

**REPEAL OF THE SEVERANCE TAX
EXEMPTION FOR STRIPPER WELLS**

2007 GENERAL SESSION

STATE OF UTAH

Chief Sponsor: Gordon E. Snow

Senate Sponsor: Kevin T. Van Tassell

LONG TITLE

General Description:

This bill amends the provisions on oil and gas severance tax revenues regarding stripper wells.

Highlighted Provisions:

This bill:

- ▶ amends the definition of a "stripper well";
- ▶ amends oil and gas severance tax provisions to eliminate the tax exemption for the first \$50,000 annually in gross value of oil and gas wells; and
- ▶ makes technical changes.

Monies Appropriated in this Bill:

None

Other Special Clauses:

None

Utah Code Sections Affected:

AMENDS:

59-5-101, as last amended by Chapter 346, Laws of Utah 2006

59-5-102, as last amended by Chapter 346, Laws of Utah 2006

Be it enacted by the Legislature of the state of Utah:



28 Section 1. Section **59-5-101** is amended to read:

29 **59-5-101. Definitions.**

30 As used in this part:

31 (1) "Board" means the Board of Oil, Gas and Mining created in Section 40-6-4.

32 (2) "Coal-to-liquid" means the process of converting coal into a liquid synthetic fuel.

33 (3) "Condensate" means those hydrocarbons, regardless of gravity, that occur naturally

34 in the gaseous phase in the reservoir that are separated from the natural gas as liquids through

35 the process of condensation either in the reservoir, in the wellbore, or at the surface in field

36 separators.

37 (4) "Crude oil" means those hydrocarbons, regardless of gravity, that occur naturally in

38 the liquid phase in the reservoir and are produced and recovered at the wellhead in liquid form.

39 (5) "Development well" means any oil and gas producing well other than a wildcat

40 well.

41 (6) "Division" means the Division of Oil, Gas and Mining established under Title 40,

42 Chapter 6.

43 (7) "Enhanced recovery project" means:

44 (a) the injection of liquids or hydrocarbon or nonhydrocarbon gases directly into a

45 reservoir for the purpose of:

46 (i) augmenting reservoir energy;

47 (ii) modifying the properties of the fluids or gases in a reservoir; or

48 (iii) changing the reservoir conditions to increase the recoverable oil, gas, or oil and

49 gas through the joint use of two or more well bores; and

50 (b) a project initially approved by the board as a new or expanded enhanced recovery

51 project on or after January 1, 1996.

52 (8) (a) "Gas" means:

53 (i) natural gas;

54 (ii) natural gas liquids; or

55 (iii) any mixture of natural gas and natural gas liquids.

56 (b) "Gas" does not include solid hydrocarbons.

57 (9) "Incremental production" means that part of production, certified by the Division of

58 Oil, Gas and Mining, which is achieved from an enhanced recovery project that would not have

59 economically occurred under the reservoir conditions existing before the project and that has
60 been approved by the division as incremental production.

61 (10) "Natural gas" means those hydrocarbons, other than oil and other than natural gas
62 liquids separated from natural gas, that occur naturally in the gaseous phase in the reservoir and
63 are produced and recovered at the wellhead in gaseous form.

64 (11) "Natural gas liquids" means those hydrocarbons initially in reservoir natural gas,
65 regardless of gravity, that are separated in gas processing plants from the natural gas as liquids
66 at the surface through the process of condensation, absorption, adsorption, or other methods.

67 (12) (a) "Oil" means:

68 (i) crude oil;

69 (ii) condensate; or

70 (iii) any mixture of crude oil and condensate.

71 (b) "Oil" does not include solid hydrocarbons.

72 (13) "Oil or gas field" means a geographical area overlying oil or gas structures. The
73 boundaries of oil or gas fields shall conform with the boundaries as fixed by the Board and
74 Division of Oil, Gas and Mining under Title 40, Chapter 6, Board and Division of Oil, Gas and
75 Mining.

76 (14) "Oil shale" means a group of fine black to dark brown shales containing
77 bituminous material that yields petroleum upon distillation.

78 (15) "Operator" means any person engaged in the business of operating an oil or gas
79 well, regardless of whether the person is:

80 (a) a working interest owner;

81 (b) an independent contractor; or

82 (c) acting in a capacity similar to Subsection (15)(a) or (b) as determined by the
83 commission by rule made in accordance with Title 63, Chapter 46a, Utah Administrative
84 Rulemaking Act.

85 (16) "Owner" means any person having a working interest, royalty interest, payment
86 out of production, or any other interest in the oil or gas produced or extracted from an oil or gas
87 well in the state, or in the proceeds of this production.

88 (17) (a) Subject to Subsections (17)(b) and (c), "processing costs" means the
89 reasonable actual costs of processing oil or gas to remove:

90 (i) natural gas liquids; or

91 (ii) contaminants.

92 (b) If processing costs are determined on the basis of an arm's-length contract,
93 processing costs are the actual costs.

94 (c) (i) If processing costs are determined on a basis other than an arm's-length contract,
95 processing costs are those reasonable costs associated with:

96 (A) actual operating and maintenance expenses, including oil or gas used or consumed
97 in processing;

98 (B) overhead directly attributable and allocable to the operation and maintenance; and

99 (C) (I) depreciation and a return on undepreciated capital investment; or

100 (II) a cost equal to a return on the investment in the processing facilities as determined
101 by the commission.

102 (ii) Subsection (17)(c)(i) includes situations where the producer performs the
103 processing for the producer's product.

104 (18) "Producer" means any working interest owner in any lands in any oil or gas field
105 from which gas or oil is produced.

106 (19) "Recompletion" means any downhole operation that is:

107 (a) conducted to reestablish the producibility or serviceability of a well in any geologic
108 interval; and

109 (b) approved by the division as a recompletion.

110 (20) "Research and development" means the process of inquiry or experimentation
111 aimed at the discovery of facts, devices, technologies, or applications and the process of
112 preparing those devices, technologies, or applications for marketing.

113 (21) "Royalty interest owner" means the owner of an interest in oil or gas, or in the
114 proceeds of production from the oil or gas who does not have the obligation to share in the
115 expenses of developing and operating the property.

116 (22) "Solid hydrocarbons" means:

117 (a) coal;

118 (b) gilsonite;

119 (c) ozocerite;

120 (d) elaterite;

- 121 (e) oil shale;
122 (f) tar sands; and
123 (g) all other hydrocarbon substances that occur naturally in solid form.

124 (23) "Stripper well" means:

125 (a) an oil well whose average daily production for the days the well has produced has
126 been [20] ten barrels or less of crude oil a day during any consecutive 12-month period; or

127 (b) a gas well whose average daily production for the days the well has produced has
128 been 60 MCF or less of natural gas a day during any consecutive 90-day period.

129 (24) "Tar sands" means impregnated sands that yield mixtures of liquid hydrocarbon
130 and require further processing other than mechanical blending before becoming finished
131 petroleum products.

132 (25) (a) Subject to Subsections (25)(b) and (c), "transportation costs" means the
133 reasonable actual costs of transporting oil or gas products from the well to the point of sale.

134 (b) If transportation costs are determined on the basis of an arm's-length contract,
135 transportation costs are the actual costs.

136 (c) (i) If transportation costs are determined on a basis other than an arm's-length
137 contract, transportation costs are those reasonable costs associated with:

138 (A) actual operating and maintenance expenses, including fuel used or consumed in
139 transporting the oil or gas;

140 (B) overhead costs directly attributable and allocable to the operation and maintenance;

141 and

142 (C) depreciation and a return on undepreciated capital investment.

143 (ii) Subsection (25)(c)(i) includes situations where the producer performs the
144 transportation for the producer's product.

145 (d) Regardless of whether transportation costs are determined on the basis of an
146 arm's-length contract or a basis other than an arm's-length contract, transportation costs
147 include:

148 (i) carbon dioxide removal;

149 (ii) compression;

150 (iii) dehydration;

151 (iv) gathering;

152 (v) separating;
 153 (vi) treating; or
 154 (vii) a process similar to Subsections (25)(d)(i) through (vi), as determined by the
 155 commission by rule made in accordance with Title 63, Chapter 46a, Utah Administrative
 156 Rulemaking Act.

157 (26) "Tribe" means the Ute Indian Tribe of the Uintah and Ouray Reservation.

158 (27) "Well or wells" means any extractive means from which oil or gas is produced or
 159 extracted, located within an oil or gas field, and operated by one person.

160 (28) "Wildcat well" means an oil and gas producing well which is drilled and
 161 completed in a pool, as defined under Section 40-6-2, in which a well has not been previously
 162 completed as a well capable of producing in commercial quantities.

163 (29) "Working interest owner" means the owner of an interest in oil or gas burdened
 164 with a share of the expenses of developing and operating the property.

165 (30) (a) "Workover" means any downhole operation that is:

166 (i) conducted to sustain, restore, or increase the producibility or serviceability of a well
 167 in the geologic intervals in which the well is currently completed; and

168 (ii) approved by the division as a workover.

169 (b) "Workover" does not include operations that are conducted primarily as routine
 170 maintenance or to replace worn or damaged equipment.

171 Section 2. Section **59-5-102** is amended to read:

172 **59-5-102. Severance tax -- Rate -- Computation -- Annual exemption -- Tax credit**
 173 **-- Tax rate reduction -- Study by Tax Review Commission -- Study by commission.**

174 (1) Each person owning an interest, working interest, royalty interest, payments out of
 175 production, or any other interest, in oil or gas produced from a well in the state, or in the
 176 proceeds of the production, shall pay to the state a severance tax on the basis of the value
 177 determined under Section 59-5-103.1 of the oil or gas:

178 (a) produced; and

179 (b) (i) saved;

180 (ii) sold; or

181 (iii) transported from the field where the substance was produced.

182 (2) (a) Subject to Subsection (2)(d), the severance tax rate for oil is as follows:

183 (i) 3% of the value of the oil up to and including the first \$13 per barrel for oil; and
184 (ii) 5% of the value of the oil from \$13.01 and above per barrel for oil.

185 (b) Subject to Subsection (2)(d), the severance tax rate for natural gas is as follows:

186 (i) 3% of the value of the natural gas up to and including the first \$1.50 per MCF for
187 gas; and

188 (ii) 5% of the value of the natural gas from \$1.51 and above per MCF for gas.

189 (c) Subject to Subsection (2)(d), the severance tax rate for natural gas liquids is 4% of
190 the value of the natural gas liquids.

191 (d) (i) On or before December 15, 2004, the Office of the Legislative Fiscal Analyst
192 and the Governor's Office of Planning and Budget shall prepare a revenue forecast estimating
193 the amount of revenues that:

194 (A) would be generated by the taxes imposed by this part for the calendar year
195 beginning on January 1, 2004 had 2004 General Session S.B. 191 not taken effect; and

196 (B) will be generated by the taxes imposed by this part for the calendar year beginning
197 on January 1, 2004.

198 (ii) Effective on January 1, 2005, the tax rates described in Subsections (2)(a) through
199 (c) shall be:

200 (A) increased as provided in Subsection (2)(d)(iii) if the amount of revenues estimated
201 under Subsection (2)(d)(i)(B) is less than the amount of revenues estimated under Subsection
202 (2)(d)(i)(A); or

203 (B) decreased as provided in Subsection (2)(d)(iii) if the amount of revenues estimated
204 under Subsection (2)(d)(i)(B) is greater than the amount of revenues estimated under
205 Subsection (2)(d)(i)(A).

206 (iii) For purposes of Subsection (2)(d)(ii):

207 (A) subject to Subsection (2)(d)(iv)(B):

208 (I) if an increase is required under Subsection (2)(d)(ii)(A), the total increase in the tax
209 rates shall be by the amount necessary to generate for the calendar year beginning on January 1,
210 2005 revenues equal to the amount by which the revenues estimated under Subsection
211 (2)(d)(i)(A) exceed the revenues estimated under Subsection (2)(d)(i)(B); or

212 (II) if a decrease is required under Subsection (2)(d)(ii)(B), the total decrease in the tax
213 rates shall be by the amount necessary to reduce for the calendar year beginning on January 1,

214 2005 revenues equal to the amount by which the revenues estimated under Subsection
215 (2)(d)(i)(B) exceed the revenues estimated under Subsection (2)(d)(i)(A); and

216 (B) an increase or decrease in each tax rate under Subsection (2)(d)(ii) shall be in
217 proportion to the amount of revenues generated by each tax rate under this part for the calendar
218 year beginning on January 1, 2003.

219 (iv) (A) The commission shall calculate any tax rate increase or decrease required by
220 Subsection (2)(d)(ii) using the best information available to the commission.

221 (B) If the tax rates described in Subsections (2)(a) through (c) are increased or
222 decreased as provided in this Subsection (2)(d), the commission shall mail a notice to each
223 person required to file a return under this part stating the tax rate in effect on January 1, 2005
224 as a result of the increase or decrease.

225 (v) The Office of the Legislative Fiscal Analyst and the Governor's Office of Planning
226 and Budget shall report the estimates prepared in the revenue forecast required by Subsection
227 (2)(d)(i) to the:

228 (A) commission on or before December 15, 2004; and

229 (B) Executive Appropriations Committee on or before January 31, 2005.

230 (3) If oil or gas is shipped outside the state:

231 (a) the shipment constitutes a sale; and

232 (b) the oil or gas is subject to the tax imposed by this section.

233 (4) (a) Except as provided in Subsection (4)(b), if the oil or gas is stockpiled, the tax is
234 not imposed until the oil or gas is:

235 (i) sold;

236 (ii) transported; or

237 (iii) delivered.

238 (b) Notwithstanding Subsection (4)(a), if oil or gas is stockpiled for more than two
239 years, the oil or gas is subject to the tax imposed by this section.

240 (5) A tax is not imposed under this section upon:

241 ~~[(a) the first \$50,000 annually in gross value of each well or wells as defined in this~~
242 ~~part, to be prorated among the owners in proportion to their respective interests in the~~
243 ~~production or in the proceeds of the production;]~~

244 ~~[(b)]~~ (a) stripper wells, unless the exemption prevents the severance tax from being

245 treated as a deduction for federal tax purposes;

246 ~~[(e)]~~ (b) the first 12 months of production for wildcat wells started after January 1,
247 1990; or

248 ~~[(d)]~~ (c) the first six months of production for development wells started after January
249 1, 1990.

250 (6) (a) Subject to Subsections (6)(b) and (c), a working interest owner who pays for all
251 or part of the expenses of a recompletion or workover may claim a nonrefundable tax credit
252 equal to 20% of the amount paid.

253 (b) The tax credit under Subsection (6)(a) for each recompletion or workover may not
254 exceed \$30,000 per well during each calendar year.

255 (c) If any amount of tax credit a taxpayer is allowed under this Subsection (6) exceeds
256 the taxpayer's tax liability under this part for the calendar year for which the taxpayer claims
257 the tax credit, the amount of tax credit exceeding the taxpayer's tax liability for the calendar
258 year may be carried forward for the next three calendar years.

259 (7) A 50% reduction in the tax rate is imposed upon the incremental production
260 achieved from an enhanced recovery project.

261 (8) The taxes imposed by this section are:

262 (a) in addition to all other taxes provided by law; and

263 (b) delinquent, unless otherwise deferred, on June 1 next succeeding the calendar year
264 when the oil or gas is:

265 (i) produced; and

266 (ii) (A) saved;

267 (B) sold; or

268 (C) transported from the field.

269 (9) With respect to the tax imposed by this section on each owner of oil or gas or in the
270 proceeds of the production of those substances produced in the state, each owner is liable for
271 the tax in proportion to the owner's interest in the production or in the proceeds of the
272 production.

273 (10) The tax imposed by this section shall be reported and paid by each producer that
274 takes oil or gas in kind pursuant to agreement on behalf of the producer and on behalf of each
275 owner entitled to participate in the oil or gas sold by the producer or transported by the

276 producer from the field where the oil or gas is produced.

277 (11) Each producer shall deduct the tax imposed by this section from the amounts due
278 to other owners for the production or the proceeds of the production.

279 (12) (a) The Tax Review Commission shall review the tax provided for in this part on
280 or before the October 2008 interim meeting.

281 (b) The Tax Review Commission shall address in its review the following statutory
282 provisions:

283 (i) the severance tax rate structure provided for in this section;

284 (ii) the exemptions provided for in Subsection (5);

285 (iii) the tax credit provided for in Subsection (6), including:

286 (A) the cost of the tax credit;

287 (B) the purpose and effectiveness of the tax credit; and

288 (C) whether the tax credit benefits the state;

289 (iv) the tax rate reduction provided for in Subsection (7);

290 (v) other statutory provisions or issues as determined by the Tax Review Commission;

291 and

292 (vi) whether the statutory provisions the Tax Review Commission reviews under this
293 Subsection (12) should be:

294 (A) continued;

295 (B) modified; or

296 (C) repealed.

297 (c) The Tax Review Commission shall report its findings and recommendations
298 regarding the tax provided for in this part to the Revenue and Taxation Interim Committee on
299 or before the November 2008 interim meeting.

300 (d) (i) The Tax Review Commission shall review the applicability of the tax provided
301 for in this chapter to coal-to-liquids, oil shale, and tar sands technology on or before the
302 October 2011 interim meeting.

303 (ii) The Tax Review Commission shall address in its review the cost and benefit of not
304 applying the tax provided for in this chapter to coal-to-liquids, oil shale, and tar sands
305 technology.

306 (iii) The Tax Review Commission shall report its findings and recommendations under

307 Subsections (12)(d)(i) and (ii) to the Revenue and Taxation Interim Committee on or before the
308 November 2011 interim meeting.

309 (13) (a) The commission shall during the 2004 interim:

310 (i) subject to Subsection (13)(b), conduct a study of the effective tax burden for the
311 taxes imposed by this part per barrel of oil or MCF of gas for the time period beginning on
312 January 1, 1984 and ending on September 30, 2004;

313 (ii) study whether the effective tax burden studied under Subsection (13)(a)(i) has
314 increased or decreased;

315 (iii) receive input from the oil and gas industry in conducting the study required by
316 Subsections (13)(a)(i) and (ii);

317 (iv) make findings and recommendations regarding whether any provision of this part
318 should be amended, including:

319 (A) whether any tax rate under this part should be amended;

320 (B) whether a minimum value of oil or gas should be established by statute;

321 (C) whether a limit should be established by statute on the amount of processing costs
322 that may be deducted under Section 59-5-103.1; and

323 (D) whether a limit other than the limit established in Section 59-5-103.1 should be
324 established by statute on the amount of transportation costs that may be deducted under Section
325 59-5-103.1; and

326 (v) report the findings and recommendations required by Subsection (13)(a)(iv) on or
327 before the October 2004 interim meeting to:

328 (A) the Revenue and Taxation Interim Committee; and

329 (B) the Utah Tax Review Commission.

330 (b) In conducting the study required by Subsections (13)(a)(i) and (ii), the commission
331 shall take into account factors including:

332 (i) the production volume of oil and gas;

333 (ii) the sales price of oil and gas; and

334 (iii) the revenues raised by the taxes imposed by this part for the time period described
335 in Subsection (13)(a)(i).

Legislative Review Note
as of 11-16-06 8:53 AM

Office of Legislative Research and General Counsel