

## **BILL ANALYSIS**

C.S.S.B. 1166  
By: Armbrister  
Energy Resources  
Committee Report (Substituted)

### **BACKGROUND AND PURPOSE**

Texas is the leading state in the Union for oil and gas production. Oil and gas prices are at a high, and it looks as if they will remain that way for sometime. Especially under these circumstances, it is critical to protect and bolster the oil and gas industry to ensure production remains a thriving commodity for both small and large producers.

Committee Substitute Senate Bill 1166 will help influence producers to begin new production, adopt orphaned wells, utilize energy efficient equipment, while encouraging environmental responsibility.

CSSB 1166 will do the following:

- Enhances the ability of the Railroad Commission to recover costs associated with well plugging and site cleanup from delinquent operators who have neglected to follow the well plugging and remediation procedures that are required by law.
- Alleviate concerns for small producers by allowing tax relief and exemptions on marginal wells produced if price levels fall below a certain threshold.
- Creates an Orphan Well Adoption program that would utilize Oilfield Cleanup Fund dollars and a severance tax abatement to establish an incentive for operators to adopt orphan wells, and
- Establish tax credits for energy efficient equipment installed and used in the production of oil and gas.

### **RULEMAKING AUTHORITY**

It is the committee's opinion that rulemaking authority is expressly granted to the Railroad Commission of Texas in SECTION 4 and SECTION 18 of this bill.

### **ANALYSIS**

SECTION 1. Amends Section 81.116(d), Natural resources Code to change Section references.

SECTION 2. Amends Section 89.043, Natural Resources Code, by amending Subsections (c) and (f) and adding Subsection (g), as follows:

(c) Provides notice requirements to operators.

(f) Makes a conforming change.

(g) Prohibits provisions of this section and Section 91.115 from applying to the proceeds from the sale of hydrocarbons that would otherwise be directed to the permanent school fund or the permanent university fund.

SECTION 3. Amends Section 89.044 (a) and (b), Natural Resources Code, as follows:

(a) Authorizes the commission or its employees or agents, the operator, or the nonoperator, on proper identification to enter the land of another for the purpose of plugging or replugging a well that has not been properly plugged.

(b) Authorizes a prospective operator who has been authorized under Section 89.047 to conduct a surface inspection of a well, on proper identification, to enter the land of another for the sole purpose of conducting the inspection.

SECTION 4. Amends Subchapter C, Chapter 89, Natural Resources Code, is amended by adding Sections 89.047 and 89.048, as follows:

Section 89.047 ORPHANED WELL REDUCTION PROGRAM.

(a) Definitions

(b) Authorizes a person and sets provisions for that person to conduct a surface inspection of the well to determine whether the person desires to be designated by the commission as the operator of the well.

(c) Requires the commission to accept the nomination and issue a written confirmation to the person of the person's authority to conduct a surface inspection of the nominated well for a stated period not to exceed 30 days, if the person is an operator in good standing and the well is not already subject to a nomination.

(d) Authorizes a person, to whom a confirmation is issued under Subsection (c), to conduct a surface inspection of the well. Provides that the person must deliver written notice to the owner of record of the surface estate and any occupant of the tract on which the well is located at least three days before the date of the inspection. Provides what the notice must include.

(f) Provides requirements for the commission to designate the person as the operator of the well.

(g) Requires a fee collected under Subsection (f) to be deposited to the credit of the general revenue fund and may be appropriated only to the commission to be used to enforce the laws and rules concerning oil and gas conservation and waste and pollution prevention.

(h) Entitles a person who is designated as the operator of an orphaned well on or after January 1, 2006, and not later than December 31, 2007, to receive:

- (1) a nontransferable exemption from severance taxes for all future production from the well as provided by Section 202.060, Tax Code;
- (2) a nontransferable exemption from the fees provided by Sections 81.116 and 81.117 for all future production from the well; and
- (3) a payment from the commission in an amount equal to the depth of the well multiplied by 50 cents for each foot of well depth if, not later than the third anniversary of the date the commission designates the person as the operator of the well, the person brings the well back into continuous active operation or plugs the well in accordance with commission rules.

(i) Provides what determines a well to be in continuous active operation for purposes of Subsection (h)(3).

(j) Provides annual payment requirements by the commission to operators under Subsection (h)(3). Provides a \$500,000 ceiling for payments and limitations on multiple payments.

Section 89.048 PLUGGING OF WELL BY SURFACE ESTATE OWNER

(a) definition

(b) Authorizes the owner of an interest in the surface estate of a tract of land on which an orphaned well is located to contract with a commission-approved well plugger to plug the well.

(c) Requires well plugger to provide notice no later than 30 days before the well is plugged, to assume responsibility for physical operation and control of the well, file financial security, and plug the well according to commission rules.

(d) Authorizes the surface owner to submit the cost of the well plugging the commission and requires the commission to reimburse the surface owner from the oil field cleanup fund in amount no greater than 50 percent of the lesser of the documented well plugging costs or an average cost incurred by the commission.

(e) Requires rulemaking from the commission

SECTION 5. SECTION 5. Section 89.083, Natural Resources Code, is amended by amending Subsection (g) and adding Subsection (g-1) as follows:

(g)(1)(c) is added to the cause of action to include hydrocarbons and their proceeds from their sale in placing a lien against an operator.

(g)(2) the cause of action against a non-operator at the time the well should have been plugged, to be secured by a first lien, superior to all preexisting and subsequent liens and security interests, on non-operators interest in the oil and gas in the land.

(g-1) Authorizes a non-operator to be made a party defendant in the suit against an operator.

SECTION 6. Subchapter D, Chapter 89, Natural Resources Code, is amended by adding Section 89.089, as follows:

Sec. 89.089. LIEN ON OPERATOR'S INTERESTS IN HYDROCARBON PRODUCTION AND PROCEEDS.

(a) Provides that the state has the first and superior lien on the interests of each operator in any hydrocarbons produced in this state and the proceeds from the sale of those hydrocarbons.

(b) Authorizes the commission to foreclose on the lien.

(d) Section 89.086 applies to a claim of a person with a legal or equitable ownership or security interest in property that is described by this section and is disposed of under Section 89.085.

(e) requires the liens to be subject to and inferior to any lien in favor of the state to secure royalty payments.

SECTION 7. Subchapter A, Chapter 91, Natural Resources Code, is amended by adding Section 91.004 as follows:

Sec. 91.004. RECOVERY OF ESTIMATED PLUGGING COSTS.

(a) Authorizes the commission to order the operator to pay for the plugging costs if the well has not been plugged within 60 days since the operator was ordered to plug the well.

(b) Provides what the plugging costs are based upon.

(c) Requires proceeds recovered to be deposited into the oilfield cleanup fund.

(d) Authorizes the commission to recover costs if the costs to the commission were more than the proceeds. Requires the commission to remit to the operator remaining dollars if the costs are less than the proceeds. Commission is not required to pay interest on the refund.

(e) Requires the attorney general, on request of the commission, to file suit to collect the amount of the estimated plugging costs from the operator, if the operator does not pay the costs within 75 days after ordered to do so. Travis County is the venue for the action.

SECTION 8. Section 91.112(a), Natural Resources Code, is amended by adding Section (a)(7) and (8), as follows:

(a)(7) Authorizes money in the fund to be used by the commission or its employees or agents for making payments to eligible operators under Sections 89.074, and

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(a)(8) making payments to eligible surface owner under Section 89.048.

SECTION 9. The heading to Section 91.113, Natural Resources Code, is amended to read as follows:

Sec. 91.113. INVESTIGATION, ASSESSMENT, PREVENTION, CONTROL, OR CLEANUP OF POLLUTION BY COMMISSION.

SECTION 10. Sections 91.113(a)-(d) and (f), Natural Resources Code, are amended to read as follows:

(a)-(d) and (f) Conforming changes.

SECTION 11. Section 91.114(d), Natural Resources Code, amends (d)(2)(A) and (B), as follows

(d)(2)(A) Requires the commission to accept the report or application or approve the certificate if, as applicable, all costs, as provided in this section, incurred by the state are paid in accordance with an agreed upon payment schedule, or

(B) the estimated plugging costs have been paid in accordance with commission order.

SECTION 12. The heading to Section 91.115, Natural Resources Code, is amended to read as follows:

Sec. 91.115. FIRST LIEN ON EQUIPMENT, STORED HYDROCARBONS, OIL AND GAS, AND PRODUCED HYDROCARBONS.

SECTION 13. Sections 91.115(a)-(f) and (h), Natural Resources Code, are amended as follows:

(a) Includes the provision that if a responsible person fails to take measures necessary to prevent the unauthorized discharge of or to control oil and gas wastes or other substances or materials as required by law or by a rule adopted or order issued by the commission, the state has the first and superior lien on responsible person's interest in (30 any hydrocarbons produced in this state and proceeds from the sale of those hydrocarbons.

(b)-(f) Conforming changes.

(h)Requires the lien provided by this section, as it relates to stored hydrocarbons, the responsible person's interest in oil and gas in the land where the prevention, control, or cleanup measures are required, and the responsible person's interest in any hydrocarbons produced in this state and the proceeds from the sale of those hydrocarbons to be subject to and inferior to any lien in favor of the State of Texas to secure royalty payments.

SECTION 14. Section 201.053, Tax Code, is amended as follows:

Sec. 201.053. GAS NOT TAXED.

(4) Excludes gas produced in this state from a well that qualifies under Section 202.060 from the tax imposed by this chapter.

SECTION 15 Section 201.058(a), Tax Code, is amended to read as follows:

(a) Conforming changes.

SECTION 16. Subchapter B, Chapter 201, Tax Code, is amended by adding Section 201.059 to read as follows:

Sec. 201.059. CREDITS FOR QUALIFYING LOW-PRODUCING WELLS

(a) Definitions

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(b) Requires the comptroller to average the gas prices from the last three months in order to define the necessary price thresholds.

(c) Entitles an operator of a qualifying marginal well to a 25 percent tax credit for marginal wells if the price of gas is between \$3.00 and \$3.50 per mcf.

(d) Entitles an operator of a qualifying marginal well to a 50 percent tax credit for marginal wells if the price of gas is between \$2.50 and \$3.00 per mcf.

(e) Entitles an operator of a qualifying marginal well to a 100 percent tax credit for marginal wells if the price of gas is less than 2.50 per mcf.

(f) Provides that reimbursement is necessary if full tax rates are paid.

SECTION 17. Section 202.052(c), Tax Code, is amended as follows:

(c) Conforming changes.

SECTION 18. Subchapter B, Chapter 202, Tax Code, is amended by adding Sections 202.058, 202.060, and 202.061 as follows:

Sec. 202.058. CREDITS FOR QUALIFYING LOW-PRODUCING OIL LEASES.

(a) definitions

(b) Provides that for purposes of qualifying lease, production per well per day is determined by computing the average daily per well production using the "p-1" monthly lease production during the three-month period by the sum of the number of well-days, where a well-day is one well producing for one day.. The commission is required to certify to the comptroller a list of qualifying wells.

(c) Requires the comptroller to average the oil prices from the last three months in order to define the necessary price thresholds.

d) Entitles an operator of a marginal well to a 25 percent tax credit for marginal wells if the price of oil is between \$25 and \$30.

(e) Entitles an operator of a marginal well to a 50 percent tax credit for marginal wells if the price of oil is between \$22 and \$35.

(f) Entitles an operator of a marginal well to a 100 percent tax credit for marginal wells if the price of oil is less than \$22 per barrel.

(g) Reimbursement is necessary if full tax rates are paid.

Sec. 202.060. EXEMPTION FOR OIL AND GAS FROM REACTIVATED ORPHANED WELLS.

(a) Definitions

(b) Requires commission to issue a certificate to the operator of the orphaned well.

(c) Provides that hydrocarbons produced from the well identified in the certificate qualify for a severance tax exemption.

(d) Grants rulemaking authority.

(e) Provides that the tax payer must apply to the comptroller for tax exemptions. Provides requirements and procedures for the application and certificate.

(f) Provides that the exemption takes effect on the first day of the month following the month in which the comptroller approves the application.

(g) Requires operator notice to the comptroller if he or she ceases operation. The exemption expires on the date the notice is received.

(h) Establishes penalties imposed by Chapters 85 and 91, Natural Resources Code for fraudulent applications.

(i) Provides that a person is liable to the state for a civil penalty if the person applies or attempts to apply the tax exemption after operation has ceased. The amount of the penalty may not exceed the sum of:

- (1) \$10,000; and
- (2) the difference between the amount of taxes paid or attempted to be paid and the amount of taxes due.

(j) Authorizes the attorney general to recover a penalty under Subsection (i) in a suit brought on behalf of the state. Venue for the suit is in Travis County.

#### Sec. 202.061. TAX CREDIT FOR ENHANCED EFFICIENCY EQUIPMENT.

(a) Definitions

(b) Entitles the taxpayer responsible for the payment of severance taxes on the production from a well in this state on which enhanced efficiency equipment is installed and used to a credit in an amount equal to 20 percent of the cost of the equipment, provided that:

- (1) the cumulative total of all severance tax credits authorized by this section may not exceed \$2,000 for any well;
- (2) the enhanced efficiency equipment installed in a qualifying well must have been purchased and installed not earlier than September 1, 2005, or later than September 1, 2009;
- (3) the taxpayer must file an application with the comptroller for the credit and must demonstrate to the comptroller that the enhanced efficiency equipment has been purchased and installed in the well within the period prescribed by Subdivision (2)
- (4) the number of applications the comptroller may approve each state fiscal year may not exceed a number equal to two percent of the producing wells in this state on September 1 of that state fiscal year, as determined by the comptroller; and
- (5) the manufacturer of the enhanced efficiency equipment must obtain an evaluation of the product under Subsection (a)

(c) Authorizes the taxpayer carry any unused credit forward until the credit is used.

SECTION 19, 20, and 21. Effective dates.

#### **EFFECTIVE DATE**

September 1, 2005, except for the following sections, which become effective, January 1, 2006:

- (1) Sections 81.116(d), 89.044, and 91.112(a), Natural Resources Code, as amended by this Act;
- (2) Sections 89.047 and 89.048, Natural Resources Code, as added by this Act;
- (3) Sections 201.053, 201.058(a), and 202.052(c), Tax Code, as amended by this Act; and
- (4) Section 202.060, Tax Code, as added by this Act.

#### **COMPARISON OF ORIGINAL TO SUBSTITUTE**

The Substitute adds tax credit for qualifying low producing wells, establishes an orphaned well adoption program, and establishes tax credits for the use of energy efficiency equipment.

The Substitute adds new language by adding the following SECTIONS:

SECTION 1, SECTION 3, SECTION 4, SECTION 8, SECTION 14, SECTION 15, SECTION 16, SECTION 17, SECTION 18, SECTION 19, SECTION 20, SECTION 21.

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