

CHAPTER 958

H.B. No. 2723

AN ACT

relating to tax and regulatory relief as incentives for the production of certain gas that is difficult or expensive to produce and relating to a reduced oil production tax rate for oil from certain enhanced recovery projects.

Be it enacted by the Legislature of the State of Texas:

SECTION 1. Section 201.057, Tax Code, is amended to read as follows:

Sec. 201.057. TEMPORARY EXEMPTION OF CERTAIN HIGH-COST GAS. (a) In this section:

(1) "Commission" means the Railroad Commission of Texas.

(2) "High-cost gas" means:

(A) high-cost natural gas as described by Section 107, Natural Gas Policy Act of 1978 (15 U.S.C. Section 3317), as that section exists on January 1, 1989, without regard to whether that section is in effect or whether a determination has been made that the gas is high-cost natural gas for purposes of that Act; or

(B) all gas produced from oil wells or gas wells within a commission approved co-production project.

(3) "Commission approved co-production project" means a reservoir development project in which the commission has recognized that water withdrawals from an oil or gas reservoir in excess of specified minimum volumes will result in recovery of additional oil and/or gas from the reservoir that would not be produced by conventional production methods and where operators of wells completed in the reservoir have begun to implement commission requirements to withdraw such volumes of water and dispose of such water outside the subject reservoir. Reservoirs potentially eligible for this designation shall be limited to those reservoirs in which oil and/or gas has been bypassed by water encroachment caused by production from the reservoir and such bypassed oil and/or gas may be produced as a result of reservoir-wide high-volume water withdrawals of natural formation water.

(4) "High-volume water withdrawals" means the withdrawal of water from a reservoir in an amount sufficient to dewater portions of the reservoir containing oil and/or gas previously bypassed by water encroachment.

(5) "Co-production" means the permanent removal of water from an oil and/or gas reservoir in an effort to lower the gas-water contact or oil-water contact in the reservoir or to reduce reservoir pressure to recover entrained hydrocarbons from the reservoir that would not be produced by conventional primary or secondary production methods.

(6) "Operator" means the person responsible for the actual physical operation of an oil or [a] gas well.

(b) High-cost gas as defined in Subsection (a)(2)(A) of this section produced from a well that is spudded or completed between May 24, 1989, [~~the date of enactment~~] and September 1, 1996, is exempt from the tax imposed by this chapter during the period beginning September 1, 1991, and ending August 31, 2001. High-cost gas as defined in Subsection (a)(2)(B) of this section produced from any well regardless of spud date or completion date is eligible for refunds of tax paid and exemption from the tax imposed by this chapter for production occurring during the period beginning the first day of the month after commission approval of a co-production project and ending August 31, 2001; provided, however, in the event co-production ceases, the exemption shall also cease on the first day of the first calendar month that begins on or after the 91st day following the date of termination of co-

production operations. Tax must be paid when due at the rate provided in Section 201.052 of this code for all high-cost gas, as defined in Subsection (a)(2)(B) of this section, produced on or before July 31, 1995. On or after September 1, 1995, the operator may apply to the comptroller for a refund and shall be entitled to receive a refund of all taxes paid on such high-cost gas produced on or after the first day of the calendar month after commission approval of the co-production project from which such gas was produced and that is otherwise eligible for the tax exemption.

(c) *The operator of a proposed or existing gas well, including a gas well that has not been completed, or the operator of any proposed or existing oil or gas well within a commission approved co-production project, may apply to the commission for certification that the well produces or will produce high-cost gas. The application may be made but is not required to be made concurrently with a request for a determination that gas produced from the well is high-cost natural gas for purposes of the Natural Gas Policy Act of 1978 (15 U.S.C. Section 3301 et seq.) or with a request for commission approval of a co-production project. The commission may require an applicant to provide the commission with any relevant information required to administer this section. For purposes of this section, a determination that gas is high-cost natural gas for purposes of the Natural Gas Policy Act of 1978 made according to the definition of high-cost natural gas provided by Section 107, Natural Gas Policy Act of 1978 (15 U.S.C. Section 3317), as that section exists on January 1, 1989, or a determination that gas is produced from within a commission approved co-production project is a certification that the gas is high-cost gas for purposes of this section, and in that event additional certification is not required to qualify for the exemption provided by this section.*

(d) *To qualify for the exemption provided by this section, the person responsible for paying the tax must apply to the comptroller. The application must contain the certification of the commission that the well produces high-cost gas. An application may not be filed before January 1, 1990, or after December 31, 1998. The comptroller shall approve the application of a person who demonstrates that the gas is eligible for the exemption. The comptroller may require a person applying for the exemption to provide any relevant information in the person's monthly report that the comptroller considers necessary to administer this section. The commission shall notify the comptroller in writing immediately if it determines that an oil or [a] gas well previously certified as producing high-cost gas does not produce high-cost gas or if it takes any action or discovers any information that affects the eligibility of gas for an exemption under this section.*

(e) *If, before the commission certifies that a well produces high-cost gas or before the comptroller approves an application for an exemption under this section, the tax imposed by this chapter is paid on high-cost gas that otherwise qualifies for the exemption provided by this section, the producer or producers of the gas are entitled to a credit against other taxes imposed by this chapter in an amount equal to the amount of the tax paid on the gas that otherwise qualified for the exemption on or after the first day of the next month after the month in which the application for certification under this section was filed with the commission. The credit is allocated to each producer according to the producer's proportionate share in the gas. To receive a credit, one or more of the producers must apply to the comptroller for the credit not later than the first anniversary after the date the comptroller approves the application for an exemption under this section. If a producer demonstrates that the producer does not have sufficient tax liability under this chapter to claim the credit within five years from the date the application for the credit is made, the producer is entitled to a refund in the amount of any credit the comptroller determines may not be claimed within that five years. Nothing in this subsection shall relieve the obligation imposed by Subsection (b) to pay tax when due on high-cost gas produced from co-production projects on or before July 31, 1995.*

(f) *An applicant for commission approval of a co-production project shall submit a written application for approval to the commission. Such application must be filed before January 1, 1994. The applicant shall provide the commission with any relevant information required to administer this section, including evidence demonstrating that the reservoir is eligible for the designation and demonstrating the minimum volumes of high-volume water withdrawal required to recover oil and/or gas from the reservoir that would not be produced by conventional production methods. A commission representative may adminis-*

tratively approve the application. If the commission representative denies administrative approval, the applicant shall have the right to a hearing upon request.

SECTION 2. Section 202.054, Tax Code, is amended to read as follows:

Sec. 202.054. QUALIFICATION OF OIL FROM NEW OR EXPANDED ENHANCED RECOVERY PROJECT FOR SPECIAL TAX RATE. (a) In this section:

(1) "Active operation" means the start and continuation of a fluid injection program for a secondary or tertiary recovery project to enhance the displacement process in the reservoir.

(2) "Commission" means the Railroad Commission of Texas.

(3) "Enhanced recovery project" means the use of any process for the displacement of oil from the earth other than primary recovery and includes the use of an immiscible, miscible, chemical, thermal, or biological process *and any co-production project.*

(4) "Existing enhanced recovery project" means an enhanced recovery project that began active operations before September 1, 1989.

(5) "Expanded enhanced recovery project" or "expansion" means the addition of injection and producing wells, the change of injection pattern, or other operating changes to an existing enhanced oil recovery project that will result in the recovery of oil that would not otherwise be recovered.

(6) "Incremental production" means the volume of oil produced by an expanded enhanced recovery project in excess of the production decline rate established under conditions before expansion for an existing enhanced recovery project.

(7) "Operator" means the person responsible for the actual physical operation of an enhanced recovery project.

(8) "Positive production response" means that the rate of oil production from the wells affected by an enhanced recovery project is greater than the rate that would have occurred without the project.

(9) "Primary recovery" means the displacement of oil from the earth into the well bore by means of the natural pressure of the oil reservoir, including artificial lift.

(10) "Production decline rate" means the projected future oil production from a project area as extrapolated by a method approved by the commission.

(11) "Recovered oil tax rate" means the tax rate provided by Section 202.052(b) of this code.

(12) "Secondary recovery project" means an enhanced recovery project that is not a tertiary recovery project.

(13) "Tertiary recovery project" means an enhanced recovery project using a tertiary recovery method listed in the federal June 1979 energy regulations referred to in Section 4993, Internal Revenue Code of 1986, or approved by the United States secretary of the treasury for purposes of administering Section 4993, Internal Revenue Code of 1986, without regard to whether that section remains in effect.

(14) "*Co-production project*" means an enhanced recovery project in which water is permanently removed from an oil and/or gas reservoir in an effort to lower the gas-water or oil-water contact in the reservoir or to reduce reservoir pressure to recover entrained hydrocarbons from the reservoir that would not be produced by conventional primary or secondary production methods.

(15) "*Commission approved co-production project*" means a reservoir development project in which the commission has recognized that water withdrawals from an oil or gas reservoir in excess of specified minimum volumes will result in recovery of additional oil and/or gas from the reservoir that would not be produced by conventional production methods and where operators in the field have begun to implement commission requirements to withdraw such volumes of water and dispose of such water outside the subject reservoir. Reservoirs potentially eligible for this designation shall be limited to those reservoirs in which oil and/or gas has been bypassed by water encroachment caused by production from the reservoir and such bypassed oil and/or gas may be produced as a result of fieldwide high-volume water withdrawals of natural formation water.

(16) "High-volume water withdrawals" means the withdrawal of water from a reservoir in an amount sufficient to dewater portions of the reservoir containing oil and/or gas previously bypassed by water encroachment.

(b) Oil produced from an enhanced recovery project other than a co-production project qualifies for the recovered oil tax rate if, before the project begins active operation, the commission approves the project and designates the area to be affected by the project. The incremental production from an expanded enhanced recovery project other than a co-production project qualifies for the recovered oil tax rate if, before the expansion begins, the commission approves the expansion and designates the area to be affected by the expansion. Oil produced from a commission approved co-production project, whether a new enhanced recovery project or an expanded enhanced recovery project, qualifies for the recovered oil tax rate following commission certification of a positive production response without regard to whether the commission approval is before or after the project began active operations; provided, however, tax must be paid when due at the rate provided in Section 202.052(a) of this code for all oil produced on or before July 31, 1995. On or after September 1, 1995, the operator may apply to the comptroller for a refund and shall be entitled to receive a refund equal to the difference between the tax paid on all oil produced from a commission approved co-production project after commission certification of a positive production response and the tax due at the recovered oil tax rate for all oil produced after commission certification of a positive production response from such co-production project. The operator of a proposed project, [or] a proposed expansion, or a proposed or existing co-production project may apply to the commission for approval of the project or expansion under this section. The commission may require an applicant to provide the commission with any relevant information required to administer this section. If approval by the commission of a unitization agreement under Subchapter B, Chapter 101, Natural Resources Code, is required for purposes of carrying out the project or expansion, the commission may not approve the project or expansion unless it approves the unitization agreement. A person may apply for approval of a proposed enhanced recovery project, [or] a proposed expansion, or a proposed co-production project under this subsection concurrently with an application for approval of a unitization agreement for purposes of carrying out the enhanced recovery project or expansion under Section 101.011, Natural Resources Code, or with an application for certification of the project or expansion as a tertiary recovery project for purposes of Section 4993, Internal Revenue Code of 1986, or may make a separate application for approval.

(c) This section applies to an enhanced recovery project that begins active operation on or after September 1, 1989, and to an expansion that the commission approves on or after September 1, 1991. An application for approval under this section must be filed on or after September 1, 1989, and before January 1, 1994, for a new enhanced recovery project, including any co-production project. An application for approval under this section must be filed on or after September 1, 1991, and before January 1, 1994, for an expansion of an existing enhanced recovery project. A project may not qualify as an expansion if the project has qualified as a new enhanced recovery project under this section. An application may be filed on or after September 1, 1989, even if a separate application for approval of the project or expansion has already been filed under Subchapter B, Chapter 101, Natural Resources Code, or for approval as a tertiary recovery project for purposes of Section 4993, Internal Revenue Code of 1986, if the operation of a new project or the expansion of an existing project, other than a co-production project, does not begin before the application for approval under this section is approved by the commission; provided, however, nothing herein shall require commission approval of a co-production project prior to commencing active operations on such project in order for such project to be eligible for the recovered oil tax rate.

(d) An applicant for commission approval of a co-production project shall submit a written application for approval to the commission. Such application must be filed before January 1, 1994. The applicant shall provide the commission with any relevant information required to administer this section, including evidence demonstrating that the reservoir is eligible for the designation and demonstrating the minimum volumes of high-volume water withdrawal required to recover oil and/or gas from the reservoir that would not be produced by conventional production methods. A commission representative may administratively approve the application. If the commission representative denies administrative approval, the applicant shall have the right to a hearing upon request.

(e) If the commission approves an enhanced recovery project or an expansion under this section, it shall issue a certification of approval for an approved project designating the area to be affected by the project.

(f) ~~[(e)]~~ The recovered oil tax rate applies only to oil produced from a new enhanced oil recovery project, *any co-production project*, or the incremental production caused by the expansion of an existing enhanced recovery project from the area the commission certifies to be affected by the project.

(g) *Subject to the provisions of Subsections (b) and* ~~[(f) Except as provided by Subsection]~~ (h) of this section, the recovered oil tax rate applies to oil on which a tax is imposed by this chapter for the 10 years beginning the first day of the month following the date the commission certifies that, in the case of an enhanced recovery project *including a co-production project*, a positive production response has occurred or, in the case of an expansion, *other than related to a co-production project*, incremental production has occurred, if the application for certification is filed:

(1) not later than three years from the date the commission approves the project if the project is designated as a new or existing project *other than a co-production project* that uses a secondary recovery process; or

(2) not later than five years from the date the commission approves the project if the project is designated as a new or existing project that uses a tertiary recovery process *or is a co-production project*.

(h) ~~[(g)]~~ The operator may designate the certification date, subject to commission approval. If the commission determines that the project has caused a positive production response or incremental production, the commission shall certify that fact.

(i) ~~[(h)]~~ Notwithstanding Subsection (g) ~~[(f)]~~ of this section, qualification for the recovered oil tax rate ends on the first day of the first calendar month that begins on or after the 91st day following the date of termination of the active operation of the enhanced recovery project or of termination of an approved expansion.

(j) ~~[(i)]~~ If the active operation of an approved enhanced recovery project or expansion is terminated, the person who immediately before the termination is the operator of the project shall notify the commission and the comptroller in writing not later than the 30th day after the last day of active operation. Any person who violates this subsection is liable to the state for a civil penalty if the person pays or attempts to pay the tax imposed by this chapter on oil from the project at the recovered oil tax rate after qualification for that rate ends under Subsection (g) ~~[(f)]~~ or (i) ~~[(h)]~~ of this section. The amount of the penalty may not exceed the sum of:

(1) \$10,000; and

(2) the difference between the amount of taxes paid or attempted to be paid and the amount of taxes due.

(k) ~~[(j)]~~ The attorney general may recover a penalty under Subsection (j) ~~[(i)]~~ of this section in a suit brought on behalf of the state. Venue for the suit is in Travis County.

(l) ~~[(k)]~~ The commission has broad discretion in administering this section and shall adopt and enforce any appropriate rules or orders that the commission finds necessary to administer this section concerning the designation, operation, and termination of enhanced recovery projects and expansions. The commission shall notify the comptroller of any action taken under this subsection. The comptroller shall have the power to establish procedures in order to comply with this Act.

(m) *Subject to the provisions of Subsection (b) of this section, if* ~~[(l) If]~~, before the comptroller approves an application for taxation at the recovered oil tax rate, the tax imposed by this chapter is paid at the rate provided by Section 202.052(a) of this code on oil that qualifies under this section for the recovered oil tax rate, the producer or producers of the oil are entitled to a credit against taxes imposed by this chapter in an amount equal to the difference between the tax paid on the oil and the tax due on the oil at the recovered oil tax rate. The credit is allocated to each producer according to the producer's proportionate share in the oil. To receive a credit, one or more of the producers of the oil must apply to the

comptroller for the credit not later than the first anniversary after the date the commission certifies that a positive production response has occurred.

(n) [~~m~~] To qualify for the taxation of oil at the recovered oil tax rate, a person responsible for paying the tax must apply to the comptroller. The application must include the certification of the commission that the project or expansion has been approved and that the project has resulted in a positive production response or that the expansion has resulted in incremental production. The comptroller shall approve the application of a person who demonstrates that the oil is eligible for taxation at the recovered oil tax rate. The comptroller may require a person applying for the recovered oil tax rate to provide any relevant information in the person's monthly report and internal records that the comptroller considers necessary to administer this section. The commission shall notify the comptroller in writing immediately if it determines that active operation of an approved enhanced recovery project or an approved expansion has been terminated or if it takes any action or discovers any information that affects the taxation of oil at the recovered oil tax rate.

SECTION 3. This Act takes effect September 1, 1993.

SECTION 4. The importance of this legislation and the crowded condition of the calendars in both houses create an emergency and an imperative public necessity that the constitutional rule requiring bills to be read on three several days in each house be suspended, and this rule is hereby suspended.

Passed by the House on May 14, 1993, by a non-record vote; passed by the Senate on May 22, 1993, by a viva-voce vote.

Approved June 19, 1993.

Effective Sept. 1, 1993.