

HOUSE BILL NO. 133

INTRODUCED BY HAYNE, IVERSON, D. BROWN, GILBERT, KEATING,  
REHBERG, GAGE, MEYER, ABRAMS, TVEIT, GERVAIS

IN THE HOUSE

JANUARY 12, 1989	INTRODUCED AND REFERRED TO COMMITTEE ON NATURAL RESOURCES.
	FIRST READING.
JANUARY 17, 1989	ON MOTION BY CHIEF SPONSOR, REPRESENTATIVES IVERSON, D. BROWN, GILBERT, REHBERG AND GERVAIS; AND SENATORS KEATING, GAGE, MEYER, ABRAMS, AND TVEIT ADDED AS SPONSORS.
JANUARY 30, 1989	COMMITTEE RECOMMEND BILL DO PASS AS AMENDED. REPORT ADOPTED.
JANUARY 31, 1989	PRINTING REPORT.
FEBRUARY 1, 1989	PASSED CONSIDERATION FOR THE DAY.
FEBRUARY 2, 1989	SECOND READING, DO PASS.
FEBRUARY 3, 1989	ENGROSSING REPORT.
FEBRUARY 4, 1989	THIRD READING, PASSED. AYES, 53; NOES, 46.
	TRANSMITTED TO SENATE.

IN THE SENATE

FEBRUARY 6, 1989	INTRODUCED AND REFERRED TO COMMITTEE ON NATURAL RESOURCES.
	FIRST READING.
MARCH 4, 1989	COMMITTEE RECOMMEND BILL BE CONCURRED IN. REPORT ADOPTED.
MARCH 6, 1989	SECOND READING, CONCURRED IN.

MARCH 8, 1989

THIRD READING, CONCURRED IN.  
AYES, 48; NOES, 1.

RETURNED TO HOUSE.

IN THE HOUSE

MARCH 9, 1989

RECEIVED FROM SENATE.

SENT TO ENROLLING.

REPORTED CORRECTLY ENROLLED.

1 HOUSE BILL NO. 133  
2 INTRODUCED BY Hayne  
3

4 A BILL FOR AN ACT ENTITLED: "AN ACT GENERALLY REVISING LAWS  
5 RELATING TO PAYMENT OF RENTALS, DELAY DRILLING PENALTIES,  
6 COMPENSATORY ROYALTIES, AND ROYALTIES ON STATE OIL AND GAS  
7 LEASES; ELIMINATING AUTHORITY TO TERMINATE LEASES IN THE  
8 ABSENCE OF DRILLING OR PAYMENT OF DELAY DRILLING PENALTIES;  
9 AMENDING SECTIONS 77-3-423, 77-3-425, 77-3-427, 77-3-432,  
10 AND 77-3-434, MCA; REPEALING SECTION 77-3-424, MCA; AND  
11 PROVIDING AN EFFECTIVE DATE."  
12

13 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

14 **Section 1.** Section 77-3-423, MCA, is amended to read:

15 "77-3-423. Annual rental. (1) The annual money rentals  
16 to be paid to the state for oil and gas leases issued on and  
17 after July 1, 1975, shall be set by the board but may not be  
18 less than \$1.50 for each acre of land leased.

19 (2) In addition to the sum of \$1.50 per acre, the  
20 rental for the first year of the lease shall also include  
21 any sum in excess of \$1.50 per acre offered and accepted for  
22 the first year's rental.

23 (3) This annual rental shall in no case be less than  
24 \$100 a year.

25 (4) The first year's rental shall be paid before the

1 issuance of the lease. The rentals for each subsequent year  
2 of the lease shall be due and payable before the beginning  
3 of such subsequent year, and upon failure to make such  
4 payment, the lease terminates unless there is a producing  
5 well on the lease. Rental paid for any year shall be  
6 credited against any royalty that accrues during that year."

7 **Section 2.** Section 77-3-425, MCA, is amended to read:

8 "77-3-425. Dry hole clause. If the first well drilled  
9 is a dry hole and if a second well is not commenced on the  
10 land covered by the lease before the next anniversary of the  
11 lease following the completion of the well, the lease may be  
12 terminated by the board unless the lessee, on or before such  
13 anniversary, ~~resumes--the--payments--of--penalties--in--the~~  
14 ~~amounts--provided--in--77-3-424--Upon--the--resumption--of--the~~  
15 ~~payment--of--such--delay--drilling--penalties--and--their--continued~~  
16 ~~payment,--the--lease--continues--in--force--during--the--primary~~  
17 ~~term--as--though--there--had--been--no--interruption--in--the--delay~~  
18 ~~drilling--penalty--payments~~ continues to pay an annual rental  
19 as set forth in 77-3-423."

20 **Section 3.** Section 77-3-427, MCA, is amended to read:

21 "77-3-427. Provision for offset wells -- compensatory  
22 royalties. (1) Oil and gas leases granted by the state shall  
23 contain suitable provisions imposing upon all lessees the  
24 obligation to drill offset wells wherever and whenever  
25 necessary to prevent waste and damage to the property of the

1 state.

2 (2) The board may allow the lessee the ~~option--of~~  
3 following options in lieu of drilling an offset well:

4 (a) releasing the lands in question; or

5 (b) paying a compensatory royalty on a nonproducing  
6 lease ~~in-lieu-of-drilling-an-offset-well~~ if it determines  
7 that such compensatory royalty will fully compensate the  
8 state for waste and damage to the property of the state. The  
9 compensatory royalty shall be based upon the estimated  
10 drainage, as determined by the board, and shall be paid on a  
11 monthly basis unless circumstances require otherwise."

12 **Section 4.** Section 77-3-432, MCA, is amended to read:

13 **"77-3-432. Royalty.** In every oil and gas lease granted  
14 by the state under this part and acts amendatory thereto,  
15 there shall be reserved to the state as consideration  
16 ~~therefor,--in--addition--to--the--rentals--as--hereinbefore~~  
17 ~~provided,~~ a royalty ~~in~~ on all oil and gas produced and saved  
18 from all lands covered thereby and not used for light, fuel,  
19 and operation purposes on the leased premises, which shall  
20 be equivalent to the full market value, as ascertained by  
21 the board at the date of such lease, of the estate or  
22 interest of the state in the lands and oil and gas deposits  
23 disposed of under such lease. Such royalty reservation shall  
24 be set by the board but may not be less than 12 1/2% on gas  
25 and not less than 12 1/2% on that portion of the average

1 production of oil or casinghead gasoline for each producing  
2 well not exceeding 3,000 barrels for the calendar month. The  
3 state may share the expense of transporting the oil to the  
4 nearest market on a basis proportional to the state's  
5 royalty interest in such oil and at a rate per mile  
6 acceptable to the department."

7 **Section 5.** Section 77-3-434, MCA, is amended to read:

8 **"77-3-434. Manner of making royalty payment.** Such A  
9 lease shall provide for the rendering of payment of such the  
10 royalty on all oil and gas produced and saved and sold or  
11 used off the premises in the following manner and upon the  
12 following terms:

13 (1) the lessee shall pay to the state in cash, for all  
14 oil and gas royalty reserved, the posted field price  
15 existing on the day such oil or gas is run into any pipeline  
16 or storage tank to the credit of the lessee, plus any bonus  
17 actually paid or agreed to be paid to the lessee for such  
18 oil or gas; or

19 (2) at the option of the state, exercised in writing  
20 by the board not ~~oftener~~ more frequently than every 30 days,  
21 the lessee shall deliver the state's royalty oil or gas free  
22 ~~of--cost--or--deductions~~ into the pipeline to which the wells  
23 of the lessee may be connected or into any storage  
24 designated by the state and connected with such wells."

25 NEW SECTION. **Section 6.** Repealer. Section 77-3-424,

1 MCA, is repealed.

2 NEW SECTION. **Section 7.** Extension of authority. Any  
3 existing authority to make rules on the subject of the  
4 provisions of [this act] is extended to the provisions of  
5 [this act].

6 NEW SECTION. **Section 8.** Effective date. [This act] is  
7 effective July 1, 1989.

-End-

## STATE OF MONTANA - FISCAL NOTE

Form BD-15

In compliance with a written request, there is hereby submitted a Fiscal Note for HB133, as introduced.

DESCRIPTION OF PROPOSED LEGISLATION:

HB 133 revises terms of state oil and gas leases, including payments of rentals, delay drilling penalties, and compensatory royalties. The bill proposes to drop lease rentals on producing leases, eliminate the non-drilling penalty that takes effect in the 6th through the 10th year of the lease, and allow the lessee to reduce the royalty with production costs and deductions. The bill also proposes to allow lessees to evade liability for drainage of the lease by offset wells drilled adjacent to the lease.

ASSUMPTIONS:

1. The number of acres leased is directly responsive to the price of oil.
2. The number of producing acres will remain constant at approximately 180,000 acres.
3. There will be continued drilling on tracts adjacent to state lands that may cause drainage of oil from state lands. Staffing requirements and workload will increase in order to detect and mitigate losses before they occur since this bill will eliminate the current ability to demand payment of past losses.
4. Oil field production and drilling will continue to cause long-term damage to state-owned surface acres. The state accepts annual rentals during production in lieu of assessed damages. Currently rentals are \$270,000 annually on producing leases.
5. In order to make oil and gas marketable, it is required to be processed and transported to market. The proposed bill will allow the lessee to deduct those costs from royalties. It is nearly impossible to determine reasonable costs and deductions. This bill would increase the need for accounting auditing and inspection staff to verify these costs.

FISCAL IMPACT:

<u>Expenditures:</u>	<u>FY90</u>			<u>FY91</u>		
	Current Law	Proposed Law	Difference	Current Law	Proposed Law	Difference
Personal Services	-0-	\$302,330	\$ 302,330	-0-	\$302,330	\$ 302,330
Operating Expenses	-0-	72,832	72,832	-0-	72,832	72,832
Equipment	-0-	15,000	15,000	-0-	-0-	-0-
	-0-	\$390,162	\$ 390,162	-0-	\$375,162	\$ 375,162
<u>Funding:</u>						
General Fund	-0-	\$390,162	\$ 390,162	-0-	\$375,162	\$ 375,162
<u>Revenue:</u>						
Trust Fund	\$270,000	-0-	(\$270,000)	\$270,000	-0-	(\$270,000)

*Ray Shackleford* 1/19/89  
 RAY SHACKLEFORD, BUDGET DIRECTOR DATE  
 OFFICE OF BUDGET AND PROGRAM PLANNING

*Harriet Hayne* 1/28/89  
 HARRIET HAYNE, PRIMARY SPONSOR DATE

Fiscal Note for HB133, as introduced

**HB 133**

~~Fiscal Note Request, HB133 as introduced~~

Form BD-15

Page 2

LONG-RANGE EFFECTS OF PROPOSED LEGISLATION:

1. If the legislation is passed, the trust will lose \$500,000 in 1994 and annually thereafter because of the elimination of the delayed drilling penalty.
2. Current bonuses, rentals and delay penalties are at their lowest level in a decade. When oil prices rise, there will be a proportional rebound in leasing activity and an increase in revenues regardless of the terms of the state leases. The amount and time of this occurrence is difficult to predict but is inevitable considering national dependence upon hydrocarbons.

**HB 133**

## STATE OF MONTANA - FISCAL NOTE

Form BD-15

In compliance with a written request, there is hereby submitted a Fiscal Note for HB133, Second Reading.

DESCRIPTION OF PROPOSED LEGISLATION:

HB133 revises terms of state oil and gas leases, including payments of rentals, delay drilling penalties and compensatory royalties. The bill proposes to drop lease rentals on producing leases and provide for refund of delay drilling penalties for years in which drilling occurs.

ASSUMPTIONS:

1. The number of acres leased is directly responsive to the price of oil.
2. Oil field production and drilling will continue to cause long-term damage to state-owned surface acres. The state accepts annual rentals during production in lieu of assessed damages under current law. These rentals currently are \$270,000 annually on producing leases.
3. Due to proposed law lost rentals on producing leases, DSL will lose income at the rate of \$27,000 in FY92, \$36,000 in FY93, \$45,000 in FY94 and additional losses of \$9,000 per year thereafter until the current income level of \$270,000 per year is reached.
4. DSL will have to inspect and assess all damages associated with drilling and production on new leases. This will require 0.50 FTE and related operating expenses in FY90 and 1.00 FTE and operating expenses in FY91 and thereafter.
5. The number of new wells will be approximately 15 per year, which is the 1988 level, and the average lease containing new wells will be approximately 400 acres.
6. Damage payments recovered by field assessment will reimburse the trust fully for actual damage done, and will improve the condition of trust lands by enforcing clean-up and reclamation.
7. In 1994, 40% of the wells drilled will be leases held 6 through 10 years and delayed drilling penalties will be refunded for any year in which a well is drilled.
8. Due to refunded delayed drilling penalties, DSL will lose \$3,000 in FY94, \$6,000 in FY95, and \$6,000 per year thereafter, based on 15 new wells per year x 40% x 400 acres x \$1.25 = \$3,000 in FY94 for year 6 of the lease, and a rate of \$2.50 for years 7 through 10.

FISCAL IMPACT:Expenditures:

	Current	FY90		Current	FY91	
	Law	Proposed	Difference	Law	Proposed	Difference
Dept. of State Lands	-0-	Law		-0-	Law	
Personal Services	-0-	\$12,500	\$12,500	-0-	\$25,000	\$25,000
Operating Expenses	-0-	1,750	1,750	-0-	3,500	3,500
Equipment	-0-	15,000	15,000	-0-	-0-	-0-
Total	-0-	\$29,250	\$29,250	-0-	\$28,500	\$28,500

Funding:

General Fund	-0-	\$29,250	\$29,250	-0-	\$28,500	\$28,500
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Revenues:

Trust Fund	\$270,000	\$270,000	-0-	\$270,000	\$270,000	-0-
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*Ray Shackelford*

2/1/89

RAY SHACKLEFORD, BUDGET DIRECTOR DATE  
OFFICE OF BUDGET AND PROGRAM PLANNING

*Harriet Hayne*

HARRIET HAYNE, PRIMARY SPONSOR

DATE

Fiscal Note for HB133, on second reading

**HB 133-Second  
Reading**



LONG-RANGE EFFECTS OF PROPOSED LEGISLATION:

In FY92 the lost trust revenue will be \$27,000 and this will accelerate to \$270,000. Damage payments and the improved condition of state lands will act as an offset to the lost rentals.

**HB 133**

APPROVED BY COMM. ON BUSINESS  
AND ECONOMIC DEVELOPMENT

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REHBERG, GAGE, MEYER, ABRAMS, TVEIT, GERVAIS

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COMPENSATORY ROYALTIES, AND ROYALTIES ON STATE OIL AND GAS  
LEASES; ~~ELIMINATING AUTHORITY TO TERMINATE LEASES IN THE~~  
~~ABSENCE OF DRILLING OR PAYMENT OF DELAY DRILLING PENALTIES;~~  
PROVIDING FOR REFUND OF DELAY DRILLING PENALTIES FOR YEARS  
IN WHICH DRILLING OCCURS; AMENDING SECTIONS 77-3-423,  
THROUGH 77-3-425, 77-3-427, AND 77-3-432, AND 77-3-434, MCA;  
~~REPEALING SECTION 77-3-424, MCA; AND PROVIDING AN EFFECTIVE~~  
DATE AND AN APPLICABILITY DATE."

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any sum in excess of \$1.50 per acre offered and accepted for  
the first year's rental.

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issuance of the lease. The rentals for each subsequent year  
of the lease shall be due and payable before the beginning  
of such subsequent year, and upon failure to make such  
payment, the lease terminates unless there is a producing  
well on the lease. Rental paid for any year shall be  
credited against any royalty that accrues during that year."

**Section 2.** Section 77-3-425, MCA, is amended to read:

"77-3-425. Dry hole clause. If the first well drilled  
is a dry hole and if a second well is not commenced on the  
land covered by the lease before the next anniversary of the  
lease following the completion of the well, the lease may be  
terminated by the board unless the lessee, on or before such  
anniversary, ~~resumes the payments of penalties in the~~  
~~amounts provided in 77-3-424. Upon the resumption of the~~  
~~payment of such delay drilling penalties and their continued~~  
~~payment, the lease continues in force during the primary~~  
~~term as though there had been no interruption in the delay~~  
~~drilling penalty payments continues to pay an annual rental~~  
as set forth in 77-3-423 RESUMES PAYMENT OF ANY DELAY  
DRILLING PENALTIES IMPOSED BY THE BOARD. UPON THE  
RESUMPTION OF PAYMENT OF ANY REQUIRED DELAY DRILLING  
PENALTIES AND THEIR CONTINUED PAYMENT, THE LEASE CONTINUES

1 IN FORCE DURING THE PRIMARY TERM AS THOUGH THERE HAD BEEN NO  
 2 INTERRUPTION IN THE DELAY DRILLING PENALTY PAYMENTS."

3 **Section 3.** Section 77-3-427, MCA, is amended to read:

4 "77-3-427. Provision for offset wells -- compensatory  
 5 royalties. (1) Oil and gas leases granted by the state shall  
 6 contain suitable provisions imposing upon all lessees the  
 7 obligation to drill offset wells wherever and whenever  
 8 necessary to prevent waste and damage to the property of the  
 9 state.

10 (2) The board may allow the lessee the ~~option of~~  
 11 following options in lieu of drilling an offset well:

12 (a) releasing the lands in question; or

13 (b) paying a compensatory royalty on a nonproducing  
 14 lease in--lieu--of--drilling-an-offset-well if it THE BOARD  
 15 determines that such compensatory royalty will fully  
 16 compensate the state for waste and damage to the property of  
 17 the state. The compensatory royalty shall be based upon the  
 18 estimated drainage, as determined by the board, and shall be  
 19 paid on a monthly basis unless circumstances require  
 20 otherwise.

21 (3) IF THE BOARD OR THE LESSEE TERMINATES THE LEASE,  
 22 THAT TERMINATION DOES NOT IMPAIR ANY IMPLIED COVENANT  
 23 AGAINST DRAINAGE OR THE RIGHT OF THE BOARD TO SEEK DAMAGES  
 24 FROM THE LESSEE FOR THE LESSEE'S FAILURE TO PROTECT THE  
 25 LEASE FROM DRAINAGE OF OIL OR GAS BY A WELL ADJACENT TO THE

1 STATE LEASE."

2 **Section 4.** Section 77-3-432, MCA, is amended to read:

3 "77-3-432. Royalty. In every oil and gas lease granted  
 4 by the state under this part and acts amendatory thereto,  
 5 there shall be reserved to the state as consideration  
 6 therefor,---in--addition--to--the--rentals--as--hereinbefore  
 7 provided, a royalty in on IN all oil and gas produced and  
 8 saved from all lands covered thereby and not used for light,  
 9 fuel, and operation purposes on the leased premises, which  
 10 shall be equivalent to the full market value, as ascertained  
 11 by the board at the date of such lease, of the estate or  
 12 interest of the state in the lands and oil and gas deposits  
 13 disposed of under such lease. Such royalty reservation shall  
 14 be set by the board but may not be less than 12 1/2% on gas  
 15 and not less than 12 1/2% on that portion of the average  
 16 production of oil or casinghead gasoline for each producing  
 17 well not exceeding 3,000 barrels for the calendar month. The  
 18 state may share the expense of transporting the oil to the  
 19 nearest market on a basis proportional to the state's  
 20 royalty interest in such oil and at a rate per mile  
 21 acceptable to the department."

22 **Section 5.** ~~Section 77-3-434, MCA, is amended to read:~~

23 ~~"77-3-434. Manner of making royalty payment. Such A~~  
 24 ~~lease shall provide for the rendering of payment of such the~~  
 25 ~~royalty on all oil and gas produced and saved and sold or~~

1 used--off--the-premises-in-the-following-manner-and-upon-the  
2 following-terms:

3 {1}--the-lessee-shall-pay-to-the-state-in-cash,-for-all  
4 oil--and--gas--royalty--reserved,-the--posted--field--price  
5 existing-on-the-day-such-oil-or-gas-is-run-into-any-pipeline  
6 or--storage-tank-to-the-credit-of-the-lessee,-plus-any-bonus  
7 actually-paid-or-agreed-to-be-paid-to-the--lessee--for--such  
8 oil-or-gas,-or

9 {2}--at--the--option-of-the-state, exercised-in-writing  
10 by-the-board-not-oftener more-frequently than-every-30-days,-  
11 the-lessee-shall-deliver-the-state's-royalty-oil-or-gas free  
12 of-cost-or-deductions into-the-pipeline-to-which--the--wells  
13 of---the--lessee--may--be--connected--or--into--any--storage  
14 designated-by-the-state-and-connected-with-such-wells."

15 NEW SECTION. --Section 6. Repealer. --Section --77-3-424,  
16 MCA, is repealed.

17 SECTION 5. SECTION 77-3-424, MCA, IS AMENDED TO READ:

18 "77-3-424. Power to terminate lease in absence of  
19 commencement of drilling or payment of delay drilling  
20 penalty. (1) In every oil and gas lease granted after March  
21 3, 1955, under this part there shall must be reserved to the  
22 board full power to declare termination of the lease at the  
23 end of the fifth year or any subsequent year of the primary  
24 term of the lease upon failure of the lessee to either:

25 (a) commence the drilling of a well for oil and gas

1 upon the leased premises; or

2 (b) pay a delay drilling penalty as follows:

3 (i) for the sixth year of the lease \$1.25 per acre per  
4 year; and

5 (ii) for the remainder of the primary term of the lease  
6 an amount per acre per year as the board may in its  
7 discretion determine.

8 (2) Notice of that determination shall must be given  
9 to the lessee, and if the lessee applies for a hearing  
10 thereon within 10 days after receipt of the notice, the  
11 determination shall-become becomes final only after such the  
12 hearing has been held.

13 (3) This annual delay drilling penalty shall must be  
14 paid each year in advance. The board shall refund delay  
15 drilling penalties paid on a lease for any year in which the  
16 lessee commences drilling on that lease.

17 (4) If a well for oil and gas is commenced, the  
18 drilling of the well shall must be prosecuted with due  
19 diligence and dispatch to such depth as is necessary to make  
20 a reasonable test for oil or gas."

21 NEW SECTION. Section 6. Extension of authority. Any  
22 existing authority to make rules on the subject of the  
23 provisions of [this act] is extended to the provisions of  
24 [this act].

25 NEW SECTION. SECTION 7. APPLICABILITY. [THIS ACT]

HB 0133/02

1 APPLIES TO ALL LEASES ENTERED INTO AFTER [THE EFFECTIVE DATE  
2 OF THIS ACT].

3 NEW SECTION. **Section 8.** Effective date. [This act] is  
4 effective July 1, 1989.

-End-

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22 THAT TERMINATION DOES NOT IMPAIR ANY IMPLIED COVENANT  
23 AGAINST DRAINAGE OR THE RIGHT OF THE BOARD TO SEEK DAMAGES  
24 FROM THE LESSEE FOR THE LESSEE'S FAILURE TO PROTECT THE  
25 LEASE FROM DRAINAGE OF OIL OR GAS BY A WELL ADJACENT TO THE

1 STATE LEASE."

2 **Section 4.** Section 77-3-432, MCA, is amended to read:

3 "77-3-432. Royalty. In every oil and gas lease granted  
4 by the state under this part and acts amendatory thereto,  
5 there shall be reserved to the state as consideration  
6 therefor, ~~in addition to the rentals as hereinbefore~~  
7 ~~provided,~~ a royalty in on ~~IN~~ all oil and gas produced and  
8 saved from all lands covered thereby and not used for light,  
9 fuel, and operation purposes on the leased premises, which  
10 shall be equivalent to the full market value, as ascertained  
11 by the board at the date of such lease, of the estate or  
12 interest of the state in the lands and oil and gas deposits  
13 disposed of under such lease. Such royalty reservation shall  
14 be set by the board but may not be less than 12 1/2% on gas  
15 and not less than 12 1/2% on that portion of the average  
16 production of oil or casinghead gasoline for each producing  
17 well not exceeding 3,000 barrels for the calendar month. The  
18 state may share the expense of transporting the oil to the  
19 nearest market on a basis proportional to the state's  
20 royalty interest in such oil and at a rate per mile  
21 acceptable to the department."

22 ~~Section 5. Section 77-3-434, MCA, is amended to read:~~

23 ~~"77-3-434. Manner of making royalty payment. Such a~~  
24 ~~lease shall provide for the rendering of payment of such the~~  
25 ~~royalty on all oil and gas produced and saved and sold or~~

1 used--off--the-premises-in-the-following-manner-and-upon-the  
2 following-terms:

3 (1)--the-lessee-shall-pay-to-the-state-in-cash, for all  
4 oil--and--gas--royalty--reserved,--the--posted--field--price  
5 existing-on-the-day-such-oil-or-gas-is-run-into-any-pipeline  
6 or--storage-tank-to-the-credit-of-the-lessee, plus-any-bonus  
7 actually-paid-or-agreed-to-be-paid-to-the-lessee--for--such  
8 oil-or-gas; or

9 (2)--at--the--option-of-the-state, exercised-in-writing  
10 by-the-board-not-oftener more-frequently than-every-30-days,  
11 the-lessee-shall-deliver-the-state's-royalty-oil-or-gas free  
12 of-cost-or-deductions into-the-pipeline-to-which--the--wells  
13 of---the--lessee--may--be--connected--or--into--any--storage  
14 designated-by-the-state-and-connected-with-such-wells."

15 ~~NEW SECTION. Section 6. Repealer. Section 77-3-424,~~  
16 ~~MCA, is repealed.~~

17 SECTION 5. SECTION 77-3-424, MCA, IS AMENDED TO READ:

18 "77-3-424. Power to terminate lease in absence of  
19 commencement of drilling or payment of delay drilling  
20 penalty. (1) In every oil and gas lease granted after March  
21 3, 1955, under this part there shall must be reserved to the  
22 board full power to declare termination of the lease at the  
23 end of the fifth year or any subsequent year of the primary  
24 term of the lease upon failure of the lessee to either:

25 (a) commence the drilling of a well for oil and gas

1 upon the leased premises; or

2 (b) pay a delay drilling penalty as follows:

3 (1) for the sixth year of the lease \$1.25 per acre per  
4 year; and

5 (ii) for the remainder of the primary term of the lease  
6 an amount per acre per year as the board may in its  
7 discretion determine.

8 (2) Notice of that determination shall must be given  
9 to the lessee, and if the lessee applies for a hearing  
10 thereon within 10 days after receipt of the notice, the  
11 determination shall-become becomes final only after such the  
12 hearing has been held.

13 (3) This annual delay drilling penalty shall must be  
14 paid each year in advance. The board shall refund delay  
15 drilling penalties paid on a lease for any year in which the  
16 lessee commences drilling on that lease.

17 (4) If a well for oil and gas is commenced, the  
18 drilling of the well shall must be prosecuted with due  
19 diligence and dispatch to such depth as is necessary to make  
20 a reasonable test for oil or gas."

21 NEW SECTION. Section 6. Extension of authority. Any  
22 existing authority to make rules on the subject of the  
23 provisions of [this act] is extended to the provisions of  
24 [this act].

25 NEW SECTION. SECTION 7. APPLICABILITY. (THIS ACT)



HB 0133/02

1 APPLIES TO ALL LEASES ENTERED INTO AFTER [THE EFFECTIVE DATE  
2 OF THIS ACT].  
3 NEW SECTION. Section 8. Effective date. [This act] is  
4 effective July 1, 1989.

-End-

## HOUSE BILL NO. 133

INTRODUCED BY HAYNE, IVERSON, D. BROWN, GILBERT, KEATING.

REHBERG, GAGE, MEYER, ABRAMS, TVEIT, GERVAIS

A BILL FOR AN ACT ENTITLED: "AN ACT GENERALLY REVISING LAWS RELATING TO PAYMENT OF RENTALS, DELAY DRILLING PENALTIES, COMPENSATORY ROYALTIES, AND ROYALTIES ON STATE OIL AND GAS LEASES; ~~ELIMINATING AUTHORITY TO TERMINATE LEASES IN THE ABSENCE OF DRILLING OR PAYMENT OF DELAY DRILLING PENALTIES; PROVIDING FOR REFUND OF DELAY DRILLING PENALTIES FOR YEARS IN WHICH DRILLING OCCURS; AMENDING SECTIONS 77-3-423, THROUGH 77-3-425, 77-3-427, AND 77-3-432, AND 77-3-434, MCA; REPEALING SECTION 77-3-424, MCA; AND PROVIDING AN EFFECTIVE DATE AND AN APPLICABILITY DATE.~~"

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

Section 1. Section 77-3-423, MCA, is amended to read:

"77-3-423. Annual rental. (1) The annual money rentals to be paid to the state for oil and gas leases issued on and after July 1, 1975, shall be set by the board but may not be less than \$1.50 for each acre of land leased.

(2) In addition to the sum of \$1.50 per acre, the rental for the first year of the lease shall also include any sum in excess of \$1.50 per acre offered and accepted for the first year's rental.

(3) This annual rental shall in no case be less than \$100 a year.

(4) The first year's rental shall be paid before the issuance of the lease. The rentals for each subsequent year of the lease shall be due and payable before the beginning of such subsequent year, and upon failure to make such payment, the lease terminates unless there is a producing well on the lease. Rental paid for any year shall be credited against any royalty that accrues during that year."

Section 2. Section 77-3-425, MCA, is amended to read:

"77-3-425. Dry hole clause. If the first well drilled is a dry hole and if a second well is not commenced on the land covered by the lease before the next anniversary of the lease following the completion of the well, the lease may be terminated by the board unless the lessee, on or before such anniversary, ~~resumes the payments of penalties in the amounts provided in 77-3-424. Upon the resumption of the payment of such delay drilling penalties and their continued payment, the lease continues in force during the primary term as though there had been no interruption in the delay drilling penalty payments~~ continues to pay an annual rental as set forth in 77-3-423 RESUMES PAYMENT OF ANY DELAY DRILLING PENALTIES IMPOSED BY THE BOARD. UPON THE RESUMPTION OF PAYMENT OF ANY REQUIRED DELAY DRILLING PENALTIES AND THEIR CONTINUED PAYMENT, THE LEASE CONTINUES

1 IN FORCE DURING THE PRIMARY TERM AS THOUGH THERE HAD BEEN NO  
2 INTERRUPTION IN THE DELAY DRILLING PENALTY PAYMENTS."

3 **Section 3.** Section 77-3-427, MCA, is amended to read:

4 "77-3-427. Provision for offset wells -- compensatory  
5 royalties. (1) Oil and gas leases granted by the state shall  
6 contain suitable provisions imposing upon all lessees the  
7 obligation to drill offset wells wherever and whenever  
8 necessary to prevent waste and damage to the property of the  
9 state.

10 (2) The board may allow the lessee the option-of  
11 following options in lieu of drilling an offset well:

12 (a) releasing the lands in question; or

13 (b) paying a compensatory royalty on a nonproducing  
14 lease in--lieu--of--drilling-an-offset-well if it THE BOARD  
15 determines that such compensatory royalty will fully  
16 compensate the state for waste and damage to the property of  
17 the state. The compensatory royalty shall be based upon the  
18 estimated drainage, as determined by the board, and shall be  
19 paid on a monthly basis unless circumstances require  
20 otherwise.

21 (3) IF THE BOARD OR THE LESSEE TERMINATES THE LEASE,  
22 THAT TERMINATION DOES NOT IMPAIR ANY IMPLIED COVENANT  
23 AGAINST DRAINAGE OR THE RIGHT OF THE BOARD TO SEEK DAMAGES  
24 FROM THE LESSEE FOR THE LESSEE'S FAILURE TO PROTECT THE  
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8 saved from all lands covered thereby and not used for light,  
9 fuel, and operation purposes on the leased premises, which  
10 shall be equivalent to the full market value, as ascertained  
11 by the board at the date of such lease, of the estate or  
12 interest of the state in the lands and oil and gas deposits  
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15 and not less than 12 1/2% on that portion of the average  
16 production of oil or casinghead gasoline for each producing  
17 well not exceeding 3,000 barrels for the calendar month. The  
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or--storage-tank-to-the-credit-of-the-lessee,--plus-any-bonus  
actually-paid-or-agreed-to-be-paid-to-the--lessee--for--such  
oil-or-gas; or

(2)--at--the--option-of-the-state, exercised-in-writing  
by-the-board-not-oftener more-frequently than-every-30-days,  
the-lessee-shall-deliver-the-state's-royalty-oil-or-gas free  
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end of the fifth year or any subsequent year of the primary  
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upon the leased premises; or

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year; and

(ii) for the remainder of the primary term of the lease  
an amount per acre per year as the board may in its  
discretion determine.

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to the lessee, and if the lessee applies for a hearing  
thereon within 10 days after receipt of the notice, the  
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HB 0133/02

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- 2 OF THIS ACT].
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-End-