OIL AND GAS TAXES

CURRENT LAW

Oil And Gas Gross Production Tax

Imposition and Rates

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

Oil. A 5% rate is applied to the gross value at the well of all oil produced, except royalty interest in oil produced from a state, federal or municipal holding and from an American Indian holding within the boundary of a reservation. Both the producer and purchaser of the oil are required to submit reports to the North Dakota Office of State Tax Commissioner on a monthly basis. The reports show the volume and taxable value of sales of the production from each well. The producer remits the tax on oil not sold at the well. The purchaser is primarily responsible for remitting the tax on oil bought during a production month. The Tax Commissioner has the authority to waive a producer's filing requirement if certain conditions are met. Purchasers are required to file monthly reports electronically.

Gas. The gross production tax on gas is an annually adjusted flat rate per mcf of all nonexempt gas produced in the state. The annual adjustments are made according to the average producer price index for gas fuels. Rates through June 30, 2003 are as follows:

Time Period	Tax Rate
July 1, 2000 - June 30, 2001	$.0452
July 1, 2001 - June 30, 2002	$.0772
July 1, 2002 - June 30, 2003	$.0824

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

Monthly reports to the North Dakota Office of State Tax Commissioner are required from both the producer and the purchaser/processor of the gas. The producer remits the tax on unprocessed gas and the purchaser/processor remits the tax on processed gas. The Tax Commissioner has the authority to waive a producer's filing requirement if certain conditions are met. Purchasers/processors are required to file monthly reports electronically.

Distribution of Revenue

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

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

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

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

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

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

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

Oil Extraction Tax

Imposition and Rates

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

- A vertical or horizontal new well, after the appropriate exemption expires.
- A workover well after the exemption expires.
- Incremental oil from a qualifying secondary or tertiary recovery project, after the 5-year or 10-year exemption expires.
- Nonincremental oil from a qualifying secondary recovery project that has reached an average production level of at least 25% over normal operations for six consecutive months.
- Nonincremental oil from a qualifying tertiary recovery project that has reached a production level of at least 15% over normal operations for one month and continues to be operated as a qualifying project.

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

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

Exemptions

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

The exemptions to the oil extraction tax are as follows:

- Royalty interest in oil extracted from a state, federal or municipal holding and from an American Indian holding within the boundary of a reservation.
- Oil extracted from a certified stripper well property. A stripper well property is property whose average daily production during a 12-month period did not exceed 10 barrels per day for a well of a depth of 6,000 feet or less, 15 barrels per day for a well of a depth of more than 6,000 feet but not more than 10,000 feet, and 30 barrels per day for a well of a depth of more than 10,000 feet.
- Oil produced during the first 15 months of production from a vertical new well. This exemption is subject to the "trigger" provisions described below.
- Oil produced during the first 24 months of production from a horizontal new well. The exemption is subject to the "trigger" provisions described below.
- Oil produced during the first 60 months of production from either a vertical new well or a horizontal new well drilled and completed on tribal trust land.
- Oil produced from a horizontal reentry well for a period of 9 months beginning on the date the well is recompleted as a horizontal well. The exemption is subject to the "trigger provisions" described below.
- Oil produced from a two-year inactive well for a period of ten years beginning the first day of the month in which the Industrial Commission's certification is received by the Tax Commissioner. The exemption is subject to the "trigger provisions" described below.
- Oil produced from a qualifying well that has been worked over. The exemption is for a 12-month period starting with the first day of the third month after completion of the workover project. A qualifying well is a well that has produced less than 50 barrels per day during the last six months of continuous production before workover. The well operator must notify the Industrial Commission before beginning the project. Project cost must exceed $65,000 or production must increase 50% or more in the first two months after project completion. The exemption is subject to the "trigger" provisions described below.
- Incremental oil from a qualifying secondary or tertiary recovery project. The exemption is 5 years for secondary recovery projects and 10 years for tertiary recovery projects from the date the incremental production begins.

"Trigger" Provisions

The reduced rate provisions and exemptions for new wells, horizontal wells, horizontal reentry wells, two-year inactive wells, workover wells, and enhanced recovery wells are ineffective if the average price of a barrel of crude oil exceeds the trigger price (thirty-five dollars and fifty cents, as indexed for inflation) for each month in any consecutive five-month period. The reduced rates and exemptions are reinstated if the average price falls below the trigger price for each month in any consecutive five-month period.

Distribution of Revenue

Revenue from the oil extraction tax is distributed as follows:

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

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

HISTORICAL OVERVIEW

Oil And Gas Gross Production Tax

Significant Changes In Law

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

1957 Session. The rate was increased from 4¼% to 5% and the revenue distribution formula was adjusted (see chart on page 51).

1981 Session. The legislature amended the revenue distribution formula (see chart on page 51).

1983 Session. The legislature required monthly rather than quarterly remittance, and raised the maximum distributions to the counties (see chart on page 51).

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

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

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

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

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

1999 Session. The legislature changed the manner in which unallocated oil and gas gross production taxes collected from unidentified sources is distributed. Previously, the unallocated taxes were distributed to the county with the lowest total gross production tax distribution for the fiscal year. After June 30, 1999, the unallocated taxes will be distributed to each county in the same proportion as total gross production tax allocations for the fiscal year.

Oil Extraction Tax

Significant Changes in Law

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

1981 Session. The legislature amended the distribution formula (see chart on page 51).

1983 Session. The distribution formula was changed (see chart on page 51). Filing requirements were changed from a quarterly to a monthly basis.

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

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

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

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

1995 Session. The stripper well definition was broadened from 20 to 30 barrels per day for wells over 10,000 feet deep. The exemption for a horizontal new well was increased from 15 to 24 months and a 9-month exemption was created for a horizontal reentry well. A 10-year exemption was created for oil from a two-year inactive well. To get the full benefit of an exemption or the 4% reduced rate, producers were given an 18-month period to file the Industrial Commission’s certification of well status with the North Dakota Office of State Tax Commissioner. For secondary recovery projects, the sunset for certification was removed. The revenue distribution formula was changed (see chart on page 51).

1997 Session. A 60-month exemption was created for production from a well drilled and completed on an Indian reservation or on tribal trust land after July 31, 1997. Previous legislation was amended to keep the current distribution factors at the current percentages (see chart on page 51).

2001 Session. The "trigger" provision for exemptions and rate reductions was amended to clarify when the trigger was to be become effective. All rate reductions and exemptions subject to the trigger provision become ineffective if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period. The reduced rates and exemptions are reinstated if the average price falls below the trigger price for each month in any consecutive five-month period. Average price is defined as the monthly average of the daily closing price for a barrel of west Texas intermediate Cushing crude oil minus two dollars and fifty cents. Trigger price is defined as thirty-five dollars and fifty cents, as indexed for inflation.

Oil and Gas Taxes Distribution Formula Changes

Gross Production Tax

		State		Counties					Maximum County Amount		
	Increments	General Fund	Oil & Gas Impact Grant Fund	Total County %	Cities	School Districts	Road and Bridge Fund	General Fund	County Population Under 3,000	3,000 to 6,000	Over 6,000
1957 Session	First 1/5:	100%									
	Remaining 4/5:										
	1st $200,000	25%		75%							
	2nd $200,000	50%		50%	15%	45%	40%				
	3rd $400,000	75%		25%							
1981 Session	First 1/5:	100% [1]									
	Remaining 4/5:									FY-1982	
	1st $ Million	25%		75%					$3.2 M	$3.5 M	$4.0 M
	2nd $ Million	50%		50%	20%	35%		45%		FY-1983	
	Over $2 Million	75%		25%					$3.8 M	$4.0 M	$4.5 M
1983 Session									$3.9 M	$4.1 M	$4.6 M
1989 Session	First 1/5:	66 2/3%	33 1/3% [2] [3]								

[1] For the 1981-83 biennium only, the legislature provided that up to $32 million of the 1/5 State General Fund share be distributed to the Highway Tax Distribution Fund and to township road and bridge funds.

[2] Up to a maximum of $5 million per biennium. The remainder is deposited in the State General Fund.

[3] Total oil collections to the State general fund are capped at $62 million per biennium. All revenue in excess of $62 million is transferred at the end of each biennium to the Permanent Oil Trust Fund.

Oil Extraction Tax

	State General Fund	Education Funds	Water Pipeline & Trust Fund
1980 Measure #6	45%	45%	10%
1981 Session	30%	60%	10%
1983 Session	90%	10%	
1995 Session:			
FY 1996 and 1997	60%	20%	20%
After FY 1997	70%	20%	10%
1997 Session:			
After FY 1997	60% [3]	20%	20%