Don J. Hutchinson - U.S. Senator Landrieu's Office

Mr. Chairman, members of the Committee. It is indeed a pleasure to be here today to make a few comments on behalf of Senator Landrieu. I think everybody in the room probably knows why she is not here. One of the things we talked this morning and she mentioned how homesick she was of – she hadn't been back in the State in 1999 yet because of the business that is taking place in Washington, D.C. and she hopes to see everybody, at least several people, next week when she makes one of her first visits of the year here. What the Senator asked me to do is to read her statement into the record which has been handed out to the members and also – I'll give this to the Board later, a copy of the legislation that has been introduced in Congress. I'll just read it verbatim, if you'll indulge me. I'm a person who usually talks a lot so I'm not used to reading a statement – but I guess that comes with the job. **(Refer to 3-page statement from Senator Landrieu)** A couple of comments that are not in the statement that the Senator wanted me to express to you, as well as members in the audience, is that – for those persons who may not be familiar with the legislation, I do have a few copies with me and if I run out I can provide some more. Senator Landrieu has challenged primarily our Washington staff to look at other options beyond tax credit is that is included in Senator Hutchinson's bill. Some of those options she wants us to look at – what can we do to assist unemployed workers who may be impacted in the area; options that will provide a pro-active and a long-term approach to addressing some of the unfortunate times that we have such as putting mechanisms in place, so that in the future when something like this happens, we can do a lot more administratively than has to be done legislatively. And finally, the senator really would like to hear from the Board members as well as the persons in the audience from the industry on any suggestions and ideas that she will take from them and push forward at the federal level. And that concludes my remarks.

STATEMENT OF SENATOR MARY L. LANDRIEU
STATE OF THE PETROLEUM INDUSTRY
LOUISIANA PRODUCERS' MEETING
DNR OFFICE OF CONSERVATION
February 10, 1999

Thank you for the opportunity today to address a number of major developments in the petroleum industry in the last few years. We have gone in an inordinately short period of time from prosperity to crisis, and while our economy is reaping benefits to consumers, it has been bad news for industry and jobs, particularly in Louisiana.

On the national level, prices for oil in the field in January were hovering between $9.50 and $10 per barrel. Gasoline prices were at an all time low, costing less than bottled water. Natural gas was selling at about $2 per million cubic feet. Oil prices have been so low that marginal and stripper wells have been shut in at an alarming rate, which in itself is costly. Stripper wells alone account for 15 percent of United States domestic crude production. This raises a national security issue. We are at an all time high in our energy imports, exceeding 50% of domestic consumption. Moreover, we currently maintain less than a 90-days supply of oil in the Strategic Petroleum Reserve.

On the international level, OPEC seems to no longer exist as a unified entity and some of its members are flooding the market with oil. China turned out not to be a burgeoning market as was expected as a result of the economic crisis in the Far East. Major oil and gas company stocks are down, and finally, our big U.S. companies are uniting to form mammoths that can withstand this environment of adversity and remain competitive, making smaller producers question their ability to persevere in the future. In the midst of all this, I look to an area that stands to lose in this scenario - my state of Louisiana. Let me recite a few facts about our situation.

Louisiana has 18,034 stripper wells that produce 10.5 million barrels a year. Average daily production is 1.61 barrels. The impact of the current oil price collapse is disastrous to Louisiana oil and gas producers at these volumes. The State Mineral Board is looking into assisting the petroleum industry to weather the downturn. Many are concerned about oil drillers and service companies cutting operations or leaving Louisiana. The Louisiana Independent Oil and Gas Association has asked Governor Foster, the Louisiana Mineral Board and the federal government for help.

The majors are hurting, too. When British Petroleum agreed to buy Amoco, Amoco pulled 280 jobs out of Louisiana, mostly in New Orleans. In October, Shell cut 700 jobs from the United States division, most in Louisiana and Texas. Just last week Texaco announced it was beginning job cuts in Louisiana, 287 state wide. There are 6,000 Exxon and Mobil workers in Louisiana and I am told some divestiture after that merger is inevitable.

Job losses by energy workers in South Louisiana affect the economy, through taxes and spending. Houma and Lafayette will take most of the hit, although New Orleans has lost some jobs, too. Other oil patch states, such as Wyoming, Oklahoma and Texas, are enduring similar difficulties.

Although I have painted a dour picture for the energy sector, there are some efforts underway to provide relief. On January 28, 1999 Senator Kay Bailey Hutchison of Texas introduced a bill, S. 325, the U.S. Energy Economic Growth Act, which I have cosponsored. The measure provides a phased in marginal well tax credit of three dollars per barrel for the first three barrels of daily production from marginal and stripper wells, and a fifty cent tax credit for the first eighteen million cubic feet of daily natural gas production. The bill also provides for tax relief on inactive wells, and the expensing of certain capital expenditures. As a cosponsor of this bill, I am hopeful that Congress will act quickly on the bill and I will work vigorously toward that end.

Members from producing states have also encouraged the Federal government, at every opportunity, to make the purchase of domestic crude for the Strategic Petroleum Reserve its top priority. We will continue to have discussions on that point with the Administration. Finally, we have fought to require the Federal government to impose new regulations on oil valuation **only after a fair method for doing so is determined.** I supported the current moratorium on regulations as I believe it is the correct thing to do while oil prices remain low.

There has been some good news in the last few days. The Administration made an announcement on February 4th that it will grant relief to small oil operators producing on public lands by allowing them to suspend operations for up to two years without losing their leases. In addition, the Administration has foreseen a four dollar per barrel increase by the end of the year 2000, and prices could start to firm up by the end of 1999. This is critically important since we have seen declines in the price of oil even since January. While it is difficult to call this more than crystal ball gazing at this time, it is a positive sign that the industry could possibly see an upturn by the final quarter of 1999.

Finally, I would encourage the State Mineral Board and the Foster Administration to take steps similar to those being contemplated by oil patch states such as Oklahoma, and Texas, to give additional tax breaks to producers on stripper and incapable wells.

If you have any questions about S. 325 or about current ongoing efforts within the Federal government to deal with the crisis we are experiencing, do not hesitate to call my offices in state or in Washington, D.C. and we will give you the most current information.

II

106TH CONGRESS
1ST SESSION

S. 325

To amend the Internal Revenue Code of 1986 to provide tax incentives to encourage production of oil and gas within the United States, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JANUARY 28, 1999

Mrs. HUTCHISON (for herself, Mr. DOMENICI, Mr. NICKLES, Mr. MURKOWSKI, Mr. BINGAMAN, Mr. BREAUX, Mr. BROWNBACK, Mr COCHRAN, Mr. CONRAD, Mr. ENZI, Mr. GRAMM, Mr. INHOFE, Ms. LANDRIEU, Mr. ROBERTS, Mr. ROCKEFELLER, Mr. STEVENS, Mr. THOMAS, Mr. BURNS, and Mr. LOTT) introduced the following bill; which was read twice and referred to the Committee on Finance

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A BILL

To amend the Internal Revenue Code of 1986 to provide tax incentives to encourage production of oil and gas within the United States, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "United States Energy Economic Growth Act".

TITLE I—PRODUCTION FROM MARGINAL AND INACTIVE WELLS

SEC. 101. TAX CREDIT FOR MARGINAL DOMESTIC OIL AND NATURAL GAS WELL PRODUCTION.

(a) CREDIT FOR PRODUCING OIL AND GAS FROM MARGINAL WELLS.—Subpart D of part IV of subchapter A of chapter 1 of the Internal Revenue Code of 1986 (relating to business credits) is amended by adding at the end the following new section:

"SEC. 45D. CREDIT FOR PRODUCING OIL AND GAS FROM MARGINAL WELLS.

"(a) GENERAL RULE.—For purposes of section 38, the marginal well production credit for any taxable year is an amount equal to the product of—

"(1) the credit amount, and

"(2) the qualified crude oil production and the qualified natural gas production which is attributable to the taxpayer.

"(b) CREDIT AMOUNT.—For purposes of this section—

"(1) IN GENERAL.—The credit amount is—

"(A) $3 per barrel of qualified crude oil production, and

"(B) 50 cents per 1,000 cubic feet of qualified natural gas production.

"(2) REDUCTION AS OIL AND GAS PRICES INCREASE.—

"(A) IN GENERAL.—The $3 and 50 cents amounts under paragraph (1) shall each be reduced (but not below zero) by an amount which bears the same ratio to such amount (determined without regard to this paragraph) as—

"(i) the excess (if any) of the applicable reference price over $14 ($1.56 for qualified natural gas production), bears to

"(ii) $3 ($0.33 for qualified natural gas production).

The applicable reference price for a taxable year is the reference price for the calendar year preceding the calendar year in which the taxable year begins.

"(B) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 2000, each of the dollar amounts contained in subparagraph (A) shall be increased to an amount equal to such dollar amount multiplied by the inflation adjustment factor for such calendar year (determined under section 43(b)(3)(B) by substituting '1999' for '1990').

"(C) REFERENCE PRICE.—For purposes of this paragraph, the term 'reference price' means, with respect to any calendar year—

"(i) in the case of qualified crude oil production, the reference price determined under section 29(d)(2)(C), and

"(ii) in the case of qualified natural gas production, the Secretary's estimate of the annual average wellhead price per 1,000 cubic feet for all domestic natural gas.

"(c) QUALIFIED CRUDE OIL AND NATURAL GAS PRODUCTION.—For purposes of this section—

"(1) IN GENERAL.—The terms 'qualified crude oil production' and 'qualified natural gas production' mean domestic crude oil or natural gas which is produced from a marginal well.

"(2) LIMITATION ON AMOUNT OF PRODUCTION WHICH MAY QUALIFY.—

"(A) IN GENERAL.—Crude oil or natural gas produced during any taxable year from any well shall not be treated as qualified crude oil production or qualified natural gas production to the extent production from the well during the taxable year exceeds 1,095 barrels or barrel equivalents.

"(B) PROPORTIONATE REDUCTIONS.—

"(i) SHORT TAXABLE YEARS.—In the case of a short taxable year, the limitations under this paragraph shall be proportionately reduced to reflect the ratio which the number of days in such taxable year bears to 365.

"(ii) WELLS NOT IN PRODUCTION ENTIRE YEAR.—In the case of a well which is not capable of production during each day of a taxable year, the limitations under this paragraph applicable to the well shall be proportionately reduced to reflect the ratio which the number of days of production bears to the total number of days in the taxable year.

"(3) DEFINITIONS.—

"(A) MARGINAL WELL.—The term 'marginal well' means a domestic well which during the taxable year has marginal production (as defined in section 613A(c)(6)).

"(B) CRUDE OIL, ETC.—The terms 'crude oil', 'natural gas', 'domestic', and 'barrel' have the meanings given such terms by section 613A(e).

"(C) BARREL EQUIVALENT.—The term 'barrel equivalent' means, with respect to natural gas, a conversion ratio of 6,000 cubic feet of natural gas to 1 barrel of crude oil.

"(d) OTHER RULES.—

"(1) PRODUCTION ATTRIBUTABLE TO THE TAXPAYER.—In the case of a marginal well in which there is more than one owner of operating interests in the well and the crude oil or natural gas production exceeds the limitation under subsection (c)(2), qualifying crude oil production or qualifying natural gas production attributable to the taxpayer shall be determined on the basis of the ratio which taxpayer's revenue interest in the production bears to the aggregate of the revenue interests of all operating interest owners in the production.

"(2) OPERATING INTEREST REQUIRED.—Any credit under this section may be claimed only on production which is attributable to the holder of an operating interest.

"(3) PRODUCTION FROM NONCONVENTIONAL SOURCES EXCLUDED.—In the case of production from a marginal well which is eligible for the credit allowed under section 29 for the taxable year, no credit shall be allowable under this section unless the taxpayer elects not to claim the credit under section 29 with respect to the well.".

(b) CREDIT TREATED AS BUSINESS CREDIT.—Section 38(b) of such Code is amended by striking "plus" at the end of paragraph (11), by striking the period at the end of paragraph (12) and inserting ", plus", and by adding at the end the following new paragraph:

"(13) the marginal oil and gas well production credit determined under section 45D(a).".

(c) CREDIT ALLOWED AGAINST REGULAR AND MINIMUM TAX.—

(1) IN GENERAL.—Subsection (c) of section 38 of such Code (relating to limitation based on amount of tax) is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

"(3) SPECIAL RULES FOR MARGINAL OIL AND GAS WELL PRODUCTION CREDIT.—

"(A) IN GENERAL.—In the case of the marginal oil and gas well production credit—

"(i) this section and section 39 shall be applied separately with respect to the credit, and

"(ii) in applying paragraph (1) to the credit—

"(I) subparagraphs (A) and (B) thereof shall not apply, and

"(II) the limitation under paragraph (1) (as modified by subclause (I)) shall be reduced by the credit allowed under subsection (a) for the taxable year (other than the marginal oil and gas well production credit).

"(B) MARGINAL OIL AND GAS WELL PRODUCTION CREDIT.—For purposes of this subsection, the term 'marginal oil and gas well production credit' means the credit allowable under subsection (a) by reason of section 45D(a).".

(2) CONFORMING AMENDMENT.—Subclause (II) of section 38(c)(2)(A)(ii) of such Code is amended by inserting "or the marginal oil and gas well production credit" after "employment credit".

(d) CARRYBACK.—Subsection (a) of section 39 of such Code (relating to carryback and carryforward of unused credits generally) is amended by adding at the end the following new paragraph:

"(3) 10-YEAR CARRYBACK FOR MARGINAL OIL AND GAS WELL PRODUCTION CREDIT.—In the case of the marginal oil and gas well production credit—

"(A) this section shall be applied separately from the business credit (other than the marginal oil and gas well production credit),

"(B) paragraph (1) shall be applied by substituting '10 taxable years' for '1 taxable years' in subparagraph (A) thereof, and

"(C) paragraph (2) shall be applied—

"(i) by substituting '31 taxable years' for '21 taxable years' in subparagraph (A) thereof, and

"(ii) by substituting '30 taxable years' for '20 taxable years' in subparagraph (B) thereof."

(e) COORDINATION WITH SECTION 29.—Section 29(a) of such Code is amended by striking "There" and inserting "At the election of the taxpayer, there".

(f) CLERICAL AMENDMENT.—The table of sections for subpart D of part IV of subchapter A of chapter 1 of such Code is amended by adding at the end the following item:

"45D. Credit for producing oil and gas from marginal wells."

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to production after the date of the enactment of this Act.

SEC. 102. EXCLUSION OF CERTAIN AMOUNTS RECEIVED FROM RECOVERED INACTIVE WELLS.

(a) IN GENERAL.—Part III of subchapter B of chapter 1 of the Internal Revenue Code of 1986 (relating to items specifically excluded from gross income) is amended by redesignating section 139 as section 140 and by inserting after section 138 the following new section:

"SEC. 139. OIL OR GAS PRODUCED FROM A RECOVERED INACTIVE WELL.

"(a) IN GENERAL.—Gross income does not include income attributable to independent producer oil from a recovered inactive well.

"(b) DEFINITIONS.—For purposes of this section—

"(1) INDEPENDENT PRODUCER OIL.—The term 'independent producer oil' means crude oil or natural gas in which the economic interest of the independent producer is attributable to an operating mineral interest (within the meaning of section 614(d)), overriding royalty interest, production payment, net profits interest, or similar interest.

"(2) CRUDE OIL AND NATURAL GAS.—The terms 'crude oil' and 'natural gas' have the meanings given such terms by section 613A(e).

"(3) RECOVERED INACTIVE WELL.—The term 'recovered inactive well' means a well if—

"(A) throughout the time period beginning any time prior to January 15, 1999, and ending on such date, such well is inactive or has been plugged and abandoned, as determined by the agency of the State in which such well is located that is responsible for regulating such wells, and

"(B) during the 5-year period beginning on the date of the enactment of this section, such well resumes producing crude oil or natural gas.

"(4) INDEPENDENT PRODUCER.—The term 'independent producer' means a producer of crude oil or natural gas whose allowance for depletion is determined under section 613A(c).

"(c) DEDUCTIONS.—No deductions directly connected with amounts excluded from gross income by subsection (a) shall be allowed.

"(d) ELECTION.—

"(1) IN GENERAL.—This section shall apply for any taxable year only at the election of the taxpayer.

"(2) MANNER.—Such election shall be made, in accordance with regulations prescribed by the Secretary, not later than the time prescribed for filing the return (including extensions thereof) and shall be made annually on a property-by-property basis."

(b) MINIMUM TAX.—Section 56(g)(4)(B) of the Internal Revenue Code of 1986 is amended by adding at the end the following new clause:

"(iii) INACTIVE WELLS.—In the case of income attributable to independent producers of oil recovered from an inactive well, clause (i) shall not apply to any amount allowable as an exclusion under section 139."

(c) CLERICAL AMENDMENT.—The table of sections for part III of subchapter B of chapter 1 of such Code is amended by striking the item relating to section 139 and inserting the following:

"Sec. 139. Oil or gas produced from a recovered inactive well.
"Sec. 140. Cross references to other Acts."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

TITLE II—OTHER INCENTIVES

SEC. 201. ELECTION TO EXPENSE GEOLOGICAL AND GEOPHYSICAL EXPENDITURES.

(a) IN GENERAL.—Section 263 of the Internal Revenue Code of 1986 (relating to capital expenditures) is amended by adding at the end the following new subsection:

"(j) GEOLOGICAL AND GEOPHYSICAL EXPENDITURES FOR DOMESTIC OIL AND GAS WELLS.—Notwithstanding subsection (a), a taxpayer may elect to treat geological and geophysical expenses incurred in connection with the exploration for, or development of, oil or gas within the United States (as defined in section 638) as expenses which are not chargeable to capital account. Any expenses so treated shall be allowed as a deduction in the taxable year in which paid or incurred."

(b) CONFORMING AMENDMENT.—Section 263A(c)(3) of the Internal Revenue Code of 1986 is amended by inserting "263(j)," after "263(i),".

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to expenses paid or incurred after the date of the enactment of this Act.

(2) TRANSITION RULE.—In the case of any expenses described in section 263(j) of the Internal

Revenue Code of 1986, as added by this section, which were paid or incurred on or before the date of the enactment of this Act, the taxpayer may elect, at such time and in such manner as the Secretary of the Treasury may prescribe, to amortize the unamortized portion of such expenses over the 36-month period beginning with the month in which the date of the enactment of this Act occurs. For purposes of this paragraph, the unamortized portion of any expense is the amount remaining unamortized as of the first day of the 36-month period.

SEC. 202. ELECTION TO EXPENSE DELAY RENTAL PAYMENTS.

(a) IN GENERAL.—Section 263 of the Internal Revenue Code of 1986 (relating to capital expenditures), as amended by section 201(a), is amended by adding at the end the following new subsection:

"(k) DELAY RENTAL PAYMENTS FOR DOMESTIC OIL AND GAS WELLS.—

"(1) IN GENERAL.—Notwithstanding subsection (a), a taxpayer may elect to treat delay rental payments incurred in connection with the development of oil or gas within the United States (as defined in section 638) as payments which are not chargeable to capital account. Any payments so treated shall be allowed as a deduction in the taxable year in which paid or incurred.

"(2) DELAY RENTAL PAYMENTS.—For purposes of paragraph (1), the term 'delay rental payment' means an amount paid for the privilege of deferring development of an oil or gas well."

(b) CONFORMING AMENDMENT.—Section 263A(c)(3) of the Internal Revenue Code of 1986, as amended by section 201(b), is amended by inserting "263(k)," after "263(j),".

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to payments made or incurred after the date of the enactment of this Act.

(2) TRANSITION RULE.—In the case of any payments described in section 263(k) of the Internal Revenue Code of 1986, as added by this section, which were made or incurred on or before the date of the enactment of this Act, the taxpayer may elect, at such time and in such manner as the Secretary of the Treasury may prescribe, to amortize the unamortized portion of such payments over the 36-month period beginning with the month in which the date of the enactment of this Act occurs. For purposes of this paragraph, the unamortized portion of

any payment is the amount remaining unamortized as of the first day of the 36-month period.

SEC. 203. EXTENSION OF SPUDDING RULE.

(a) IN GENERAL.—Section 461(i)(2)(A) of the Internal Revenue Code of 1986 (relating to special rule for spudding of oil or gas wells) is amended by striking "90th day" and inserting "180th day".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1998.

SEC. 204. ENHANCED OIL RECOVERY CREDIT EXTENDED TO CERTAIN NONTERTIARY RECOVERY METHODS.

(a) IN GENERAL.—Clause (i) of section 43(c)(2)(A) of the Internal Revenue Code of 1986 (defining qualified enhanced oil recovery project) is amended to read as follows:

"(i) which involves the application (in accordance with sound engineering principles) of—

"(I) one or more tertiary recovery methods (as defined in section 193(b)(3)) which can reasonably be expected to result in more than an insignificant increase in the amount of crude oil which will ultimately be recovered, or

"(II) one or more nontertiary recovery methods which are required to recover oil with traditionally immobile characteristics or from formations which have proven to be uneconomical or noncommercial under conventional recovery methods."

(b) QUALIFIED NONTERTIARY RECOVERY METHODS.—Section 43(c)(2) of the Internal Revenue Code of 1986 is amended by adding at the end the following new subparagraphs:

"(C) QUALIFIED NONTERTIARY RECOVERY METHOD.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'qualified nontertiary recovery method' means any recovery method described in clause (ii), (iii), or (iv), or any combination thereof.

"(ii) ENHANCED GRAVITY DRAINAGE (EGD) METHODS.—The methods described in this clause are as follows:

"(I) HORIZONTAL DRILLING.—The drilling of horizontal, rather than vertical, wells to penetrate any hydrocarbon-bearing formation which has an average in situ calculated permeability to fluid flow of less than or equal to 12 or less millidarcies and which has been demonstrated by use of a vertical wellbore to be uneconomical unless drilled with lateral horizontal lengths in excess of 1,000 feet.

"(II) GRAVITY DRAINAGE.—The production of oil by gravity flow from drainholes that are drilled from a shaft or tunnel dug within or below the oil-bearing zone.

"(iii) MARGINALLY ECONOMIC RESERVOIR REPRESSURIZATION (MERR) METHODS.—The methods described in this clause are as follows, except that this clause shall only apply to the first 1,000,000 barrels produced in any project:

"(I) CYCLIC GAS INJECTION.—The increase or maintenance of pressure by injection of hydrocarbon gas into the reservoir from which it was originally produced.

"(II) FLOODING.—The injection of water into an oil reservoir to displace oil from the reservoir rock and into the bore of a producing well.

"(iv) OTHER METHODS.—Any method used to recover oil having an average laboratory measured air permeability less than or equal to 100 millidarcies when averaged over the productive interval being completed, or an in situ calculated permeability to fluid flow less than or equal to 12 millidarcies or oil defined by the Department of Energy as being immobile.

"(D) AUTHORITY TO ADD OTHER NONTERTIARY RECOVERY METHODS.—The Secretary shall provide procedures under which—

"(i) the Secretary may treat methods not described in clause (ii), (iii), or (iv) of subparagraph (C) as qualified nontertiary recovery methods, and

"(ii) a taxpayer may request the Secretary to treat any method not so described as a qualified nontertiary recovery method.

The Secretary may only specify methods as qualified nontertiary recovery methods under this subparagraph if the Secretary determines that such specification is consistent with the purposes of subparagraph (C) and will result in greater production of oil and natural gas."

(c) CONFORMING AMENDMENT.—Clause (iii) of section 43(c)(2)(A) of the Internal Revenue Code of 1986 is amended to read as follows:

"(iii) with respect to which—

"(I) in the case of a tertiary recovery method, the first injection of liquids, gases, or other matter commences after December 31, 1990, and

"(II) in the case of a qualified nontertiary recovery method, the implementation of the method begins after December 31, 1998."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years ending after December 31, 1998.

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