Oil and Gas Production Flaring

This act creates tax incentives to encourage the collection and use of natural gas that would otherwise be flared. The act:

- Expands a sales tax exemption to include tangible personal property used to construct or expand gas collection systems.
- Creates a gross production tax exemption for certain gas collected and used at the well site.
- Creates an oil extraction tax exemption for the liquids produced in association with a collection system.

North Dakota Industrial Commission Department of Mineral Resources, Oil and Gas Division (NDIC) rules allow for the flaring of natural gas for a period of one year from the date of first production. After the one-year period, the NDIC requires flaring to cease and the producer must begin to pay royalties to royalty owners for the value of any flared gas. Producers are also required to pay gross production tax on the flared gas.

When the one-year period for flaring expires, the producer must cap the well or connect it to a gas gathering line, unless the NDIC approves an exemption. A temporary exemption from the gross production tax is available for a period of two years and 30 days from the time of first production. This applies to oil and gas wells employing a collection system to avoid flaring if the well is:

- Equipped with an electrical generator that consumes at least 75% of the gas from the well; or
- Equipped with a system that intakes at least 75% of the gas and gas liquids from the well for beneficial consumption by means of compression to liquid for use as fuel, transport to a processing facility, production of petrochemicals or fertilizer, conversion to liquid fuels, or separating and collecting in excess of 50% of the propane and heavier hydrocarbons; or
- Equipped with other value-added processes as approved by the NDIC, which reduce the volume or intensity of the flare by more than 60%.

Liquids produced from a qualifying collection system utilizing absorption, adsorption, or refrigeration are exempt from oil extraction tax for a period of two years and thirty days from the time of first production. Upon application to, and approval by, the NDIC for qualification of a collection system, the Tax Commissioner's Office will issue a notice informing the producer that a well has qualified for the applicable exemption and provide the required reporting procedures. Sales and use tax exemptions are available for material used in the construction or expansion of a facility to compress, process, gather, collect, or refine gas.

Submitted as:
North Dakota
HB 1134
Status: Signed into law on June 18, 2013.

Suggested State Legislation

(Title, enacting clause, etc.)

Section 1. [*Short Title*] An Act relating to changes to gross production tax and oil extraction tax.

Section 2. [*Flaring of gas restricted - Imposition of tax - Payment of royalties – Industrial commission authority*.]

(1) As permitted under rules of the industrial commission, gas produced with crude oil from an oil well may be flared during a one-year period from the date of first production from the well.

(2) After the time period in subsection 1, flaring of gas from the well must cease and the well must:

(a) Capped;

(b) Connected to a gas gathering line;

(c) Equipped with an electrical generator that consumes at least seventy - five percent of the gas from the well;

(d) Equipped with a system that intakes at least seventy-five percent of the gas and natural gas liquids volume from the well for beneficial consumption by means of compression to liquid for use as fuel, transport to a processing facility, production of petrochemicals or fertilizer, conversion to liquid fuels, separating and collecting over fifty percent of the propane and heavier hydrocarbons; or

(e) Equipped with other value-added processes as approved by the industrial commission which reduce the volume or intensity of the flare by more than sixty percent.

(3) An electrical generator and its attachment units to produce electricity from gas and a collection system described in subdivision (d) of subsection 2 must be considered to be personal property for all purposes.

(4) For a well operated in violation of this section, the producer shall pay royalties to royalty owners upon the value of the flared gas and shall also pay gross production tax on the flared gas at the rate imposed under [insert citation].

(5) The industrial commission may enforce this section and, for each well operator found to be in violation of this section, may determine the value of flared gas for purposes of payment of royalties under this section and its determination is final.

(6) A producer may obtain an exemption from this section from the industrial commission upon application that shows to the satisfaction of the industrial commission that connection of the well to a natural gas gathering line is economically infeasible at the time of the application or in the foreseeable future or that a market for the gas is not available and that equipping the well with an electrical generator to produce electricity from gas or employing a collection system described in subdivision (d) of subsection 2 is economically infeasible.

Section 3. [*Sales and use tax exemption for materials used in compressing, processing, gathering, collecting, or refining of gas.*]

(1) Gross receipts from sales of tangible personal property used to construct or expand a system used to compress, process, gather, collect, or refine gas recovered from an oil or gas well in this state or used to expand or build a gas processing facility in this state are exempt from taxes under this chapter. To be exempt, the tangible personal property must be incorporated

into a system used to compress, process, gather, collect, or refine gas. Tangible personal property used to replace an existing system to compress, process, gather, collect, or refine gas does not qualify for exemption under this section unless the replacement creates an expansion of the system.

(2) To receive the exemption under this section at the time of purchase, the owner of the gas compressing, processing, gathering, collecting, or refining system must receive from the tax commissioner a certificate that the tangible personal property used to construct or expand a system used to compress, process, gather, collect, or refine gas recovered from an oil or gas well in this state or used to expand or build a gas processing facility in this state which the owner intends to purchase qualifies for exemption. If a certificate is not received before the purchase, the owner shall pay the applicable tax imposed by this chapter and apply to the tax commissioner for a refund.

(3) If the tangible personal property is purchased or installed by a contractor subject to the tax imposed by this chapter, the owner of the gas compressing, processing, gathering, collecting, or refining system may apply to the tax commissioner for a refund of the difference between the amount remitted by the contractor and the exemption imposed or allowed by this section. Application for a refund must be made at the times and in the manner directed by the tax commissioner and must include sufficient information to permit the tax commissioner to verify the sales and use taxes paid and the exempt status of the sale or use.

(4) For purposes of this section, a gas collecting system means a collection system described in subdivision (d) of subsection 2 of [Section 2].

Section 4. [*Temporary exemption for oil and gas wells employing a system to avoid flaring.*] Gas is exempt from the tax under [insert citation] for a period of two years and thirty days from the time of first production if the gas is:

(1) Collected and used at the well site to power an electrical generator that consumes at least seventy - five percent of the gas from the well; or

(2) Collected at the well site by a system that intakes at least seventy - five percent of the gas and natural gas liquids volume from the well for beneficial consumption by means of compression to liquid for use as fuel, transport to a processing facility, production of petrochemicals or fertilizer, conversion to liquid fuels, separating and collecting over fifty percent of the propane and heavier hydrocarbons, or other value-added processes as approved by the industrial commission.

Section 5. [*Temporary exemption for oil and gas wells employing a system to avoid flaring.*] Liquids produced from a collection system described in subdivision (d) of subsection 2 of [Section 2] utilizing absorption, adsorption, or refrigeration are exempt from the tax under [insert citation] for a period of two years and thirty days from the time of first production.

Section 6. [*Severability*.] Insert severability clause.

Section 7. [*Repealer*.] Insert repealer clause.

Section 8. [*Effective Date.*] Insert effective date.