes.

Citation: House Bill 2823 amending: K.S.A. 79-331

Effective date: April 13, 2000

Goal: To change the oil/gas valuation method for county property tax purposes.

Active supporters: KIOGA, KPC and the KCC.

Refundable Income Tax Credit for Property Taxes Paid

Past Gov. Bill Graves signed legislation which provided an income tax credit to working interest owners equal to 75% of the 1998 personal property tax paid on the working interest of an oil lease, from which the average daily production per well is 15 barrels or less. The property tax must have been levied for property tax year 1998 and timely paid during the income tax year in which the credit is taken. By making the credit effective for the tax year beginning after December 31, 1997, immediate relief is available. For taxable years commencing after December 31, 1998, an income tax credit is allowed equal to 50% of the property tax paid for wells producing 15 barrels or less per day when the price per barrel is \$16 or less. The amount of the credit which exceeds the tax liability is refundable.

Citation: 1999 Kan. Sess. Laws, Ch. 154, New § 2

Effective date: May 27, 1999; no sunset

Impact: \$8.2 million immediately available to operators with continued future relief for

KANSAS (continued)

marginal wells when oil prices are \$16 per barrel or less.

Royalty Interests, Statute of Limitations on FERC-Ordered Refunds

The period of time during which first sellers of natural gas could commence a civil action against royalty interest owners to obtain refunds of reimbursements for ad valorem taxes on royalty interests during the years 1983 through 1988 was declared expired and the refund claims were deemed to be uncollectible. The Legislature reaffirmed that the Kansas five year statute of limitations found in K.S.A. 60-511 applied to these claims created when the Federal Energy Regulatory Commission (FERC), more than 15 years after its initial determination, reversed its long-standing policy that the Kansas ad valorem tax, which was based on production, was a severance tax and could be added to the maximum lawful price set by the NGPA at that time. FERC ordered first sellers to refund the amount of the ad valorem tax. This statute and that part of the FERC order relating to penalty and interest is under court challenge in both state and federal courts.

Citation: K.S.A. 55-1624

Effective date: April 30, 1998

Incremental Production

A severance tax exemption for a period of seven years is given to the incremental production resulting from a production enhancement project begun on or after July 1, 1998. Incremental severance and production is defined as production in excess of base production. Base production is the average monthly amount of production for the 12-month period immediately prior to the project beginning date, minus the monthly rate of production decline. The monthly rate of production decline would be determined with reference to the same 12-month period used to determine the base production. The monthly rate of production decline is the decline that would have occurred except for the enhancement project. The credit does not apply in any fiscal year if in the preceding calendar year the price exceeded, in the case of oil, \$20 per barrel; or, in the case of natural gas, \$2.50 per Mcf. Language was added to clarify the existing law to include wells that have an established incline in production volumes and for wells that have had casing failures (or for other reasons lack production volumes) immediately prior to the enhancement project.

Citation: K.S.A. 1999 Supp. 79-4217

Effective date: July 1, 2000

Goal: To promote old wells producing after enhancements, through tax relief.

Active supporters: KIOGA, KPC and the KCC.

Marginal/Stripper Wells

The existing severance tax exemptions for marginal/stripper wells was expanded to increase exemptions and to allow for further increases in exemption amounts if oil prices decrease. The 2 BOPD exemption on oil produced from a lease or production unit increased to an average daily production of 5 BOPD. The 3 BOPD exemption for wells with a completion depth of 2,000 feet or more increased to an average daily production of 6 BOPD. Further exemptions were provided for if the price of oil decreases. Oil priced at \$16 or less now has a 7 BOPD exemption; should oil drop to \$13 per barrel, the exemption is 10 BOPD exemption. Tertiary recovery from a water flood process from wells of 2,000 feet or less now has a 6 BOPD exemption and wells in excess of 2,000 feet have a 7 BOPD exemption.

KANSAS (continued)

The exemption is 10 BOPD if the oil price reaches \$14 per barrel. Tertiary recovery oil priced at \$16 or less now has an 8 BOPD exemption and \$14 oil would have a 10 BOPD exemption. The exemption for gas severed from a well having a gross value of not more than \$81 per day during a calendar month was increased to \$87.

Citation: K.S.A. 79-4217(b)(1) and (b)(2)

Effective date: May 1, 1998; no sunset

Goal: To prevent premature plugging of wells.

Idle Wells

The "Three Year Inactive Wells Act" allows a 10-year exemption from severance tax for inactive wells returned to production. To qualify, a well must have been inactive prior to July 1, 1993, and must have produced no more than one of the 36 months prior to filing with the KCC for approval. This bill applies only to wells placed back in production prior to July 1, 1996.

Citation: K.S.A. 79-4217(b)(5)

Effective dates: July 1, 1996, through July 1, 2006

Secondary/Tertiary Recovery

Incremental production resulting from a tertiary recovery process is exempt from severance and production taxes.

Citation: K.S.A. 79-4217

New Wells/New Pools

Production from new pools is exempt from severance tax for 24 months from commencement of production.

Citation: K.S.A. 79-4217(b)(4)

Goal: To encourage exploration.

Impact: Industry spokesmen believe this is a very important exemption to Kansas' producers because it serves as a motivator for new exploration.

Natural Gas Severance Tax Reduction

Legislators enacted an annual stepped reduction in severance tax on natural gas from 7% to 4.33% over a three-year period. The final reduction took place in July 1996.

Citation: Kan. Sess. Laws Chapter 79, Article 4217

Effective date: July 1, 1994

Impact: The fact that natural gas has overtaken oil as Kansas' greatest-valued petroleum product is in part attributable to incentives such as this one.

Services

Electricity and other utilities used in the severance of oil and gas are exempt from state sales tax.

Citation: Kan. Sess. Laws Chapter 79, Article 3606

Effective date: July 1, 1994; no sunset. Natural gas used in injection projects, for fuel in recovery operations, or from a well having an average daily production with a value not more than \$87, is exempt from severance and production tax.

Citation: Kan. Sess. Laws Chapter 79, Article 4217(b)(1)

Effective date: July 1, 1994; no sunset

KANSAS (continued)

Kansas Geological Survey

The Kansas Geological Survey (KGS) conducts research and provides information about the state's petroleum resources. The KGS conducts programs for the petroleum industry so the state will continue to enjoy the benefits of revenue generated by the industry. The KGS provides the petroleum industry with the benefits of research and information, much as the state land grant schools provide support to the agricultural industry.

Citation: Kan. Sess. Laws Chapter 76, Articles 322 through 326

Effective date: 1998

Goal: To encourage the development of natural resources of economic value.

Impact: Oil fields have been discovered based on KGS research. The KGS is widely recognized as being the source of much petroleum information and for its work on problems posed by the industry. The survey frequently appears before legislative committees in support of tax incentives and provides technical assistance to the industry.

Active supporters: State legislative support exists.

Digital Petroleum Atlas, Kansas Geological Survey

This is a long-term program to develop a prototype digital petroleum atlas for the United States, starting with Kansas and extending into the adjoining mid-continent region. Extensive data sets about typical plays, details from pools in production and technologies that have provided the most effective exploration, development, production and additional recovery efforts are assembled and provided to operators in digital form. Hard copies are also available. The program focuses on helping operators determine why pools produce and behave the way they do so that analog techniques can be used where appropriate, regardless of the age of the rock and geography of pool setting. Currently the program is 80% supported by federal funds and 20% supported by Kansas general funds.

Citation: Direct congressional appropriation, through the U.S. Department of Energy

Effective dates: August 1995; new appropriation in 1996

Goal: To lower exploration and production costs and increase success rates by facilitating technology and information transfer.

Petroleum Research Section (PRC), Kansas Geological Survey

The PRC conducts research and provides instructional services for the Kansas petroleum industry. It uses a wide variety of technologies and has a broad range of scientific interests. Most members of the section have industry experience. The section also operates the Kansas Well Core Library in Lawrence, which is open to the public.

Goal: To stem the decline in Kansas' oil production by providing research and petroleum data to the industry.

Impact: Reviews of the section's research and workshops have been very strong. The discovery of the Bluebell Field in Kansas has been attributed to work done by this group. The Petroleum Research Section is a national leader in making petroleum data available electronically, especially through the Internet.

University of Kansas Energy Research Center

The Kansas Geological Survey and the University of Kansas fund an integrated energy research program focused on petroleum. The Research Center coordinates information relating to ongoing petroleum research, and makes that information available to industry.

Goal: To stimulate energy research and assist in gaining funding. To help maintain the

KANSAS (continued)

Kansas energy industry.

Impact: The program has contracted more than \$6.6 million in support of energy research. Many conferences and short courses have been held. The program integrates staff in 18 university departments that conduct energy research.

Active supporters: Kansas Geological Survey and academic units of the University of Kansas, including the geology department and the Tertiary Oil Recovery Project.

Technical Information Services for the Petroleum Industry

Through Technical Information Services, the Kansas Geological Survey provides public access to petroleum data, including scout tickets and well log data. The Well Sample Library in Wichita operates the sample cuts, archives well samples and makes these materials available to operators.

Effective date: 1987 (with earlier precursors)

Goal: To encourage oil and gas production by making useful data available to producers; counteract the loss of infrastructure in the independent industry.

Active supporters: Kansas Geological Survey.

KENTUCKY

Credit for Production From Recovered Inactive Oil Wells and Gas Wells

These two incentives give producers a credit on the 4.5% severance tax imposed on production from oil and gas wells that are brought back into production after having been inactive for two years, or plugged and abandoned.

Citation: KRS 137.132 and KRS 143A.033

Effective date: July 15, 1998; no sunset

Goal: To recover inactive or abandoned wells.

Active supporters: Kentucky Oil and Gas Association, Kentucky Division of Oil and Gas.

Investigation of Abandoned Wells

This statute allows producers with a proper testing permit to test inactive wells for 60 days prior to posting bond for the well.

Citation: KRS 353.730

Effective date: July 15, 1998; no sunset

Goal: To recover inactive or abandoned wells.

Active supporters: Kentucky Oil and Gas Association, Kentucky Division of Oil and Gas.

LOUISIANA

Severance Tax Relief; Act 74

Production from oil and gas wells shall be exempt from severance tax for a period of two years when returned to service after being inactive for two or more years or having 30 days or less of production during the past two years.

Effective dates: July 1, 2002 through June 30, 2006

Goal: To provide tax relief to companies that bring inactive wells back to production.

Active supporters: Reps. Daniel and Johns; and Sens. Malone and Theunissen.

LOUISIANA (continued)

Act 31

Provides exemptions from state and local sales and use taxes for repairs and/or materials used on drilling rigs and equipment used exclusively for exploration and development of minerals outside the territorial limits of the state in the Outer Continental Shelf.

Effective date: July 1, 2002

Goal: To provide tax relief.

Active supporters: Representatives Murray and Thompson; and Senator Romero.

Act 2 of 1994

This act, reenacting La. R.S. 47:633, reduced severance taxes on the following categories of wells in order to stimulate exploration and development:

1. Stripper Oil Wells and Incapable Oil Wells

Oil wells producing less than 10 barrels of oil per day are exempt from severance taxes during any month in which oil prices average less than \$20 per barrel. When oil prices are greater than \$20 per barrel, severance tax is reduced by 75% to 3.125%. Wells producing more than 10 and less than 25 barrels of oil per day with at least a 50% saltwater cut are taxed at 6.25%, a 50% reduction.

Citation: La. R.S. 47:633, S.B. 31 (1994), La. R.S. Ann. of 1950, (renewed by Act 16 of 1996)

Effective dates: July 1994.

2. Horizontal/New Discovery/Deep Gas or Condensate Wells

Severance taxes for oil or gas from horizontally drilled wells or recompletions, certified new discovery oil and natural gas wells, and gas or condensate produced from wells drilled to at least 15,000 feet are suspended from the date of first production for a period of 24 months (extended in 1996 Act 16 and in 1998 Act 7), or until payout of the well cost, whichever comes first. Payout of the well cost shall be determined by the Department of Natural Resources. To be eligible, new discovery wells must be completed in a new reservoir before Sep. 30, 2000.

Citations: Act 2 (S.B. No. 31); S.B. 32, amending La. R.S. Ann. 47:633(7)(c)(iv)(a) and 648.2(1)(c), La. R.S. Ann. of 1950; 1996 Act 16

Effective date: July 7, 1994; no sunset

Goal: To encourage horizontal, new and deep well drilling. This is consistent with the public policy of Louisiana to promote economic growth and revitalize and stimulate the petroleum industry, which is in decline due to world markets and trends.

Impact: According to a study by the Louisiana State University Center for Energy Studies, the program has been marginally effective in meeting its goals. Many of the new discoveries are deep wells that also qualify for reduced severance tax under Act 2 of 1994.

Active supporters: Governor's Energy Committee.

Produced Water Injection

To help accomplish the objective of reducing the discharge of produced water and to help ease the tremendous financial burden placed on the oil and gas industry, it is the

LOUISIANA (continued)

purpose of this section to provide an economic incentive to producers of oil and gas by allowing them to realize a severance tax savings (20% on incrementally produced oil and gas) if they inject produced water into an oil or gas reservoir for the purpose of increasing the recovery of hydrocarbons.

Citation: La. R.S. 47:633.5

Orphan Well Plugging

Act 404, passed by the Legislature in 1993 and amended by Act 297 of 1995, establishes an orphan well plugging and site restoration fund, which is overseen by an Oil Field Site Restoration Committee. This fund receives monies from a production fee totaling \$0.01 per barrel of oil or condensate and \$0.002 per Mcf of gas. The bill also provides that at the time of property transfer, a site-specific trust account may be established to provide funds for site restoration. These accounts are based on an assessment of the full cost of restoration following a detailed review of site conditions and disclosure of known problems by the seller. Once established, the accounts remain with the site through subsequent property transfers. If an account is established and fully funded, the transferring party is not held liable by the state for future restoration costs. The 1995 amendment provides that contractors bidding on plugging and site restoration projects shall take the salvage value of equipment left on-site into account in making a bid.

Citation: 1993 La. Act 404; amended by 1995 La. Act 297

Tertiary Recovery

No severance tax shall be due on production from a qualified tertiary recovery project approved by the Secretary of the Department of Natural Resources until the project has reached payout. Payout is calculated from the total of production from investment costs; expenses particular to the tertiary project, not to include charges attributable to primary and secondary operations on that reservoir; and interest at commercial rates.

Citation: La. R.S. Ann. 47:633.4

Effective date: July 12, 1984; no sunset

Goal: To provide an economic incentive to producers to invest in tertiary recovery projects to enhance Louisiana's crude oil production, to the ultimate benefit of the state and the people.

Impact: Enhanced oil recovery projects have taken place, but it is unknown how many would have taken place in the absence of an incentive. One large project is currently active. Industry investment in the project is approximately \$30 million. While the effectiveness of the program has not been studied, analysis of statistics from the Louisiana Department of Natural Resources and Department of Revenue and Taxation would be informative.

Active supporters: Oil and gas industry, legislative leaders.

Marginal Gas Wells

Gas wells producing less than 250 Mcf per day are taxed at a reduced rate of \$0.013/Mcf.

Citation: La. R.S. 47:633

MARYLAND

There are currently no oil or gas incentive programs in Maryland.

MICHIGAN

Marginal/Stripper Wells

Severance taxes are reduced from 6.6% to 4% for production from stripper oil wells. The severance tax rate for all gas production is 4%. Stripper oil wells are defined by the state as wells with an average maximum daily production less than or equal to 10 BOPD.

Production from marginal oil properties receives the same reduction when average per well production is:

- 20 BOPD or less for properties with average completion depths greater or equal to 2,000 feet but less than 4,000 feet;
- 25 BOPD or less for properties with average completion depths greater or equal to 4,000 feet but less than 6,000 feet;
- 30 BOPD or less for properties with average completion depths greater or equal to 6,000 feet, but less than 8,000 feet;
- 35 BOPD or less for properties with average completion depths of at least 8,000 feet.

Citation: 1929 Mich. Pub. Acts 48

Effective date: March 19, 1996; no sunset

Goal: To increase well life and volume of production.

Impact: This program encourages marginal and stripper wells to produce and not be plugged and abandoned.

Active supporters: Petroleum industry and Michigan state government.

Note: *The Michigan Court of Appeals, on July 23, 1996, held in an unpublished case that severance tax is not due on gas used on-site to purify gas, as purification costs are part of the costs of production. This decision is favorable to oil and gas producers.*

MISSISSIPPI

Enhanced Oil Recovery

Reduces the assessed tax rate to 3% of the value of the oil produced by an enhanced oil recovery method in which carbon dioxide is used when transported by a pipeline to the oil well, has been expanded to include any other enhanced oil recovery method approved and permitted by the State Oil and Gas Board on or after April 1, 1994.

Citation: Miss. Code Ann. § 27-25-503 (1) (2001)

Effective date: April 1, 1994; no sunset

Goal: To encourage the use of enhanced recovery methods of production.

Impact: Believed to have increased the use of enhanced oil recovery techniques.

Active supporters: Mississippi Independent Producers and Royalty Owners Association (MIPRO) and Mid-Continent Oil and Gas Association (MCOGA).

Carbon Dioxide Reductions and Exemptions

As noted above under **Enhanced Oil Recovery**, there is a reduction in the rate of the privilege tax to 3% for oil leases using enhanced production methods in which carbon dioxide is used. This appears in Miss. Code Ann. § 27-25-503.

Mississippi law also provides that gas, including carbon dioxide, used for purposes of

MISSISSIPPI (continued)

injection shall be exempt from the state's 6% privilege tax. This exemption only applies to carbon dioxide to be used for enhanced oil recovery projects within the state of Mississippi.

Citation: Miss. Code Ann. § 27-25-703 (2) (2001)

MISSOURI

Plugging

In lieu of fines for regulatory violations, operators are offered the opportunity to do community service by plugging a comparable number of orphan wells selected by the state.

Five counties out of 160 now produce oil or natural gas.

Note: Missouri does not tax oil or natural gas production.

MONTANA

RENEWED Horizontally Recompleted Wells

Horizontally recompleted oil wells pay a reduced production tax rate on the incremental production for the first 18 months of production after recompletion. This incentive is suspended when the price of West Texas Intermediate crude oil exceeds \$30 per barrel for a calendar quarter and reactivates when the price of oil drops below \$30 per barrel. Wells that have not produced for five years or more are treated, for tax purposes, as new wells. (See also: **Horizontal Wells** section.)

Citation: Mont. Code Ann. tit. 15, Chapter 9 (1993)

Effective dates: January 1, 1994; no sunset

Goal: To encourage the use of advanced technologies in oil production.

Impact: It is reported that major producers have drilled more horizontal wells than anticipated, which may be at least partially in response to this incentive program. The recent 4% per year decline in production has nearly leveled off.

Active supporters: Montana Petroleum Association (MPA), Shell Western Exploration and Production, Burlington Resources Oil and Gas (formerly Meridian Oil), oil and gas county commissioners and land and mineral owners associations.

Horizontal Wells

Production taxes for oil or gas wells that are completed horizontally or for horizontally recompleted oil wells that have not been producing for five years or more are exempt from production taxes, except for the 0.5% resource indemnity tax for the first 18 months of production.

Citation: Mont. Code Ann. tit. 15, Chapter 9 (1993); amended Chapter 554 (1999)

Effective dates: December 31, 1993; January 1, 1999

Impact: With the increase in oil prices in the years of 2000-2001, operators in existing fields have used the idle well, horizontal recompletion incentive and have increased production. The horizontal incentive has been popular since its inception in 1993.

MONTANA (continued)

New Wells

Oil or gas production from new wells, or wells that have not produced for five years, are exempt from production taxes, except for the 0.5% resource indemnity tax, for the first 12 months of production.

Citation: Mont. Code Ann. tit. 15, Chapter 451 (1995)

Effective date: January 1, 1996

Goal: To stimulate exploration and new production.

Impact: The incentive is a factor in the more favorable tax climate for new production, and keeps Montana competitive with neighboring states for drilling dollars.

Active supporters: MPA, Northern Montana Oil and Gas Association (NMOGA), oil and gas county commissioners, land and mineral owners associations.

Secondary/Tertiary Recovery

Production taxes are reduced for incremental production from secondary and tertiary recovery projects. Incremental secondary production is taxed at 8.5%. Incremental tertiary production is taxed at 5.8%. This incentive is suspended when the price of West Texas Intermediate crude oil exceeds \$30 per barrel for a calendar quarter and reactivates when the price of oil drops below \$30 per barrel.

Citation: Mont. Code Ann. tit. 15, Chapter 9 (1993); amended Chapter 451 (1995)

Effective date: January 1, 1994

Goal: To extend economic life of depleted wells and fields through advanced technology application.

Impact: Oil production for 1995 is virtually flat, with 1994 production stemming an annual decline of 4% per year in previous years. This incentive coupled with the state's horizontal wells incentive is credited with stemming this decline.

Active supporters: MPA, Shell Western Exploration and Production, Burlington Resources Oil and Gas, oil and gas county commissioners, land and mineral owners associations.

Marginal/Mini Stripper Wells (3 barrels per day or less)

Oil from a well which produces 3 barrels per day or less is exempt from production taxes, except the 0.5% resource indemnity tax. A suspension clause eliminates this tax exemption when West Texas Intermediate crude oil prices reach \$38 per barrel for a calendar quarter and reactivates when the price drops below \$38 per barrel. Montana defines a stripper oil well as a well that produces less than 15 barrels per day.

Citation: Mont. Code Ann. tit. 15, Chapter 488 (1999); amended Chapter 421 (2001)

Effective date: July 1, 1999

Goals: To keep marginal wells in production, preserve jobs and prevent premature abandonment.

Impact: Incentive trigger price raised to \$38 West Texas Intermediate in 2001 session. Operators testified that wells were kept in production and employees were hired to service the wells.

Active supporters: NMOGA, MPA, county commissioners, land and mineral owner associations.

Marginal/Stripper Wells (10 -15 barrels per day)

The production tax rate on the first 10 barrels produced from a stripper oil well is 5.5%.

MONTANA (continued)

The production tax rate is 9% on the next 10 - 15 barrels of oil produced from a stripper well. Lower tax rates are provided for stripper well production when the price of West Texas Intermediate crude oil remains below \$30 per barrel in a calendar quarter. Montana defines a stripper oil well as a well that produces less than 15 barrels per day.

Citation: Mont. Code Ann. tit. 15, Chapter 530 (1999)

Goal: To increase Montana's oil production, keep marginal wells in production and maintain the jobs associated with these wells.

Services

Crude oil or gas used by operators in connection with operations is tax exempt.

Citation: Mont. Code Ann. § 15-36-305

Effective date: Title chapter currently in effect

Goal: To make the tax code more equitable by not taxing production which is actually a cost of doing business and not to be sold for a profit.

NEBRASKA

Marginal/Stripper Wells

A severance tax reduction from 3% to 2% is available for oil wells that produce less than 10 BOPD.

Citation: Neb. Rev. Stat. tit. 57, §§ 701 through 719

NEVADA

Reduced Administrative Fee for New Production

The amount of the administrative fee that a producer or purchaser of oil or natural gas must pay on new production pursuant to subsection 2 of Nevada Revised Statute 522.150 is one-half cent (5 mills) per barrel of oil or per 50,000 cubic feet of natural gas, as appropriate. New production is defined as production from new wells or existing wells completed in new intervals as determined by the Commission on Mineral Resources. Any qualifying well will receive a reduced administrative fee for one full year. Upon completion of a qualifying well, the producer will submit a Form 5, "Well Completion Report." The production date as reported on the Form 5 will be the effective date for the reduced fee.

Citation: NAC 522.343; NRS 522.040,50

Effective date: January 27, 2000

NEW MEXICO

Credit for Produced Water

This new law provides for a tax credit of \$1,000 per acre-foot of cleaned produced water that is pumped into the Pecos River. The pumping of the water must be in compliance with state and federal clean water regulations. This law allows for an annual tax credit up to an amount of \$400,000.

Citation: NMSA 7-2-18.9

NEW MEXICO (continued)

Effective date: Repealed as of January 1, 2006; repeal passed in 2002.

Goal: To help New Mexico meet its regulatory obligation to deliver water to Texas.

Stripper Wells

Reduces both severance and emergency school taxes for stripper well properties having average daily production of less than 10 barrels or 60 MCF per eligible well. Severance taxes are reduced from 3.75% to 1.875% or 2 13/16% and emergency school taxes are reduced from 4% to 2% or 3% for gas and from 3.15% to 1.58% or 2.36% for oil during periods of low prices (less than \$1.15 and between \$1.15 and \$1.35 per MCF for gas and less than \$15 and between \$15 and \$18 per barrel for oil).

Citation: Oil Conservation Division Rule 33; §§ 7-29B-1 through 7-29B-6, NMSA 1978, as amended

Effective date: June 18, 1999; no sunset

Goal: To encourage production from marginal wells and avoid premature abandonment and plugging.

Well Workover Project

Reduction in severance taxes from 3.75% to 2.45% for oil and gas produced from wells having qualified workover operations performed. Does not apply when oil price is \$24 or more per barrel.

Citation: OCD Rule 32; §§ 7-29B-1 through 7-29B-6, NMSA 1978, as amended

Effective dates: June 16, 1995; amendment effective June 1, 1999. Prior to that time, 1.875% rate applies to only the incremental production; no sunset

Goal: To encourage operators to perform workover operations to increase production and avoid premature abandonment and plugging.

Production Restoration Project

Exemption from severance tax (3.75%) for wells that had fewer than 31 days of production in any period of 24 consecutive months after January 1, 1993, which are brought back into production. Does not apply when the oil price is \$24 or more per barrel.

Citation: OCD Rule 31; §§ 7-29B-1 through 7-29B-6, NMSA, 1978 as amended

Effective date: June 16, 1995; no sunset

Goal: To encourage operators to return wells to production and avoid premature abandonment and plugging.

State Royalty Reductions

A lower royalty rate (5%) applies to oil wells operated pursuant to a state oil and gas lease if the wells averaged: (i) less than 3 BOPD for the preceding 12-month period but not more than 5 BOPD for any month during that 12 month period if producing from shallower than 5,000 feet; and (ii) less than 6 BOPD for the preceding 12-month period but not more than 10 BOPD for any month during that 12-month period for production from 5,000 feet or deeper. Certain conditions apply and an application and fee are required.

Citation: § 19-10-5.1, NMSA 1978, as amended

Effective date: May 18, 1994; no sunset

Goal: To encourage production from marginal wells and avoid premature plugging and abandonment.

NEW MEXICO (continued)

Enhanced Oil Recovery Projects

Severance tax reduced from 3.75% to 1.875% for oil produced from the date of positive production response. OCD approval is required. Does not apply when the oil price is \$28 or more per barrel.

Citation: OCD Rule 30; Enhanced Oil Recovery Act, §§ 7-29A-1 through 7-29A-5, NMSA 1978

Effective dates: March 6, 1992, for carbon dioxide injection projects; January 1, 1994, for processes other than carbon dioxide; no sunset

Goal: To encourage the use of enhanced recovery techniques, including waterflooding, pressure maintenance and tertiary recovery projects or expansions.

NEW YORK

New York State Energy Research and Development Authority

The New York State Energy Research and Development Authority (NYSERDA) was created by the state's Legislature in 1975 as a public benefit corporation. One goal of NYSEDA's research and development program is to expand the use of New York state's indigenous and renewable energy resources. NYSEDA's natural gas program has evolved into a multi-faceted research and development program structured around the following goals: to help develop new natural gas reserves through innovative exploration methods and reservoir studies; to enhance existing reservoir production by developing or demonstrating new technology and products; to increase natural gas storage from depleted natural gas fields and bedded salt; to improve industry environmental performance; and to conduct extensive industry outreach to educate firms on opportunities for economic production in New York state. Over the last nine years, NYSEDA has provided more than \$6 million for over 70 natural gas and petroleum projects. Information on NYSEDA's programs can be found at www.nyserda.org.

Current Initiatives:

REVISED Natural Gas and Petroleum Exploration and Production for Economic Development Program

The program is expected to create economic activity in New York State through the identification, development and use of indigenous natural gas and petroleum production. Selected projects will target resource exploration and development projects that can bring new production online within a reasonable time frame (less than three years). All oil or gas-bearing formations will be considered. Eligible project types include: resource characterization studies use technologies, such as remote sensing, aeromagnetism, seismic or geologic modeling, to identify prospects in oil- or gas-bearing formations (up to \$50,000 per project); prospect development projects will identify and develop specific reservoirs with the goal of leasing, testing and developing a reservoir (up to \$75,000 per project); and, end-use economic development projects will use indigenous resources to fuel a New York State end-use partner (up to \$150,000 per project). These projects will be tied to job creation or other economic development activity. Projects can include all elements of identifying, producing and distributing the resource to move the fuel to the end user (pipeline or liquefied natural gas). Release of the solicitation is expected in late 2004.

NEW YORK (continued)

Natural Gas Storage Program

The program is designed to evaluate and develop advanced natural gas storage concepts to enhance the reliability of New York State's electric-generation system. The program selected three Phase 1 projects that targeted new technological concepts to increase storage capacity. The PON targeted four areas: 1) innovative concepts to create underground natural gas storage (particularly in central and eastern New York state), 2) innovative on-site storage for power plants, 3) small-scale storage concepts, and 4) gas to liquids technology. The three Phase 1 feasibility studies are now competing for Phase 2 development funding of up to \$800,000 with NYSERDA providing a maximum of 50% of the project cost and may require repayment of NYSERDA's investment with the project's success. Stage 2 project(s) will be selected in late 2004.

NORTH DAKOTA

North Dakota has a gross production tax of 5% and an extraction tax of 6.5% on oil. The following incentives relate only to a reduction on the extraction tax. In all cases the gross production tax is assessed.

Shallow Gas Wells

Shallow gas wells from new or recompleted wells drilled and completed after June 30, 2003 are exempt from gross production taxes for the first 24 months of gas sales.

Citation: NDCC 57-51-01

Effective dates: July 1, 2003, through June 30, 2007

Goal: To foster and encourage exploration, development and production of natural gas resources.

Active supporters: Oil and Gas District Legislators, the North Dakota Petroleum Council and the NDIC.

Extraction Tax Trigger

The new trigger price for excise tax incentive elimination on oil production will occur if West Texas Intermediate crude oil averages \$38 per month for five consecutive months. The trigger price will be adjusted for inflation on an annual basis by the North Dakota Tax Department. For an operator, this can immediately reduce taxes after approval. The reduction is 2.5 - 6.5%. The North Dakota Industrial Commission (NDIC) Oil & Gas Division and the North Dakota Petroleum Council are monitoring the effectiveness of this incentive.

Citation: Senate Bill 2205

Effective date: August 1, 2001; no sunset

Goal: The previous trigger price was \$33 and the trigger mechanism was unclear. The tax trigger nearly tripped in 2000 and would have cost oil producers in North Dakota \$20 million in the first six months. The new trigger raises the trigger price significantly and will provide more stability for oil producers and hopefully result in more exploration and production.

Active supporters: North Dakota Petroleum Council member companies.

Statutory Unit Ratification

The new law lowers the percentage of working interests and mineral owners approval required to form and dissolve an oil production unit from 70% to 60%. The NDIC Oil & Gas

NORTH DAKOTA (continued)

Division and the North Dakota Petroleum Council are monitoring the effectiveness of this incentive.

Citation: Senate Bill 2120

Effective date: August 1, 2001; no sunset

Goal: Lowering the unitization percentage has been a controversial issue for more than twenty years; the lower percentage will help production companies in their secondary recovery methods.

Active supporters: North Dakota Petroleum Council member companies.

Abandonment of Wells—Suspension of Drilling

This rule defines what constitutes abandonment of a well in the state of North Dakota. The rule also dictates how soon after abandonment a well is to be plugged and the drill site reclaimed. By giving the well temporarily abandoned status, the NDIC director may waive this requirement for one year. The director may extend a well's temporarily abandoned status for one year. The director also may approve suspension of the drilling of a well. If suspension is approved, a plug must be placed at the top of the casing. Unless authorized by the director, a well must be plugged and its site reclaimed if drilling has been suspended for 30 days.

Citation: 43-02-03-55

Effective date: August 1, 1999

Goal: To prevent the permanent plugging of wells due to low oil prices.

Active supporters: NDIC.

Application for Stripper Well Property Determination

This rule gives the requirements for an operator desiring to classify a property as a stripper well property for the purposes of exempting production from extraction taxes.

Citation: 43-02-08-02

Effective date: August 1, 1999

Goal: To eliminate application costs.

Active supporters: NDIC.

Application for Workover Project Determination

Applicants have the burden of establishing entitlement to the exemption provided in NDCC § 57-51.1-03 and upon completion of the workover project shall submit all information necessary for a determination by the director.

Citation: 43-02-09-04

Effective date: August 1, 1999

Active supporters: NDIC.

Horizontal Reentry Well Exemption

Oil produced from a horizontal reentry well during the first nine consecutive months starting with the date the well was recompleted as a horizontal well is exempt from the oil extraction tax. The designation of a horizontal re-entry well is given to a well initially drilled and completed as a vertical well which is re-entered and recompleted as a horizontal well after March 31, 1995. This designation may also apply to the re-entry and recompletion of a vertical well that is classified by the NDIC as a dry hole.

Citation: Rule 81-09-03-10

NORTH DAKOTA (continued)

Effective date: April 1, 1995; no sunset

Goal: To increase oil production from a reservoir.

Active supporters: Oil and gas industry.

Tribal Lands Oil Tax Exemption

Initial production of oil from a well is exempt from extraction tax (6.5%) for 60 months if:

- the well is located on a reservation, or
- the well is located on trust land held for a tribe, or
- the land is held by a tribe at the time this Act was passed.

Citation: N.D. Cent. Code 51-51.1-03(8)

Effective date: July 31, 1997; no sunset

Goal: To encourage petroleum development upon tribal lands.

Active supporters: Private individuals and independent producers.

Marginal/Stripper Wells

Oil produced by stripper wells is exempt from extraction taxes. Stripper wells are defined as wells with average daily production for the past 12 months of up to 10 BOPD at a depth of less than 6,000 feet; up to 15 BOPD at a depth of 6,000 to 10,000 feet; and up to 30 BOPD at depths greater than 10,000 feet. Stripper wells must be certified by the NDIC.

Citation: N.D. Admin. Code Chapter 81-09-03 § 07

Effective date: August 1, 1987; no sunset

New Wells

Production from new wells drilled and completed after April 27, 1987, is exempt from extraction taxes for the first 15 months of production and taxed at a rate of 4% thereafter (reduced from 6.5%).

Citation: N.D. Admin. Code Chapter 81-09-03 § 06

Effective date: July 1, 1987; no sunset

Horizontal Wells

Production from new horizontal wells drilled and completed after April 27, 1987, but before April 1, 1995, is exempt from extraction taxes for the first 15 months following well completion, and is then taxed at a rate of 4% thereafter. Oil produced from a horizontal well drilled and completed after March 31, 1995, is exempt for the first 24 months. See trigger provisions above.

Citation: N.D. Admin. Code Chapter 81-09-03 § 06

Effective date: April 1, 1995; no sunset

Impact: Excellent, according to the North Dakota Petroleum Council (NDPC), which finds that horizontal drilling has increased. The NDPC attributes the quadrupling of drilling activity to this incentive, plus new technology, new finds and good oil prices. The NDIC's Oil and Gas Division statistics are expected to show an increase in permits and a decline in the rate of well plugging. As an unexpected benefit, while pursuing new horizontal plays, two new plays and two new fields have been discovered.

Idle Wells

Production from oil wells that have been inactive for at least two years and are returned to production is exempt from extraction taxes for 10 years, beginning the first day of the

NORTH DAKOTA (continued)

month in which NDIC certification is received by the Tax Commissioner.

Citation: N.D. Admin. Code Chapter 81-09-03 § 11

Effective date: April 1, 1995; no sunset

Impact: According to NDPC, this and most of the other incentives have been successes.

Active supporters: This and the following incentives were promoted by the NDPC dating back to 1987. In most efforts, it received vigorous support from oil producing counties, rural electric cooperatives and economic development organizations.

Workovers

Production resulting from qualifying workover projects is exempt from extraction taxes for 12 months, beginning the third month after completion of the workover project, and is taxed at 4% thereafter. Wells which have produced less than 50 BOPD during the last six months of continuous production before workover qualify for this exemption. The operator must notify the NDIC before beginning the project. The project must cost at least \$65,000, or production must increase 50% or more in the first two months after project completion. See trigger provisions above.

Citation: N.D. Admin. Code Chapter 81-09-03 § 08

Effective date: August 1, 1989; no sunset

Impact: There has been a substantial increase since implementation of this program.

Secondary/Tertiary Recovery

Incremental oil from secondary recovery projects is exempt from extraction taxes for five years, and incremental oil from tertiary projects is exempt for 10 years from the date incremental production commences. All oil from a qualifying secondary or tertiary recovery project is taxed at a reduced rate of 4% once the five- or ten-year exemption has expired. Non-incremental oil from a qualifying secondary recovery project when its average production level has increased to at least 25% over normal operations for six months is taxed at a reduced rate of 4%. Non-incremental oil from a qualifying tertiary recovery project that produces at least 15% above normal operations for one month and continues to operate as a qualified project is taxed at a reduced rate of 4%.

Citation: N.D. Admin. Code Chapter 81-09-03, 05, 05.1, 05.2, N.D. Cent. Code 57-51

Effective date: August 1, 1987; no sunset

Goals: To encourage use of secondary and tertiary recovery technologies and to encourage new investment in unitized fields.

Impact: Secondary and tertiary recovery projects have increased significantly.

Services

Natural gas used on-site in the production of oil or gas is exempt from production taxes.

Citation: N.D. Admin. Code Chapter 81-09-02 § 16

Effective date: Adopted August 1, 1986, and amended July 1, 1989; no sunset

Note: According to the NDPC, North Dakota was the only state in 1995 to increase oil production after 10 consecutive years of decline. The most significant incentives have been the 15-month holiday for new wells drilled after April 1987, the incremental exemption for secondary and tertiary recovery projects and the 24-month tax holiday for all horizontal wells drilled after March 1995. A great deal of the North Dakota incentive program information herein is derived from the North Dakota Revenue Department tax incentive

NORTH DAKOTA (continued)

program summary, published April 1996.

OHIO

Emergency and Hazardous Chemical Inventory Form

In lieu of Ohio oil/gas well owners filing hazardous chemical inventory forms under the Community Right to Know Act, the well owners will be deemed to have complied by virtue of having filed well completion and annual production statements with the Division of Mineral Resources Management (DMRM). The well completion and annual statement of production forms were amended to include the number of storage tanks associated with the well and the storage capacity of those tanks. This information along with detailed well information can be found on the Division's web site (<http://www.ohiodnr.com/mineral/index.html>). Additionally, a link is provided in DMRM's web site to the "Oil and Gas Well Emergency Response System" that was developed with U.S. Department of Energy (DOE) funding through the Argonne National Lab. This site provides emergency responders with well owner contact phone numbers, emergency officials phone numbers and site specific information on a well by well basis.

Citation: OAC 3750

Effective date: September, 2001; no sunset

Goal: Provide for broader based availability of information in the event of emergencies.

Impact: Lessen reporting requirements for Ohio oil/gas well owners and to provide for web based availability of well specific information to emergency providers.

Active Supporters: Ohio oil/gas well owners, Division of Mineral Resources, and the Ohio Oil and Gas Association.

Plugging

A landowner grant program has been established for the plugging of orphan wells. Between \$300,000 and \$500,000 per year will be set aside to fund this program. Eligible landowners can plug the orphan wells on their land sooner and have more control in the plugging process than in the state's traditional bid process. The landowners must receive bids from contractors for a plugging plan that complies with state regulations and submit an application to the Division of Mineral Resources Management. If approved, the landowner will be reimbursed for the cost of plugging.

Citation: Ohio Revised Code § 1509.071

Effective date: October 25, 1995

Goal: To encourage landowner-initiated plugging of orphan wells at a lower cost to Ohio.

Impact: This program provides the division with a second effective mechanism to plug orphan wells in Ohio.

Active Supporters: Ohio Oil and Gas Association.

Amendment to Plugging

This amendment permits the division to transfer to landowners or their agents for production, a well eligible for plugging under this program if Ohio's well ownership requirements are met. Wells previously abandoned will become property of the state. Landowners or registered well owners can take over the well for production.

OHIO (continued)

Ohio Oil and Gas Energy Education Program (OOGEEP)

With the passage of Substitute Senate Bill 46 in December, 1997, and the approval of independent producers and royalty owners in a required referendum held in March 1998, the Ohio Oil and Gas Energy Education Program (OOGEEP) became effective on April 1, 1998.

OOGEEP is a nonprofit organization and is funded entirely by independent producers and royalty owners through an assessment on the production of all crude oil and natural gas in Ohio. The assessment on crude oil is equal to one cent (\$0.01) per gross barrel and one-tenth of one cent (\$0.001) per gross thousand cubic feet of natural gas. All first purchasers of crude oil and natural gas are required to collect the assessment and submit quarterly payments directly to OOGEEP.

The OOGEEP Operating Board consists of six independent producers and one member representing a farmer's organization. As outlined in the Ohio Revised Code, they are appointed by the Ohio Department of Natural Resources, Division of Minerals Resources Management (formerly known as the Division of Oil and Gas), Technical Advisory Council based upon recommendations from a qualified producers organization and an organization representing farmers, such as the Ohio Oil and Gas Association and the Ohio Farm Bureau.

OOGEEP has completed a comprehensive oil and gas training guide, *Responding To Oilfield Emergencies Field Guide One*; a training CD; and its first permanent training facility in an effort to assist and support local emergency responders. These tools will enable them to understand and implement effective emergency response practices at typical oilfield and production sites. Ohio is the first state to offer such a safety training program to its emergency responders.

The training guide, training CD and workshops cover the following topics:

- Overview of the oil and gas industry;
- Communicating the emergency;
- Evaluating the emergency;
- Responding to drilling site emergency;
- Description and pictures of typical equipment found at an oilfield site; and
- Related informational resources.

In addition to the Oilfield Emergency Response program, OOGEEP facilitates other educational programs that encourage oil and gas education curricula in classrooms; promote public awareness about the industry, and educate and promote safety information.

Citation: Ohio Revised Code §§ 1510.01 - 1510.13

Effective Date: April 1, 1998

Goals: OOGEEP's goals include facilitating educational programs; encouraging oil and gas education curriculum in classrooms; promoting public awareness about the industry; educating and promoting safety information on related facilities and equipment; and demonstrating to the general public the importance and economic significance of the industry.

Active supporters: Active supporters of the Oilfield Emergency Response program include:

OHIO (continued)

OOGEEP, Ohio Oil & Gas Association, Ohio Department of Natural Resources Division of Mineral Resources Management and various emergency response agencies.

OKLAHOMA

Reduction in the State's Gross Production Tax on Oil

The gross production tax rate levied on oil was changed from a rate of 7% to a variable rate of either 7%, 4% or 1%.

Effective with the January 1999 production month, the gross production tax rate on oil is as follows:

- If the average price of Oklahoma oil as determined by the Tax Commission equals or exceeds seventeen dollars (\$17.00) per barrel, the tax shall be levied at seven percent (7%).
- If the average price of Oklahoma oil as determined by the Tax Commission is less than seventeen dollars (\$17.00) but equal to or exceeds fourteen dollars (\$14.00) per barrel, the tax shall be levied at four percent (4%).
- If the average price of Oklahoma oil as determined by the Tax Commission is less than fourteen dollars (\$14.00) per barrel, the tax shall be levied at one percent (1%).

Citation: Okla. Stat. tit. 68, § 1001 (B) (2002)

Effective dates: January 1, 1999, through June 30, 2007.

Note: Effective July 1, 2003, the average price as computed by the Oklahoma Tax Commission for both oil and natural gas shall be used to determine the applicable tax rate for the second month following production.

Citation: Okla. Stat. tit. 68, § 1001 (B)(3) (2002)

State's Gross Production Tax on Natural Gas

The gross production tax rate levied on natural gas was changed from a fixed rate of 7% to a variable rate of either 7%, 4% or 1%.

Effective with the July 2002 production month, the gross production tax rate on natural gas is as follows:

- If the average price of Oklahoma natural gas as determined by the Tax Commission equals or exceeds two dollars and ten cents (\$2.10) per Mcf, the tax shall be seven percent (7%).
- If the average price of Oklahoma natural gas as determined by the Tax Commission is less than two dollars and ten cents (\$2.10) but is equal to or exceeds one dollar and seventy-five cents (\$1.75) per mcf, then the tax shall be four percent (4%).
- If the average price of Oklahoma natural gas as determined by the Tax Commission is less than one dollar and seventy-five cents (\$1.75) per Mcf, then the tax shall be one percent (1%).

Citation: Okla. Stat. tit. 68, § 1001 (B) (2002)

Effective dates: July 1, 2002, through June 30, 2007.

OKLAHOMA (continued)

Note: Effective July 1, 2003, the average price as computed by the Oklahoma Tax Commission for both oil and natural gas shall be used to determine the applicable tax rate for the second month following production

Citation: Okla. Stat. tit. 68, § 1001 (B)(3) (2002)

NEW Change in Filing Date of Gross Production Tax Payment and Report

The Oklahoma Senate changed the date by which Gross Production Tax payments and reports become delinquent. Originally Gross Production Tax was to be remitted to the Oklahoma Tax Commission by the last day of the month following the month oil and gas is produced for tax purposes. This bill changes the remittance date to the twenty-fifth (25th) day of the second month following production.

Originally the Gross Production Tax report was to be postmarked no later than the tenth (10th) day of the second month following production. The bill changes the report date to the twenty-fifth (25th) day of the second month following production.

Citation: SB 1081 §§ 1,2 and 3

Effective Date: Signed by the governor on June 4, 2004.

Goal: Changing the payment and reporting dates allows industry more time to compile production and sales information that would ensure more accurate tax reporting.

In order to offset any revenue impact that would result from moving the payment and reporting date back, the bill provides for a one time payment of Gross Production Tax that would be based on the average remittance of Gross Production Tax for a previous period of either six (6) or twelve (12) months, to be paid by each company remitting Gross Production Tax. Companies required to remit the one time estimated payment would be allowed to reduce their surety by the amount of such payments.

Citation: SB 1081 § 4

Effective Date: Signed by the governor on June 4, 2004.

Sales Tax Exemption on Sale of Electricity and Associated Delivery and Transmission Services Sold for Operation of Reservoir Dewatering Project and/or Unit

The increased use of dewatering methods in certain carbonate and shale reservoirs in Oklahoma, which typically have a high water cut during the initial phase of hydrocarbon production, stimulated interest in providing a tax incentive to encourage the use of such technology. Reservoir dewatering projects have substantial costs associated with electricity and associated delivery and transmission services caused by the use of high capacity downhole pumps to accelerate the removal of formation water. Likewise, there is added electricity expense caused by operation of large capacity disposal wells configured to receive the high volume of produced water. Once the water is removed at accelerated rates, oil and gas production, which otherwise would be uneconomic under traditional production methods, has often increased substantially. Also, increased development of natural gas from coal seams in Eastern Oklahoma, which involves the dewatering of the coal seam to enhance gas production, spurred interest in this incentive. In some areas of the state, electricity sold by public utilities with certified service territories, is subject to state sales tax. To encourage oil and gas development in such areas, the Oklahoma Legislature enacted S.B. 871 (2002) to provide for the Oklahoma Corporation Commission

OKLAHOMA (continued)

to classify areas and reservoirs as "reservoir dewatering projects" and/or "reservoir watering units", wherein the statutory criteria of an initial water to oil ratio greater than or equal to five to one (5 to 1) is proved to exist. The regulations implementing S.B. 871 provided for a conversion factor to calculate an water to gas ratio to equate to the 5 to 1 water to oil ratio. Once classified as a "reservoir dewatering project", request is made to the Oklahoma Tax Commission for a sales tax exemption letter, which the operator uses in its relationship with the electricity supplier to gain an exemption of the state sales tax otherwise charged for sales of electricity and associated delivery and transmission services for operation of the project.

Citation: Okla. Stat. tit. 68, § 1357 (2002)

Effective date: Enacted on July 1, 2002; effective January 1, 2004 for operations commencing after July 1, 2003.

Goal: To increase the use of reservoir dewatering technology associated with the drilling, exploration and production of hydrocarbon resources from certain carbonate, shale and coal seam reservoirs in the state. To provide a state tax incentive for such drilling, exploration and production enterprises through a reduction of the state's sales tax burden on the sale of electricity and associated delivery and transmission services, which are an inherently high expense for reservoir dewatering operations.

Active supporters: Independent oil and gas producers who have been actively pursuing reservoir dewatering projects in Oklahoma have promoted this incentive. Initially this involved operators who have drilled and produced oil and gas from certain carbonate and shale reservoirs, which typically have a high water to oil ratio during initial recovery phases. Such reservoirs historically have sustained poor economic returns because of high water production and modest hydrocarbon recovery. Use of high-volume formation water recovery and disposal methods proved to increase oil and gas recovery from such fields, thus interest grew in providing tax incentives for this enterprise. Later, gas producers interested in stimulating development of natural gas from Eastern Oklahoma coal seams promoted this incentive where it was possible to gain a sales tax reduction in the cost of electricity purchased for reservoir dewatering operations.

Tax Exemption for Secondary Recovery Project

The incremental production from approved secondary oil recovery projects begun on or after July 1, 1988, and before July 1, 2000, is eligible for an exemption of gross production tax for a period of ten (10) years or expire upon project payback, whichever occurs first.

Citation: Okla. Stat. tit. 68, § 1001(D)(1),(2) (2002)

Effective dates: July 1, 1988, through June 30, 2000

Goal: To encourage operators to increase ultimate recovery by employment of secondary recovery techniques.

Tax Exemption for Secondary Recovery Properties

The incremental production from approved secondary recovery properties approved or having an initial beginning date on or after July 1, 2000, and prior to July 1, 2006, is exempt from gross production tax for a period of five (5) years or ending upon termination of the secondary recovery process. The operator is not required to submit capital expenses or project costs.

Citation: Okla. Stat. tit. 68, § 1001 (D)(3) (2003)

OKLAHOMA (continued)

Effective dates: July 1, 2000, through June 30, 2006

Tax Exemption for Tertiary Recovery

The incremental production from approved tertiary recovery projects begun on or after July 1, 1988, and before July 1, 2006, is exempt from gross production tax for a period of ten (10) years or expire upon project payback, whichever comes first. Project payback provides for recovery of capital and operating expenses. Administration expenses and capital expenses of pipelines built to transport carbon dioxide to a project are excluded.

Citation: Okla. Stat. tit. 68, § 1001(D)(4) (2003)

Effective dates: July 1, 1988, through June 30, 2006

Goal: To encourage operators to increase ultimate recovery by employment of tertiary recovery techniques.

Gross Production Incentive Rebates:

Horizontally Drilled Wells

Wells qualifying for this rebate must be drilled in a manner which encounters and subsequently produces from a geological formation at an angle in excess of seventy (70) degrees from the vertical and which laterally penetrates a minimum of one hundred and fifty (150) feet into the pay zone of the formation. For wells producing after July 1, 1994 and prior to July 1, 2002, the rebate shall be 24 months or ending upon payback. For wells producing after July 1, 2002 and prior to July 1, 2006, the rebate shall be 48 months or ending upon payback.

Citation: Okla. Stat. tit. 68, § 1001(E) (2003)

Effective dates: 1990; through June 30, 2006

Goal: To encourage the use of new technology and increase recovery.

Reestablished Production from Non-Productive Wells

A well on which work to re-establish production commenced on or after July 1, 1994, and on or before June 30, 1997, that has not produced oil, natural gas, or oil and natural gas for a period of not less than two (2) years, as evidenced by the appropriate forms on file with the Oklahoma Corporation Commission reflecting the well's status.

A well on which work to reestablish production commenced on or after July 1, 1997, and on or before June 30, 2006, that has not produced oil, natural gas, or oil and natural gas for a period of not less than one (1) year, as evidenced by the appropriate forms on file with the Oklahoma Corporation Commission reflecting the well's status.

A well which, after July 1, 1997, experiences mechanical failure or loss of mechanical integrity, as defined by the Corporation Commission, including, but not limited to, casing leaks, collapse of casing, loss of equipment in a wellbore or any similar event which causes cessation of production and results in a workover of the well, as evidenced by the use of a workover rig or other mechanical device being placed over the well to repair the well or equipment.

Qualified wells are exempt for a period of 28 months from the date production was re-established.

OKLAHOMA (continued)

Citation: Okla. Stat. tit. 68, § 1001(F) (2003)

Effective dates: 1990; through June 30, 2006

Goal: To increase production from existing fields.

Production Enhancements (Re Completions & Workovers)

Re Completions

(A) For production enhancement projects having a project beginning date prior to July 1, 1997, any downhole operation in an existing oil well or natural gas well that is conducted to establish production of oil or natural gas from any geological interval not currently completed or producing in such existing oil or natural gas well.

(B) For production enhancements projects having a project beginning date on or after July 1, 1997, and prior to July 1, 2003, any downhole operation in an existing oil well or natural gas well that is conducted to establish production of oil or natural gas from any geologic interval not currently completed or producing in such existing oil or natural gas well within the same or a different geologic formation.

Workovers

Any downhole operation in an existing oil or natural gas well that is designed to sustain, restore or increase the production rate or ultimate recovery in a geologic interval currently completed or producing in said existing oil or natural gas well. For production enhancement projects having a project beginning date prior to July 1, 1997, "workover" includes, but is not limited to acidizing, reperforating, fracture treating, sand/paraffin removal, casing repair, squeeze cementing, or setting bridge plugs to isolate water productive zones from oil or natural gas productive zones, or any combination thereof. For production enhancement projects having a project beginning date on or after July 1, 1997, and prior to July 1, 2006, "workover" includes, but is not limited to acidizing; reperforating; fracture treating; sand, paraffin, or scale removal or other wellbore cleanouts; casing repair; squeeze cementing; installation of compression on a well or group of wells or artificial lifts on oil, natural gas, or oil and natural gas, wells, including plunger lifts, rod pumps, submersible pumps and coiled tubing velocity strings; downsizing existing tubing to reduce well loading; downhole commingling; bacteria treatments; upgrading the size of pumping unit equipment; setting bridge plugs to isolate water production zones; or any combination thereof. "Workover" shall not mean the routine maintenance, routine repair, or like-for-like replacement of downhole equipment such as rods, pumps, tubing, packers, or other mechanical devices.

Qualified production enhancements shall be exempt for a period of 28 months from the date of first sale after project completion.

Citation: Okla. Stat. tit. 68, § 1001(G) (2003)

Effective dates: July 1, 1994, through June 30, 2006

Goal: To encourage operators to increase production from existing fields by performing the described operations.

Deep Wells

For purposes of qualifying for the exemption, "depth" means the length of a maximum

OKLAHOMA (continued)

continuous string of drill pipe utilized between the drill bit face and the drilling rig's kelly bushing.

Deep wells spudded between July 1, 1994, and June 30, 1997, and drilled to a depth of 15,000 feet or greater shall be exempt from gross production tax beginning with the date of first sale for a period of twenty-eight (28) months.

Deep wells spudded between July 1, 1997, and June 30, 2002, and drilled to a total depth of 12,500 feet or greater shall be exempt from gross production tax for a period of twenty-eight (28) months beginning with the date of first sale.

Deep wells spudded between July 1, 2002, and June 30, 2006, and drilled between a depth of 12,500 feet and 14,999 feet shall be exempt from gross production tax for a period of twenty-eight (28) months beginning with the date of first sale. Deep wells spudded between July 1, 2002, and June 30, 2006, and drilled between a depth of 15,000 feet and 17,499 feet shall be exempt from gross production tax for a period of forty-eight (48) months beginning with the date of first sale. Deep wells spudded between July 1, 2002, and June 30, 2006, and drilled to a total depth of 17,500 feet or greater shall be exempt from gross production tax for a period of sixty (60) months beginning with the date of first sale.

Citation: Okla. Stat. tit. 68, §§ 1001(H) (2003)

Effective dates: July 1, 1994, through June 30, 2006

Goal: To stimulate natural gas development in Oklahoma.

New Discovery Wells

New Discovery is defined as production of oil, natural gas or oil and natural gas from:

(A) A well, spudded or reentered prior to July 1, 1997, which discovers crude oil in paying quantities, and is located more than one (1) mile from the nearest oil well producing from the same interval.

(B) A well, spudded or re-entered on or after July 1, 1997, and prior to July 1, 2006, which discovers crude oil in paying quantities, and is located more than one (1) mile from the nearest oil well producing from the same interval of the same formation.

(C) A well, spudded or re-entered prior to July 1, 1997, which discovers crude oil in paying quantities beneath current production in a deeper producing formation, located more than one (1) mile from the nearest oil well producing from the same deeper interval.

(D) A well, spudded or re-entered on or after July 1, 1997, and prior to July 1, 2006, which discovers crude oil in paying quantities beneath current production in a deeper producing interval, located more than one (1) mile from the nearest oil well producing from the same interval of the same formation.

(E) A well, spudded or re-entered prior to July 1, 1997, which discovers natural gas in paying quantities, and is located more than two (2) miles from the nearest natural gas well producing from the same interval.

OKLAHOMA (continued)

(F) A well, spudded or re-entered on or after July 1, 1997, and prior to July 1, 2006, which discovers natural gas in paying quantities, and is located more than two (2) miles from the nearest natural gas well producing from the same interval.

(G) A well, spudded or re-entered prior to July 1, 1997, which discovers natural gas in paying quantities beneath current production in a deeper producing interval, that is located more than two (2) miles from the nearest natural gas well producing from the same deeper interval.

(H) A well, spudded or re-entered on or after July 1, 1997, and prior to July 1, 2006, which discovers natural gas in paying quantities beneath current production in a deeper producing interval, that is located more than two (2) miles from the nearest natural gas well producing from the same deeper interval.

Qualified new discovery wells shall be exempt for a period of twenty-eight (28) months from the date of first sales.

Citation: Okla. Stat. tit. 68, §§ 1001(I) (2003)

Effective dates: July 1, 1997, through June 30, 2006

Economically At-Risk Oil Leases

Operators may apply to the Oklahoma Tax Commission for a rebate of 6/7ths of the gross production tax upon demonstrating that they operate an oil lease that is economically at-risk. A lease must operate at a net loss or net profit which is less than the severance tax paid for the lease during the previous tax year. Gross production tax exemptions under this section are limited to production from calendar years 1997 and 1998.

Citation: Okla. Stat. tit. 68, § 1001.3 (2000)

Effective date: January 1, 1999

Three-Dimensional Seismic Technology

Operators producing oil, natural gas, or oil and natural gas from a well, the drilling of which is commenced after July 1, 2000 and prior to July 1, 2006, located within the boundaries of a three-dimensional seismic shoot and drilled based upon three-dimensional seismic technology, may apply to the Tax Commission for a rebate of gross production tax paid in the previous fiscal year upon qualifying such well with the Oklahoma Corporation Commission.

Qualified projects shall be exempt for a period of eighteen (18) months from the date of first sale for seismic shot prior to July 1, 2000. Projects shot after July 1, 2000 and prior to July 1, 2006 shall be exempt for a period of twenty-eight (28) months from the date of first sale.

Citation: Okla. Stat. tit. 68, § 1001 (J) (2003)

Effective dates: July 1, 2000, through June 30, 2006

Active Supporters: Oklahoma Corporation Commission and oil and natural gas operators in the state.

Note on the Rebate Price Cap

The exemption as it pertains to each project with the exception of horizontally drilled wells, is contingent upon the average calendar year price of oil and natural gas. In the

OKLAHOMA (continued)

event the average calendar year price of Oklahoma oil or natural gas as determined by the Tax Commission should exceed the established price cap provided for by statute, the exemption for the affected product would be canceled for the applicable fiscal year period.

An example of the average price exceeding the cap occurred in calendar year 2001 wherein the established price cap for natural gas was three dollars and fifty cents (\$3.50) per mmbtu. The average price of natural gas in 2001 was three dollars and seventy cents (\$3.70) per mmbtu. The price cap for natural gas was exceeded and the exemptions from production tax on natural gas were canceled for the production period of July 2001 through June 2002.

Since the inception of the exemptions, the price cap has been amended several times for both products. The price cap applicable to the most current calendar year (2002) is thirty dollars (\$30.00) per barrel of oil and five dollars (\$5.00) per one thousand cubic feet (mcf) of natural gas. Based on the average price of both oil and natural gas for the calendar year 2002 as determined by the Tax Commission, neither product exceeded the established cap. Therefore, the exemptions for the production period of July 2002 through June 2003 shall be eligible for rebate beginning July 1, 2003.

Special Programs

The Oklahoma Commission on Marginally Producing Oil and Gas Wells collects and distributes information on stripper production and performs many other activities useful to the petroleum industry, especially small operators. It is funded by small oil and gas taxes from nonexempt production. Producers can opt out of paying.

The Oklahoma Energy Resources Board (OERB) was established for energy education and the remediation of abandoned oil field sites. The OERB conducts educational programs for children, and spends at least half of its funding on oil field cleanup projects. The OERB also studies remediation technology using U.S. Department of Energy funds.

Small Business Linked Deposit Program

Provides low-interest loans to qualifying businesses, including oil-related businesses.

OREGON

Oregon currently has no oil or gas incentive programs.

PENNSYLVANIA

Electronic Transactions Act

In December 1999 the Pennsylvania legislature passed this version of the Uniform Electronic Transactions Act. This legislation can be considered an incentive in that it allows for the electronic submission of permit applications and required reports.

Citation: 73 P.S. § 2260.101 et seq.

Effective date: January 15, 2000

PENNSYLVANIA (continued)

Grandfathering Pre-Act Wells from Bonding

Bonding is not required for any well drilled prior to April 18, 1985, the date of the Oil and Gas Act, or for on-site disposal of residual waste at these well sites.

Citation: 71 P.S. § 1934-A

Effective date: November 26, 1997; no sunset

Goal: To allow operators more working capital.

Active supporters: Independent oil producers.

Orphan Wells

Permit fees are waived for producers who recondition an orphan well from the Department of Environmental Protection's plugging inventory and return it to production.

Citation: Pa. Laws 223, Chapter 6, § 601(c): Waiver for Rehabilitation of Abandoned or Orphan Wells

Effective date: August 1, 1992; no sunset

Goals: To bring wells back into service and remove them from the state's plugging list and to increase production while saving plugging costs for the state.

Impact: One producer in Pittsburgh has taken advantage of the program. There have been other inquiries about the program to the Department of Environmental Protection.

SOUTH DAKOTA

NEW Unit Ratification

Lowers the percentage of working interest and mineral interest owners needed to ratify unit operations, from 75% to 60% in cases of compulsory unitization. This incentive is to be granted by the South Dakota Department of Environment and Natural Resources Oil and Gas Section.

Citation: HB 1014

Effective dates: July 1, 2004

Goals: To encourage additional oil and gas development by expediting unitization, which encourages increased oil and gas production through enhanced recovery project; it is good conservation practice to utilize aging, depleted vertical wells for drilling horizontal laterals to reach areas in the reservoir unaffected even after thirty or forty years of production from the vertical wells.

Active supporters: Industry.

NEW Risk Compensation

Rule specifies risk compensation allowed in cases of forced pooling and compulsory unitization. Allows cost plus 200% in compulsory pooling where interest is derived from a lease or other contract and allows cost plus 100% where interest is not subject to a lease or other contract. Allows cost plus 200% in compulsory unitization where interest is derived from a lease or other contract and allows cost plus 100% where interest is not subject to a lease or other contract. This incentive is to be granted by the South Dakota Department of Environment and Natural Resources Oil and Gas Section.

Citation: Chapter 72:10:18

Effective dates: July 1, 2004

Goals: To encourage additional oil and gas development by allowing easier formation of drilling units and unitized areas.

SOUTH DAKOTA (continued)

Active supporters: Industry.

Oil Field Services

An oil field services sales tax provision provides a 1% tax exemption on oil field services. The effective tax rate is 3%.

Citation: S.D. Codified Laws Ann. § 10-45-5.3

Effective dates: July 1, 1982; amended July 1, 1991; no sunset

Goals: To maintain a competitive oil field services industry in South Dakota, and to stimulate oil and gas exploration.

Impact: This incentive is thought to have had little impact.

Voluntary Environmental Audit

Voluntary environmental audit privilege provides limited immunity for violations of environmental law, rule, regulation or permit enforced by the Department of Environment and Natural Resources which are discovered and reported to the department within 30 days. The department is prohibited from prosecuting those violations if they are corrected within 60 days. If the violations are not corrected within 30 days, a written compliance schedule may be negotiated between the department and the operator. The department is prohibited from requesting the results of an environmental audit.

The environmental audit may not be used as a civil or criminal defense if the producer:

- Willfully and knowingly committed the violation;
- Has a pattern of repeated violations;
- Has not corrected the violation within 60 days of discovery;
- Has been penalized for a violation within two years of disclosure of the present violation.

Citation: S.D. Codified Laws Ann. §§ 1-40-33 through 36; § 1-40-3

Effective date: July 1, 1996

Goal: To encourage self evaluation and improve the environment by enabling businesses to perform self-assessment and to report and voluntarily mitigate environmental problems without the threat of penalty.

Impact: Not yet known.

Active supporters: Introduced by the Senate Agriculture and Natural Resources Committee on behalf of the Department of Environment and Natural Resources; supported by the Industry and Commerce Association (ICA), the South Dakota Retailers Association and others.

Natural Gas Sold Out of State

The mineral severance tax is imposed at the time natural gas is sold or consumed, whichever occurs first. This effectively eliminates severance tax on natural gas sold out of state.

Citation: S.D. Codified Laws Ann. § 10-39A-3.1

Effective dates: March 8, 1978; amended July 1, 1991

Goal: To encourage development of the natural gas industry in South Dakota.

Impact: Relatively little impact, as very little natural gas is sold out of state.

Active supporters: This program came about as a committee bill sponsored by the Department of Environment and Natural Resources.

SOUTH DAKOTA (continued)

Oil and Gas Royalty Increment Status

The Commissioner of School and Public Lands can grant significantly lower state royalty rates on school and public lands, when no lease has been issued within the last 10 years, and no prospecting or exploration permit for oil and gas has been issued in the last five years. There cannot have been oil or gas production on the state-owned land or land within the immediate area. The rate may be lowered to 1/16 for the first three years of the lease, 1/12 for the second three years, and a minimum of 1/8 thereafter.

Citation: S.D. Codified Laws Ann. §§ 5-7-41 through 45

Effective date: July 1, 1993; no sunset

Goals: To encourage the development of oil and gas on public lands and to avoid any substantial impact on privately owned minerals immediately adjacent to these leased minerals.

Impact: The effectiveness of this program has not been studied, but it is believed to have been very effective in increasing the number of leases granted on certain lands that otherwise would remain unleased. According to the Department of Environment and Natural Resources, this is reflected in oil and gas auction results in Hyde and Buffalo counties.

Active supporters: Department of School and Public Lands.

TENNESSEE

Tennessee currently has no oil or gas incentive programs.

TEXAS

Extended Tax Rate Reductions - High Cost Gas Incentive

Extension on the tax rate reduction for high-cost natural gas wells. There is a reduction for up to 120 months or until cumulative value of exemption equals 50% of drilling and completion cost. The total allowable credit for taxes paid for reporting periods before the date the application is filed may not exceed the total tax paid on the natural gas that otherwise qualified for the exemption or tax reduction and that was produced during the 24 months immediately preceding the month in which the application for certification under this section was filed with the commission. The 78th Texas legislature removed the filing deadline and made the severance tax exemption permanent.

Citation: H.B. 2424, 2425

Effective date: September 1, 1999; no sunset

Goal: To increase exploration for deep/high cost gas production.

Active supporters: Railroad Commission of Texas (RRC), Texas Independent Producers and Royalty Owners (TIPRO), Texas Oil and Gas Association (TXOGA), and regional oil and gas associations.

Severance Tax Administration

Removal of accelerated biennial due date ("speed up") for natural gas severance taxes and penalties for speeding up late payments. Eliminates early payment of natural gas tax in odd-numbered years.

Agency: Comptroller of Public Accounts.

TEXAS (continued)

S.B. 290 Production Qualification Query System

This Internet-based query system was developed to provide quick and easy access to oil leases and gas wells that meet the production criteria specified in SB290 for a temporary severance tax exemption. Depending on the price certified by the Comptroller, these wells and leases may be exempt from severance tax payments. Wells can no longer qualify for S.B. 290. Due to the lack of traffic on this query, it was removed from the RRC Web site. Information concerning wells that qualify for SB 290 continues to be available through an Open Records request through the Commission's Information Technology Services Department.

Citation: S.B. 290

NEW Texas Oil and Gas Production Query System (PDQ)

Texas created an Internet-based production query system to provide quick and easy access to Texas oil and gas production information.

Effective dates: In June 2004, PDQ provided enhanced features such as the ability to view: production in multiple year date ranges, production disposition by codes and volumes, operator and field name changes over selected date ranges, common reservoir production data by selecting fields that contain the reservoir name and specific lease queries without going through the general menu. In March 1998, production information for 1997 and 1996 was made available on the RRC Web site through the ACTI Production Query System. In September 1998, production from 1993 through the current production month became available.

Goal: To use the technology to provide the global community with oil and gas information as a means of promoting further domestic exploration and production.

Impact: The production query system is being widely used. The public can access production totals by county, field, district, lease or operator.

Active supporters: Industry, royalty owners, public.

Flared Casinghead Gas

If an operator markets casinghead gas that had previously been released to the air (vented or flared) for 12 months or more in compliance with RRC rules and regulations, the operator may receive a severance tax exemption for that gas for the life of the oil well or lease.

Citation: § 202.058

Effective date: September 1, 1997

Goal: To conserve natural gas.

Impact: This incentive pertains to a small number of wells.

Active supporters: RRC, TIPRO, TXOGA and regional associations.

Two-Year Inactive Wells

This incentive mirrors the successful three-year inactive wells incentive originally passed in 1993. Any oil or gas well that has not produced in more than one month in the last 24 is eligible for a 10-year severance tax exemption upon a return to beneficial production.

Citation: § 202.056

Effective dates: September 1, 1997, to August 31, 2009, for application for certification; February 28, 2010, for certification; severance tax exemption is for up to 10 years from date of RRC certification.

TEXAS (continued)

Goal: To encourage the return to productivity of inactive wells, with the resulting benefits to the state economy; to reduce the need for state and industry-funded plugging.

Impact: This incentive is based on Texas' Three-Year Inactive Wells program, which enjoyed such success that at least nine states adopted similar programs, but was allowed to expire. In the year prior to the Three-Year Inactive Wells incentive, 368 wells inactive for three years or more were brought back into production. Following enactment, from September 1993 through February 1996, 6,071 wells were returned to production, with an annual average of 2,428 reactivated wells. This increase of 670% in inactive wells returned to production is valued at an estimated \$565 million at the wellhead and approximately \$1.65 billion to the economy of Texas each year. This benefit to the state is estimated to be enough to create 10,792 new jobs.

Active supporters: RRC, TIPRO, TXOGA and regional associations.

The Two-Year Inactive Well Program was originally scheduled to expire in August 1999. The 76th Texas Legislature extended the program for 10 years, until February 2010. The current Two-Year Inactive well incentive became effective Sept. 1, 1999. Following enactment, from September 1997 to June 2004, 10,074 wells were returned to production with an annual average of approximately 1,700 wells.

Marginal Gas Wells

The RRC can exempt marginal gas wells from otherwise applicable production limitations if the wells are located in gas fields without special field rules. A marginal gas well is defined in the Texas Natural Resources Code as a gas well incapable of producing more than 250,000 cubic feet of gas per day under normal operating conditions. Prior to this legislation, the TRC was precluded from exempting individual marginal wells that exist in fields with other wells capable of producing above marginal limits. This legislation replaced the RRC's requirement to limit production from gas wells producing more than 100,000 cubic feet of gas per day unless it is a marginal well in a field for which special field rules are not in effect.

Citation: H.B. 1178; amends Tex. Nat. Res. Code Ann. § 86.091

Effective date: May 16, 1997

Goal: To relieve regulatory burden of testing marginal gas wells.

Impact: Raises the production limitations on marginal gas wells and reduces industry expense associated with testing of gas wells.

Enhanced Oil Recovery

Severance tax is reduced by 50% (from 4.6% to 2.3%) for oil production from new enhanced oil recovery projects and incremental production from expanded projects for 10 years after RRC certification of production response. The RRC certification is a three-step process: first, (form H-12), the operator seeks approval and area certification for the new/expanded project; second, (form H-13), the operator seeks Railroad Commission certification that the project evidences a positive production response (an increased rate of production attributable to the project); third, (form H-14), the operator files an annual status report without which the credits are not validated. The application for positive production response certification must be filed within three years of project approval for secondary enhanced recovery, and within five years for tertiary recovery. The 78th Texas legislature removed filing deadline and made the severance tax exemption permanent.

TEXAS (continued)

Citations: HB 2424

Effective dates: Effective 1989, and 1991 for expanded projects; no sunset

Goal: To encourage additional recovery of the state's oil reserves through the use of enhanced oil recovery technology, and to extend the lives of wells with the resulting benefit to the Texas economy through job creation and additional severance taxes.

Marginal Wells on State Land

The Texas School Land Board may grant a reduced royalty rate for a period of two years for marginally economic state leases. To qualify, the lease must produce an average of 15 BOPD per well, or an average of 90 Mcf of gas per day per well. Once the reduced rate is granted, royalty rates will not increase for that lease for two years. Additional reductions can be applied for at the expiration of the two-year period. This tax reduction applies when oil prices average less than \$25 per barrel.

Citation: Tex. Nat. Res. Code Ann. § 32.067, and Tex. Admin. Code tit. 31, § 9.7

Effective date: Sept. 1, 1995

Goal: To extend the lives of leases on state lands.

Paperwork Reduction

Producers may delay payment of royalties until they reach a total of \$100 or 12 months proceeds have accumulated, whichever comes first. Annual reporting for the lease may not exceed \$3,000.

Citation: H.B. 1593

Effective date: June 15, 1995

Goal: To help the state and operators avoid the costs of administering small royalty checks.

Royalty Reduction

Royalty rates are reduced for production early in the terms of leases. For submerged areas, production in years one and two earns a royalty of 20%; production in years three and four earns 22%. For uplands production, year one earns a royalty rate of 20%; production in year two earns 22.5%.

Citation: School Land Board rule

Goal: To maintain overall royalty revenue while providing an operator greater working interest revenue.

Impact: The effectiveness of this incentive has not been studied, but it is reported that more activity occurs earlier in the terms of leases since the rule took effect than prior to implementation of the incentive. The program benefits both the state and operators.

Active supporters: TIPRO, Texas Mid-Continent Oil and Gas Association, and Industry.

UTAH

Workovers/Recompletions

A working interest owner who pays for all or part of the expenses of a recompletion or workover is entitled to a tax credit equal to 20% of those expenses. The tax credit may not exceed \$50,000 per well during each calendar year until Dec. 31, 1994, and \$30,000 per well during each calendar year, beginning Jan. 1, 1995.

UTAH (continued)

Citation: Utah Code Ann. § 59-5-102(6)

Effective date: January 1, 1990; no sunset

Goal: To encourage investment in and continued production of wells, increase recovery, delay abandonment, establish new production and provide for economic gains in areas of the state which have oil and gas activity. Since the cost of a workover is only a fraction of the cost to drill a new well, a workover incentive is expected to extend the producing life of wells in the Uintah Basin, thereby creating jobs and tax revenue in that region.

Impact: This is an effective and widely used incentive.

Active supporters: Petroleum industry, county and state governments.

Graduated Severance Tax Rate

For oil, the severance tax rate is 3% up to and including the first \$13 per barrel, and 5% of the value exceeding \$13 per barrel. The severance tax rate for natural gas is 3% for the first \$1.50 per Mcf, and 5% of value above \$1.50.

Citation: Utah Code Ann. § 59-5-102(2)

Effective date: Jan. 1, 1992; no sunset

Goal: To provide tax relief during periods of low prices, encouraging continued production.

Marginal/Stripper Wells

Stripper wells are tax exempt unless the exemption prevents the severance tax from being treated as a deduction for federal tax purposes. Stripper wells are defined as wells which produce an average of less than 20 BOPD for one year, or 60 Mcf or less of natural gas per day for 90 consecutive days.

Citation: Utah Code Ann. § 59-5-102(5)(b)

Effective date: Jan. 1, 1984; no sunset

Goal: To encourage continued production activity and to avoid premature abandonment of marginal wells.

Field Exemption

The first \$50,000 annually in gross value of each well or field is exempt from severance taxes, to be prorated proportionally among the interest owners.

Citation: Utah Code Ann. § 59-5-102(5)(a)

Effective date: Jan. 1, 1947; no sunset

Goal: To encourage exploration activity.

Wildcat Wells

No severance tax is imposed on the first 12 months of production from wildcat wells started after January 1, 1990.

Citation: Utah Code Ann. § 59-5-102(5)(c)

Effective date: Jan. 1, 1990; no sunset

Goal: To encourage exploration activity.

New Wells

The first six months of production from new wells started after Jan. 1, 1984, but before January 1, 1990, and development wells started after Jan. 1, 1990, is exempt from severance taxes.

Citation: Utah Code Ann. § 59-5-102(5)(d)

UTAH (continued)

Effective dates: Jan. 1, 1984, (new wells); no sunset, and Jan. 1, 1990 (development wells); no sunset

Goal: To encourage exploration activity.

Enhanced Recovery

A 50% reduction in severance tax is available for the incremental production achieved from an enhanced oil or gas recovery project.

Citation: Utah Code Ann. § 59-5-102(7)

Effective date: January 1, 1996; no sunset

Goals: To encourage initiation of enhanced recovery projects and use of marginal wells, increase production and avoid premature abandonment of marginal wells.

Active supporters: Industry and state government.

VIRGINIA

REVISED Direct Sales of Natural Gas by Producers

Producers of natural gas may sell directly to as many as 35 commercial and industrial customers without having to become certified as a public utility. Certain public schools are also customers not to be classified as a public utility. The customer limit was raised during the 1997 Virginia General Assembly session from a 10-customer limit. The number of schools are not limited and it does not count against the "fewer than 35" requirement.

Citation: Va. Code Ann. § 56-265.1 (amended by 2004 Va. Acts 748,1028)

Effective dates: 1990, amendment effective July 1, 2004

Goal: To allow gas producers to sell natural gas to commercial, industrial and public schools in areas not served by local gas utilities.

Impact: Several companies have extended service under this program.

Active supporters: Virginia gas producers, local economic development officials.

Escrow of Coalbed Methane Conflicting Ownership Claims

Established under section 45.1-361.22 of the Virginia Gas and Oil Act, the Virginia Gas and Oil Board may escrow proceeds from a coal seam natural gas production well in a unit where there are conflicting claims to ownership of the gas. The Board pays the escrowed proceeds when there is a final decision of a court of competent jurisdiction or agreement among all conflicting claimants addressing the ownership of the gas.

Citation: Va. Code Ann. § 45.1-361.22

Effective date: July 1, 1990; no sunset

Goals: To allow production of coal seam natural gas in areas with conflicting claims of ownership.

Impact: The Virginia Department of Mines, Minerals and Energy has determined that this section of the Virginia Code has been one key factor that has led to increases in coal seam natural gas production from nominal levels in 1989 to over 50 BCF/year.

Active supporters: The Virginia Oil and Gas Association, and coal seam natural gas operators.

Coalfield Employment Enhancement Tax Credit

One cent per million BTUs of coal seam natural gas production is credited to the producer.

VIRGINIA (continued)

Citation: Va. Code Ann. § 58.1 - 439.2

Effective dates: July 1, 1996, to Jan. 1, 2008

Goals: To preserve and expand the coal industry and related jobs, and to encourage production of coal seam natural gas.

Impact: Production of coal seam natural gas has increased since this incentive was passed. It is not known to what extent this incentive affected the increase.

Active supporters: Virginia's coal producers.

Sales and Use Tax Exemptions

Raw materials, fuel, power, energy, supplies, machinery, tools and repair/replacement parts used directly in the drilling, extraction, refining or processing of natural gas or oil and reclamation of the well area are exempt from the 3.5% state sales and use tax, and the 1% local sales and use tax. Exemption includes all phases of production and processing, including gathering, until gas is pipeline quality.

Citation: Va. Code Ann. § 58.1-609.3(12)

Effective dates: July 1, 1994, through June 30, 2006

Goal: To stimulate investment in Virginia by providing sales and use tax exemptions similar to exemptions offered in other Appalachian Basin states.

Impact: Initial, onetime revenue impact for Virginia's economy is estimated at \$1 million.

The 1996 impact is estimated at \$250,000 to \$325,000 (approximately \$2,300 to \$2,700 per conventional well, and \$1,400 to \$1,800 per coalbed methane well). As a result, some producers have increased investment in Virginia.

Active supporters: Virginia Oil and Gas Association.

Pollution Control Equipment and Facilities Tax Exemptions

Certified pollution control equipment and facilities, including real and tangible property, which are certified by the Department of Mines, Minerals and Energy to be in conformity with state requirements, are exempted from state and local sales and use taxes and are eligible for exemption from local tangible personal property taxes.

Citation: Va. Code Ann. § 58.1-609.3(9), § 58.103660

Effective dates: July 1, 1994, to June 30, 2006

Goal: To promote the production of oil and gas in Virginia.

Impact: Some producers have increased investment in Virginia as a result of the approximately \$25,000 to \$30,000 (\$100 to \$150 per well) annual savings.

Active supporters: Virginia Oil and Gas Association.

Virginia Department of Mines, Minerals and Energy, Division of Mineral Resources

The Division of Mineral Resources conducts research and provides information about the state's gas and oil resources for Virginia's gas and oil industry. The division maintains all information on coreholes, geologic features in gas and oil bearing areas, and a database on wells drilled in the Commonwealth.

Effective date: Virginia's geological survey was started in 1835.

Goal: Enhance the development and conservation of energy and mineral resources in a safe and environmentally sound manner to support a more productive economy.

Impact: Customers continually rate the services of the division as very useful.

Active Supporters: Gas and oil operators.

VIRGINIA (continued)

Consent to Stimulate Coalbed Methane

The Virginia Gas and Oil Act requires a producer of coal seam natural gas to obtain consent from the coal operator of each coal seam located within 750 horizontal feet of a well or 100 vertical feet of any coal seam to be stimulated. A 1997 amendment to this requirement provides that this consent shall be deemed to be granted for any tract where title to the coal is held by multiple owners who have not leased the tract for coal development when the gas operator obtains consent from the co-owners holding a majority interest in the tract.

Citation: Va. Code Ann. § 45.1-361.29.F.2 (amended by 1996 Va. Acts 759 and 765)

Effective date: July 1, 1997

Goal: To allow production of coal seam natural gas when the consent to stimulate cannot be obtained from all co-owners of a tract of coal.

Impact: It is too early to determine the effects of this change.

Active Supporters: Virginia Oil and Gas Association.

WEST VIRGINIA

Severance Tax Exemption

Imposes a tax equal to 5% of the gross value produced for the privilege of severing natural gas or oil. Effective taxable periods beginning on or after Jan. 1, 2000. An exemption from the severance tax is granted for natural gas provided free to surface owners.

The exemption is granted to low-volume wells, producing less than 5 Mcf of natural gas per day or oil wells that produced an average of less than one-half barrel of oil per day during the calendar year immediately preceding a given taxable period. Natural gas or oil produced from a well that has not produced marketable quantities for five consecutive years immediately preceding the year in which the well is placed back into production and begins producing marketable quantities is also exempted for a maximum of 10 years.

Citation: H.B. 2749

Effective date: May 12, 1999

Goal: To maintain the production of marginal oil and gas wells.

Bona Fide Future Use Program

Wells that have not been producing in the previous 12 months can be designated as having a "bona fide future use." Such a designation would keep idled wells from being deemed abandoned and avoid subjecting them to a plugging obligation.

Citation: WV Code Chapter 22, Article 6-19

Effective date: July 1, 1993

Goal: To stimulate returning existing, idled wells to production and encourage new wells.

Direct Use Sales Tax Exemption

When the exemption from sales tax for contractors was removed in 1989, subcontractors were included for the oil and gas industry, even though contract drillers were still exempt from sales tax on purchases used directly in the production of oil and gas. The 1994 Legislature clarified in Senate Bill 328 that this "direct use" exemption was available also to oil and gas subcontractors.

Effective dates: 1989 and 1994

WEST VIRGINIA (continued)

Natural Gas Vehicle Incentive

In April 1996, then Gov. Gaston Caperton signed a bill creating a tax credit that will be available for a period of 10 years. The credit can be applied for a vehicle converted to run on natural gas or the purchase of a factory-built natural gas vehicle. The credit will be worth \$3,750 for a light duty vehicle under 10,000 pounds gross vehicle weight (GVW), \$9,250 for a medium duty vehicle with 10,000 to 26,000 pounds GVW, and \$50,000 for a heavy duty vehicle of more than 26,000 pounds GVW.

Citation: WV Code Chapter 11, Article 6D

Effective date: April 1996

WYOMING

Tertiary Production

Tertiary production resulting from projects certified by the Wyoming Oil and Gas Conservation Commission (WOGCC) after March 31, 2003 and before March 31, 2008, is exempt from the 2% of severance taxes imposed by Wyo. Stat. 39-14-204(a)(iii) for a period of five years from the date of first tertiary production. An exemption under this subsection shall not be granted in those months when the price received by the producer for the tertiary production equals or exceeds \$27.50 per barrel. A taxpayer claiming a tax reduction under this subsection is prohibited from claiming a tax reduction provided by subsection (f) or (g) of this section.

Citation: Wyo. Stat. § 39-14-205 (c)

Effective dates: March 31, 2003 through March 31, 2008

Goal: To encourage discovery of new reserves and continued production of older reservoirs. The May 1, 2000, amendment's goal was the exclusion of coalbed methane wells.

Active Supporters: WOGCC.

Idle Wells

A five-year severance tax reduction from 6% to 1.5% is available on oil produced from previously idle wells. Wells must not have produced for at least the two consecutive years prior to January 1, 1995. This tax reduction applies for the first 60 months of renewed production or until the average price of oil reaches a level of \$25 per barrel averaged over the preceding six months, whichever occurs first.

Citation: Wyo. Stat. § 39-14-205(h)

Effective date: Jan. 1, 1995; no sunset

Impact: 115 wells were restored to production in the 1994 - 2003 time period resulting in \$1.6 million in severance and ad valorem taxes.

Active supporters: Petroleum industry, WOGCC and pro-business legislators.

Marginal/Stripper Wells

Wells which produce an annual average of less than 15 BOPD while the price of oil is less than \$20 per barrel are taxed at 4% (reduced from 6%). When the price of oil is \$20 or more, wells producing 10 BOPD or less receive the 2% tax reduction.

Citation: Wyo. Stat. § 39-14-205(a)(xx)(A)(B)

Effective date: Jan. 1, 1995; no sunset

Goal: To encourage continued production from low-volume, marginal wells.

WYOMING (continued)

Impact: Wyoming recognizes that high severance tax rates contribute to premature abandonment. Stripper production was 15.4% of total state production in 2002, when 8,430,429 barrels of oil qualified for this reduction. The importance of this incentive continues to grow as Wyoming's fields continue to mature.

Active supporters: Petroleum industry, WOGCC and pro-business legislators.

Environmental Audit Privilege

This privilege gives oil and gas companies complete immunity from fines and penalties of the Department of Environmental Quality for violations that are reported to the department along with remediation plans.

Citation: Wyo. Stat. §§ 35-11-1105 and 1106

Effective date: Feb. 18, 1995

Goal: To encourage environmental compliance.

Active supporters: Mineral industry, other Wyoming industries and pro-business legislators.

State-Funded Demonstration Project

The state of Wyoming, concerned with the economic and employment costs of abandonment of marginal wells, has funded a demonstration project which should benefit wells in danger of abandonment. The new technology is a hydraulic fracture technique for sandstone reservoirs. This technique is expected to produce oil economically from shallow sandstone formations, reducing the rate of abandonment for many marginal wells.

Effective date: Rock Creek Enterprises conducted the demonstration in April 1996.

Goal: To encourage production from marginal wells as a result of more efficient recovery.

Federal Incentive Programs

BUREAU OF LAND MANAGEMENT (BLM)

Royalty Rate Reduction for Stripper Oil Property

The operator or owner of a federal stripper oil property that is producing less than 15 BOPD average qualifies for a royalty rate reduction from the normal royalty rate of 12.5%. This royalty rate reduction is based on a sliding scale.

Citation: 61 FR 4748, 4750; 43 C.F.R. §§ 3103.4-1, 3103.4-4

Effective date: 1992; extended indefinitely in 1997

Goal: To extend the economic life of property and enhance production.

Heavy Oil Royalty Rate Reduction

Operators of properties that produce "heavy oil," crude oil with a gravity of less than 20 degrees API (American Petroleum Institute), are eligible for a royalty rate reduction. The royalty rate reduction is based on a sliding scale for qualifying heavy oil properties. The sliding scale is intended to somewhat offset the reduced prices paid for oil as gravity decreases. For example, at 20 degrees API gravity the royalty rate is 12.5%, which can be reduced to a minimum of 0.5% based on the corresponding API gravity of the oil.

Citation: 61 FR 4748, 4750; 43 C.F.R. §§ 3103.4-1, 3103.4-3

Effective date: Feb. 8, 1996

Goals: To extend the economic life of the property and to enhance production.

Impact: The BLM reports that 30 California applicants qualified during the first eight months the incentive was in effect. Applicants in Louisiana, Nevada and Wyoming also have taken advantage of this incentive.

Fuel Substitution

A royalty rate reduction is available for operators who choose to burn clean fuel for on-lease beneficial use. The conversion for this exchange is BTU for BTU (1:1).

Note: Any operator can request a royalty rate reduction on a federal lease property. A royalty rate reduction will be granted only on an economic basis after strict scrutiny.

DEPARTMENT OF COMMERCE

Emergency Oil and Gas Guaranteed Loan Program

Provides \$500 million in loan guarantee authority to a board comprised of the Secretary of Commerce and the chairmen of the Securities and Exchange Commission and the Federal Reserve. Individual loans for as much as \$10 million are eligible for guarantees of up to 85%. The authority to guarantee loans under this program expired on Dec. 31, 2001. There are no minimum loan guarantee amounts and all loans must be repaid no later than Dec. 31, 2010.

Citation: Public Law 106-51; 13 CFR Chapter V, Part 500; 64 FR 57946; 15 U.S.C.S. § 1841

Effective date: Dec. 27, 1999

Eligibility: Any independent oil and gas company that is a small business concern under Section 3 of the Small Business Act that is an oil field service company whose main

DEPARTMENT OF COMMERCE (continued)

business is providing tools, products, personnel and technical solutions on a contractual basis to exploration and production operators that drill, complete wells and produce, transport, refine and sell hydrocarbons and their by-products as its main commercial business. The company also must have experienced layoffs, production losses or financial losses since the beginning of the oil import crisis, after Jan. 1, 1997.

Goal: To assist the independent oil and gas producers in the United States with recovery from the low price period, while sustaining domestic oil production.

INTERNAL REVENUE SERVICE (IRS)

The Jobs and Growth Tax Relief Reconciliation Act of 2003

Major changes affecting business tax returns made by this legislation include:

- The Act provides an additional first-year depreciation deduction equal to 50% of the adjusted basis of qualified property, effective for taxable years ending after May 5, 2003. Qualified property is defined in the same manner as for purposes of the 30% additional first year depreciation provided by the Jobs Creation and Workers Assistance Act of 2002, except that the applicable time period for acquisition (or self-construction) of the property is modified. In general, in order to qualify for the 50% additional first-year depreciation deduction, the property must be acquired after May 5, 2003, and before Jan. 1, 2005. Property does not qualify if it was acquired pursuant to a binding written contract in effect before May 6, 2003.
- Section 179 of the Internal Revenue Code allows for the recovery of all or part of the cost of certain qualified property, up to a limit, by deducting it in the year in which the property is placed in service. For tax years beginning in 2001 and 2002, the limit was generally \$24,000, except if the cost of the qualifying section 179 property placed in service in a year was over \$200,000, the dollar amount was reduced (but not below zero) by the amount of the cost over \$200,000. The Act increases the section 179 expensing limit to \$100,000 for property placed in service in taxable years beginning in 2003, 2004 and 2005. In addition, the phase-out of the limit, (currently \$200,000) is modified so that the phase-out starting point is increased to \$400,000 for property placed in service in 2003, 2004 and 2005. Both the \$100,000 limit and \$400,000 starting point are indexed annually for inflation in 2004 and 2005.

Citation: Public Law 108-27

Effective date: May 28, 2003

Extension of the Suspension of the 100% Net-Income Limit

Two methods of depletion are allowable under the Code: (1) the cost depletion method and (2) the percentage depletion method. Under the percentage depletion method, generally 15% of the taxpayer's gross income from the property is allowed as a deduction in each taxable year. (§ 613 (c)) The amount deducted generally may not exceed 100% of the net income from that property in any year. (§ 613 (a)) The Taxpayer Relief Act of 1997 suspended the 100% of net income limitation for production from marginal wells for

IRS (continued)

the taxable years beginning after 1997 and before Jan. 1, 2001.

The provision extends the period when the 100% net-income limitation is suspended to include taxable years beginning after Dec. 31, 2001 and before Jan. 1, 2004.

Citation: I.R.C. § 613A

Special Depreciation Allowance A special depreciation allowance can be claimed for qualified property placed in service after Sept. 10, 2001. The allowance is an additional deduction of 30% of the property's depreciable basis. To figure the depreciable basis, multiply the property's cost or other basis by the percentage of business/investment use and then reduce that amount by any Section 179 deduction and certain other deductions and credits for the property. The allowance is deductible for both regular tax and alternative minimum tax (AMT) purposes. There is no AMT adjustment required for any depreciation figured on the remaining basis of the property. In the year in which the allowance is claimed (generally the year the property is placed in service), the depreciable basis of the property is reduced by the allowance before figuring the regular depreciation deduction.

Qualified Property

To qualify for the special depreciation allowance, property must meet the following requirements. It is new property of one of the following types:

- Property depreciated under the modified accelerated cost recovery (MACRS) with a recovery period of 20 years or less.
- Water utility property.
- Computer software that is not a Section 197 intangible.
- Qualified leasehold improvement property.

Citation: I.R.C. 179

Natural Gas Vehicles

A \$2,000 adjustment to gross income on federal taxes is available for the purchase of a natural gas powered vehicle (NGV). This adjustment can be applied for a vehicle converted to run on natural gas or for the purchase of a factory-built NGV. In the case of any natural gas powered truck or van with a gross vehicle weight (GVW) rating greater than 10,000 pounds but not greater than 26,000 pounds, the allowable deduction is \$5,000. For a natural gas powered truck or van with a gross vehicle weight rating greater than 26,000 pounds, or any bus which has a seating capacity of at least 20 adults (not including the driver), the deduction is \$50,000. The deduction pertains only to that portion of equipment installed (including installation costs) to convert a vehicle to the use of natural gas, or in connection with the exhaust from such vehicles.

Citation: I.R.C. 179A

Effective date: Property placed in service after June 30, 1993, and before Jan. 1, 2005

MINERALS MANAGEMENT SERVICE (MMS)

Federal Oil and Gas Royalty Simplification and Fairness Act of 1996

The Royalty Simplification and Fairness Act (RSFA) streamlines the audit and appeal

MMS (continued)

process, shortens records retention requirements, alters reciprocal interest requirements with industry receiving interest on overpayments, limits the liability period to seven years and specifies liable parties, and reduces reporting requirements through prepayments of royalties on marginal properties.

Citation: 30 U.S.C.S. §§ 1701 et seq.; 104 H.R. 1975

Effective date: Provisions are effective beginning Sept. 1, 1996.

Goal: To decrease the time required for collections owed to the U.S. government, to lessen burdensome and costly record keeping, to quicken resolution of money disputes and correction of underpayment/overpayment problems, and to provide a more cost-effective approach to royalty management by streamlining and simplifying certain royalty requirements and practices.

Impact: The RSFA amends portions of the Federal Oil and Gas Royalty Management Act of 1982 to provide that owners of operating rights in a federal oil and gas lease are primarily liable for royalty payments on their portions of their lease, and that owners of record title for such leases are secondarily liable. This required the collection of data connecting the lessees with the parties who are currently paying and reporting on federal leases, an increased administrative burden on industry and government.

Active supporters: U.S. Sens. Don Nickles and Pete Domenici; U.S. Reps. Ken Calvert, Calvin Dooley, Billy Tauzin and Frank Lucas. Former U.S. Sen. Frank Murkowski and former U.S. Rep. Bill Brewster.

OTHER PROGRAMS

The MMS has a number of initiatives designed to encourage offshore domestic oil and natural gas production.

UPDATED Deep Gas Incentive

This incentive is for the exploration and development of deep gas deposits in shallow water (less than 200 meters). The program provides, for leases issued from 2001 through 2003, a royalty suspension on the first 20 BCF of gas produced from a new deep gas reservoir 15,000 feet TVD or deeper. The incentive is specified in the Notice of OCS Lease Sale and in the lease instrument. The Final Rule of Relief or Reduction in Royalty Rates-Deep Gas Provisions was published on Jan. 26, 2004, with a Technical Amendment published on April 30, 2004. The rule provides, for leases issued before 2001 and after 2003, a royalty suspension volume (RSV) up to 15 BCF on gas produced from a well completion 15,000 to less than 18,000 feet TVD and up to 25 BCF for 18,000 feet TVD or deeper. The maximum RSV per lease is 25 BCF. The rule also provides a royalty suspension supplement (RSS) up to 5 BCFE for unsuccessful wells drilled to a target reservoir 18,000 feet TVD or deeper. The RSS must be applied to royalties due on future oil and gas production on the same lease. Two RSS's are available per lease and they must be earned prior to production from a deep well. Lessees of leases issued from 2001 through 2003 had an option to replace, before Sept. 1, 2004, the deep gas royalty relief terms in the lease instrument with the terms in the final rule.

Citation: 30 CFR 203.0 AND 203.40-48

Date of Proposed Rule: May 3, 2004

Goal: Exploration and development of offshore deep gas resources.

MMS (continued)

End-of-Life Leases

A lease operator may apply for end-of-life royalty relief if royalty payments exceed 75% of net revenue for a 12-month period. The royalty rate will be reduced by one-half. This incentive is applicable to producing leases in the Gulf of Mexico and Pacific Outer Continental Shelf (OCS).

Citation: 30 CFR 203.50-56

Effective date: Feb. 17, 1998

Goal: Extend the economic life of producing leases.

The following incentives are available only for the Gulf of Mexico OCS.

Eligible Leases

Under the Deepwater Royalty Relief Act of Nov. 28, 1995 royalty relief (no application required) is provided for deepwater leases that were issued from 1996 through 2000. A royalty suspension volume is assigned, based on water depth, to a field rather than each lease. Royalty suspension volumes are 17.5 million BOE for water depths from 200 to 399 meters, 52.5 million BOE from 400 to 799 meters, and 87.5 million BOE for 800 meters and greater.

Citation: 30 CFR 260.110(d)

Effective dates: Feb. 17, 1998; updated as 30 CFR 260.112-117, effective March 26, 2001

Goal: To encourage development of deepwater resources.

Royalty Suspension (RS) Leases

An automatic royalty suspension volume is provided for post 2000 deepwater leases as specified in the Notice of OCS Lease Sale and the lease document. The royalty suspension volumes in a recent lease sale were 5 million BOE for water depths from 400 to 799 meters, 9 million BOE for water depths from 800 to 1,599 meters and 12 million BOE for 1,600 meters and greater.

Citation: 30 CFR 260.120-124

Effective date: March 26, 2001

Goal: To encourage the development of deepwater resources.

Subsalt Lease Term Extension

This incentive encourages drilling of wells with subsalt hydrocarbon objectives. The program provides up to a two-year extension of the five-year primary lease term, thus allowing the operator additional time to refine subsalt imaging techniques and to process and interpret such imaging.

Citation: Notice to Lessees and Operators No. 2000-G22

Goal: Development of offshore subsalt resources.

Deepwater Discretionary Royalty Relief for Pre-Act (Deepwater Royalty Relief Act of November 28, 1995) and Post 2000 Leases

This rule provides a royalty suspension incentive that applies specifically to oil and gas fields and projects that would otherwise be uneconomical when considering sunk costs and payment of royalties. The incentive is applicable to deepwater, 200 meters and greater, and the operator must receive approval through an application process.

MMS (continued)

Citation: 30 CFR Part 203.60-91

Effective: Feb. 14, 2002

Goal: Increase development of offshore deepwater resources.

International Incentive Programs

CANADA

FEDERAL PROGRAMS

Atlantic Canada Investment Tax Credit (ACITC)

The federal government offers a tax credit specific to investments in Atlantic Canada. ACITC provides a credit equal to 10% of the cost of certain investments. Among those investments are the costs associated with bringing an offshore well into production. The ACITC is not refundable for foreign corporations, but is refundable under certain circumstances for Canadian-controlled private companies. This tax credit can be used to reduce federal income taxes in one of two ways. It can be used to offset federal income taxes otherwise payable, or it can be used to receive a full or partial refund in the year that the expenses are incurred.

Citation: Canadian Income Tax Act, Subsection 127(9)

Objective: To specifically promote economic development in the Atlantic provinces and the Gaspé region.

ALBERTA

Enhanced Oil Recovery Royalty Relief

Introduced in 1977, this program offsets the costs of enhanced oil recovery (EOR) after the less costly primary and secondary extraction methods have been exhausted. The program's goal was to facilitate the use of EOR methods for conservation of petroleum resources and to prolong the economic production life of mature oil pools. The Alberta Department of Energy (ADOE) shares in the costs of EOR projects by reducing the royalty payable on incremental oil production. The allowable EOR costs are incremental to the base case recovery scheme and must be approved by the ADOE.

The ADOE will provide greater royalty relief in recognition of the higher costs associated with the carbon dioxide (CO₂) EOR. The ADOE will also provide some temporary program features in order to encourage industry to undertake CO₂ EOR projects.

The EOR Royalty Relief program is open to applications for new projects and expansion of existing projects.

The key criteria for EOR project approval are:

- The project must be on enhanced recovery scheme.
- The project must use the injection of hydrocarbons, carbon dioxide, nitrogen, chemicals or other material approved by the ADOE.
- The project is likely to produce more oil from the pool than could be produced under the base recovery scheme.
- The costs to implement and operate the project are significantly greater than the costs to implement and operate the base recovery scheme.
- The ADOE in reviewing any project for approval may take into consideration

ALBERTA (continued)

whether the royalty reduction is in the public interest.

Citation: A.R. 348/93

Effective date: Jan. 1, 1977; no sunset

Goal: To encourage the use of enhanced oil recovery methods to conserve the province's petroleum resources.

CO₂ Projects Royalty Credit

Alberta believes that a producer's ability to undertake certain projects is often limited by the related technical and financial risk. This program provides a reduction in royalties to encourage producers to undertake demonstration CO₂ projects.

The royalty credit program is a temporary feature of Alberta's royalty system and has the following attributes:

- A maximum of \$15 million will be provided over five years in the form of oil and/or natural gas royalty credits to offset up to 30% of companies' allowed costs in approved CO₂ projects.
- A maximum of \$5 million in royalty credits may be approved for a single CO₂ project.
- Approval of applications will be constrained by total program funding, time limit for the program, and project selection criteria.
- The royalty credit is not ring-fenced to production from the project site. Royalty credits may be applied against the payment of petroleum or natural gas royalty owing to the Crown.
- The royalty credit can be claimed periodically upon commencement of CO₂ injection, as expenses are incurred, without awaiting production from the project site.

Citation: A.R. 120/2003

Effective dates: Jan. 1, 2003, through June 30, 2008

Goal: To promote development of CO₂ enhanced oil and natural gas recovery industry in Alberta.

Deep Gas Royalty Holiday

This is Alberta's only royalty reduction program for natural gas and was initiated by the government in 1985. The goal of the program was to encourage exploration for deep natural gas pools. As deep wells are very expensive to drill, the program provides a reduction in royalty for wells dependent upon depth drilled beyond 2,500 meters. The Deep Gas Royalty Holiday (DGRH) was last reviewed in 1999.

The DGRH applies to all new wells drilled into previously undefined natural gas pools or extensions of existing pools located below 2,500 meters. The drilling spacing unit must be wholly outside of the deep natural gas pools as defined by the Alberta Energy and Utilities Board. The royalty holiday is defined in terms of a dollar amount applied against royalties. The benefit applies until the value of the natural gas and by-products exempted equals the amount determined by a depth-based schedule. The maximum value of the holiday is \$3.6 million, and the entitlements must be used within 10 years from the finished drilling date. Submission of an application is required to apply for the benefits.

Citation: A.R. 351/93

Effective date: May 31, 1985; no sunset

ALBERTA (continued)

Goal: To encourage the discovery of deep natural gas pools.

Third Tier Exploration Oil Royalty Holiday

A third tier exploratory well is an oil well or an oil sands well that was spudded after Sept. 30, 1992 and classified as a new field wildcat (NFW), or a new pool wildcat (NPW), or a deeper pool test (DPT). Initiated by the industry, the goal of this program is to encourage the discovery of new oil pools in a mature basin. The results of a review conducted in 2000 showed that the policy has been effective in achieving its goal as it caused higher exploration activity resulting in more new discoveries.

This program reduces royalty on the new oil well that results in the discovery of a new productive pool. The royalty holiday is effective from the first production month until the accumulated royalty holiday reaches \$1 million or 12 production months, whichever occurs first. This program allows an earlier payout of successful exploration well costs. Wells producing from third-tier vintage oil pools receive a lower royalty rate. This lower royalty rate plus the holiday is meant to reflect the higher costs of finding and developing smaller oil pools. Wells that commence production on or after Oct. 1, 1992, will be reviewed by the ADOE to assess eligibility. The royalty holiday will be established for qualifying wells when the ADOE calculates royalty for the month that initial oil production is reported. The holiday is retroactive, to the month when production commenced. No application is required for the program.

Citation: A.R. 16/93

Effective date: Oct. 1, 1992; no sunset

Goal: To encourage the discovery of new oil reservoirs.

Reactivated Well Holiday

A reactivated well is an oil well or oil sands well that was reactivated on or after Oct. 1, 1992, after the well did not produce any substance during its qualifying period. The program was introduced by the government of Alberta in 1992 with the goal of encouraging reactivation of shut-in oil or oil sands wells. The policy has been positive for sustaining the production from mature oil pools.

The program provides a royalty holiday for the wells that are successfully reactivated to help earlier recovery of the reactivation costs. Non-producing wells that commence production on or after Oct. 1, 1992, will be reviewed by the ADOE to establish the royalty holiday for the qualifying wells. The royalty holiday is available from the reactivation date until a cumulative of 8,000 cubic meters of oil has been produced from the reactivated well. No application is required for the program.

Citation: A.R. 352/92

Effective date: Oct. 1, 1992; no sunset

Goal: To encourage reactivation of non-producing wells.

Low Productivity Well

Initiated by the oil producers in 1991, the ADOE developed this policy to alleviate the royalty burden on low productivity oil wells. The goal of the program is to ensure that royalty is not a barrier to the incremental investments necessary to increase production from low productivity oil wells. The program provides a maximum royalty rate of 5% of

ALBERTA (continued)

production for wells currently producing at modest levels.

Well production history will be reviewed by the ADOE to establish royalty adjustment for eligible wells when the royalty is calculated. The program ensures that the royalty rate applying to the first 16,000 cubic meters of oil or oil sands production from each eligible well will be the lower of 5% or the rate determined by the oil royalty formula. No application is required for the program.

Citation: A.R. 350/92

Effective date: Oct. 1, 1992; no sunset

Goal: To encourage additional production from low productivity wells.

Horizontal Re-entry Well Royalty Reduction

This is a permanent royalty policy that was proposed and supported by the petroleum industry. The goal is to prolong the economic production life of mature oil pools by using horizontal well technology, thereby conserving the province's oil resources. The program was last reviewed in 2000.

The royalty rate will be capped for oil produced from an eligible horizontal extension. The cap will be the royalty rate associated with the average production volume for the latest 12 months when production occurred before re-entry. For a well with a 12-month production average of up to 184 cubic meters per month, royalty will be capped at one half that rate for the incremental production that exceeds the qualifying average. To obtain the capped royalty for horizontal re-entry oil well production, a written application is to be submitted to the ADOE.

Citation: A.R. 348/92

Effective date: Oct. 1, 1992; no sunset

Goal: To encourage incremental production from mature pools.

Experimental Project Petroleum Royalty Regulation

The policy was introduced in 1979 to encourage the development of new and improved methods for crude oil recovery. The program reduces the royalty associated with experimental projects.

The experimental schemes approved by the Alberta Energy and Utilities Board are eligible for a flat royalty rate of 5% of the production during the experimental royalty period. To obtain the 5% experimental royalty rate, an operator must file a letter with the ADOE requesting approval of the scheme, and specification of an experimental royalty period.

Citation: A.R. 65/92

Effective date: 1972; no sunset

Goal: To encourage development of new and improved oil recovery methods.

Otherwise Flared Solution Gas Royalty Waiver

The Otherwise Flared Solution Gas (OFSG) royalty waiver program was introduced to encourage the reduction of solution gas flaring in the province. For those wells approved under this program, the Crown royalty is waived on uneconomic solution gas and gas by-products.

ALBERTA (continued)

Royalty is waived on solution gas production from wells approved for OFSG status by the Alberta Energy and Utilities Board (AEUB). The AEUB may determine that a portion of the solution gas production is economic to conserve. In these cases, an apportionment factor (A-factor) will be used to determine the applicable royalty waiver. An application is required in order to receive benefits under the program.

Citation: A.R. 220/2002

Effective date: Jan. 1, 2002; no sunset

Goal: To reduce the volume of solution gas being flared in Alberta.

BRITISH COLUMBIA

NEW Deep Gas Re-entry Royalty Program

For a deep re-entered well, a deep re-entry deduction amount may be deducted from a reporting entity's royalty payable if the well has a reentry date after Nov. 30, 2003 and before July 1, 2008. A royalty tax reduction of 23% of drilling and completion costs.

Effective date: Nov. 30, 2003 to July 1, 2008

Goal: To encourage exploration and development of deep gas resources by enhancing drilling economics.

Active supporters: Ministry of Energy and Mines.

NEW Deep Gas Discovery Royalty Program

Deep Discovery Wells would qualify for the lesser of either a three-year royalty holiday or 283,000,000 m³ of royalty free gas.

A Deep Discovery Well is a well that has a pay the top of which has a True Vertical Depth deeper than 4000m and has a rig release date after Nov. 30, 2003 and before July 1, 2008, and its surface location is at least 20 kilometers away from the surface location of any well in a recognized pool of the same formation.

Effective date: Nov. 30, 2003; to July 1, 2008

Goal: To encourage exploration and development of deep gas resources by enhancing drilling economics.

Active supporters: Ministry of Energy and Mines.

REVISED Deep Gas Royalty Program

It is estimated that approximately 12 tcf, or 40% of the remaining marketable natural gas in British Columbia is deep natural gas. Deep natural gas resources are very important for future development of the natural gas sector in British Columbia. Deep natural gas drilling has higher costs and lower success rates as compared to conventional development drilling.

The deep well royalty program will provide a royalty credit amounting to approximately 23% of the drilling and completion costs. The amount of royalty credit depends on drilling location and depth.

Additionally, a deep well-depth deduction amount may be deducted from a reporting entity's royalty payable if:

BRITISH COLUMBIA (continued)

- the well in which the deep well events are located has a spud date after Nov. 30, 2003 and before July 1, 2008.
- the well depth deduction amount is based on the deepest productive deep well event in the well.

Effective dates: Nov. 30 to July 1, 2008

Goal: To encourage exploration and development of deep natural gas resources by enhancing drilling economics.

Active supporters: Ministry of Energy and Mines.

EXTENDED Coalbed Gas Royalty

- Includes produced water handling costs in the producer cost of service allowance to address the added water management costs;
- Creates a royalty bank to collect excess allowance to be used against future assessed coal seam natural gas royalties;
- Increase the marginal well adjustment factor threshold to 600,000 cubic feet per day from 180,000 cubic feet per day to address the lower production rates; and
- Provides a \$50,000 royalty credit for coal seam natural gas wells drilled before July 1, 2008.

The Royalty Tax reduction is 10 - 12%.

Effective date: March 1, 2002

Goal: Encourage coal seam natural gas development.

Active supporters: Ministry of Energy and Mines.

Marginal Gas Well Royalty Program

Qualifying marginal natural gas wells based on depth and initial production rates will have reduced royalties. The Royalty Tax reduction is 10 - 13%.

Effective dates: July 1, 2003; to July 1, 2009

Goal: The purpose of this targeted relief is to induce activity that would not otherwise happen under the predicted future economic environment utilizing the current fiscal regime.

Active supporters: Canadian Association of Petroleum Producers (CAPP), and the Ministry of Energy and Mines.

Marginal Gas Well Royalty Reduction

Natural gas wells near the end of their economic life receive reduced royalty rates to extend well production. The Royalty Tax reduction is 10 - 12%.

Citation: B.C. Reg. 495/92

Effective date: April 1, 2001

Goal: Extend marginal well production and maximize royalties.

Active supporters: Ministry of Energy and Mines.

Royalty Credits for Infrastructure Program

Provides royalty credits of up to \$10 million annually (plus possibly an additional \$20 million based on business cases) towards the construction, upgrading and maintenance of road infrastructure in support of resource exploration and development.

Effective date: July 1, 2003

BRITISH COLUMBIA (continued)

Goal: Improve access to resources, extend the drilling season, increase economic activity in British Columbia's heartlands communities and increase revenue to the province.

Active supporters: Ministry of Energy and Mines.

Summer Royalty Program

The summer royalty program provides a credit of the lesser of \$100,000 or 10% of drilling and completion costs for oil and natural gas wells drilled between April 1, and Nov. 30.

Effective dates: July 1, 2003; to Dec. 1, 2005

Goal: Extend drilling season and for opportunities producing and selling time for oil and natural gas products.

Active supporters: Ministry of Energy and Mines.

Heavy Oil Royalty

Heavy oil wells are subject to lower royalty rates reflecting the higher operating costs and lower market value. The Royalty Tax reduction is 7 - 16%.

Citation: B.C. Reg. 495/92

Effective date: Aug. 1, 1999

Goal: To enhance heavy oil resource development and maximize royalties.

Active supporters: Ministry of Energy and Mines.

Incremental Oil

Incremental oil includes oil that would not have been recovered without a new pressure maintenance scheme, an improved pressure maintenance scheme or other enhanced oil recovery scheme methods, but does not include heavy oil.

Incremental oil will be considered as either new oil or third tier oil and be subjected to a lower royalty rate. The Royalty Tax reduction is 10 - 25%.

Citation: B.C. Reg. 495/92

Effective date: Aug. 1, 1999

Goal: To encourage enhanced oil recovery and maximize royalties.

Active supporters: Ministry of Energy and Mines.

PROPOSED INCENTIVE

Net Profit Royalty Regime for Development of Unconventional Gas Resources

Proposing net profit royalty regime for the commercial production of unconventional resources such as tight gas, shale gas, coal seam natural gas as well as enhanced gas recovery and remote area resources.

Goal: To facilitate the development of unconventional gas resources in British Columbia.

Active supporters: Ministry of Energy and Mines.

NEWFOUNDLAND AND LABRADOR

Generic Onshore Royalty Regime

Overview

The royalty regime is designed to be sensitive to the levels of risks and profits associated

NEWFOUNDLAND AND LABRADOR (continued)

with the area in question and to be comparative with the royalty regimes in other districts, while providing an equitable sharing of revenues.

The similarity in the offshore and onshore geology, coupled with the potential for the discovery of hydrocarbon accumulations both in the onshore and nearshore areas, have led to increased interest by the petroleum industry in developing the western Newfoundland area. The establishment of a royalty regime contributes to lowering the risks to the petroleum industry as well as fully assessing the petroleum potential in this area.

This system is based on extensive economic analysis and is designed:

- to reflect the attractiveness of the province's onshore petroleum resources;
- to be sensitive to small and marginal prospects;
- to be competitive with the royalty systems applied in other jurisdictions; and
- to ensure a minimum level of fiscal benefits to Newfoundland and Labrador.

The royalty holiday provides the most assistance to small and marginal prospects, ensuring that no royalty will be paid on the first 2 million barrels, or equivalent, of production. The basic royalty ensures that beyond 2 million barrels, the province will receive a minimum of 5% of gross revenue. The profit sensitive component is designed to reflect changing economic circumstances and to ensure our competitiveness with the systems applied in other jurisdictions. Unless a certain profit level is exceeded, then no additional royalty beyond the 5% basic will be levied. If, however, such a profit level is exceeded, then government revenue will increase as project profitability increases.

The discovery of hydrocarbons in Newfoundland and Labrador has the potential to create new economic opportunities. The development of a viable petroleum industry in western Newfoundland could represent a new industry whose magnitude will be very dependent on the success of the current round of exploration programs.

Definitions

Gross revenue: gross sales revenue less transportation costs to point of sale.

Net revenue: gross revenue less uplifted costs.

Costs: exploration, capital, and operating.

Uplifts: gross-up of costs (proxy for overheads).

Return allowance: allowance for a rate of return on investment (proxy for cost of capital).

Components of Royalty Regime

The regime has three basic components that are:

1. Royalty Holiday

2 million barrels or equivalent (the 2 million-barrel holiday in the onshore was used as an incentive to attract exploration and development of onshore petroleum resources);

2. Basic Ad Valorem Royalty

5% of gross revenue;

NEWFOUNDLAND AND LABRADOR (continued)

3. Two Tier Net Profits Royalty

- a. **Incremental Royalty — Tier 1:** 20 percent of net revenue after a rate of return of 5% plus the long-term government bond rate.
Type: Net profit based.
Term: Commences upon incremental royalty tier 1 payout and continues to the end of production.
Amount: Net revenue multiplied by the tier 1 incremental royalty rate and basic royalty is creditable against tier 1 incremental royalty.
When: Eligible costs have been repaid, including eligible capital and operating costs; basic royalty; and a tier 1 incremental royalty return allowance.
- b. **Incremental Royalty--Tier 2:** 5% of net revenue after a rate of return of 15% plus the long-term government bond rate.
Type: Net profit based.
Term: Commences upon incremental royalty tier 2 payout and continues to the end of production.
Amount: Net revenue multiplied by the tier 2 incremental royalty rate.
When: Eligible costs have been repaid, including eligible capital and operating costs; basic royalty; incremental royalty — tier 1; and a tier 2 incremental royalty return allowance.

Effective: 1994

Goal: To facilitate exploration and development through fiscal framework certainty.

Generic Offshore Royalty Regime

In 1996, the province announced the establishment of a generic offshore royalty regime that applies to the development of all petroleum resources in the Newfoundland and Labrador offshore area, with the exception of the Hibernia and Terra Nova projects.

This generic offshore royalty regime will translate into increased industry activity, more employment and a stronger provincial economy. It will also provide government with a new source of revenue. The basic royalty commences at a low rate (1%) and increases as certain cumulative levels of production are reached or when costs are recovered, providing an incentive to develop small and marginal prospects by ensuring that minimal royalties are paid on these types of fields. Once cumulative production reaches 50 million barrels (mmbbls), or 20% of the initially established reserves from the project, the province will receive 2.5% of gross revenue increasing to 5% and then to 7.5% at higher levels of cumulative production. If all costs are recovered early from the project, the royalty rate will increase to 5% regardless of the cumulative production level.

Components of Royalty Regime

The regime has two basic components that are:

1. Basic Ad Valorem Royalty

- 1 to 7.5% of gross revenue
- a. 1% until the earliest of:
 - 20% of reserves

NEWFOUNDLAND AND LABRADOR (continued)

50 million barrels of production

- Cost recovery

b. 2.5% until the earliest of:
100 million barrels of cumulative production
Cost recovery
- c. 5% for the next 100 million barrels of production
- d. 7.5% thereafter

2. Two Tier Net Profit Incremental Royalty

- a. **Tier 1:** 20% of net revenue after a rate of return of 5% plus the long-term government bond rate.
Type: Net profit based.
Term: Commences upon incremental royalty tier 1 payout and continues to the end of production.
Amount: Net revenue multiplied by the tier 1 incremental royalty rate and basic royalty is creditable against tier 1 incremental royalty.
When: Eligible costs have been repaid, including eligible capital and operating costs; basic royalty; and a tier 1 royalty return allowance.
- b. **Tier 2:** 10% of net revenue after a rate of return of 15% plus the long-term government bond rate.
Type: Net profit based.
Term: Commences upon incremental royalty tier 2 payout and continues to the end of production.
Amount: Net revenue multiplied by the tier 2 incremental royalty rate.
When: Eligible costs have been repaid, including eligible capital and operating costs; basic royalty; incremental royalty — tier 1; and a tier 2 royalty return allowance.

Effective: 1996

Goal: To promote exploration and development while ensuring that the province receives a fair share of offshore petroleum revenues.

The two tier net royalty is profit sensitive. It is designed to reflect changing economic circumstances and to ensure competitiveness with royalty systems in other jurisdictions. When a certain profit level is achieved, the net royalty is applied with the province receiving the greater of the gross or tier one net royalty payable. If profits increase beyond that level, government revenue will also increase. If these profits increase significantly, then government revenue will also increase as the tier two net royalty component will levy an additional 10% of net revenue.

NOVA SCOTIA

Research and Development Tax Credit

The province of Nova Scotia offers a research and development tax credit, which is similar to the federal Scientific Research and Experimental Development incentive program. Nova Scotia taxpayers, who engage in qualified research, are eligible for this incentive.

Acknowledgments

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Definitions

Abandoned wells are wells which have been permanently plugged. The remaining petroleum production potential of these wells is often lost forever.

Bcf is an acronym for "billion cubic feet" of gas.

BOPD is an acronym for "barrels of oil per day."

Development wells are new wells drilled into existing reservoirs and are also known as "in-fill" wells.

Discovery wells are wells drilled to extract petroleum from a previously unproduced pool.

Enhanced oil recovery usually refers to the employment of tertiary recovery and secondary recovery methods. These higher technology, more expensive techniques include miscible fluid displacement, microemulsion flooding, thermal methods, and other chemical flooding methods.

Idle wells are oil or gas wells which have not been abandoned, but are not currently producing. Idle wells are also referred to as "inactive" or "shut-in" wells.

Incremental production is the increase in the amount of oil or gas produced as a direct result of an enhanced recovery or enhanced production project.

Mcf is an acronym for "thousand cubic feet."

Marginal wells are low-producing wells on the margin of profitability. States differ in the maximum a well can produce and qualify as a marginal well.

Orphan wells are idle wells whose owners are unknown, cannot be located, or are insolvent.

Primary recovery of oil is powered by the pressure energy existing in the reservoir. Further production requires the artificial introduction of energy.

Recompletion is a downhole operation in an existing well which initiates production in a geologic interval not currently producing in that well.

Secondary recovery generally consists of the injection of water in a controlled fashion into a known reservoir in order to displace the oil from the rock and push it to a producing well.

Severance tax is an excise tax levied on a barrel of oil or cubic foot of gas produced within a state. It is also called "production tax." Severance taxes are of two types: *ad valorem*, which is a percentage of the value of the product; and *specific* per barrel/Mcf, which is based on units of production (i.e., \$1/barrel).

Stripper wells are low-volume wells in the final stages of production. Exact definitions, as used in state incentive programs, vary from state to state. Since production from these wells is quite low, they are also marginal wells.

Tertiary recovery involves steam flooding or the injection of carbon dioxide gas to manipulate the reservoir and improve recovery.

Workovers are well-servicing operations designed to maintain, restore or increase the productivity of an oil or gas well and extend the well's economic life. Workovers can include such operations as repairing the cement casing in the well hole, re-acidizing, re-perforating, and removing accumulated sand or paraffin from the wellbore. These are standard operations that are not considered to be enhanced recovery projects.

About the Interstate Oil and Gas Compact Commission

The IOGCC is the only organization of its kind. It represents the governors of states that produce more than 99 percent of the domestic onshore oil and natural gas.

The organization's mission is to promote the conservation and efficient recovery of domestic oil and natural gas resources, while protecting health, safety and the environment.

Since its creation in 1935, the IOGCC has assisted states in balancing a multitude of interests - maximizing domestic oil and natural gas production, minimizing the waste of irreplaceable natural resources and protecting human and environmental health - through sound regulatory practices. The IOGCC plays an active role in Washington D.C., serving as the voice of the states on oil and natural gas issues and advocating states' rights to govern the resources found within their borders.

Member States

Alabama	(1945)
Alaska	(1957)
Arizona	(1955)
Arkansas	(1941)
California	(1974)
Colorado	(1935)
Florida	(1945)
Illinois	(1935)
Indiana	(1947)
Kansas	(1935)
Kentucky	(1942)
Louisiana	(1941)
Maryland	(1959)
Michigan	(1939)
Mississippi	(1948)
Montana	(1945)
Nebraska	(1953)
Nevada	(1955)
New Mexico	(1935)
New York	(1941)
North Dakota	(1953)
Ohio	(1943)
Oklahoma	(1935)
Pennsylvania	(1941)
South Dakota	(1955)
Texas	(1935)
Utah	(1957)
Virginia	(1982)
West Virginia	(1945)
Wyoming	(1955)

Associate States

Georgia	(1946)
Idaho	(1960)
Missouri	(1995)
North Carolina	(1971)
Oregon	(1954)
South Carolina	(1972)
Washington	(1967)

International Affiliates

Alberta	(1996)
British Columbia	(2002)
Egypt	(1999)
Republic of Georgia	(2001)
Newfoundland and Labrador	(1997)
Nova Scotia	(1997)
Venezuela	(1997)



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