SEVERANCE TAX CODE REVISIONS

2011 GENERAL SESSION

STATE OF UTAH

Chief Sponsor: Brian S. King

Senate Sponsor: ____________

LONG TITLE

General Description:

This bill makes changes to oil and gas severance taxes.

Highlighted Provisions:

This bill:

> makes changes to oil and gas severance tax exemptions;

> adjusts oil and gas severance tax rates; and

> makes technical and conforming changes.

Money Appropriated in this Bill:

None

Other Special Clauses:

This bill takes effect on January 1, 2012.

Utah Code Sections Affected:

AMENDS:

59-5-101, as last amended by Laws of Utah 2009, Chapter 344

59-5-102, as last amended by Laws of Utah 2010, Chapter 323

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

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


As used in this part:
(1) "Board" means the Board of Oil, Gas, and Mining created in Section 40-6-4.

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

(3) "Condensate" means those hydrocarbons, regardless of gravity, that occur naturally in the gaseous phase in the reservoir that are separated from the natural gas as liquids through the process of condensation either in the reservoir, in the wellbore, or at the surface in field separators.

(4) "Crude oil" means those hydrocarbons, regardless of gravity, that occur naturally in the liquid phase in the reservoir and are produced and recovered at the wellhead in liquid form.

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

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

(7) "Enhanced recovery project" means:

(a) the injection of liquids or hydrocarbon or nonhydrocarbon gases directly into a reservoir for the purpose of:

(i) augmenting reservoir energy;

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

(iii) changing the reservoir conditions to increase the recoverable oil, gas, or oil and gas through the joint use of two or more well bores; and

(b) a project initially approved by the board as a new or expanded enhanced recovery project on or after January 1, 1996.

(8) (a) "Gas" means:

(i) natural gas;

(ii) natural gas liquids; or

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

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

(9) "Incremental production" means that part of production, certified by the Division of Oil, Gas, and Mining, which is achieved from an enhanced recovery project that would not have economically occurred under the reservoir conditions existing before the project and that has been approved by the division as incremental production.

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

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

(12) (a) "Oil" means:
   (i) crude oil;
   (ii) condensate; or
   (iii) any mixture of crude oil and condensate.
   (b) "Oil" does not include solid hydrocarbons.

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

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

(15) "Operator" means any person engaged in the business of operating an oil or gas well, regardless of whether the person is:
   (a) a working interest owner;
   (b) an independent contractor; or
   (c) acting in a capacity similar to Subsection (15)(a) or (b) as determined by the commission by rule made in accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act.

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

(17) (a) Subject to Subsections (17)(b) and (c), "processing costs" means the reasonable actual costs of processing oil or gas to remove:
   (i) natural gas liquids; or
   (ii) contaminants.
   (b) If processing costs are determined on the basis of an arm's-length contract,
processing costs are the actual costs.

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

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

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

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

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

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

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

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

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

  (b) approved by the division as a recompletion.

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

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

  (22) "Solid hydrocarbons" means:

  (a) coal;

  (b) gilsonite;

  (c) ozocerite;

  (d) elaterite;

  (e) oil shale;

  (f) tar sands; and

  (g) all other hydrocarbon substances that occur naturally in solid form.
(23) "Stripper well" means:
(a) an oil well whose average daily production for the days the well has produced has been [26] 10 barrels or less of crude oil a day during any consecutive 12-month period; or
(b) a gas well whose average daily production for the days the well has produced has been 60 MCF or less of natural gas a day during any consecutive 90-day period.

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

(25) (a) Subject to Subsections (25)(b) and (c), "transportation costs" means the reasonable actual costs of transporting oil or gas products from the well to the point of sale.
(b) If transportation costs are determined on the basis of an arm's-length contract, transportation costs are the actual costs.
(c) (i) If transportation costs are determined on a basis other than an arm's-length contract, transportation costs are those reasonable costs associated with:
(A) actual operating and maintenance expenses, including fuel used or consumed in transporting the oil or gas;
(B) overhead costs directly attributable and allocable to the operation and maintenance;
and
(C) depreciation and a return on undepreciated capital investment.
(ii) Subsection (25)(c)(i) includes situations where the producer performs the transportation for the producer's product.
(d) Regardless of whether transportation costs are determined on the basis of an arm's-length contract or a basis other than an arm's-length contract, transportation costs include:
(i) carbon dioxide removal;
(ii) compression;
(iii) dehydration;
(iv) gathering;
(v) separating;
(vi) treating; or
(vii) a process similar to Subsections (25)(d)(i) through (vi), as determined by the
commission by rule made in accordance with Title 63G, Chapter 3, Utah Administrative
Rulemaking Act.

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

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

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

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

(30) (a) "Workover" means any downhole operation that is:
(i) conducted to sustain, restore, or increase the producibility or serviceability of a well
in the geologic intervals in which the well is currently completed; and
(ii) approved by the division as a workover.

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

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

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

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

(a) produced; and

(b) (i) saved;

(ii) sold; or

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

(2) (a) [Subject to Subsection (2)(d), the] The severance tax rate for oil is [as follows:
(i) 3% of the value of the oil up to and including the first $13 per barrel for oil; and (ii) 5% of
the value of the oil [from $13.01 and above per barrel for oil].

(b) [Subject to Subsection (2)(d), the] The severance tax rate for natural gas is [as
follows: (i) 3% of the value of the natural gas up to and including the first $1.50 per MCF for
gas; and (ii) 5% of the value of the natural gas [from $1.51 and above per MCF for gas].

(c) [Subject to Subsection (2)(d), the] The severance tax rate for natural gas liquids is
[4%] 5% of the value of the natural gas liquids.

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

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

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

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

[(B) decreased as provided in Subsection (2)(d)(iii) if the amount of revenues
estimated under Subsection (2)(d)(i)(B) is greater than the amount of revenues estimated under
Subsection (2)(d)(i)(A);]

[(iii) For purposes of Subsection (2)(d)(ii):]

[(A) subject to Subsection (2)(d)(iv)(B):]

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

[(ii) if a decrease is required under Subsection (2)(d)(ii)(B), the total decrease in the
tax rates shall be by the amount necessary to reduce for the calendar year beginning on January
1, 2005 revenues equal to the amount by which the revenues estimated under Subsection
(2)(d)(i)(B) exceed the revenues estimated under Subsection (2)(d)(i)(A); and]

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

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

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

(3) If oil or gas is shipped outside the state:
(a) the shipment constitutes a sale; and
(b) the oil or gas is subject to the tax imposed by this section.

(4) (a) Except as provided in Subsection (4)(b), if the oil or gas is stockpiled, the tax is
not imposed until the oil or gas is:
(i) sold;
(ii) transported; or
(iii) delivered.
(b) Notwithstanding Subsection (4)(a), if oil or gas is stockpiled for more than two
years, the oil or gas is subject to the tax imposed by this section.

(5) [A] The following are exempt from a tax [is not] imposed under this section
[upon]:

(a) a stripper [well] well, unless:
(i) the exemption prevents the severance tax from being treated as a deduction for
federal tax purposes; or
(ii) (A) for an oil stripper well, the average crude oil price for the prior calendar year as
reported by the United States Department of Energy is greater than or equal to $40 per barrel;
or
(B) for a gas stripper well, the average wellhead price for the prior calendar year as
reported by the United States Department of Energy is greater than or equal to $1.50 per
thousand cubic feet;
(b) the first 12 months of production for wildcat wells started after January 1, 1990; or
(c) the first six months of production for development wells started after January 1,
1990.
(6) (a) Subject to Subsections (6)(b) and (c), a working interest owner who pays for all or part of the expenses of a recompletion or workover may claim a nonrefundable tax credit equal to 20% of the amount paid.

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

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

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

(8) The taxes imposed by this section are:

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

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

(i) produced; and

(ii) (A) saved;

(B) sold; or

(C) transported from the field.

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

(10) The tax imposed by this section shall be reported and paid by each producer that takes oil or gas in kind pursuant to agreement on behalf of the producer and on behalf of each owner entitled to participate in the oil or gas sold by the producer or transported by the producer from the field where the oil or gas is produced.

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

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

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

(c) The Utah Tax Review Commission shall report its findings and recommendations under this Subsection (12) to the Revenue and Taxation Interim Committee on or before the November 2011 interim meeting.

Section 3. Effective date.
This bill takes effect January 1, 2012.

Legislative Review Note
as of 2-2-11 11:31 AM

Office of Legislative Research and General Counsel
FISCAL NOTE

SHORT TITLE: Severance Tax Code Revisions

SPONSOR: King, B.

2011 GENERAL SESSION, STATE OF UTAH

STATE GOVERNMENT (UCA 36-12-13(2)(b))
Enactment of this bill could increase the General Fund by $11,282,000 in FY 2012 and by $26,500,000 in FY 2013.

STATE BUDGET DETAIL TABLE

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LOCAL GOVERNMENTS (UCA 36-12-13(2)(c))
Enactment of this bill likely will not result in direct, measurable costs and/or benefits for local governments.

DIRECT EXPENDITURES BY UTAH RESIDENTS AND BUSINESSES (UCA 36-12-13(2)(d))
Enactment of this bill could increase the net costs to businesses involved in mining exploration and production by $11,282,000 in FY 2012 and by $26,500,000 in FY 2013. Actual impact on businesses will depend on the number of workover wells and total number of wells from which businesses are producing.

Office of the Legislative Fiscal Analyst

Page 1 of 1