Approved: Feb. 21, 1996
Date

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION.

The meeting was called to order by Chairperson Audrey Langworthy at 11:00 a.m. on February 14, 1996 in Room 519--S of the Capitol.

Members present: Senator Langworthy, Senator Corbin, Senator Martin, Senator Bond, Senator Clark, Senator Feleciano, Jr., Senator Hardenburger, Senator Lee, Senator Ranson, Senator Sallee and Senator Wisdom.

Committee staff present: Tom Severn, Legislative Research Department
Chris Courtwright, Legislative Research Department
Don Hayward, Revisor of Statutes
Elizabeth Carlson, Secretary to the Committee

Conferees appearing before the committee: Don Schnacke, KIOGA
David Bleakley, EKOGA
Bill Fuller, Kansas Farm Bureau
Tom Day, Kansas Corporation Commission

Others attending: See attached list

SUBCOMMITTEE MEETING DATES ANNOUNCED

Senator Langworthy reminded the committee of the subcommittee meetings to be held:

> The Subcommittee on **HB 2114--CONCERNING SALES TAX EXEMPTION CERTIFICATES** will meet Thursday,February 15, at 11:00 a.m in Room 519-S. The subcommittee is composed of Senator Hardenburger, Chair, and members Senator Ranson and Senator Martin.
>
> The Subcommittee on **SB 448--TAXATION OF FINANCIAL INSTITUTIONS** will meet Monday, February 19, at 11:00 a.m. in Room 519-S. The subcommittee is composed of Senator Bond, Chair, and members Senator Langworthy and Senator Martin
>
> The Subcommittee on **SB 455--PROCEDURES AND PRACTICES OF THE BOARD OF TAX APPEALS** will meet Tuesday, February 20, at 11:00 a.m. in Room 519-S. The subcommittee is composed of Senator Corbin, Chair, and members Senator Langworthy and Senator Martin

SB 566--OIL AND GAS; TAX CREDIT FOR PLUGGING CERTAIN ABANDONED WELLS

PROPONENTS

Don Schnacke, Executive Vice President of the Kansas Independent Oil and Gas Association, appeared in support of **HB 566** (Attachment 1) He gave some background information regarding what prompted this legislation. He said it came from Proposal No. 27 from the 1995 interim Special Committee on Energy and Natural Resources. The report from the interim committee does not include some 91,000 plus oil and gas well that have been abandoned and not plugged. The KCC staff testified there may be up to 14,000 of these wells that pose a threat to the environment and they are now preparing a list of sites that need action. **SB 566** is part of a solution to an apparent large liability facing the State of Kansas. This bill states that any taxpayer who plugs a well that was drilled prior to 1970 would receive a 50 percent state income tax credit. **SB 566** would also require the KCC to waive the agency's plugging fee of $35 on wells that would be voluntarily plugged and qualify for the tax credit. Mr. Schnacke listed 5 reasons for passing this legislation. He said **SB 566** is a package deal of many subjects which were discussed in the interim committee. He recommended passage of the bill.

Senator Langworthy asked Shirley Sicilian, Research and Analysis, Department of Revenue, to pass to the committee the explanation of how the Department of Revenue arrived at the amount of $226,111 loss of revenue in 1997. (Attachment 2)

There were questions from the committee about how many people would take advantage of this bill if it was passed. Mr. Schnacke said Bill Fuller who is testifying later before the committee might have some information on a better number since they had worked with farmers in plugging water wells and heard their concerns about oil and gas wells. Mr. Schnacke said he thought there needs to be a lot more money put into the Kansas Corporation Commission Conservation Division to assist in this plugging program. Senator Martin asked if the program was looking at approximately 200 wells per year rather than the entire 91,000 plus wells. Mr. Schnacke said when the KCC comes up with their list of 14,000 wells, the emphasis would be on the priorities of which wells need to be plugged first.

Senator Bond asked what the law is today regarding plugging. Mr. Schnacke said some of these wells started as early as 1880 when there were no regulations in Kansas. The procedures back in the early days were not good so there was a lot of leakage of the pipes. The wells could be drilled with no worry about contamination of water and then just left abandoned. The majority of these wells are in southeast Kansas and he thought they would find 90 to 95 percent of the these abandoned wells located there. He said this is not a western Kansas problem. In 1935, the first regulations were applied in Kansas. Presently if a well is drilled and if it is a dry hole, it must be plugged before the rig is removed. He said if a landowner becomes the owner of this property, the landowner is the responsible party. A lot of people don't have the money to plug the wells. After 1970, which is the date used in **SB 566**, there should be a responsible party. This is an incentive bill for farmers and owners, rather than operators. Some wells are just a nuisance to a farmer. The farmer may want to plow the field and he cannot because of the wells or the pipes. The wells are plugged with cement so there will be no contamination. Mr. Schnacke said the list of wells from the KCC is necessary so it is known which of the wells have the first priority to be plugged.

Senator Sallee said there is a potential problem of water pollution. Most of the abandoned well sites are all right but they need to be plugged so a problem cannot occur.

Senator Lee asked what it is going to cost the state? She said the Department of Revenue uses the figure of 68,250 wells with a long range fiscal impact of $155 to $180 million or $12 to $17 million per year. That is much different than the figures of 200 abandoned wells and the fiscal impact of $500,00 per year which Mr. Schnacke used. Mr. Schnacke said he did not know how they came up with that figure. Senator Lee asked if a cap was placed on the fiscal impact per year of $500,000, would that be acceptable? Mr. Schnacke said he was amenable to that because he thought the program should be started as soon as possible. Also, he said, the period of time could be cut from the 10 years used in **SB 566** to 2 or 3 years if that is what the Legislature would want.

David Bleakley, President, Eastern Kansas Oil and Gas Association, said his association supports **SB 566** and feels this tax incentive would create benefits to the state, the taxpayers, landowners and the oil and gas industry. (Attachment 3) He gave 5 reasons for his support of the bill. He said the tax incentive was an important component that the KCC and other oil and gas industry associations discussed during the interim. It would help address this problem and far outweigh its cost benefit to the state and its citizens. Mr. Bleakley said the figures used in the fiscal note are much less than the figures that were used this summer in the interim committee meetings. He said there are a lot of people in the industry that are broke and do not have the money to plug the wells. If an incentive is given to plug these wells, it will be a benefit to the state in the long run because it will cost the state the full price to plug the wells later. The state is responsible for these wells and this would be an incentive to get rid of them. He urged the committee to vote in favor of **SB 566.**

Bill Fuller, Kansas Farm Bureau, said the plugging of abandoned wells protects the water quality and eliminates safety hazards both of which are high priorities for farmers and ranchers. (Attachment 4) He said they believe that **SB 566** would be an incentive and provide financial assistance to plug these wells which are threats to water quality and safety. Mr. Fuller said he had personally conducted 203 abandoned water well plugging demonstrations and the most frequent question he was asked was what could be done about the abandoned oil and gas wells on their land. He said they had referred many farmers and ranchers to the KCC for advice and assistance but few wells have been plugged. The cost is often prohibitive because, unlike water wells, plugging gas and oil wells requires special training and equipment. Mr. Fuller said there is a program for cost sharing in the water well plugging through the state water plan and the Conservation Commission. He said Farm Bureau would recommend the funds in **SB 566** be sunsetted so that people are encouraged to do the plugging now rather than wait for some later time. He encouraged favorable consideration of **SB 566.**

OPPONENT

Tom Day, legislative liaison for the KCC, appeared in opposition to **SB 566.** (Attachment 5) He said Section 1 of the bill should be addressed by the Department of Revenue for its fiscal implications. He said the waiver of all fees would have an adverse impact on the revenue of the Conservation Division of the KCC. The KCC will also spend time and resources in determining if the wells qualify for the tax credit. He said it is estimated that between 2,800 and 3,200 wells are plugged at the expense of operators each year. If it is determined the operator is unable to pay, the Conservation Division becomes responsible for seeing that the well is plugged. It is their priority to plug those wells that pose the most threat to the environment or public safety. Mr. Day said there should be a provision in **SB 566** so a combination of business entities could not duplicate tax credits or inflate costs associated with plugging. The reason the KCC opposes the bill, he said, is because there is a potential shortfall of approximately $175,000 for the Conservation Commission in FY 1997 and the potential of **SB 566** costing another $221,000 based on the cost of the waivers of plugging fees. Mr. Day said the KCC would not oppose the bill if Section 2, lines 29-32 were stricken. Abandoned and unplugged wells are a big problem and the KCC, the Governor's office and the Legislature's Energy and Natural Resources Committees should work together to find additional sources of revenue for the fund. He said this bill alludes to the fact that the party could plug any well, it does not address the idea that it must be an abandoned well. The KCC has waived fees for the plugging of wells in southeast Kansas but if there is a responsible party, this is not done.

Senator Sallee stated the bill says any wells prior to 1970. Senator Sallee also said he did not have a problem with changing the word "shall" to "may" waive the fee.

Mr. Day presented a problem which might occur if the responsible party dies and the heirs become the responsible party, these heirs might not have the money to pay for plugging the well. In such a case, the fee would be waived but they are still the responsible party.

Senator Clark asked if records were kept on where the wells are drilled. Mr. Day replied yes, but he did not know how many years this had been done. He said one of the problems is that they do not know where all these wells are located.

Senator Langworthy closed the hearing on **SB 566.**

SB 539--EXTENSION OF THE PROPERTY TAX LID

Senator Bond made a motion to pass favorably **SB 539.** The motion was seconded by Senator Martin. The motion passed.

The meeting adjourned at 12:05 p.m.

The next meeting is scheduled for Wednesday, February 21, 1996.

SENATE ASSESSMENT AND TAXATION COMMITTEE
GUEST LIST

DATE: Feb 14, 1996

NAME	REPRESENTING
Don Schnacke	KIOGA
Tom Day	KCC
David Bleakley	EKOGA
Doug Smith	SW KS Royalty Owners Assn
DAVID B. SCHLOSSER	PETE McGILL & ASSOC.
Tom Bruno	Allen & Assoc.
Whitney Damron	Kansas Bar Association
Jack Glaves	[illegible]
RICHARD BODENHAUSEN	TAXPAYERS
Martha Neu Smith	KMHA
Christy Bailey	Senator Kerr
Bill Fuller	Kansas Farm Bureau
Jennifer [illegible]	Overland Park Chamber of Commerce
Dave Holthaus	Western Resources
[illegible] Robyn	
[illegible] Hein	Hein, Ebert & Weir

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Statement of Donald P. Schnacke, Executive Vice President
Kansas Independent Oil & Gas Association
before the
Senate Assessment & Taxation Committee
February 14, 1996

RE: SB 566 - Income Tax Credit for Well Plugging

I am Donald P. Schnacke, Executive Vice President of the Kansas Independent Oil and Gas Association, a 59-year old statewide association of independent oil and gas producers and supporting industry. We are appearing today in support of HB 566.

Chairperson Langworthy asked that I give the Committee background information regarding what prompted this proposed legislation.

During the 1996 interim committee studies by the Special Committee on Energy and Natural Resources under Proposal No. 27, the subject of paying for the cost of handling the remediation of 17 sites transferred from KDH&E to the KCC was assigned to the Committee by the LCC. Considerable testimony was received and Proposal No. 27 reflects the findings of the Committee and their recommendations. HB 2955 was introduced as a result of the interim study and hearings have been held. That legislation is pending.

What is not in the report under Proposal No. 27 is an extensive record of testimony and concern expressed about the fact that some 91,000+ oil and gas wells have apparently been abandoned and not plugged. The State Corporation Commission and staff testified there may be up to 14,000 of these wells that pose a threat to the environment. The Committee asked the KCC to prepare a list of these sites and evaluate their impact on the environment and the need for action and plugging. That list is now being prepared by KCC staff.

During the interim study, the Chairman, Rep. Carl Holmes, asked KIOGA to come up with an industry recommendation to address the cost of increased plugging of old wells, but also asked for our recommendations to address the plugging of wells in the future.

We prepared a recommendation. Our plan, in addition to addressing the cost of increased plugging and the plugging of wells currently being drilled, contained the subject of SB 566 which is being heard today. We asked that SB 566 be introduced and considered while all other aspects of our proposal were being explored. It is part of a solution to an apparent large liability issue facing the State of Kansas

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The State Corporation Commission Conservation Division is a $5.1 million agency that regulates our industry. The majority of the money used arises from a conservation fee fund (CFF), of which $500,000 a year is typically used for plugging wells. We are advised by the KCC staff that the 3-year average for plugging wells statewide is $3,175 per well. Whatever number of wells are finally identified by the KCC, the future fiscal liability will be considerable. 91,000 wells equates to $273 million; 14,000 wells equates to $42 million.

HB 2599 may not do well in the 1996 session as it is tied to the use of severance tax money which we all know is general fund money. Our proposal to Rep. Holmes for future wells and increased plugging of old wells arises from the diversion of new severance tax money that was never counted in the general fund, federal royalty money, and a small increase in the conservation fee fund. Some modifications in this plan might meet the budgetary constraints currently being followed during this session. No bill has yet been introduced.

The proposal under SB 566 simply states that any taxpayer who plugs a well that was drilled prior to 1970, 26 years ago, would receive a 50% state income tax credit for undertaking that effort. Income tax credits are not new to the Kansas legislature or to this Committee. The last time we asked for an income tax credit was in 1987 when we asked that a credit be granted for expenditures in research and development projects, which in those days were tied, but not limited, to tertiary oil recovery projects. This credit was extended two years in 1993 and expired December 31, 1995. We have had one company which is exploring beginning a CO2 recovery project and has suggested the income tax credit should be extended.

SB 566 would require the KCC to waive the agency's plugging fee of $35 on wells that would be voluntarily plugged and qualify for the tax credit. We are advised by KCC staff that waiver of this fee is a normal practice when such a request is made.

Those among my membership who have reviewed SB 566 and given careful thought to its merits believe:

1. The private sector would be able to plug wells more cheaply than the state would. Any state administered fund would have a substantial percentage of its revenues dedicated to administrative costs, while a tax credit program would have more of its dollars going directly to alleviating the problem.

2. The bill, as drafted, provides incentives to others besides just oil and gas operators. Should a landowner or potential landowner wish to avail himself of this credit in order to remove an environmental problem and enhance the value of the land, he would be able to do so notwithstanding the fact that he may not have contributed to the problem and may not be an oil and gas operator. This could also work to the benefit of an operator where for one reason or another the non-operated interests are unable or unwilling to participate in the plugging costs.

3. Each year certain lands go unleased because a potential lessee becomes aware of unplugged wells and is unwilling to lease this acreage because he would assume the plugging obligation.

4. The current law which gives an operator the obligation to plug a well which was drilled prior to the time he leased the acreage is considered unfair by most operators. This is analogous to an owner of real estate over a superfund site who has not contributed to the pollution. This bill would give the individual who didn't create the problem an incentive to alleviate the problem for which he feels he is unfairly liable. This would go a long way toward removing the ill will that many operators have toward the state since the law was changed in the 1980's to create this responsibility.

5. This credit would allow for a more efficient market for producing oil and gas properties. As larger companies leave the state or otherwise sell to smaller companies, the existence of plugging obligations often serve as a stumbling block to the completion of these transactions. This incentive will help reduce the disincentive to transfer properties from less efficient to more efficient operators who will continue to produce the state's valuable resources.

In the interest of getting independent and private initiatives started in Kansas, we recommend you authorize the income tax credit incentive to plug wells, whether it be a farmer, landowner, royalty owner, interest holder, or operator who cannot financially or will not plug the wells without some incentive to do so. We recommend the passage of SB 566.

Donald P. Schnacke

DPS:pp

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MEMORANDUM

TO:	Ms. Gloria M. Timmer, Director Division of Budget	DATE:	February 12, 1996
FROM:	Kansas Department of Revenue	RE:	Senate Bill 566 as Introduced

BRIEF OF BILL

Senate Bill 566, as Introduced, would add a new credit to Kansas income tax statutes for taxpayers who plug abandoned oil and gas wells. The credit would be equal to 50% of the cost of plugging the well, and would apply against the taxpayer's income tax liability. The amount of credit exceeding the taxpayer's liability could be carried over in succeeding years until used.

The credit would only apply to wells drilled before January 1, 1970 and would only be available for taxable years commencing in 1997 through 2005.

Sec. 2 of the bill provides for the Kansas Corporation Commission (KCC) to waive their well plugging fee, currently at $35.00, on wells for which a tax credit is allowed.

This act would take effect July 1, 1996.

FISCAL IMPACT:

The total possible income tax revenue loss from this bill is estimated to be somewhere between $108.3 million to $155.5 million, over the 9 year period. There are 68,250 abandoned wells which would qualify for this credit. Assuming one ninth (1/9) of these wells were plugged each year, the annual fiscal impact would be between $12.0 million and $17.3 million a year. The lower fiscal impact is based on a three year average cost of plugging a well. The higher fiscal impact is based on current plugging costs. The KCC could have an additional loss of up to $226,000, as explained below.

EXHIBIT I is the worksheet used to compute these estimates. The current total of 91,000 abandoned wells in the state were divided between geographical areas in the same percentage as actual 1994 pluggings. It is necessary to spread the total wells to geographical areas because the cost of plugging a well is primarily determined by its depth. In the East, wells are very shallow so the cost to plug one of these wells is only $2,500 as contrasted to the $8,000 cost to plug a deep well in western Kansas. No records were kept in 1901 when drilling first started in Kansas and the records of the KCC only go back 25 years so it was necessary to estimate the number of wells drilled before 1970 which would qualify for the credit. For want of a better number, it was assumed that only 75% of the current 91,000 abandoned wells in the state or only 68,250 wells would qualify for the credit.

The number of qualifying wells, by district, were then multiplied by the current estimated cost of plugging a well in that district to obtain a properly weighted total cost of about $311.0 million to plug all of the qualifying wells. This total cost of $311.0 million, divided by the total number of abandoned wells, 91,000, produces a statewide weighted average cost of $4,556 to plug a well. The bill would allow only 50% of the plugging cost as a credit so the average allowed credit would be $2,278.

Based on this set of numbers and the assumptions detailed in the footnotes of EXHIBIT I, the total possible fiscal impact would be $155.5 million (i.e., $2,278 X 68,250 = $155.5 million). Assuming one ninth of this total would be used each year, the average annual loss in income tax revenue would be $17.3 million a year.

An alternate fiscal impact was computed using the same methodology and numbers except that the average plugging cost was a statewide three year average of $3,175, according to the KCC. Using 50% of this or $1,588 times 68,250 qualifying wells produces a long range impact of only $108.4 million, as shown in

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the bottom half of EXHIBIT I. Assuming one ninth of this total would be used each year, the average annual loss in income tax revenue would be $12.0 million a year.

There are several other considerations not incorporated in these estimates which are serious enough to be mentioned. First, the current cost of plugging wells was used throughout the nine (9) year period. Whether this cost will rise or fall over the years is unknown. The three year average cost quoted as $3,175 is less than the 1993 cost of $5,597 which indicates average costs are falling; however, this trend may be offset by inflation. Therefore, it was assumed the plugging cost would remain at the current level.

Second, the current number of 91,000 abandoned wells was used for the entire nine year period. This does not tell the whole story. According to the KCC, this number will grow by an estimated 450 abandoned wells per year. This nominal growth could have been included in the computations; it was not included because it is believed that many marginal wells and shut-in wells would actually be plugged, rather than abandoned, because of the financial incentive for plugging provided by this bill. This would decrease the number of wells abandoned each year.

Third, it was assumed the fiscal impact could be spread equally over each of the 9 years for which the credit could be claimed. This is equivalent to almost 7,600 abandoned wells being plugged each year (68,250 divided by 9). Currently, the industry and the KCC combined are plugging only 2,500 per year--only a third of the above 7,600. Although the 7,600 may seem to be unreasonably high, it is believed that farmers and others that had nothing to do with the abandonment could and would use the incentive of this bill so plugging would be expected to increase above current levels. In addition, the oil and gas operators who in the past have just walked away from their wells would now find it financially possible to plug the well so, again, the number of pluggings would be expected to increase above the current level and the number of abandonments to decrease.

Regardless of which scenario is assumed, this estimated fiscal impact should be regarded as conservatively low.

It is anticipated that this bill would also result in a revenue loss of up to $226,000 to the KCC. According to the latest information available from the KCC, their assessments on the current plugging fee of $35.00 amounted to total fee collections of $226,111.26 for FY 1995. Because Section 2 of the bill would require the KCC to waive these fees on all wells receiving a tax credit under this bill, most if not all of this revenue could be lost.

ADMINISTRATIVE IMPACT:

It is expected that most of these credits will be claimed on Corporate Income Tax forms. Therefore, the Business Tax Bureau would need one TE III @ $30,083 to audit and to record these credits and carryover amounts, to maintain a data base, and to answer taxpayers questions about this new credit. This position would also require fiscal year 1997 One-Time Operating Expense expenditures of $4,700 and fiscal year 1997 Annual Other Operating Expenditures of $276. Note: the one-time expenses include microcomputer system, Herman Miller workstation, chair, electrical outlets, telephone and installation of cables. The annual expense includes the annual fee for a telephone line.

The Income and Inheritance Tax Bureau would have to redesign the current income tax form K-40, adding an additional credit computation to be included on page two, Part D. A schedule would need to be developed containing supporting documentation required from the Kansas Corporation Commission, verifying drilling dates and plugging cost. This effort will require no additional personnel or costs from this bureau. However, depending on the volume of Individual Income Tax forms filed claiming this credit, it is possible some additional manpower may be necessary.

ADMINISTRATIVE PROBLEMS AND COMMENTS:

Any forms the Department would design would include a certification from the taxpayer regarding the completion of the plugging and the costs. However, in later audits, it would be difficult for the Department's unfamiliar staff to find the well, and even more difficult to determine whether the well had actually been satisfactorily plugged. Language should be added to require the KCC to physically audit the satisfactory completion of the plugging and to furnish the taxpayer with a certification to that effect. The taxpayer would then be required to furnish the Department with the KCC certification at the time of claiming the credit. Without such a certification, the Department's enforcement of this legislation would be difficult.

The Department can visualize a number of problems being generated by the requirement contained on line 18 and 19, "drilling of which was commenced prior to January 1, 1970." With 95 years of drilling in the state and 70 years of no records, it was estimated that 75% of the abandoned wells were drilled before 1970. However, the overriding consideration is that this restriction on the credit would be difficult to verify by many taxpayers so they would be unable to file a claim. For the 25% drilled after 1970, the Department and/or the KCC would still be saddled with a significant additional administrative burden--checking <u>all</u> credit claims to be sure the well was not drilled after 1970.

<u>LEGAL IMPACT:</u>

There is a typo at line 22, "taxpayers" should be "taxpayer's."

There are no notable legal ramifications for the Department.

APPROVED BY:

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John LaFaver
Secretary of Revenue

PARKS

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KANSAS DEPARTMENT OF REVENUE - RESEARCH AND REVENUE ANALYSIS **EXHIB.**

S.B. 566 - COMPUTATION OF FISCAL IMPACT

	KANSAS GEOGRAPHICAL AREA			
DESCRIPTION	EASTERN DISTRICT 3	CENTRAL DISTRICT 2	WESTERN DISTS. 1 & 4	TOTAL
1994 PLUGGINGS:				
UIC (1)	72	91	170	333
OTHER (2)	791	382	1,723	2,896
STATE TOTAL	863	473	1,893	3,229
% OF STATE TOTAL	26.73%	14.65%	58.62%	100.00%
TOTAL ABANDONED WELLS (3)	24,324	13,332	53,344	91,000
QUALIFYING ABANDONED WELLS (4)	18,243	9,999	40,008	68,250
AVERAGE PLUGGING COST PER WELL (5)	$8,000	$6,500	$2,500	
TOTAL PLUGGING COST IN MILLIONS (6)	$145.944	$64.994	$100.020	$310.958
WEIGHTED AVERAGE COST PER WELL (7)				$4,556
AVERAGE ALLOWED CREDIT (8)				$2,278
TOTAL CREDIT LIABILITY IN $MILLIONS (9)			TOTAL FISCAL IMPACT	**$155.479**
ALTERNATE COMPUTATION BASED ON KCC 3 YEAR AVERAGE COST:				
AVERAGE PLUGGING COST (10)				$3,175
AVERAGE ALLOWED CREDIT (11)				$1,588
TOTAL CREDIT LIABILITY IN $MILLIONS (12)			ALTERNATE TOTAL FISCAL IMPACT	**$108.347**

FOOTNOTES:

(1) Used for disposal or injection of water.
(2) Oil and gas production well.
(3) Current actual KCC count from field trip maps, by section within county.
(4) It was assumed that 75% of the 91,000 wells were drilled before 1970.
(5) KCC and contractor's current cost.
(6) Total abandoned wells times average current cost.
(7) Total plugging cost divided by total abandoned wells.
(8) 50% of cost is allowed as an income tax credit.
(9) Average allowed credit times number of qualifying abandoned wells.
(10) 3 year historical average cost per well.
(11) 50% of cost is allowed as an income tax credit.
(12) Average allowed credit times number of qualifying wells.

J.P. 2/14/96 10:45 AM

SENATE COMMITTEE ON ASSESSMENT AND TAXATION
February 14, 1996
RE: SB 566 - OIL & GAS TAX CREDIT FOR PLUGGING ABANDONED WELLS

Testimony of David Bleakley - President
Eastern Kansas Oil and Gas Association
&
Director of Acquisitions & Land Management
Colt Energy, Inc.

The Eastern Kansas Oil and Gas Association (EKOGA) strongly supports SB 566.

Our association represents and supports eastern Kansas oil and gas producers, service companies, royalty owners and associated businesses along with the overall welfare of the Kansas oil and gas industry in this state.

In testimony supporting SB 566, EKOGA feels this tax incentive would create the following benefits to the State, the tax payers, landowners and the oil and gas industry:

1) give oil and gas producers an incentive to plug historically older wells (pre-1970) on abandoned leases without responsible parties which are currently the states responsibility. This would allow producers to plug older wells the state wants plugged and drill new wells on these leases still containing recoverable reserves under <u>new</u> well construction rules and regulations and assume the responsibility for these new wells.

2) give landowners an incentive to plug historically older wells (pre-1970) abandoned on their land without responsible parties which are currently the states responsibility. This would allow the landowners an incentive to cleanup their own land and these older wells the state wants plugged.

3) relieve the State of the financial and custodial responsibility to plug abandoned and possible future abandoned wells they currently have.

4) implement an important component of an overall plan that was discussed between the KCC and industry over the past summer to address abandoned wells and older wells that have the potential to become abandoned.

5) save tax payers money in the long run by offering an incentive now instead of the state paying the whole cost to plug later.

EKOGA took part in several meetings this past summer and fall with the KCC and other oil and gas industry associations. We discussed and explored ways to address the abandoned well problem. A tax incentive was an important component the group agreed on that would help address this problem and far outweigh its cost benefit to the State and its citizens.

Therefore, Mr. Chairman and members or this Committee, we urge you to vote in favor of SB 566.

Thank you for your time.

David P. Bleakley

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PUBLIC POLICY STATEMENT

SENATE COMMITTEE ON ASSESSMENT & TAXATION

RE: SB 566 - Providing an Income Tax Credit for Plugging Abandoned Oil and Gas Wells.

February 14, 1996
Topeka, Kansas

Presented by:
Bill R. Fuller, Associate Director
Public Affairs Division
Kansas Farm Bureau

Chairperson Langworthy and members of the Committee:

Plugging abandoned wells protects water quality and eliminates safety hazards. Both are high priorities for the farm and ranch members of the 105 county Farm Bureaus in Kansas.

My name is Bill Fuller. I am the Associate Director of the Public Affairs Division for Kansas Farm Bureau. We express our support for the plugging of abandoned oil and gas wells. We believe SB 566 will provide many landowners with the incentive and financial assistance to plug many of these threats to water quality and safety.

One of my responsibilities is to coordinate Farm Bureau's natural resource and environmental programs. Four years ago, Farm Bureau developed and

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launched a statewide campaign toward plugging the estimated 250,000 abandoned water wells in Kansas. More than 240 demonstrations were conducted in 102 counties, many with the assistance of the Extension Service, Conservation Districts, 4-H Clubs and FFA Chapters. More than 7500 Kansans attended the demonstrations to become aware of the hazards and learn the process of plugging abandoned water wells.

After personally conducting 203 abandoned water well plugging demonstrations, I must tell you a frequent question is, "What can I do about the abandoned oil and gas wells on my land?" We have referred dozens to the Kansas Corporation Commission for advice and assistance. Feedback indicates few wells have been plugged.

Landowners want to do the right thing. Unfortunately, the cost is often prohibitive. Unlike water wells, plugging gas and oil wells requires special training and equipment, and in most cases is not a job most landowners should undertake. Unfortunately, few are plugged.

We believe the 50 percent state income tax credit is an incentive that will result in the plugging of many abandoned oil and gas wells in Kansas. We respectfully encourage favorable consideration of SB 566.

Thank You!

Testimony on behalf of the
Kansas Corporation Commission
Before the Senate Committee on Assessment and Taxation
February 14, 1996

Senate Bill 566

Madam Chair and members of the committee, my name is Tom Day. I am the legislative liaison for the Kansas Corporation Commission. I appear before you today in opposition to Senate Bill 566.

Senate Bill 566 provides a tax credit equivalent to 50% of the amount of money expended in the plugging of a well which was drilled prior to January 1, 1970. The credit will be available for any such plugging commenced after December 31, 1996 and prior to January 1, 2006. The tax credit will be provided to any individual who incurs such expenses. Section 1 of the bill, along with the fiscal implications for that section, should be addressed by the Department of Revenue.

Section 2 of SB 566 waives all fees which are associated with well plugging. This waiver would have an adverse impact on the revenue base of the Conservation Division of the Corporation Commission. It is the Commission's position that an operator who drills a well should be held accountable for the plugging of the same if it is either a dry hole or has outlived its economic life. Furthermore the Division would note that quite often operators have a production company and a service company; a provision should be added so that a combination of business entities could not duplicate tax credits or inflate costs associated with pluggings. In addition it will be necessary for the Commission to expend time and resources to determine when wells were drilled in order to advise Department of Revenue as to whether the well in question qualifies for the tax credit.

During the 1995 Interim Session, the Legislative Budget Committee was assigned the topic 'conservation fee fund'. The impetus for the study was a shortfall to the State Corporation Commission's Conservation Fee Fund in FY 1994. One of the sources of revenue to the Fund are plugged well inspection and supervision fees, which amounts to $35 per well or $.0325 per foot of well depth plugged--whichever is greater. During FY 95, the plugged well and supervision fee receipts amounted to $226,111.26. One of the Division's activities that has received considerable attention during the 1994 and 1995 Legislative Sessions has been well plugging. This requires that when a well ceases production the operator must plug it so the groundwater will be protected from pollution. Operators must notify the Conservation Division that they plan to plug a well so the staff can approve the proposed plugging method, and whenever possible, actually observe the well being plugged to be sure it is done correctly. The plugging cost is borne by the operator. It is estimated that between 2,800 and 3,200 wells are plugged at the expense of operators each year.

When the Conservation Division cannot determine who the operator is or the operator is unable to pay, the Division becomes responsible for seeing that the well is plugged. Payment for this activity is made from the Conservation Fee Fund. For the most part, these wells are discovered when the staff is in the field in connection with other duties or when someone makes a complaint. The Conservation Division's priority is to plug those wells that pose the most threat to the environment or public safety.

During recent budget hearings with the Senate Ways and Means subcommittee charged with reviewing the agency's budget, the subcommittee devoted much of its attention to the Commission's Conservation Fee Fund, which accounts for approximately 40 percent of the Commission's total revenues, and funds expenditures for the Conservation Division and for well plugging. The subcommittee was concerned to learn that the most recent projections of receipts indicate that estimated expenditures in FY 1997 will exceed receipts by approximately $175,000.

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attach 5-1

This shortfall, coupled with the potential of losing $221,000 based on waivers of plugging fees addressed in Senate Bill 566, is the reason the Corporation Commission opposes this bill. The efforts of KIOGA and other associations in the oil and gas industry to eliminate problems such as abandoned wells and the state's responsibility to plug those wells is laudable. However, potentially eliminating $221,000 from the Commission's budget is not the answer. The Commission would, however not oppose the bill if Section 2, lines 29-32, were stricken. (Balloon amendment attached)

The potential for a negative condition in the Conservation Fee Fund comes at a time when the Legislature and the Corporation Commission continue to be concerned about the magnitude of the problem of abandoned, unplugged wells. Because of the decline in oil production and the resulting depression of the oil industry, there has been an increase in the number of abandoned wells in all parts of the state. The potential of another shortfall in the Fee Fund underscores the importance of the efforts to develop a joint, consensus plan that will involve the Commission, the Governor's office, the Legislature's Energy and Natural Resources Committees, and the oil and gas industry in order to identify additional sources of revenue to the fund.

Thank you for the opportunity to present the Corporation Commission views on Senate Bill 566. I will be happy to answer any questions the committee may have.

K.C.C.

SENATE BILL No. 566

By Committee on Energy and Natural Resources

1-31

AN ACT relating to oil and gas; concerning the plugging of certain abandoned wells; granting certain credits against tax liability under the Kansas income tax act; and providing for the waiving of certain fees.

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

Section 1. (a) For any taxable year commencing after December 31, 1996, and before January 1, 2006, a credit shall be allowed against the tax imposed by the Kansas income tax act on the Kansas taxable income of a taxpayer for expenditures made for the purpose of plugging any oil or gas well in this state, drilling of which was commenced prior to January 1, 1970, in accordance with the rules and regulations of the state corporation commission applicable thereto, in an amount equal to 50% of such expenditures made in the taxable year.

If the amount of such tax credit exceeds the taxpayers income tax liability for such taxable year, the amount thereof which exceeds such tax liability may be carried over for deduction from the taxpayer's income tax liability in the next succeeding taxable year or years until the total amount of the tax credit has been deducted from tax liability.

(b) The secretary of revenue shall adopt such rules and regulations as may be necessary to carry out the purposes of this section.

Sec. 2. The state corporation commission shall waive all fees, fixed by rules and regulations of the commission for the plugging of oil and gas wells, upon the plugging of wells for which a tax credit is allowed pursuant to section 1 of this act.

DELETE SECTION 2

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.

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