

October 7, 2004

North Dakota Oil Producers and Purchasers:

RE: Oil Extraction Tax Price Trigger

North Dakota Century Code (N.D.C.C.) § 57-51.1-02 establishes an oil extraction tax at a rate of 6.5% and subsequently N.D.C.C. §§ 57-51.1-02 and 57-51.1-03 provide incentives for rate reductions and exemptions for various qualifying wells and projects located within the state of North Dakota. These code sections also contain what is referred to as a “trigger” provision that specifically inactivates some of the incentives if the average price of a barrel of crude oil exceeds the trigger price for each month in any consecutive five-month period, and reinstates the incentives if the average price of a barrel of crude oil is less than the trigger price for each month in any consecutive five-month period.

The “average price of a barrel of crude oil” referenced in N.D.C.C. §§ 57-51.1-02 and 57-51.1-03 is defined in N.D.C.C. § 57-51.1-01(2) as follows:

“Average price” of a barrel of crude oil means the monthly average of the daily closing price for a barrel of west Texas intermediate cushing crude oil, as those prices appear in the Wall Street Journal, midwest edition, minus two dollars and fifty cents. When computing the monthly average price, the most recent previous daily closing price must be considered the daily closing price for the days on which the market is closed.

For administration of this section, the Tax Commissioner has determined that the referenced closing price is the NYMEX Light Sweet Crude Oil contract price.

The “trigger price” referenced in N.D.C.C. §§ 57-51.1-02 and 57-51.1-03 is defined in N.D.C.C. § 57-51.1-01(11) as follows:

“Trigger price” means thirty-five dollars and fifty cents, as indexed for inflation. By December thirty-first of each year, the tax commissioner shall compute an indexed trigger price by applying to the current trigger price the rate of change of the producer price index for industrial commodities as calculated and published by the United States department of labor, bureau of labor statistics, for the twelve months ending June thirtieth of that year and the indexed trigger price so determined is the trigger price for the following calendar year.

Following the statutory guidelines, the Tax Commissioner has determined that the trigger price for calendar year 2004 is \$35.11, and the average prices for the five month period of May 2004 through September 2004 were:

<u>May</u>	<u>June</u>	<u>July</u>	<u>August</u>	<u>September</u>
\$37.58	\$35.63	\$38.20	\$42.48	\$43.21

Based on these prices, the Tax Commissioner has determined that the tax incentives subject to the trigger price became ineffective for production periods beginning October 1, 2004, and until such time as the statutory provisions for reinstatement are met.

The Tax Commissioner surveyed active filers of the T12 "Oil Gross Production and Oil Extraction Tax Report" and established the following method for administration of the statutory rate change:

1. Beginning October 1, 2004, the well codes for vertical and horizontal new wells (EN, HE, and NW), work-over wells (WP and W4), two-year inactive wells (IE), qualified enhanced recovery projects (SR, TR, and R2), and horizontal reentry wells (HR) will be terminated and replaced with well code "PT".
2. Inventory in storage, at the close of business on September 30, 2004, for any of the terminated well codes, must be reported as a "split" entry, in the month of sale, at the well code in effect when the oil was produced.
3. Production from stripper wells (S1, S2, and S3 well codes), incremental production from qualified enhanced recovery projects (R1 well code), new wells drilled on "Indian land" (FE well code), and old wells (WW well code) will continue to use the appropriate well codes currently assigned.
4. A notification letter will be mailed to all producers and purchasers the first week of the month following a five month period resulting in a "reverse oil price trigger".
5. Upon reinstatement of the applicable incentives, the well codes noted in #1 above will be reactivated for any remaining time periods established.
6. Inventory in storage, at the close of business on the last day of the 5th month in which the reverse trigger re-establishes the incentives, must be reported as a "split" entry, in the month of sale, using the "PT" well code and the 6.5% rate.

The Tax Commissioner's goal for implementation of reporting procedures required for the statutory price increase is to make the process as smooth as possible. If we can provide assistance in making this happen for your company, please contact us at (701) 328-2705 or by e-mail [oiltax@state.nd.us](mailto:oiltax@state.nd.us).

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