

Approved: 2-19-98
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 17, 1998, in Room 519--S of the Capitol.

Members present: Senator Langworthy, Senator Corbin, Senator Lee, Senator Bond, Senator Donovan, Senator Goodwin, Senator Hardenburger, Senator Karr, Senator Praeger, Senator Steffes and Senator Steineger.

Committee staff present: Tom Severn, Legislative Research Department
Shirley Higgins, Secretary to the Committee

Conferees appearing before the committee: Senator Steve Morris
Dick Brewster, Amoco Corporation
Don Schnacke, Kansas Independent Oil and Gas Association
David Bleakley, Eastern Kansas Oil and Gas Association
Randy Allen, Kansas Association of Counties
Wayne Woolsey, Woolsey Petroleum Corporation

Others attending: See attached list

The minutes of February 12 were approved.

Senator Langworthy announced that the subcommittee on **SB 541**, dealing with the privilege tax on financial institutions, consists of Senator Corbin, Chair, and Senators Praeger and Lee.

SB 603--Severance tax exemption for incremental production resulting from production enhancement projects.

Senator Steve Morris testified in support of **SB 603** which would encourage producers of natural gas in the Hugoton field to make improvements in existing marginal wells. The bill is a small step to slow down the decline in the Hugoton field production. (Attachment 1) Senator Morris supports an amendment which would reduce the payout period from ten years to seven years and also supported an amendment regarding an administrative change.

Dick Brewster, Director of Public and Government Affairs for Amoco Corporation, testified in further support of **SB 603** which would apply statewide. Mr. Brewster noted that the bill exempts from the severance tax incremental (added) production of gas and oil when that incremental production results from any of the specific production enhancement projects defined in the bill. He explained that incremental production refers to production volumes from an oil or gas well which are in excess of the current base production. He pointed out that Oklahoma has similar incentives, and a study conducted by the University of Oklahoma concluded that the state is richer because of the incentives. He emphasized that the bill provides that there will be no severance tax relief unless the project results in increased production. (Attachment 2) Mr. Brewster distributed copies of an outline of proposed amendments and a balloon of **SB 603**. (Attachment 3) Essentially, the project payback portion of the bill is eliminated, and the Corporation Commission is required to develop rules and regulations by which applications for project exemptions are accepted.

Senator Langworthy raised the question as to what provisions there were in the bill to prevent an abuse problem. Mr. Brewster responded that Oklahoma and New Mexico have not experienced an abuse problem, and he saw no threat of widespread abuse occurring in Kansas.

Don Schnacke, Kansas Independent Oil and Gas Association, testified in support of the passage **SB 603**. He noted that a number of other states have already put in place similar incentive legislation. He contended that the bill would result in an increase of gas production and reserves and would protect marginal production. He viewed the bill as waiving the severance tax collection that the state never had in the beginning while

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ASSESSMENT AND TAXATION, Room 519-S
Statehouse, at 11:00 a.m. on February 17, 1998.

prohibiting the waste of the state's natural resources. (Attachment 4) Although he had not seen an official fiscal report on the bill, he understood that financially there would be no fiscal impact, but rather the impact regarded the need to employ more persons to monitor the program. He recently met with officials at the Department of Revenue at which time it was determined that a streamlined procedure was being developed whereby persons could verify project exemptions under oath, subject to audit. Therefore, there would be no need for extra employees in the field to monitor projects.

David Bleakley, Eastern Kansas Oil and Gas Association, gave final testimony in support of **SB 603**. He echoed testimony given by Mr. Brewster and Mr. Schnacke indicating the need for incentives to help the oil and gas industry survive. He commented that the longer the wells are kept open and available for extraction, the longer the state of Kansas will receive revenue. Furthermore, through the help of incentives, jobs will be maintained, and perhaps further jobs will be created.

Senator Bond moved to conceptually amend **SB 603** as suggested by Mr. Brewster subject to the revisor wording amendments in statutory language.

Senator Karr suggested that the motion to amend be held until such time as the revisor has prepared a balloon of the bill.

Senator Bond withdrew his motion to conceptually amend the bill. Senator Langworthy will request that the revisor prepare the balloon for the committee's consideration by the end of the week.

HCR 5004--Relating to exemption of property used for oil and gas development, exploration and production purposes.

Senator Langworthy noted that the bill passed the House very early last year by a vote of 111 to 11.

Randy Allen, Kansas Association of Counties, testified in support of **HCR 5004**. He noted that, if enacted, the resolution would give boards of county commissioners the discretion to exempt certain property used for oil and gas development, exploration, and production purposes from taxation and that there was no mandate on county government associated with **HCR 5004**. (Attachment 5)

Don Schnacke, Kansas Independent Oil and Gas Association, testified in support of the passage of **HCR 5004**. He explained that the resolution is a rural county economic development measure that would stimulate increased drilling and production and does not remove existing property from the tax rolls. (Attachment 6)

Wayne Woolsey, Woolsey Petroleum Corporation, appeared in support of the passage of **HCR 5004** which would qualify his corporation for the type of incentives that he feels are necessary to follow through with activity in Wichita County and other high-risk areas of oil and gas exploration. (Attachment 7)

David Bleakley, Eastern Kansas Oil and Gas Association, gave final testimony in support of **HCR 5004**. He sees the resolution as giving the counties a tool to use to help induce economic stimulation mainly to rural areas that need as much stimulation as possible. (Attachment 8)

There being no others wishing to testify, the hearing on **HCR 5004** was closed.

The meeting was adjourned at 12:03 p.m.

The next meeting is scheduled for February 18, 1998.

SENATE ASSESSMENT AND TAXATION COMMITTEE GUEST LIST

DATE: February 17, 1998

NAME	REPRESENTING
Steven Brun Kan	Ks Dept of Revenue
David Bleakley	EKOGA
Jim Allen	EKOGA
Jack Graves	Weske + K-N
Ken Peterson	KS Petroleum Council
Clark Duffey	" " "
Randy Allen	Kansas Assoc. of Counties
Ed My	Sumit
Doug Smith	SWKROA
Tom PALACE	KOMA
STEVE KEARNEY	KOMA
Tom Bruno	Allent Assoc.
J. P. SMALL	MOBIL
Don Hollibaugh	Western Res
Steve Montgomery	CAS
RICHARD PRODEWAD	TATPDES
I. Don Schmitt	ICIOGA
I. Wayne Woolsey	WOOLSEY Petroleum Corporation
Tom Kirk	AMERICAN PIPELINE

STEVE MORRIS

SENATOR, 39TH DISTRICT

600 TRINDLE

HUGOTON, KS 67951

(316) 544-2084

STATE CAPITOL BUILDING, ROOM 143-N

TOPEKA, KS 66612

(785) 296-7378



TOPEKA

SENATE CHAMBER

COMMITTEE ASSIGNMENTS

CHAIRMAN: AGRICULTURE
SRS TRANSITION OVERSIGHT

VICE CHAIR: ENERGY AND NATURAL RESOURCES

MEMBER: ORGANIZATION, CALENDAR AND
RULES
STATE BUILDING CONSTRUCTION
UTILITIES
WAYS AND MEANS

Testimony before the Senate Assessment and Taxation Committee February 17, 1998

Madam Chairman and Members of the Committee:

Thank you for the opportunity to testify in favor of SB 603. This is a bill that will encourage producers of natural gas in the Hugoton Field to make improvements in existing marginal wells.

Many wells have production levels that have dropped significantly in recent years. Current techniques used to increase production from these marginal wells are very expensive, and in most cases, probably will not be used.

For this reason, this bill proposes incentives that would encourage production companies to use production increasing techniques to raise the production levels of these wells. The difference between the production level prior to improvements being made and the production level after improvements will be exempt from severance tax. The KCC would certify production prior to improvements.

It is general knowledge that the Hugoton Field is in a decline, which indicates lower state revenues and lower economic benefits for the producers, royalty owners, county governments and the economy in general. This is a small step to help stop this decline. *slow*

Associated with this decline are low pressures at the well-head. Irrigators in the region depend on these wells for fuel for their irrigation engines. In many cases, the pressures are too low to allow for irrigation. An additional provision in this bill would exempt irrigation gas from severance tax. This would encourage the producers to work with irrigators, but yet have a very minor impact on state revenue. These producers would have an economic incentive to invest in equipment or new techniques to ensure the irrigators a reliable supply of irrigation gas.

Thank you for your consideration. I would be glad to stand for questions.

Stephen R. Morris

*Senate Assessment & Taxation
2-17-98
Attachment 1*

Madam Chair, members of the committee; My name is Dick Brewster, and I appear here today on behalf of Amoco Corporation, an integrated energy producer, refiner and marketer, one of the largest producers of natural gas in Kansas.

I appreciate very much the opportunity to offer these comment on Senate Bill No. 603, a bill which we strongly support, and a bill we believe will benefit oil and gas producers in the state, and the State of Kansas as well.

Senator Morris has offered some amendments to the bill as it is drafted. We believe the amendments will clarify meanings and simplify procedures and make it less burdensome to the Kansas Revenue Department, and the Kansas Corporation Commission. The proposed amendments were developed in extended conversations with Senator Morris and many of the other large gas producers in Kansas, and with representatives of smaller gas and oil producers as well. I won't take the committee's time to go through them now, but will be happy to answer any questions you might have about those amendments.

I do want to take your time to discuss the purpose of the bill, and what I believe it can accomplish, and to speak to some anticipated questions as well. I will try to be brief.

The purpose of the bill simply is to encourage investment in and development of Kansas gas and oil producing areas by those in a position to make those investments. It is also intended to encourage producers to invest in equipment and techniques to ensure the continued ability to provide irrigation gas.

S. B. No. 603 has statewide application. Many of my remarks today will speak to the bill's impact on gas production in Southwest Kansas, because that's what my employer does. But keep in mind, the bill will encourage investment in oil and gas properties throughout the state.

First, the bill exempts from the severance tax, gas used as fuel for irrigation purposes. We believe this provision could encourage producers to invest in some techniques and equipment to allow continued supplies of irrigation gas. You already know that declining pressures and other factors have jeopardized the ability of some producers in Southwest Kansas to supply irrigation gas to farmers. If a producer has the choice of selling un-taxed gas to an irrigator, or selling taxed gas to the more "normal" market, the choice is obvious.

I do not know how much of the Hugoton gas production is sold for irrigation. But I can tell you that Amoco sells less than 3% of its total gas production to irrigators, and Amoco is one of the leading providers of irrigation gas. It is therefore my belief that the fiscal impact of this provision of the bill would be very small. That 3% figure would apply only to gas, of course, and only to gas in production areas where there is widespread irrigation. And that may be a very small price to pay as contrasted with forcing irrigators to turn to more costly fuel sources, or revert to dryland farming.

Second, Senate Bill No. 603 exempts from the severance **incremental, or added,** production of gas and oil, when that incremental production results from any of the specific "production enhancement projects," defined in the bill. Incremental production refers to production volumes from an oil or gas well that would not be produced, except for an enhancement project being performed on the well, volumes which are in excess of current base production from a well.

The rationale goes this way: without additional investment, there would be no incremental gas produced; without the incentives provided in this bill, much of the investment would not take place. Therefore, without the incentives, there will be little incremental production of gas and oil. So, there is no tax loss to the state.

The logic of this argument rests on the validity of the second statement: that without the incentives, there would be no major investment. And, frankly, I would expect to be challenged on that assertion. And, indeed, if the major investment needed to provide incremental gas and oil production would be done without the incentives, this bill should not be passed.

I have read what I understand to be the Economic Impact Statement of S. B. 603 from the Kansas Corporation Commission. The statement indicates that some of the activities for which the incentive is provided in S. B. 603 are "routine," indicating they should not be included in the list for the incentives offered by the bill.

First, let me note that these incentives, listed under the "workover" provisions of the bill, mirror the incentives in current Oklahoma law. Second the Commission statement apparently does not take into account that the severance tax relief comes **only on incremental** production, and not on all the production from the well or wells included in a project. Thus, a simple "acidizing job," to use the example in the KCC document, would not get a producer any severance tax relief, unless it resulted in increased production.

The Commission cites "opportunity for abuse," as a reason for a significant staff increase if this bill is approved. Another approach might be to allow producers to report the needed information under oath, and be subject to audit and severe penalties, if false reports are found.

I firmly believe that without incentives provided in this bill, major oil and gas investment dollars will be spent outside the State of Kansas. Currently, similar incentives exist in Oklahoma and New Mexico, and a number of other states have developed or are developing incentive programs for the oil and gas industry.

Oklahoma exempts 6/7 of its severance tax on incremental production resulting from certain enhancement activities. So, take Amoco as an example: If we think we should invest \$500,000 in well workovers to provide incremental production from existing fields, we now have a choice: We can spend that money in Oklahoma, where we receive a rebate of 6/7 of the state's severance tax on the incremental production. (One percent is earmarked for teacher retirement and is not rebated.) Or we can spend it in Kansas, where we will pay 4.33% severance tax, AND property taxes, which equate to over 10% of the value of the gross production, on the incremental production we produce with that half million-dollar investment. (There is no property tax in Oklahoma on oil and gas production.)

I submit that without an incentive, investment dollars for mature production areas, like Kansas and much of Oklahoma, will be spent outside the state of Kansas.

Two years ago, the University of Oklahoma did a study to determine the value of Oklahoma's production enhancement incentives. The conclusion: the state is richer because of the incentives. Additional jobs, payroll, sales and income taxes far more than offset the severance tax not collected on the incremental production.

And the study concludes that the incentives were valuable in causing the additional investment in Oklahoma, indicating that **but for the incentives, much of the activity and investment would not have taken place.** It is for this reason, I believe incentives will cause significant investment to be made in the oil and gas fields in Kansas.... **Investment that would not be made without the incentives.**

Some highlights of the Oklahoma Study:

"Thirty-eight percent of companies with multi-state operations allocated a larger percentage of lease development spending to Oklahoma due to the tax incentives."

"Sixty-three percent of companies used all or part of the gross production tax rebate to further develop leases in Oklahoma."

Of all incentive applications filed under the Oklahoma law up to the end of last February, 83% were for enhancement projects; projects of the type listed in S. B. 603.

As would be expected, the report contains a lot of numbers which are unique to Oklahoma, and which would be irrelevant to Kansas. But the following might be exemplary:

A summary of enhancement project tax incentive in the Oklahoma report:

Average workover and recompletion cost:	\$249,637
Economic impacts per enhancement project:	
Drilling related	
Employment	9
Personal Income	\$180,363
Production related (initial year)	
Employment	2
Personal income	\$36,869

Estimated Tax Revenue Impacts Related to One Enhancement Project

Benefits	State	State & Local
Workover/recompletion related	\$16,221	\$21,416
Production related (20 years)	\$36,864	\$39,488
Total benefits:	\$53,085	\$60,904
<u>Benefits Attributable to Tax Incentive</u> (Assumes 25% attributable to incentives)	<u>\$13,271</u>	<u>\$15,226</u>
Costs		
Gross production tax Refund	\$9,630	
Multiplier Impact on reduced Government spending	\$553	
<u>Total Costs</u>	<u>-\$10,183</u>	

The study was conducted by David Penn, Assistant Director and Research Fellow at the Center for Economic and Management Research, College of Business Administration, University of Oklahoma.

Madam Chair, members of the committee, I can recall when I was allowed to serve as a member of the Kansas House of Representatives, and a member of the House Energy Committee in the late 1970's. Some of you may recall that it was a wide spread belief that the U.S. was running out of natural gas. We stopped the use of gas for heat to generate electricity, we stopped gas utilities from advertising to get more customers, and the Federal bureaucracy got involved in a complex formula to determine which gas customers could be interrupted and which could not.

A man by the name of George Simms lobbied for Mobil at that time, and I asked him one day if we were really running out of gas. He said no, "we're only running out of gas that we can afford to produce at current prices." And he explained some things to me about the oil and gas business.

For example, he explained to me that there are a number of factors which determine the "life" of an oil or gas well. One of those factors is simply the volume of reserves in place. Certainly we all know that we can never recover all the reserves in place, no matter what we try. But modern technology allows the recovery of a much higher percentage of the gas or oil in place than was true a generation ago.

George went on to help me understand that pre-mature abandonment of an oil or gas well takes place when there are recoverable reserves left in place. And economic factors most often lead to premature abandonment. If the cost of recovering gas or oil, the cost of producing and selling these commodities, exceeds the price for which it can be sold, abandonment must take place. And, certainly the extent to which the commodity is taxed plays an important role in determining the economics of maintaining production.

I am not here to suggest that Kansas' Hugoton gas field is in immediate threat of abandonment. It is not, though there are areas of the state in which gas or oil production is being abandoned daily. I am suggesting to you that gas and oil wells and fields throughout Kansas can have their economic life extended significantly if producers can invest in some of the production enhancement techniques outlined in S.B. No. 603. And I am suggesting that this kind of investment is much more likely if there is an incentive to producers to make such investments.

Specifically, regarding the Hugoton gas production area, incentives and additional investment can extend the field's life, in the longer term, and in the more near term can increase volumes and in some cases pressure. If this can happen, everyone gains. Producers gain by having more gas to sell. Royalty owners gain by receiving more royalty payments on that increased volume of gas produced. Irrigation farmers gain by being able to continue using natural gas to power their irrigation engines. And the State of Kansas gains in economic growth in the area, producing more income and sales tax revenues, and in the long term, by ultimately receiving more severance tax revenues.

Again, I appreciate the chance to appear today, and will look forward to responding to any questions you might have.

Respectfully submitted,

Dick Brewster

Proposed Changes in S. B. No. 603
Presented to Senate Committee on Assessment and Taxation
February 18, 1998

Page 4, line 21, 22 and 23 Elimination of the reference to "project payback."
It would be too costly for the state and producers to try to track payback, and a fixed period of years makes more sense. It would be rare that such a project would not pay out in 7 years, or that it would continue to produce incremental gas or oil after 7 years.

Page 4, line 21 The "date of completion" is replaced with "startup date" because in some cases, the project may be ongoing. In the case of a water flood, for example, as long as the project was operating, there would be no date of completion. Incentive legislation in most states refers to start up date, and not completion date.

Page 4, line 41 The addition of language allowing a producer, for example, to contract with a third party to do some work which might qualify and bring in incremental production.

Page 5, lines 21, 22 and 23 Again elimination of reference to payback.

Page 5, line 27 Eliminates reference to secretary of revenue, needed for the amendment to line 36 and following.

Page 5, line 30 clarifies that the commission must develop procedures as well as rules and regulations.

Page 5, lines 32 and 33 again, eliminates project payback language.

Page 5, line 34 is designed to allow for projects that benefit production from a group of wells, thus not restricting the benefit to one well at a time... which would discourage investment. A project involving a group of wells, or a field, or an area, would be a more economical project.

Page 5, new paragraph (C) clarifies and simplifies procedure for revenue department and KCC.

Respectfully Submitted,

Dick Brewster

Senate Assessment & Taxation
2-17-98
Attachment 3

SENATE BILL No. 603

By Committee on Assessment and Taxation

2-5

9 AN ACT relating to severance taxation; providing for exemptions there-
10 from; amending K.S.A. 79-4217 and repealing the existing section.
11

12 *Be it enacted by the Legislature of the State of Kansas.*

13 Section 1. K.S.A. 794217 is hereby amended to read as follows.

14 794217. (a) There is hereby imposed an excise tax upon the severance
15 and production of coal, oil or gas from the earth or water in this state for
16 sale, transport, storage, profit or commercial well, subject to the following
17 provisions of this section. Such tax shall be borne ratably by all persons
18 within the term "producer" as such term is defined in K.S.A. 794216,
19 and amendments thereto, in proportion to their respective beneficial in-
20 terest in the coal, oil or gas severed. Such tax shall be applied equally to
21 all portions of the gross value of each barrel of oil severed and subject to
22 such tax and to the gross value of the gas severed and subject to such tax.
23 The rate of such tax shall be 8% of the gross value of all oil or gas severed
24 from the earth or water in this state and subject to the tax imposed under
25 this act. The rate of such tax with respect to coal shall be \$1 per ton. For
26 the purposes of the tax imposed hereunder the amount of oil or gas pro-
27 dined shall be measured or determined. (1) In the case of oil, by tank
28 tables compiled to show 100% of the full capacity of tanks without de-
29 for overage or losses in handling; allowance for any reasonable
30 and bona fide deduction for basic sediment and water, and for correction
31 of temperature to 60 degrees Fahrenheit will be allowed; and if the
32 amount of oil severed has been measured or determined by tank tables
33 compiled to show less than 100% of the full capacity of tanks, such amount
34 shall be raised to a basis of 100% for the purpose of the tax imposed by
35 this act; and (2) in the case of gas, by meter readings showing 100% of
36 the full volume expressed in cubic feet at a standard base and flowing
37 temperature of 60 degrees Fahrenheit, and at the absolute pressure at
38 which the gas is sold and purchased; correction to be made for pressure
39 according to Boyle's law, and wed for specific gravity according to the
40 gravity at which the gas is sold and purchased, or if not so specified,
41 according to the test made by the balance method.

42 (b) The following shall be exempt from the tax imposed under this
43 section.

1 (1) The severance and production of gas which is: (A) Injected into
2 the earth for the purpose of lifting oil, recycling or repressuring; (B) used
3 for fuel in connection with the operation and development for, or pro-
4 duction of, oil or gas in the lease or production unit where severed; (C)
5 lawfully vented or flared; (1) severed from a well having an average daily
6 production during a calendar month having a gross value of not more
7 than \$81 per day, which well has not been significantly curtailed by reason
8 of mechanical failure or other disruption of production; in the event that
9 the production of gas from more than one well is gauged by a common
10 meter, eligibility for exemption hereunder shall be determined by com-
11 puting the gross value of the average daily combined production from all
12 such wells and dividing the same by the number of wells gauged by such
13 meter; (£) inadvertently lost on the lease or production unit by reason of
14 leaks, blowouts or other accidental losses; (F) used or consumed for do-
15 mestic or agricultural purposes on the lease or production unit from which
16 it is severed; a' (G) placed in underground storage for recovery at a later
17 date and which was either originally severed outside of the state of Kansas,
18 or as to which the tax levied pursuant to this act has been paid; or (H)
19 *used or consumed in this state as fuel for the purpose of irrigating land*
20 *devoted to agricultural use;*

21 (2) the severance and production of oil which is: (A) From a lease or I
22 production unit whose average dally production is two barrels or less per
23 producing well, which well or wells have not been significantly curtailed
24 by reason of mechanical failure or other disruption of production; (I)
25 from a lease or production unit, the producing well or wells upon which
26 have a completion depth of 2,000 feet or more, and whose average dally
27 production is three barrels or less per producing well or, if the price of
28 oil as determined pursuant to subsection (d) is \$30 or less, whose average
29 daily production is four barrels or less per producing well, or, if the price
30 of oil as determined pursuant to subsection (d) is \$24 or less, whose
31 average daily production is five barrels or less per producing well, or, if
32 the price of oil as determined pursuant to subsection (d) is \$16 or less,
33 whose average daily production is six barrels or less per producing well,
34 or, if the price of oil as determined pursuant to subsection (d) is \$10 or
35 less, whose average dally production is seven barrels or less per producing
36 well, which well or wells have not been significantly curtailed by reason
37 of mechanical failure or other disruption of production; (C) from a lease
38 or production unit, whose production results from a tertiary recovery
39 process. "Tertiary recovery process" means the process or processes de-
40 scribed in subparagraphs (1) through (9) of 10 C.F.R. 212.78(c) as in
41 effect on June 1, 1979(D) from a lease or production unit, the producing
42 well or wells upon which have a completion depth of less than 2,000 feet I
43 and whose average dally production resulting from a water flood process,

1 is three barrels or less per producing well, which well or wells have not
2 been significantly curtailed by reason of mechanical failure or other dis-
3 ruption of production; (E) from a lease or production unit, the producing
4 well or wells upon which have a completion depth of 2,000 feet or more,
5 and whose average dally production resulting from a water flood process,
6 is four barrels or less per producing well or, if the price of oil as deter-
7 mined pursuant to subsection (d) is \$30 or less, whose average daily pro-
8 duction is five barrels or less per producing well, or, if the price of oil as
9 determined pursuant to subsection (d) is \$24 or less, whose average daily
10 production is six barrels or less per producing well, or, if the price of oil
11 as determined pursuant to subsection (d) is \$16 or less, whose average
12 daily production is seven barrels or less per producing well, or, if the price
13 of oil as determined pursuant to subsection (d) is \$10 or less, whose
14 average dally production is eight barrels or less per producing well, which
15 well or wells have not been significantly curtailed by reason of mechanical
16 failure or other disruption of production; (V) test, frac or swab oil which
17 is sold or exchanged for value; or (O) inadvertently lost on the lease or
18 production unit by reason of leaks or other accidental means;

19 (3) (A) any taxpayer applying for an exemption pursuant to subsec-
20 tion (b)(2)(A) and (B) shall make application annually to the director of
21 taxation therefor. Exemptions granted pursuant to subsection (b)(2)(A)
22 and (B) shall be valid for a period of one year following the date of cer-
23 tification thereof by the director of taxation; (18) any taxpayer applying for
24 an exemption pursuant to subsection (b)(2)(D) or (E) shall make appli-
25 cation annually to the director of taxation therefor. Such application shall
26 be accompanied by proof of the approval of an application for the utili-
27 zation of a water flood process therefor by the corporation commission
28 pursuant to roles and regulations adopted under the authority of K.S.A.
29 55-152 and amendments thereto and proof that the oil produced there-
30 from is kept in a separate tank battery and that separate books and records
31 are maintained therefor. Such exemption shall be valid for a period of
32 one year following the date of certification thereof by the director of
33 taxation;

34 (4) the severance and production of gas or oil from any pool from
35 which oil or gas was first produced on or after April 1, 1983, as determined
36 by the state corporation commission and certified to the director of tax-
37 ation, and continuing for a period of 24 months from the month in which
38 oil or gas was first produced from such pool as evidenced by an affidavit
39 of completion of a well, filed with the state corporation commission and
40 certified to the director of taxation. Exemptions granted for production
41 from any well pursuant to this paragraph shall be valid for a period of 24
42 months following the month in which oil or gas was first produced from
43 such pool. The term "pool" means an underground accumulation of oil

1 or gas in a single and separate natural reservoir characterized by a single
 2 pressure system so that production from one part of the pool affects the
 3 reservoir pressure throughout its extent;

4 (5) the severance and production of oil or gas from a three-year in-
 5 active well, as determined by the state corporation commission and cer-
 6 tified to the director of taxation, for a period of 10 years after the date of
 7 receipt of such certification. As used in this paragraph, "three-year in-
 8 active well" means any well that has not produced oil or gas in more than
 9 one month in the three years prior to the date of application to the state
 10 corporation commission for certification as a three-year inactive well. An
 11 application for certification as a three-year inactive well shall be in such
 12 form and contain such information as required by the state corporation
 13 commission, and shall be made prior to July 1, 1996. The commission
 14 may revoke a certification if information indicates that a certified well was
 15 not a three-year inactive well or if other lease production is credited to
 16 the certified well. Upon notice to the operator that the certification for a
 17 well has been revoked, the exemption shall not be applied to the pro-
 18 duction from that well from the date of revocation; and

19 (6) (A) *The incremental severance and production of oil or gas which*
 20 *results from a production enhancement project begun on or after July 1,*
 21 *1998, shall be exempt for a period of 10 7 (seven) years from the start up date of completion*
 22 *of such project, or until project payback, whichever comes first, or for the*
 23 *time period otherwise specified in this subsection. As used in this section:*

24 (1) *"Incremental severance and production" means the amount of oil*
 25 *or natural gas which is produced as the result of a production enhance-*
 26 *ment project which is in excess of the base production of oil or natural*
 27 *gas, and is determined by subtracting the base production from the total*
 28 *monthly production after the production enhancement projects is com-*
 29 *pleted*

30 (2) *"Base production" means the average monthly amount of pro-*
 31 *duction for the twelve-month period immediately prior to the production*
 32 *enhancement project beginning date, minus the monthly rate of produc-*
 33 *tion decline for the well or project for each month beginning 180 days*
 34 *prior to the project beginning date. The monthly rate of production de-*
 35 *cline shall be equal to the average extrapolated monthly decline rate for*
 36 *the well or project for the twelve-month period immediately prior to the*
 37 *production enhancement project beginning state, as determined by the*
 38 *state corporation commission based on the production history of the well,*
 39 *field or project, its current status, and sound reservoir engineering prin-*
 40 *ciples'*

41 (3) *"Production enhancement project" means performing or causing to be performed, the*
 following:

42 (i) *'Workover' means any downhole operation in an existing oil or*
 43 *gas well that is designed to sustain, restore or increase the production*

1 rate or ultimate recovery of oil or gas, including but not limited to aci--
 2 dizing, reperforation, fracture treatment, sand/paraffin/scale removal or
 3 other wellbore cleanouts, casing repair, squeeze cementing, initial instal-
 4 lation, replacement or enhancement of artificial lifts on gas wells including
 5 plunger lifts, rods, pumps, submersible pumps and coiled tubing velocity
 6 strings, downsizing existing tubing to reduce well loading, downhole com-
 7 mingling, bacteria treatments, upgrading the size of pumping unit equip-
 8 ment, setting bridge plugs to isolate water production zones, or any com-
 9 bination of the aforementioned operations; "workover" shall not mean the
 10 routine maintenance, routine repair, or like for-like replacement of down
 11 hole equipment such as rods, pumps, tubing packers or other mechanical
 12 device.

13 (ii) recompletion to a different producing zone in the same well bore;

14 (iii) secondary recovery projects;

15 (iv) addition of mechanical devices to dewater a gas or oil well;

16 (v) initial installation, replacement or enhancement of surface equip-
 17 ment;

18 (vi) installation or enhancement of compression equipment, line loop-
 19 ing or other techniques or equipment which increases production from a
 20 well or a group of wells in a project. ~~The severance tax exemption on~~
 21 ~~incremental production achieved by this activity shall be for a period of~~
 22 ~~seven years from the date of completion of the project, and shall not be~~
 23 ~~limited or extended based on project payback;~~

24 (vii) new discoveries of oil or gas which are discovered as a result of
 25 the use of new technology, including but not limited to, three dimensional
 26 seismic studies.

27 ~~(B) The secretary of revenue in conjunction with The state corporation~~
 28 ~~commission shall adopt rules and regulations necessary to efficiently and~~
 29 ~~properly administer the provisions of this paragraph (6) including rules,~~
 30 ~~and regulations and procedures for the qualification of production enhancement projects,~~
 31 ~~the procedures for determining the monthly rate of production decline,~~
 32 ~~the establishment appropriate payback indicators for the determination~~
 33 ~~of project payback for each of the exemptions authorized by this para-~~
 34 ~~graph (6), criteria for determining the share of incremental production attributable to each well~~
 35 ~~when a production enhancement project includes a group of wells, and criteria for determining~~
 36 ~~the startup date for any project for~~
 37 ~~which an exemption is claimed, and determining new qualifying technol-~~
 38 ~~ogies for the purposes of paragraph (6)(A)(4)(vii).~~

**(C) Any taxpayer applying for an exemption pursuant to this section shall apply
 for such exemption to the state corporation commission. Upon determination that
 the project qualifies for an exemption pursuant to this section and applicable rules and
 regulations, the commission shall certify the same to the secretary of revenue. The secretary
 shall exempt from the tax imposed by this section, the incremental severance of oil or
 gas as determined by the commission, and shall refund any taxes paid between the
 project startup date and the certification of qualification by the commission.**

37 ~~(D) The provisions of this paragraph (6) shall not affect any other~~
 38 ~~exemption allowable pursuant to this section.~~

39 ~~(6) (7) for the calendar year 1988, and any year thereafter, the sev-~~
 40 ~~erance or production of the first 350,000 tons of coal from any mine as~~
 41 ~~certified by the state geological survey.~~

42 (c) No exemption shall be granted pursuant to subsection (b)(3) or
 43 (4) to any person who does not have a valid operator's license issued by

1 the state corporation commission, and no refund of tax shall be made to
2 any taxpayer attributable to any production in a period when such tax-
3 payer did not hold a valid operator's license issued by the state corporation
4 commission.

5 (d) On April 15, 1988, and on April 15 of each year thereafter, the
6 secretary of revenue shall determine from statistics compiled and pro-
7 vided by the United States department of energy, the average price per
8 barrel paid by the first purchaser of crude oil in this state for the six-
9 month period ending on December 31 of the preceding year. Such price
10 shall be used for the purpose of determining exemptions allowed by sub
11 section (b)(2)(B) or (E) for the twelve-month period commencing on May
12 1 of such year and ending on April 30 of the next succeeding year.

13 Sec. 2. K.S.A. 79-4217 is hereby repealed.

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



KANSAS INDEPENDENT OIL & GAS ASSOCIATION

105 S. BROADWAY • SUITE 500 • WICHITA, KANSAS 67202-4262
(316) 263-7297 • FAX (316) 263-3021

800 S.W. JACKSON • SUITE 1400 • TOPEKA, KANSAS 66612-1216
(913) 232-7772 • FAX (913) 232-0917

**Before the Senate Assessment and Taxation Committee
February 17, 1998**

**RE: SB 603 - Exemption from the State Severance Tax for Production
Enhancement Projects.**

I am Don Schnacke representing the Kansas Independent Oil & Gas Association, a 60 year old association representing Independent oil and gas operators throughout Kansas and the supporting industry. We are appearing here in support of the passage of SB 603.

The State of Kansas actively participates and belongs to the Inter-State Oil & Gas Compact Commission. Prior Kansas Governors, in my time representing KIOGA, have served as its Chairman, including Governors Bennett, Hayden and Finney. Governor Graves is a very active and interested participant in IOGCC affairs.

One important initiative of the IOGCC is to urge producing states to incorporate into state laws and policies, initiatives to maximize oil and gas recovery, and to prolong the premature abandonment and plugging of marginal oil and gas wells. Kansas is a leader in the nation in the number of marginal wells and marginal production.

In examining the January 1997 IOGCC document "Investments in Energy Security - State Incentive to Maximize Oil and Gas Recovery", we note a number of states have already put in place incentive legislation similar to SB 603. These states include New Mexico, North Dakota, Oklahoma, Utah, Wyoming, Texas, Alabama, Alaska, Arkansas, Florida, Louisiana, Mississippi, and Montana. These laws all encourage producers to invest in their producing wells. In the case of SB 603, the severance tax is exempted on the incremental increased production, not to exceed that amount that is invested, and in all cases not to exceed 10 years. One way of looking at it is waiving the severance tax collection that the state never had in the beginning, while prohibiting the waste of our state's natural resources.

*Senate Assessment + Taxation
2-17-98
Attachment 4*

P.2

Testimony of Donald P. Schnacke

The state severance tax has been in place since 1983. It was enacted in an atmosphere of re-electing an incumbent Governor, with the promise it would reduce property taxes, raise teacher salaries, and pave roads in Kansas. We all know today that has not happened, except from our industry's point of view, it placed a double tax burden on the production of oil and gas and removed close to \$1.5 billion from the industry that could have been used for the general support of the industry and the drilling for new production. Over the years we have had to address the severance tax in many ways with exemptions and protection of marginal production, and attempt to keep this important industry from collapsing. With today's oil prices in the \$12-13 range, and close to the \$10.50 in 1986, when the industry did collapse, we are looking for all the help we can get, in lieu of our common goal of the outright repeal of the severance tax in Kansas.

SB 603 is incentive legislation that waives the severance tax on the success of further investment to stimulate production. The KIOGA Officers and Board of Directors believe SB 603 would be of help to the Kansas oil and gas industry. We urge your support and passage of SB 603.

Donald P. Schnacke

DPS:sm



KANSAS
ASSOCIATION OF
COUNTIES

TESTIMONY
concerning House Concurrent Resolution No. 5004

Given by Randy Allen, Executive Director, Kansas Association of
Counties before the Senate Assessment and Taxation Committee
February 17, 1998

Senator Langworthy and members of the Senate Assessment and
Taxation Committee. My name is Randy Allen, and I am speaking today in
support of HCR 5004. This resolution, if enacted and the language subsequently
amended into the Kansas Constitution, would give boards of county commis-
sioners the **discretion** to exempt certain property used for oil and gas develop-
ment, exploration, and production purposes from taxation.

In some of our counties which have not experienced such a strong
economic recovery as others, the capacity for county commissioners to
encourage economic development in this way is certainly appealing. This is not a
“one size fits all” solution; rather, it clearly recognizes that our 105 counties’
economies are all somewhat different. Trego and Wichita counties, both
members of our Association, have demonstrated their interest in granting such
exemptions and would surely consider such action should the Constitution be
amended to allow such a policy decision to be made at the local level.

There is **no mandate** on county government associated with HCR 5004.
The board of county commissioners in each county could decide whether an
exemption makes sense to them. I urge your favorable consideration of the
resolution.

700 SW Jackson
Suite 805
Topeka KS 66603
785•233•2271
Fax 785•233•4830
email kac@ink.org

The Kansas Association of Counties, an instrumentality of member counties Under K.S.A. 19-2690, provides
legislative representation, educational and technical services and a wide range of informational services to its
member counties. Inquiries concerning this testimony should be directed to the KAC by calling (785) 233-2271.

Senate Assessment & Taxation
2-17-98
Attachment 5



KANSAS INDEPENDENT OIL & GAS ASSOCIATION

105 S. BROADWAY • SUITE 500 • WICHITA, KANSAS 67202-4262
(316) 263-7297 • FAX (316) 263-3021

800 S.W. JACKSON • SUITE 1400 • TOPEKA, KANSAS 66612-1216
(913) 232-7772 • FAX (913) 232-0917

Before the Senate Assessment and Taxation Committee
February 17, 1998

*RE: HCR 5004- Constitutional Amendment to Exempt Oil & Gas Properties from Property
Tax for Exploration & Production Activity*

I am Don Schnacke representing the Kansas Independent Oil & Gas Association, a 60 year old association representing independent oil and gas operators throughout Kansas and the supporting industry. We are appearing here in support of the passage of HCR 5004.

HCR 5004 is a rural county economic development measure that would stimulate increased drilling and production and does not remove existing property from the tax rolls.

KIOGA is doing all it can to stimulate increased activity and investment in Kansas oil and gas fields activity. Since 1986 when oil prices collapsed and nearly 20,000 Kansans were put out of work, we have slowly made some progress.


One important area we have explored is the use of the ad valorem tax exemption authority arising from Section 13, Article 11 of the Kansas Constitution. Two Kansas counties, Trego and Wichita, have offered oil producers modest tax relief if they will expend money, drill for oil and gas, and find new production. After Wichita County and a Kansas producer entered into their agreement, the State Board of Tax Appeals rejected the application.

BOTA rejected the application because the terms and facts presented did not fit the language presented in the Constitution. We would agree that the constitutional provisions better fit the traditional machine shop, warehouse, manufacturing mode than that applicable to an oil and gas operation. The legislative challenge is to seek legislation that would clearly allow oil and gas producers to qualify under the constitutional authority. I talked to the BOTA Chairman after their order was issued and he believes a legislative solution for clarification is the answer. He regretted turning down the Wichita County application.

We believe the producing counties which have very little opportunity for economic development except farming and ranching should be given the opportunity that other Kansas counties now enjoy - the opportunity to attract capital expenditure into their counties, the creation of jobs, and expansion of their ad valorem tax base by working directly with the oil and gas industry.

There are others here to support the passage of HCR 5004. We would conclude by requesting that this committee look favorably on this legislation and recommend its passage.

DPS:sm

Senate Assessment + Taxation
2-17-98
Attachment 



WOOLSEY PETROLEUM CORPORATION

125 N. MARKET, SUITE 1000, WICHITA, KANSAS 67202-1775 (316) 267-4379
FAX (316) 267-4383

*Statement of I. Wayne Woolsey, President
Woolsey Petroleum Corporation*

BEFORE THE SENATE ASSESSMENT AND TAXATION COMMITTEE
FEBRUARY 18, 1998

RE: HCR 5004 – CONSTITUTIONAL AMENDMENT TO EXEMPT OIL AND GAS
PROPERTIES FROM PROPERTY TAX FOR EXPLORATION AND
PRODUCTION ACTIVITY

I am Wayne Woolsey, President and owner of Woolsey Petroleum Corporation, an independent oil and gas company located in Wichita. I am appearing here in support of passage of HCR 5004.

For over 25 years, Woolsey Petroleum Corporation has been effectively engaged in the drilling and production of oil and gas. During this time we have been responsible for the drilling of over 500 wells. We have a field office at Medicine Lodge in Barber County with 10 full time local employees responsible for the operations of over 100 producing wells, 165 miles of gas gathering pipeline and a natural gas processing plant. Within Barber County we drill, produce, transport, and process burner tip quality gas for the city of Medicine Lodge, the local gypsum wallboard plant and other markets in the area. Our activity in the area creates considerable other business and numerous local jobs with the associated service companies required to maintain our business.

Four years ago we made application in Wichita County for a partial abatement in county taxes under the Amendment to the State Constitution, Article II, Section 13. It was our understanding that this Amendment allowed for some local tax relief for companies willing to make a meaningful investment towards economic development. Our application was turned down at the State Board of Tax Appeals level because it was the opinion of the Board that the language in the Amendment did not fit the oil and gas industry. The Board did encourage us to seek clarification through new legislation that would clearly allow oil and gas producers to qualify under the constitutional authority. We strongly believe that our investment can lead to as much or more tax revenue and job creation as any other industry that is currently entitled to this type of economic development incentive. The oil and gas industry is a very important part of the economy of Kansas.

Although oil and gas companies carry out many types of activity in the production of oil and gas, **nothing** stimulates a rural economy more quickly than the discovery of a new oil and gas field. A new discovery well attracts additional investment and business activity of other oil and gas companies.

Our proposal in Wichita County, a county that has almost no existing oil and gas production, was to initially spend over \$3,000,000 in the development and drilling of eight separate wildcat drilling blocks consisting of over 23,000 acres of oil and gas leases. This play was indicated to have the potential of three 20,000,000 barrel oil fields. With **one** 20,000,000 barrel field discovery, estimating the price of oil at \$20 per barrel, a county tax of 10% **would yield nearly \$40,000,000 in county tax revenue**. This would establish, over the next fifteen years, approximately 60 full-time employees.

Based to some degree on our 1994 application for county tax relief, we did raise sufficient capital to drill five wells and have completed one that is indicated to be a profitable well. We believe Wichita County is a promising area for additional seismic and drilling, and see similar potential in several other counties in Kansas, including Barber County.

We ask that you approve HCR 5004 so that we can qualify for the type of incentives that we feel are necessary to follow through with activity in Wichita County and other high-risk areas of oil and gas exploration.

*Senate Assessment & Taxation
2-17-98
Attachment 7*

SENATE COMMITTEE ON ASSESSMENT AND TAXATION

February 17, 1998

**RE: HCR 5004 - CONSTITUTIONAL AMENDMENT TO EXEMPT OIL & GAS
PROPERTIES FROM PROPERTY TAX FOR EXPLORATION**

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

The Eastern Kansas Oil and Gas Association (EKOGA) strongly supports HCR 5004.

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 HCR 5004, EKOGA feels this tax incentive or any incentive for that matter that helps an industry that is so important to the states economy is worthy of consideration.

I wish I could stand before you today and tell you our industry is in great shape and the revenues derived by the state are going to be bigger than ever this year but, I can't. Our industry (except for a few short months off and on) has been flat on is back since 1986, the year of the oil bust. Now, almost 12 years later prices currently being paid for a barrel of oil in this state are lower (adjust for inflation) than the lowest point in 1986.

We see HCR 5004 as giving the counties the option to help induce economic stimulation mainly to rural areas that need as much stimulation as possible themselves. This resolution gives the counties a tool to use if they can see the benefit to the county and it gives our industry a chance to enter into something beneficial to help keep this industry alive and viable for the future.

Therefore, we see any incentive to help preserve this industry and the jobs and revenue it generates for the state economy as important to help this industry survive.

Therefore, Mr. Chairman and members of this Committee, we urge you to vote in favor of HCR 5004.

Thank you for your time.

David P. Bleakley

*Senate Assessment & Taxation
2-17-98
Attachment 8*