MINUTES

MONTANA HOUSE OF REPRESENTATIVES
54th LEGISLATURE - REGULAR SESSION

COMMITTEE ON TAXATION

Call to Order: By **CHAIRMAN CHASE HIBBARD**, on March 31, 1995, at 8:00 a.m.

ROLL CALL

Members Present:
Rep. Chase Hibbard, Chairman (R)
Rep. Marian W. Hanson, Vice Chairman (Majority) (R)
Rep. Robert R. "Bob" Ream, Vice Chairman (Minority) (D)
Rep. Peggy Arnott (R)
Rep. John C. Bohlinger (R)
Rep. Jim Elliott (D)
Rep. Daniel C. Fuchs (R)
Rep. Hal Harper (D)
Rep. Rick Jore (R)
Rep. Judy Murdock (R)
Rep. Thomas E. Nelson (R)
Rep. Scott J. Orr (R)
Rep. Bob Raney (D)
Rep. John "Sam" Rose (R)
Rep. William M. "Bill" Ryan (D)
Rep. Roger Somerville (R)
Rep. Robert R. Story, Jr. (R)
Rep. Emily Swanson (D)
Rep. Jack Wells (R)
Rep. Kenneth Wennemar (D)

Members Excused: None.

Members Absent: None.

Staff Present: Lee Heiman, Legislative Council
Donna Grace, Committee Secretary

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Committee Business Summary:
Hearing: SB 97
SB 219
SB 338
SB 390

Executive Action: None.

HEARING ON SB 97

Opening Statement by Sponsor:

SEN. MIKE FOSTER, Senate District 20, Townsend, stated that SB 97 addresses dependent care. Currently the statutes provide for a deduction for dependent care costs and SB 97 which change that to a tax credit of 25% of what can be claimed on the federal tax return. The statute is worthless because it is difficult to receive a deduction for child care. For the entire state, total deductions are approximately $60,000. A tax credit would assist young married couples and single parents. He called attention to the contingent voidness clause which had been added to the bill.

Proponents' Testimony:

None.

Opponents' Testimony:

None.

Questions From Committee Members and Responses:

REP. ELLIOTT asked if the minimal amount of child care deduction was because of the requirement to itemize deductions. **SEN. FOSTER** said that was the reason. By moving to a credit, it would not be necessary to itemize.

Bob Turner, Department of Revenue (DOR), without objection, explained that the reason the credit is not used is because, under the present deduction, the deduction must be reduced if the adjusted gross income is over $18,000 and if it is over $27,000, no deduction is given. At the federal level, the minimum is $480 and the maximum is $1,440 depending on the number of children. For Montana purposes the minimum would be $120 and the maximum would be a $350 credit.

REP. ROSE asked if the bill would conflict with the health care bill if it is passed. **SEN. FOSTER** said it would have no effect whatsoever.

CHAIRMAN HIBBARD asked what the $10,000 operating expense noted on the fiscal note was for. **Mr. Turner** said it was for one-time programming costs.

CHAIRMAN HIBBARD asked what would happen when the income level was insignificant and there would be nothing to deduct a credit from. **Mr. Foster** said the credit cannot be carried forward and the only way to get the credit would be if there is a tax liability. It is not a refund credit.

REP. STORY asked if this bill was included in the ending fund balance. **SEN. FOSTER** said it was not included because the bill had not been approved. It could affect the ending fund balance and that is why a contingent voidness amendment was added to the bill.

Closing by Sponsor:

SEN. FOSTER advised that there were proponents for the bill at the Senate hearing. He said the cost would be $3.2 million and he would have no objection if the 25% was adjusted to reduce the cost. He would like to see the bill passed to help young couples and single parents.

HEARING ON SB 219

Opening Statement by Sponsor:

SEN. STEVE DOHERTY, Senate District 24, Great Falls, said the bill initially had attempted to address a U.S. Supreme Court decision. Several years ago the Legislature passed legislation which said that individuals who possess dangerous drugs had to pay a property tax on them. Some folks up in the Fort Benton area decided to go into business raising "something other than wheat," were caught, and were subject to the property tax. Their attorneys took the case to the Supreme Court, saying that it placed them in double jeopardy because they were being punished criminally as well as civilly. In a 5 - 4 decision, the state lost. After a thorough consideration of the decision, SB 219 was drafted and comments were received from the Department of Revenue and the Department of Justice saying the bill was a good idea, but a wiser course would be to change the tax to a fine. The bill, as it has now been amended, would meet constitutionality tests.

Proponents' Testimony:

None.

Opponents' Testimony:

None.

Questions From Committee Members and Responses:

REP. SOMERVILLE asked why the amount of fine was set at 35%. **SEN. DOHERTY** said that was the amount that was in the original bill and would produce approximately the same amount of revenue as the tax.

REP. ROSE asked where the fine would go. **SEN. DOHERTY** said the fine would go directly into the general fund. Prior to the time the tax was declared unconstitutional, the DOR did collect about $100,000.

REP. NELSON said the bill refers to "market value" and he thought "street value" might be better language. **SEN. DOHERTY** replied that they are probably the same thing. The Court would have to determine the value.

REP. BOHLINGER asked what sort of revenue might be raised through the collection of the 35% fine. **SEN. DOHERTY** said it was a matter of "good news and bad news" because if the state is collecting a lot of money, it means there is a lot of activity. If less is collected, it means there is less activity. **Mr. Woodgerd, DOR Attorney,** advised that the $100,000 was collected over a period of six years. He said much more than that was assessed but never collected. Most people who are caught do not have much money.

REP. HARPER said the tax was reviewed during the last session and there was actually a net loss because the amount expended for collection was more than what was collected. He asked if it was worth the effort. **Mr. Woodgerd** said it was true that the expenditures were more than what was collected. That was one of the reasons they spoke with Sen. Doherty about changing the tax to a fine. There will be a minimal amount of extra effort involved in collection of the fine.

REP. HARPER asked if all that would have to be proven to have the fine assessed would be that the defendant was in possession of the drugs. **SEN. DOHERTY** said the person would have to be found guilty of possession.

{Tape: 1; Side: B.}

REP. BOHLINGER asked how vigorously the government could pursue the collection of the fine. If a person is found guilty of possessing and selling drugs, he asked if the government could take possession of all assets and dispose of them to meet the requirements of the bill. **SEN. DOHERTY** said it was his understanding that if an individual was caught, and there are any assets, they may be sold to pay the fine and any other costs. **REP. BOHLINGER** asked if the cost of prosecution under present law would be borne by the dealer because he can be assessed for the costs. **SEN. DOHERTY** said there are certain costs that can be assessed to recoup some money that would go to the Drug Task Force.

CHAIRMAN HIBBARD asked why it was easier to collect a fine than a property tax. **SEN. DOHERTY** said he had reviewed the Supreme Court decision and he thought it was a wrong decision. A better argument came from the minority that the state should have been able to collect the money as a property tax.

REP. ARNOTT noted that the fiscal note says "the bill will be challenged in court and there is a significant chance that the state will lose." **REP. DOHERTY** replied that the statement was the reason for the amended bill.

Closing by Sponsor:

REP. DOHERTY thanked the Committee for the hearing. He said the bill would not have the constitutional problem the previous legislation had.

HEARING ON SB 390

Opening Statement by Sponsor:

SEN. GREG JERGESON, Senate District 46, Chinook, said he was the chief sponsor of SB 390, a companion bill to HB 248 which has passed both houses of the Legislature. The bill would extend the time a drivers' license is valid from four to eight years and sets the fee for the eight-year license at $24. The bill is motorist-friendly because it will reduce the annual cost of a license.

Proponents' Testimony:

Brenda Nordlund, Department of Justice, said she would support SB 390. She said this was an opportune time to reduce the license fee in recognition of the fact that the term of the license would be extended. She pointed out that the bill coordinates with HB 248 and SB 83 which was the de-earmarking bill which changes the way state traffic education is funded.

Opponents' Testimony:

None.

Questions From Committee Members and Responses:

REP. HARPER said people's physical characteristics change considerably over a period of eight years. He asked if this would have any effect on safety. **SEN. JERGESON** said the issue had been discussed in the Senate because it was a major concern. He noted that family members, medical practitioners, or other people in contact with a driver can refer a person to the agency for review of their driving situation. **REP. ROSE** noted that this issue is covered by current law. **Ms. Nordlund** said the Department of Justice regularly receives requests from relatives, physicians and law enforcement officials for reevaluation of drivers. When a request is received, they investigate the validity of the request and, if valid, they proceed with the reevaluation which might include a road test, a knowledge test or a report from a physician on the condition of the driver. She noted that they do not accept anonymous requests.

At **REP. SWANSON'S** request, **SEN. JERGESON** explained the fiscal note. **Ms. Nordlund** explained how the traffic education program would be funded following the passage of SB 83.

{Tape: 2; Side: A.}

Closing by Sponsor:

SEN. JERGESON said he realized the issue was complicated but the basic premise is simple that, having made the decision to go with the eight-year drivers' license, they would not want to give the public the impression that they were being "gouged" by paying $32 for a license and, therefore, the fee was being reduced to $24.

HEARING ON SB 338

Opening Statement by Sponsor:

SEN. GREG JERGESON, Senate District 46, Chinook, opened the hearing by stating that in 1987 the Montana Legislature passed a 24-month holiday from state severance tax for new oil and gas production as an incentive to increase production. That legislation contained a trigger mechanism which said the incentive would sunset when the price of West Texas Crude reached a certain level. During the Gulf War there was spike in the price of oil and the ceiling established in the legislation was met and triggered an end to the incentive holiday. There was no mechanism in the legislation to restore the holiday when the price went back down. It was not anticipated that the price of oil would change because of a crises in world politics that would be temporary in nature. The purpose of SB 338 would be to restore the holiday because it is an to increase production of oil and gas in the State of Montana. The industry is currently in difficulty because commodity prices are low and it is important to maintain and encourage this vital industry. EXHIBIT 1.

Proponents' Testimony:

Pete Madison, Vice President, Entech Oil Division, testified in support of the bill. A copy of his testimony is attached. EXHIBIT 2.

Frank B. Haughton said he was a small independent who first identifies, with the help of a geologist, areas in Montana that warrant the drilling of a well and then acquires the necessary leases that puts money in the pockets of Montana mineral owners, and then raises the capital necessary to drill the wells. He indicated it was his firm belief that Montana has the potential for a very large undiscovered oil and gas reserve -- much larger than what remains in Texas, Oklahoma and some of the more developed areas. Because of the lack of money in Montana, he goes out of state to the oil centers to raise money from sizeable independent oil companies. It requires a tremendous amount of capital to drill a well and he assured the Committee that from his experience, the largest single hurdle to attracting money to Montana is the tax burden that is imposed on operators compared to that of surrounding states. He said Montana production has declined by 25% in the last five years and he had no doubt that passage of SB 338 would make Montana more competitive and turn that figure around.

Amy Nance Cebull, Director of Human Resources, Nance Petroleum Corp., Billings, strongly urged the Committee to support the passage of SB 338 which would provide an economic stimulus to the oil industry. A copy of her testimony is attached. EXHIBIT 3.

Les Fuglevand, Can-Am Drilling, Chinook, said his company provides drilling services to drilling rigs. He thanked the Committee for passing the horizontal drilling incentive in 1993. His company was a direct beneficiary of that legislation and he would urge the Committee to support SB 338. It makes good sense to extend incentives.

{Tape: 2; Side: B.}

Chip Youlden, JN Exploration and Production, said he was in favor of SB 338. It would help his company and the State of Montana by making Montana more competitive with the other oil and gas producing states and Canadian provinces in attracting investment capital and it would provide economic stimulation to the state, providing higher severance tax and more jobs. Montana has the highest taxes on oil and gas production of all the states. Implementation of this bill would create an incentive in Montana for the drilling of new wells and make the state more competitive. When commodity prices are low, they must look at the economics on each well they drill and passage of SB 338 would stimulate the economy.

Dennis Iverson, Northern Montana Oil and Gas Association, said oil and gas taxes are an extremely important part of the total tax revenue. Because of lower prices and lower production that revenue is declining. Nothing can be done about the price of oil but incentives can be given to encourage production. He said the bill was a good idea and he asked for the Committee's support.

Debbie Miller, Geophysicist, North American Resources, and **Past President, Billings Geophysicist Society,** spoke in support of SB 338. She said the geophysical industry is of ever increasing importance in exploration and development of oil and gas. In the last ten years major technological advances have been made which allow companies a clear picture for use in evaluation of a drilling site which increases the success rate. However, the technology is very expensive and does not get used unless it is an economically viable project. Therefore, SB 338, which is intended to generate activity in the drilling industry, would also increase seismic exploration in the state, bringing jobs and dollars to the state. She encouraged Committee Members to support the bill.

Gail Abercrombie, Executive Director, Montana Petroleum Association, provided copies of letters received in her office from counties, the Montana Association of Professional Landmen, oil and gas producers and others in support of SB 338. EXHIBIT 4. She also provided an illustration showing how the incentive would promote production. EXHIBIT 5. She asked the Committee to support the bill.

Greg Oblander, Montana Power, said SB 338 would make economics better in the state. He emphasized that the bill does not just provide an incentive to the oil and gas companies; it also provides economic opportunities for all the associated industries and would have a positive effect on the independent land managers, the geologists, dirt contractors, surveyors, drilling contractors, pipeline companies and many others. The legislation would have long-term positive effect on the State of Montana and he asked for the Committee's support.

Gloria Paladichuk, Richland Development Corp., said the horizontal drilling incentive had produced several new wells in her area. They must compete with North Dakota and are aware of the different taxing situation in the two states. The oil and gas industry is important to Richland County and the entire state. She encouraged the Committee to give positive support to the bill.

Jim Halverson, Association of Oil, Gas and Coal Counties, said the most potential for oil and gas production is in the eastern and north central parts of the state where the people are struggling with decreasing property values, fewer jobs and minimal business opportunities. It is difficult to entice new business into those areas because of the remoteness and limited access to transportation. Other than agriculture, the oil and gas industry has been the salvation of eastern Montana in the past and could be again in the future because the reserves are there. This incentive would encourage exploration and production. Because of the potential for jobs and oil and gas revenues, he said his association supports SB 338.

Jim Tutweiler, Montana Chamber of Commerce, said he would not argue the points of economic development, competitiveness or production incentives because they have all been well presented to the Committee. He said the Taxation Committee is of vital importance to the oil and gas industry because the entire industry is a product of international competition and the Committee does have control of some aspects such as the production cost mechanism. He said he hoped the Committee would favorably consider SB 338.

Rex Manuel, Cenex Petroleum Division, went on record in support of SB 338. EXHIBIT 6.

Jim Paladichuk read a statement in support of the legislation from **Dennis Haider, Vice President of Operations, Williston Basin Interstate Pipeline Company.** EXHIBIT 7.

Bill Vaughey, Havre, stated that he was an independent explorer for oil and gas and had been in Montana since 1968 and he strongly supports SB 338. He presented copies of his written testimony to Committee Members. EXHIBIT 8.

<u>Opponents' Testimony</u>:

None.

{Tape: 3; Side: A.}

<u>Questions From Committee Members and Responses</u>:

REP. ROSE asked what Montana would have to do to have as much development as Alberta has. **Mr. Madison** replied that they don't need to be as competitive with Alberta as they do with North Dakota, Wyoming and Colorado. Montana is closer to the market than Alberta is and there are three refineries in Billings that will process Montana's crude oil. The fact is that there isn't enough oil in Montana. All oil produced in Montana is processed in Montana. The companies need help in making their products competitive. They put their money where the best economics are. He advised that there are a total of 680 drilling rigs in the United States, 370 are running in Alberta, and only five or six are running in Montana. If that could be increased to what it was, 20 to 30 rigs, the oil industry would be back in Montana.

REP. BOHLINGER asked what the tax burden per barrel of oil in Alberta would be. **Mr. Madison** said it was very small, less than 1%. However, the province owns all the royalties and they are set at between 25% and 30%. When his company looks at economics, they look at royalties and taxes together and therefore Alberta is about the same as Montana. **REP. BOHLINGER** asked if Entech had taken advantage of the incentives provided by the special session. **Mr. Madison** said they had not because they do not have oil prospects in Montana that would lend themselves to horizontal drilling. He said there is no tax incentive for horizontal drilling for gas.

REP. ELLIOTT said that four years ago geologists who worked for the State of Montana had indicated that Montana was a played out field except for the Rocky Mountain Front. He asked if there were new areas that had been discovered. **Ms. Miller** said she was probably not the expert to discuss the issue, however, new technology has been utilized in finding new reservoirs very successfully in eastern Montana. There are small pools which are highly profitable. She identified other basins and said that Montana is not played out because there are a lot of areas where there has been no drilling.

REP. ELLIOTT said he had been told by oil economists that the greatest incentive for exploration would be a stable oil price. He asked if that was true. **Mr. Haughey** said that when the price goes up, it goes up everywhere, and they are trying to be competitive irrespective of the price of oil. **REP. ELLIOTT** said he understood one of the advantages of an incentive was in raising venture capital. **Mr. Haughey** agreed that it was.

REP. REAM asked he thought this bill would add new categories to the tax simplification bill. **Mr. Hoffman** said that was correct. **REP. REAM** asked what the relative fiscal impact of this bill would be. **Mr. Hoffman** explained that the tax rates. When the fiscal note was prepared, they analyzed what the impact would be for the 24-month holiday because it would amend current law by exempting new production from the severance tax for the first 24 months. The fiscal note is a full reflection of the 24-month holiday on the severance tax. **Mr. Hoffman** said this bill would amend SB 412 and coordination language is included. **REP. REAM** requested the DOR to furnish additional fiscal information.

REP. ARNOTT asked why more new wells were being drilled in North Dakota and Wyoming than there were in Montana. **Mr. Fuglevnd** said is was difficult to compare the number of wells because of the difference in drilling depths. **REP. ARNOTT** said a number of bills dealing with the oil industry had been introduced in the session and she would like to know which one would be the industry's preference. **Mr. Iverson** said the incentives help increase production and the simplification bill is necessary but what he would like would be to see the basic rates adjusted downward. **Ms. Abercrombie** said the only bills still alive were the stripper bill, the simplification bill, and the bill under discussion. She said they were all important.

REP. BOHLINGER asked for comments on the statement that only 5% of the reserves in Montana have been explored. **Mr. Youlden** said the figure had been provided by his exploration manager who has a great deal of experience. He also provided information on a previous question by stating that in 1993, the total number of wildcat wells drilled in Montana was 19, North Dakota had 35, Wyoming had 78 and Colorado had 99. **REP. BOHLINGER** noted that if only 5% of the reserves have been discovered, Montana has a very young field. He asked if the figure was low because of the tax burden. **Mr. Youlden** said the business is driven by the price of oil and natural gas and last year had the lowest price in ten years. Prices drive the economics on reserves. He did not believe it was totally the tax burden.

{Tape: 3; Side: B.}

REP. BOHLINGER asked Ms. Miller to comment on the state of Montana's oil reserves. **Ms. Miller** said there are several publications put out by the U.S.G.S. estimating the amount of reserves remaining and that is probably where the 5% figure came from. She said there are conventional and unconventional reservoirs. Horizontal drilling is not the normal method and is considered unconventional. Montana is different geologically from the neighboring states and it has a large mountainous area, the overthrust belt, that has a very deep frontal basin and a lot of people feel that the Rocky Mountain Front has a large reserve. There has been some drilling in Montana, but in Canada where the same geological formations exist, it has been estimated that there are three trillion cubic feet of gas. The bill would provide one more step in helping show that the economics are here. There are many kinds of issues that are being juggled by the industry all the time and if one is made a little better through the tax incentive, activity will be increased.

REP. SWANSON asked the representative from Meridian Oil to explain what the 1993 tax incentive had allowed them to do. **Mr. Kaleczyc** said SB 18 extended the local tax holiday to horizontal drilling, not from the state severance tax. SB 18 extended it for an additional six months for a horizontal well. SB 338 addresses state severance tax and not local taxes. The second component of SB 18 for secondary and tertiary recovery meant that if an oil company put new money into an existing field in order to develop the operation, there would be a decrease in the state severance tax. Senator Jergeson's bill will put back into law what would have been there had it not been for the price spike during the Gulf war. The bill will benefit mostly the small producers who are primarily doing vertical wells.

REP. ELLIOTT said Meridian and Shell were the two biggest players in Montana. He asked Mr. Kaleczyc if he was in favor of the bill. **Mr. Kaleczyc** said he was in favor of the bill and he did not testify because Meridian is a member of the Montana Petroleum Association and he did not wish to be redundant. **REP. ELLIOTT** said he thought it was unusual that one of the largest producers in the state did not testify in support of the bill. **REP. ELLIOTT** asked how Mr. Kaleczyc felt about horizontal wells being exempted. **Mr. Kaleczyc** said it would not be a good idea because, if the mix is changed in terms of the tax structure by excluding horizontal wells, the affect for the first 24 months of activity, there would be to create a lesser rate for a vertical well than a horizontal well and for a company like Meridian, looking at the tax structure, they might very well discontinue horizontal drilling in Montana. **REP. ELLIOTT** asked if he saw anything wrong with helping out the "little guy." **Mr. Kaleczyc** said he didn't see anything wrong with helping out all of the industry. Meridian is in support of Sen. Jergenson's bill, and they make business decisions every day, and one of the decisions would be where they would drill wells if they had a choice. Meridian operates in a number of states and if they are going to drill in Montana they will have to decide what kind of wells to drill. If vertical wells will produce a lower operating cost because of tax incentives, it changes the economic consideration and it might be to Meridian's advantage to drill a vertical well which would reverse the tax policy that the Legislature adopted in SB 18. **REP. ELLIOTT** asked if it was true that 85% of the production from a horizontal well was accomplished in the first 18 to 24 months. **Mr. Kaleczyc** said that might be true for some wells but it would not be true across the board. He said that was a rumor that circulated at one time during the consideration of SB 18. **REP. ELLIOTT** said it was not a rumor, there was documented evidence.

REP. ELLIOTT said he had heard testimony that the taxes on oil were lower in Wyoming and North Dakota than they were in Montana. He said it was his experience in speaking with the Commissioners in those states that the states are being "played off against one another by the oil industry." He asked if that was true. **Mr. Hoffman** said he had talked with officials in Wyoming about what was going on in the legislative arena and he had stated that what was going on in Montana was being discussed as part of legislative action in Wyoming. He said he could not speak for North Dakota.

REP. ROSE commented that he understood that 190,000 acres of land was under lease in Sheridan County at $20 an acre for a total of $3.8 million which is a large contribution to the economy of that county. He asked if that was correct. **Mr. Houghton** replied that he had been active in Sheridan County and during an 18-month period between mid-1993 and the end of 1994, there was just under 200,000 acres under lease in Sheridan County alone. **Mr. Houghton** pointed out that Daniels County is an unexplored county and, because of information which was the result of seismic technology, a company has now leased over 200,000 acres in that county, half of which is state land. They have made a significant discovery which is 50 miles from existing production in a remote area. Nine wells have been drilled, with seven producers.

REP. ROSE asked if information was available on royalties collected, and rents and bonuses paid on state school trust lands from oil leases. **Mr. Hoffman** replied that he could get that information.

REP. RANEY asked how long it would be before there would be rigs in the field if this bill was passed. **Mr. Iverson** said that the last time an incentive was given, the results were immediate and he would expect that to be the case now. **REP. RANEY** asked if it would be logical to place a sunset on the bill. **Mr. Iverson** said there is a sunset for each individual operator because the tax break is applicable for two years. **REP. RANEY** referred to the state's experience with the tax break given for coal. The tax was cut in half and it did not result in more production or more jobs. He said there should be a way to end the break if it does not work. **Mr. Iverson** said he was sure that there would be some impact from the bill in his part of the country. **REP. RANEY** suggested some alternatives, such as cutting the holiday to 12 months or cutting the tax in half. **Mr. Iverson** suggested that the Committee would want to take a good look at all the spinoffs that would occur before deciding to cut anything. For instance, on the average, one drilling rig operating one year in the state would produce $150,000 in salaries and there are many more positive impacts.

{Tape: 4; Side: A.}

REP. ARNOTT asked Mr. Madison if he wished to comment on the bill. **Mr. Madison** replied that his testimony had been misunderstood. He said Montana would be the winner if this bill is passed, not Entech. He said the bill should not be made into a "big guy, little guy" bill. He said his company doesn't need the help because they have more opportunities for their dollars than they do projects and the opportunities don't have to be in the State of Montana, but there are opportunities in Montana and what Montana needs to do is get the companies back, and drilling, in the state and, to do that, they must be competitive. Put a sunset on the bill and the companies will go right back to Alberta or Colorado. He also emphasized that the horizontal and vertical drilling should not be confused because they are totally different. Horizontal drilling is a development tool that is used for extracting more oil, faster, after the exploratory vertical well is producing. He said the problem is getting the dollars back into the state to make Montana a winner.

REP. HANSON asked what would happen if the Legislature does not give the tax incentive. **Mr. Iverson** stated that, historically, the independent companies have done most of the exploration in Montana and, without any help, they would leave the state.

REP. REAM asked what the average life of a well would be. **Mr. Hoffman** said he could not give any information on the horizontal wells because they are a very recent development. Wells drilled in the 30's and 40's continue to produce. What usually happens is the larger companies come in and develop an area and when it is no longer economic for them, they sell to the small independents who continue to operate because their objectives are different.

CHAIRMAN HIBBARD said the title of the bill says there is a 24-month exemption and, yet, the Committee has been talking about inserting a tax rate for the second 12 months. He asked if he was correct that only a certain tax was being exempted and the companies would still have some tax liability. **Mr. Hoffman** said this legislation is predicated on the fact that there is more than one tax -- the net proceeds tax of 7% on wells drilled after 1985, a 5% state severance tax, a .5% RIT tax, and a .2% privilege and license tax which adds up to 12.7% that comes on after all the holidays have ended. Under current law, there is a 12-month holiday from the 7% net proceeds tax and this bill would impose a 24-month holiday from the state severance tax. This is what is causing the confusion between one holiday and the other one. **CHAIRMAN HIBBARD** asked if the simplification bill was passed, whether there would still be a tax burden for the first and second year. **Mr. Hoffman** said that was correct. He said the chart that was handed out at the hearing on SB 412 did not reflect any of the bills that are in the legislative process.

CHAIRMAN HIBBARD asked why this bill did not have a contingent voidness amendment. **Mr. Hoffman** said his understanding was that the Senate felt these impacts were for activities that had not yet occurred.

__Closing by Sponsor__:

CHAIRMAN HIBBARD advised that Rep. Devaney had agreed to close the hearing in place of Sen. Jergenson who was involved in Senate floor debate on HB 2.

REP. CHARLES DEVANEY, House District 97, Plentywood, told the Committee he had agreed to close on this bill because he would be carrying the bill on the House floor. He reviewed the impacts the oil industry has on communities in Montana. An incentive can do much more than what is indicated in a fiscal note. He said he hoped the Committee would pass the bill to the House floor for debate.

ADJOURNMENT

Adjournment: 11:35 a.m.

Chase Hibbard

CHASE HIBBARD, Chairman

Donna Grace

DONNA GRACE, Secretary

CH/dg

HOUSE OF REPRESENTATIVES

Taxation

ROLL CALL DATE March 31, 1995

NAME	PRESENT	ABSENT	EXCUSED
Rep. Chase Hibbard, Chairman	✓		
Rep. Marian Hanson, Vice Chairman, Majority	✓		
Rep. Bob Ream, Vice Chairman, Minority	✓		
Rep. Peggy Arnott	✓		
Rep. John Bohlinger	✓		
Rep. Jim Elliott	✓		
Rep. Daniel Fuchs	✓		
Rep. Hal Harper	✓		
Rep. Rick Jore	✓		
Rep. Judy Rice Murdock	✓		
Rep. Tom Nelson	✓		
Rep. Scott Orr	✓		
Rep. Bob Raney	✓		
Rep. Sam Rose	✓		
Rep. Bill Ryan	✓		~~✓~~
Rep. Roger Somerville	✓		
Rep. Robert Story	✓		
Rep. Emily Swanson	✓		
Rep. Jack Wells	✓		
Rep. Ken Wennemar	✓		

EXHIBIT 1
DATE 3-31-95
~~HB~~ SB 338

Senate Bill 338

During the Special Session held in November of 1993 the Legislature enacted an incentive for the oil industry to drill horizontal wells, also included were some incentives for secondary and tertiary recovery projects. The incentive for horizontal wells drilled after 12/31/93 is an 18 month holiday from the 7% net proceeds tax. Therefore, under current law the production from horizontal wells is taxed at 5.7% for the first 18 months and then they are taxed at 12.7% thereafter.

SB 338 as now written provides a 24 month holiday from the 5% state severance tax for horizontal and vertical wells drilled after 3/31/95. Horizontally drilled wells would be taxed at .7% for the first 18 months of production, 5.7% after 18 months but less than 24 months, and 12.7% after 24 months.

During the hearing in the Senate Taxation Committee no testimony was given that the incentive in SB 338 would be in addition to the incentive granted in November of 1993 for horizontal wells. It is uncertain whether the members of the Committee, or the Senate as a whole realized they were granting additional incentives to horizontal wells.

However, any change in fiscal note would be minimal by excluding horizontal wells from SB 338, because we have limited production data on newly drilled horizontal wells. The fiscal note for the biennium shows a decrease of $1,264,000, which only includes about $80,000 for horizontal wells.

TESTIMONY OF R. P. MADISON

BEFORE THE MONTANA LEGISLATURE

ON SENATE BILL 338

My name is Pete Madison. I am Vice President of the Entech Oil Division. I appear in support of Senate Bill 338.

In my testimony here today I want to emphasize two points. First, we've got a fairly significant oil operator staffed by Montana people located right here in Butte and Billings. Second, this Montana oil company invests all its money outside of Montana.

Entech, Inc. is a subsidiary of the Montana Power Company. The Oil Division of Entech is involved in crude oil and natural gas exploration, production, and marketing activities - normally referred to as the "upstream" segment of the oil business. We operate in Alberta, Canada, in the Rocky Mountain states, Kansas, and Oklahoma.

The Entech Oil Division is based in Butte, Montana, where we employ 45 people directly. We have an exploration office in Billings with 10 employees. I was born and raised in Big Sandy and obtained my engineering degree from Montana State at Bozeman. My Montana background is typical of our 55 employees. Virtually all of us are Montana natives who have been educated in our Montana schools, primarily at Montana Tech.

In the past five years we have invested $208 million in drilling and related oil and gas production projects. The disappointing fact is that of the $208 million invested in the last five years, only $1.6 million or 8/10 of 1% was invested in the state of Montana.

In 1995 the Entech Oil Division has a capital budget of approximately $35 million and again, only a minimal amount will be invested in the state of Montana.

The obvious question is, ***"why does this independent oil and gas exploration and production company based in Butte, Montana and made up of Montana natives, educated in Montana schools, invest virtually all its capital in areas other than in Montana, specifically in Alberta, directly to the north and in Wyoming, Colorado, Kansas, and Oklahoma to the south?"***. The answer is that like most independent oil companies we have more projects, investment opportunities, than we do capital. We put our limited capital dollars in the best projects. To decide which projects are the best we run rigorous economic analyses. Then, all else being equal, we put our money in the projects that give us the greatest rate of return. The projects that are located in Montana are usually penalized by higher production taxes which moves Alberta and Wyoming projects ahead of them. At times, we are able to put incentives that some states or Alberta have in place at the time. Those incentives of course improve the economics and move those projects higher in the ranking. For example, several years ago we had some marginal oil development opportunities in Canada. The oil business in Canada was in the doldrums and to encourage activity, specifically in crude oil, the Alberta government put in place an incentive to encourage the drilling of oil wells. The incentive was a five year royalty holiday for new oil wells. In Alberta you don't have production taxes but you do have 25 to 30% royalty. That compares to Montana where we have roughly 12 1/2% royalty and 12 1/2 to 15% production taxes. So you can see that a five year royalty holiday in Alberta is a tremendous incentive. When we put that incentive in our economics for the Alberta projects, they moved to the top and we invested considerable amounts of our capital resources in Canada that year.

The point is that incentives do work. Incentives are not subsidies. They encourage investments. Incentives to me are a win/win situation. If we can be encouraged to invest drilling dollars in Montana, it's because those projects are the best place to put our drilling dollars. If we hit, the State wins because there is, of course, additional production that will produce royalties and production taxes after the incentives expire. I can testify that when Alberta put in the five-year royalty holiday for new oil wells, the drilling activity increased over night. In fact it became difficult to get a drilling rig because they were all busy. The recent horizontal drilling incentive that the special session authorized is another positive example of what incentives can do.

Lastly, I'd like to say something about oil and gas prices. I know you will hear testimony that says when oil and gas prices are low, incentives don't do any good and there won't be any drilling anyway but when prices come back the drilling dollars will follow regardless of incentives. My response is that if oil prices increase, they will increase in North Dakota, Wyoming, Colorado, and in Alberta too. Montana will be in the same position of having to compete for limited capital dollars with the states around us. It's a competitive game we're in and we need to find some edge that will help Montana compete for its share of the oil activity.

I believe that Senate Bill 338 is a good measure and a positive incentive that should lure some drilling dollars into Montana. The Entech Oil Division and its Montana employees prefer to drill in Montana rather than having to travel and invest in the states all around us. Please support Senate Bill 338.

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EXHIBIT 3
DATE 3/31/95
SB 338

Testimony - SB 338

Good morning, I am Amy Nance Cebull. I am a corporate director and director of Human Resources for Nance Petroleum Corporation in Billings. Our company is a small, family-owned independent oil and gas exploration and production company operating primarily in the Williston Basin of Eastern Montana and Western North Dakota. We have been in business in Montana since 1969 and employ about 20 people including petroleum engineers, geologists, geophysicists, land people and accounting staff.

We strongly urge this committee to support the passage of SB 338 which will give economic stimulus to the oil and gas business in this state.

Our business is a very high risk business -- it is a business where we are wrong more times than we are right. In deciding where to spend capital expenditure budget, we have to be very effective and cautious, and we have to spend our dollars in the most prudent manner possible. A stimulus such as SB 338 will allow Montana to compete with other states who are vying for the same dollars, and who already provide such incentives.

EXHIBIT 4 EXHIBIT ~~3~~ 4
DATE 3/31/95
SB 338

CURTIS C. MOXLEY
Commissioner

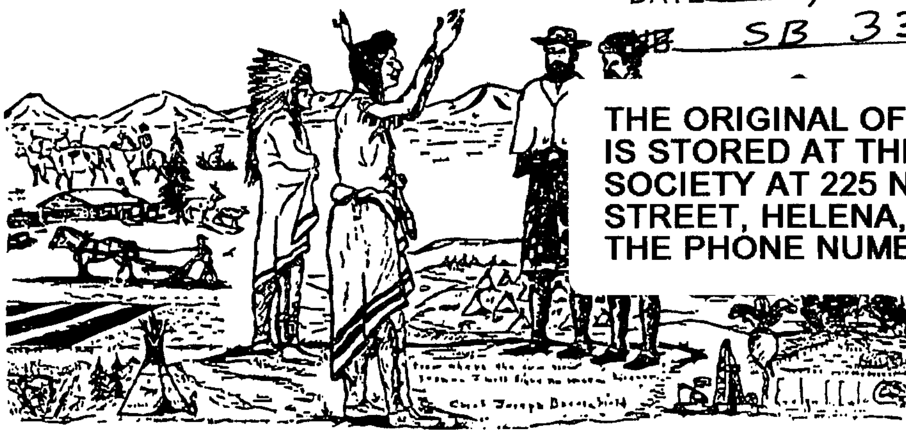
ARTHUR KLEINJAN
Commissioner

KEITH BENSON
Commissioner

SANDRA L. BOARDMAN
Clerk and Recorder/Assessor

SHIRLEY GRUBB
Treasurer

PERRY W. MILLER
Justice of Peace



THE ORIGINAL OF THIS DOCUMENT IS STORED AT THE HISTORICAL SOCIETY AT 225 NORTH ROBERTS STREET, HELENA, MT 59620-1201. THE PHONE NUMBER IS 444-2694.

JOHN C. MC KEON
District Judge

KAY O'BRIEN JOHNSON

MARVIN A. EDWARDS
Coroner

B.W. MC GUIRE
Justice of Peace

BLAINE COUNTY

Chinook, Montana 59523

TO: Chase Hibbard, Chair House Taxation Committee and all House Members

FROM: Blaine County Commissioners

RE: SB 338 Oil & gas new well incentive to establish a 24-month state severance tax holiday for oil & gas wells drilled after 3/31/95

DATE: March 29, 1995

Please convey our support for SB 338 to the House Taxation Committee. We feel this legislation would increase drilling and production in Montana, which increases tax revenue for the state and county.

There is also additional spin off for all businesses, which would be effected by this increase. We strongly urge the passage of this bill, it can only translate into increased revenue for government and private business.

Keith L Benson Chairman

Curtis C. Moxley Commissioner

Arthur Kleinjan Commissioner

EXHIBIT #5
DATE 3/31/95
SB 338

SB 338

REINSTATEMENT OF 24-MONTH STATE SEVERANCE TAX HOLIDAY FOR NEW OIL AND GAS PRODUCTION

ESTIMATED INCREASES IN REVENUES FROM NEW OIL & GAS ACTIVITIES

Drilling contractors anticipate a response in drilling activity of 10 to 25 additional rigs active in Montana per year. Property taxes, depending on the county, range from $10,000 for a shallow depth rated rig to $250,000 for a deep rig. Taking a conservative average of $15,000 per rig in property taxes and using the low end of the estimated response to the incentive, ten additional drilling rigs would bring in **$150,000 per year** in property taxes.

Payroll per day for a drilling rig is $2,500. Multiply that times the 10 added rigs and times the average 200 days per year that each rig is active, yields an annual payroll of $5 million. State income taxes at 5.3% bring in **$265,000 per year** to the state.

Motel rooms are budgeted at $250 per day for the rig hands. State accomodations taxes apply and would amount to **$20,000 per year** for the 200 days per year for the 10 rigs..

Other taxes and royalties accrue to the state from the first production. In 1994, the year following the passage of the horizontal drilling incentive, drilling permits for horizontal wells increased over 100 percent (21 in 1993; 46 in 1994). This is a good measure of the response to an incentive because the price of oil, although low, was static, and thus, a stable factor.

Using a very conservative assumption that increases in response to the reinstatement of the 24-month state severance tax holiday will be just half of the response to the horizontal incentive, a fifty percent increase will be assumed.

Using the production and price figures from the fiscal note and Board of Oil and Gas Conservation drilling permit information, a fifty percent increase in response to the new production incentive would bring to the state **$428,000 per year** in state royalties, in the state's share of federal royalties and in income taxes on royalties paid to private mineral owners.

The above figures equal **$863,000 per year**. Not calculated were the increases in income taxes for motel, restaurant and other ancillary services providers, nor were increased motor fuels taxes estimated. Also, not calculated were increased net proceeds taxes to the counties and schools.

With SB 338's incentive in place, any project we have in Montana will be much more attractive for our investment. In our 1995 capital budget of about $7 million, we are evaluating at least two deep tests in Roosevelt County and others in Western North Dakota each costing about $1 million. Naturally, we are going to be very careful of where we spend that money. Tax burdens per barrel of oil on our neighboring state of North Dakota are $.84, while Montana's are $1.70. Obviously, North Dakota is more attractive to drilling investment than Montana.

There are only 5 rigs running in Montana today, there should be considerably more. In the last ten years, employment in the oil and gas business in Montana has declined 72%, and revenue to state and local governments has declined 51% -- a $60 million loss. There is no reason why those dollars cannot come back into the economy if this state stimulates business.

Our company has been in Montana a long time, and we intend to stay longer assuming the business climate is conducive to growth. We are not asking for a subsidy or hand-out. We are asking for a stimulus that makes Montana competitive with other states in the Northern Rockies. Hopefully, passage of this bill help will revive a very important and core business in Montana. At least it is a beginning step in the right direction.

Thank you for your consideration and for the opportunity to give you our perspective.

EXHIBIT 6
DATE 3-31-95
~~HB~~ SB 338

CENEX

CENEX, Inc.
Exploration & Production Dept.
P. O. Box 80770
Billings, MT 59108-0770
(406)-655-6200
Fax: (406)-655-6250

March 28, 1995

The Honorable Chase Hibbard
Montana House of Representatives (Taxation Committee)
Capitol Station
Helena, MT 59620

RE: SB 338 - New Production Incentive

Dear Mr. Chairman:

Since 1946 CENEX has been a Montana oil producer with a history of exploration efforts. During 1994 we experienced the lowest crude oil price since 1979 and the industry is experiencing the lowest drilling rate in two decades.

SB 338 is designed to stimulate new drilling for new production to counter the downward trend. This effort has proven successful in other areas.

As a Montana operator, we urge your favorable consideration of SB 338.

Thank you.

Sincerely,

J. R. Keating
J. R. Keating
Vice President

JRK/jlb

2220 Grant Road, Suite 101
Billings, MT 59102-7430

E. HIBIT 7
DATE 3-31-95
~~HB~~ SB 338

WILLISTON BASIN
INTERSTATE PIPELINE COMPANY
A Subsidiary of MDU Resources Group, Inc.

Suite 300
200 North Third Street
Bismarck, ND 58501
(701) 221 1200

March 30, 1995

To: The House Taxation Committee
Montana House of Representatives

RE: SB 338 - NEW PRODUCTION INCENTIVE BILL

Williston Basin Interstate Pipeline Company is a significant producer of natural gas in the State of Montana, primarily from Phillips and Fallon Counties. Our company also has production in the State of North Dakota.

It is no understatement to mention that taxation plays an integral role in the economics of Williston Basin's short and long-range production development planning, particularly involving decisions on where to invest our production dollars. Existing production taxes between the States of North Dakota and Montana are significantly different at the present time. For example, at a wellhead price of $1.00 per thousand cubic feet for natural gas, the gross tax on production from a new well drilled in Montana would be nearly four times (4X) that of North Dakota's tax (after one year). At a price of $2.00 per thousand cubic feet, Montana's gross production tax would be nearly eight times (8X) that of North Dakota's tax on the same production, not to mention the ease and simplicity of applying the North Dakota tax.

While we are not a producer in the States of Wyoming and South Dakota or the Provinces of Alberta and Saskatchewan, through our business we are familiar with similar taxes and/or royalties disparities to Montana's. As not only a producer, but a transporter of gas product from various third party producers in the State of Montana, the competitive advantage provided to other governmental jurisdiction producers needs to be balanced, and bringing the tax situation into line is one way to do this.

Therefore, we are in support of Montana Senate Bill 338 with respect to new production incentives and urge your support of its passage. Not only will this provide an incentive for our company to potentially drill more wells in the State of Montana than originally planned (and resulting in providing benefits to the State of Montana that would not exist absent this incentive), but it will also send a positive signal to the natural gas industry, both in state and out of state, that is desperately needed to look at Montana for new production.

Again, we urge your support for SB 338 and thank you for your attention and consideration.

Respectfully,

Dennis L. Haider
Vice President - Operations

jaw

W. M. VAUGHEY, JR.
P.O. BOX 46
HAVRE, MONTANA 59501-0046
(406) 265-5421

EXHIBIT 8
DATE 3-31-95
~~HB~~ SB 338

March 2, 1995

The Honorable Chase Hibbard, Chairman
House Taxation Committee
Montana State House of Representatives
Capitol Station
Helena, MT 59620

RE: In strong support of Senate Bill 338 Oil and Gas New Well Incentive - Establishes a 24-month state severance tax holiday for oil or gas wells drilled after 3/31/95; includes wells not having produced for 5 years.

Dear Representative Hibbard:

I am an independent explorer for oil and gas with offices in Havre since 1968. For a number of years I was primarily a natural gas producer, that production coming from the Tiger Ridge Gas Field area here in Northcentral Montana. The above measure seeks to replace 1985 legislation which was lost, in a sense, on a fluke oil price spike which occurred in 1991.

The main thrust of my testimony in support of reinstating this law is as follows. During the period 1968-1985, I never even considered attempting to attract out-of-state investment dollars to drill wildcat tests in Montana. Our total tax burden on petroleum at the wellhead was then and is now the highest in the United States. Instead I just drilled gas tests with my longtime parnters here in Northcentral Montana.

However, the 1985 bill and a companion measure still on the books which gives a one-year tax holiday on the net proceeds tax for any newly-completed well changed the whole fact situation from my viewpoint. For the first time I began to look at Montana geological prospects. One generated by a group of Golden, Colorado, geologists struck my fancy. It related to oil in the Madison formation in Pondera and Teton counties. Based on a belief in that geology I went to Texas and attracted a number of investors in underwriting a wildcat program to test the Madison theory. As a result, seven blocks of oil and gas leases comprising nearly 20,000 acres were taken in 1989, and in the summer of 1990 five wildcat tests were drilled. Sad to say, the Madison geological theory was a "bust," and all five wildcats were dry. That fact notwithstanding, the whole program caused in excess of $400,000 to pass through the hands of Montanans.

While this is a small story in the setting of petroleum industry operations, many like it can be told--stories made possible by the predecessor of SB 338 being on the books for the period it was.

Montana's drastically low present exploration levels speak volumes to the need for reinstatement of this measure. I urge your Committee to give SB 338 a DO PASS recommendation.

Sincerely,

Bill

W. M. Vaughey, Jr.

WMV/blp

cc: All House Taxation Committee Members

HOUSE OF REPRESENTATIVES

VISITOR'S REGISTER

Taxation COMMITTEE BILL NO. SB 97

DATE 3/31/95 SPONSOR(S) Sen. Foster

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	BILL	OPPOSE	SUPPORT

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.

HOUSE OF REPRESENTATIVES

VISITOR'S REGISTER

Taxation COMMITTEE BILL NO. SB 219

DATE 3/31/95 SPONSOR(S) Sen Doherty

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	BILL	OPPOSE	SUPPORT

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.

HOUSE OF REPRESENTATIVES

VISITOR'S REGISTER

Taxation COMMITTEE BILL NO. SB 338

DATE 3/31/95 SPONSOR(S) Sen. Jergeson

PLEASE PRINT PLEASE PRINT PLEASE PRINT

STAN VALECZ-VC MERIDIAN OIL X

NAME AND ADDRESS	REPRESENTING	BILL	OPPOSE	SUPPORT
Frank B. Haughton Jr	Independent	338		✓
Chip Youlden	JN Exploration & Production	338		✓
BILL VAUGHEY	INDEP OIL & GAS PRODUCER	338		✓
JIM TUTWILER	MT CHAMBER	SB 338		✓
REX MANUEL	CENEX	SB 338		✓
Brian Cebull	Nance Petroleum	SB 338		✓
Amy Cebull	Nance Petroleum Corp.	SB 338		✓
DEBBIE MILLER	Billing Geophy. Soc.	SB 338		✓
Les Euglevand	CAN-AM Drilling Fluids	SB 338		✓
JIM HALVERSON	ASS - OIL-GAS-COAL CO	SB 338		X
DENNIS IVERSON	NMOGA	SB 338		✓
Jim PALADICHUK	WBIP	SB 338		✓
Pete MADISON	ENTECH MPA	SB 338		✓
Gloria Paladichuk	Richland Development	338		✓

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.

GAIL ABERCROMBIE MT Petroleum Assn SB 338 ✓

Greg Oblander MT Power SB 338 ✓

John D. [illegible] Beer, Rep [illegible] ✓

HOUSE OF REPRESENTATIVES

VISITOR'S REGISTER

Taxation COMMITTEE BILL NO. SB 390

DATE 3/31/95 SPONSOR(S) Sen. Jergeson

PLEASE PRINT PLEASE PRINT PLEASE PRINT

NAME AND ADDRESS	REPRESENTING	BILL	OPPOSE	SUPPORT
Brenda Nordlund	Dept of Justice	SB 390		X

PLEASE LEAVE PREPARED TESTIMONY WITH SECRETARY. WITNESS STATEMENT FORMS ARE AVAILABLE IF YOU CARE TO SUBMIT WRITTEN TESTIMONY.