Oil and Natural Gas Taxing in New Mexico

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Crude Oil and Natural Gas Severance Tax

- §7-29-1: Severance tax levied on all products severed and sold at the rate of 3.75%.
- Allowable deductions:
  - o Royalties paid to the federal, state or Indian government.
  - o Trucking expenses to the first place of sale.
  - o Gathering and pipeline transportation expenses to the first place of sale.
  - o Processing costs when the actual prices is determined at a point other than at the production unit.
- Constitutional distributions to General Fund 4.7% of 5-year average market value after debt service.

Crude Oil and Natural Gas Conservation Tax

- § 7-30-1: tax on all products that are severed and sold, at .0019% (nineteen-hundredths) for natural gas and crude oil. When WTI exceeds $70 barrel, crude oil increases to .0024% (twenty-four hundredths).
- Allowable deductions:
    - Royalties paid to the federal or state government.
    - Royalties paid to any Indian tribe, Indian pueblo or Indian that is a ward of the United States.
    - Trucking expenses of any product from the production unit to the first place of sale.
    - Gathering and pipeline transportation expenses to the first place of sale.
- Reclamation Fund flows to the General Fund
    - Conservation tax.
        - ✓ The missing trigger from 2010 Regular Session Legislation.

Crude Oil and Natural Gas Emergency School Tax

- § 7-31-1: Privilege tax levied on all products severed at or near the wellhead:
  - Rate for crude oil is 3.15%; and
  - Rate for natural gas is 4%.
- Allowable deductions:
  - Royalties paid to the federal, state and Indian tribe, Indian pueblo or Indian that is a ward of the U.S.
  - Trucking expenses to the first place of sale.
  - Gathering and pipeline transportation expenses to the first place of sale.
  - Processing costs when the actual prices is determined at a point other than at the production unit.
- The Emergency School tax flows to the General Fund.

Natural Gas Processer Tax

- §7-33-1 Natural Gas Processors tax is a privilege tax on processors for the privilege of operating a natural gas processing plant in New Mexico (In lieu of GRT §7-9-34)
  - The tax is imposed on the amount of MMBTU's of natural gas delivered to the processor at the inlet of the natural gas processing plant. The rate is determined by multiplying the rate of sixty-five hundredths of one cent ($.0065) per mmbtu by a fraction, the numerator of which is the annual average taxable value per mcf of natural gas produced in New Mexico during the preceding calendar year and the denominator of which is one dollar thirty-three cents ($1.33) per mcf. The resulting tax rate shall be rounded to the nearest one-hundredth of one cent per mmbtu.
  - Any Indian nation, tribe or pueblo or Indian is liable for the tax to the extent authorized or permitted by law.
- Allowable deductions:
  - Natural gas used for natural gas processing by the processor; returned to the lease from which it is produced; legally flared by the processor; or lost as a result of natural gas processing plant malfunctions or other incidences of force majeure.
- Natural Gas Processer Tax flows to the General Fund.

Crude Oil and Natural Gas

Ad Valorem Production Tax

- §7-32-1: Ad Valorem Production Tax:
  - Production levied on the assessed value of products which are severed and sold from each production unit in an amount equal to 150% (one hundred fifty percent) of the value of products. The assessed value of products shall be determined by applying the uniform assessment ratio to the taxable value of products.
  - The ad valorem tax rate is a composite of rates imposed by local taxing authorities, including counties and school districts. Ad valorem production tax rates change with every September production, due November 25.
  - the Ad Valorem Production tax is effectively a tax on product reserves
- Allowable deductions:
  - Royalties paid to the federal, state and Indian tribe, Indian pueblo or Indian that is a ward of the U.S.
  - Trucking expenses to the first place of sale.
  - Gathering and pipeline transportation expenses to the first place of sale.
  - Processing costs when the actual prices is determined at a point other than at the production unit.
- Ad Valorem Production Tax flows to the state and distributed to the county taxing district.

Crude Oil and Natural Gas

Ad Valorem Equipment Tax

- §7-34-1: Ad Valorem Equipment Tax
  - The tax is levied on the assessed value of the equipment at each production unit, in lieu of property tax on that equipment.
  - The taxable value of the equipment of each production unit is an amount equal to twenty-seven percent (27%) of the value of the products of each production unit. The assessed value is determined by applying the uniform assessment ratio to the taxable value.
- Proceeds from the oil and gas ad valorem production equipment tax flow to the municipalities, community college districts and school districts in the county in which the equipment resides.

Crude Oil and Natural Gas Incentives

- Following are incentives for the production of crude oil and natural gas:
  - § 7-20-4.A: Enhanced Oil Recovery Incentive (EOR) based on WTI less than $28 barrel.
  - §7-29-4.A(4)(5): Well Workover Incentive based on WTI less than $24 barrel or BTU equivalent for natural gas.
  - §7-29-4.A (6)(7)(8)(9): Stripper Well Incentive based on natural gas selling between $1.15 -$1.35 mcf or crude oil selling between $15 - $18 barrel
  - §7-29-4.B (1)(2): Well Restoration Incentive based on WTI price less than $24 barrel or BTU equivalent for natural gas.
- New Mexico incentives allowed only a lesser percentage amount on the taxes due, rather thank a full exemption from primarily the Severance Tax Act, so as not to have an impact on the General Fund.
- Incentive currently on the books were conducive when they were passed; have not been used in 10+ years and should not be included in percentage ranges in taxation schedules.

Crude Oil and Natural Gas Advance Payment

- The Advance payment is the aggregate amount of tax, net of any refunds or credits paid by a person during the preceding 12 month period ending March in addition to any oil and gas conservation tax, penalty and interest due.
  - Each year, prior to July 1, each person required to pay the Oil and Gas Conservation Tax shall compute the average tax for the period ending March 31 of that year for making an advance payment.
  - Every month, persons paying the Oil and Gas Conservation Tax shall pay an advance payment in an amount equal to the applicable average tax which is then credited against the amount due.

Crude Oil and Natural Gas Revenues to the State

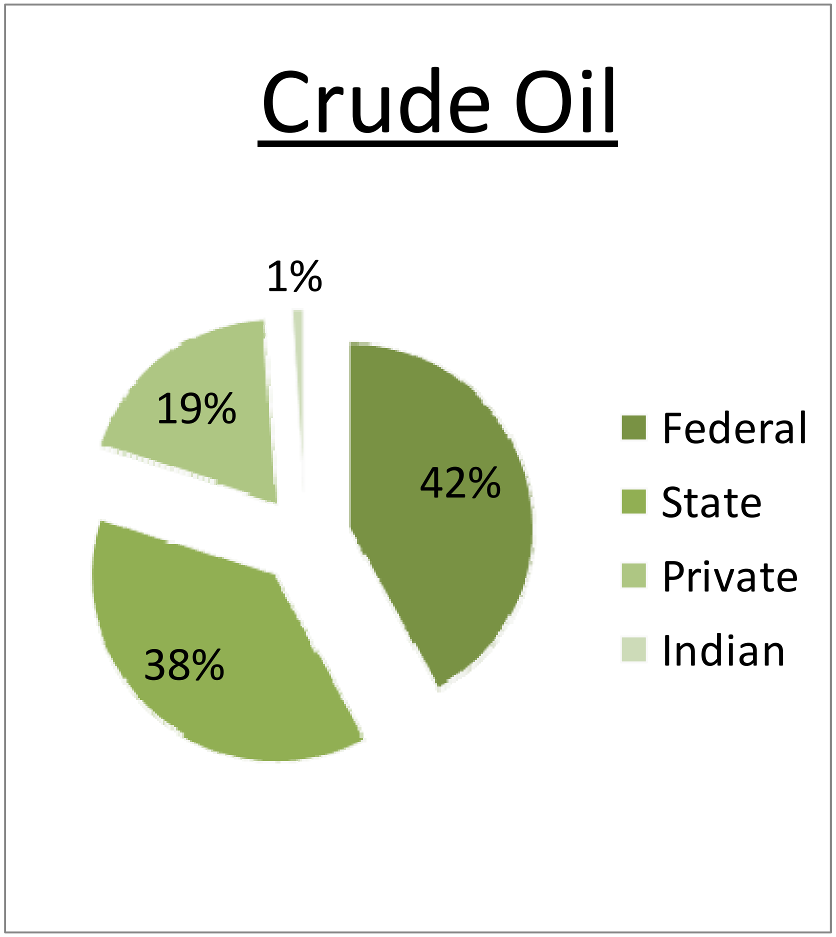
- 48% of all royalties (12.5%) paid to the federal government from oil and gas produced from federal mineral ownership in New Mexico.
- 12.5% to 18% royalty payments on all oil and gas produced from state minerals.
- Bonus payments for leasing state and federal minerals.
- State taxes on oil and gas:
  - 4% emergency school tax on natural gas, 3.15% on crude oil;
  - 3.75% severance tax;
  - 1 to 1.5% ad valorem tax (based on a formula),
  - 0.19% conservation tax on crude oil, 0.24% on natural gas; and
  - $0.0082/MMBTU natural gas processors tax (based on a formula).
- Investment earnings on the Severance Tax and Land Grant Permanent funds.

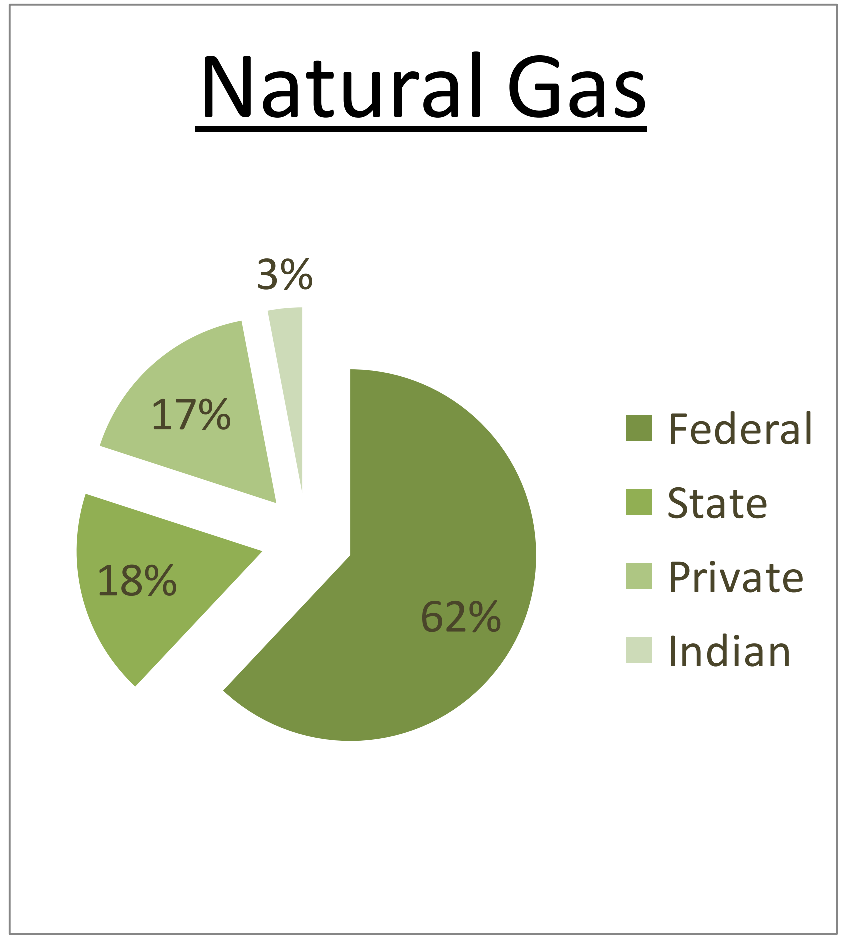
Who Pays Crude Oil and Natural Gas Taxes in New Mexico

- **Glossary of terms**:
  - **Producer** – A producer of oil and gas, also sometimes referred to as an Operator, or the Oil Company, who may or may not own the mineral.
  - **Mineral Owner** – Owner of the rights and interests in a mineral estate (where interests in a landed estate have been severed) along with the right to execute a lease on the same.
  - **Mineral Rights** – The ownership of the minerals under the surface, with the owner having the right to capture or recover and the right to delegate owner rights to another party to recover mineral by negotiating a lease agreement.
  - **Producing Mineral Owner** - An owner of minerals that are currently being produced and sold. Payments made to producing mineral owners are known as royalty payments or royalties.
  - **Royalty** - Revenue generally from the production of oil or gas, free of costs (except taxes unless exempted; federal mineral and state mineral).
  - **Royalty Interest** – An interest in an oil and natural gas lease that gives the owner of the interest the right to receive a portion of the production from the leased acreage (or of the proceeds of the sale thereof), but generally does not require the owner to pay any portion of the costs of drilling or operating the wells on the leased acreage.
  - **Working Royalty Interest -** shares in the costs of production in a mineral property.
  - **Overwriting Royalty Owner** – a royalty owner who sells his royalty but retain an overwriting royalty percentage.

New Mexico

Oil & Gas Production by Mineral Ownership





Oil Conservation Division - December 2008

New Mexico
Tax Credits, Deductions & Exemptions

- Dr. Tom Clifford in September, 2010, did a presentation for LFC and discussed the difference between tax credits, deductions, and exemptions and stated:
- "*WHAT PREFERENCES ARE NOT TAX EXPENDITURES? Tax expenditures do not include provisions that define the proper scope of the tax base, prevent double taxation or avoid interference in interstate commerce*."
  - In our review of the various taxes paid for the production of crude oil and natural gas, transportation and processing are deducted from the tax base as the tax is based on severed and sold, at or near the wellhead. In those cases where the product is purchased at the well head, the purchaser deducts the cost of transportation and processing from the purchase price.
  - Many of the deductions are to avoid double-taxation and anti-pyramiding.
  - Within the presentation, the only "exemption" claimed for oil and gas was royalty payments to the federal, state and tribal governments, which is allowed by statute. Charging taxes to the federal, state and tribal governments cannot an exemption, and the state derives benefit from both federal and state royalties.

Royalty Payments

- Private Mineral Ownership:
  - The private mineral owner pays the severance taxes (deducted from his gross amount) and derives income from the royalty payments.
- State and Federal Royalty:
  - The mineral owner on federal and state royalties, is the government, and the state does not charge the various severance taxes. Yet, the state does derive benefits from the royalty payments.
    - 48% of the federal royalty is returned to the state.
    - State royalty income is distributed to 41 beneficiaries including state schools and universities, hospitals, the Las Vegas Mental Hospital, School for the Deaf, visually impaired, the penitentiary/
    - State land office rents and bonuses are deposited in the general fund.

New Mexico Revenues From Crude Oil & Natural Gas

	FY 2008	FY 2009	FY 2010*
State General Fund:			
Oil and Gas Emergency School Tax	$557,668,091	$370,353,954	$324,543,970
Oil and Gas Conservation Tax	29,115,356	18,916,799	16,352,738
Natural Gas Processors Tax	30,617,748	40,341,003	40,436,731
Sub-Total: General Fund Taxes	$617,401,195	$429,611,756	$381,333,439
Federal Mineral Leasing Royalties	$564,181,973	$507,228,551	$355,302,274
State Land Office Rents, Bonuses, Etc.	46,084,845	36,442,282	67,701,590
Sub-Total: Rents and Royalties	$610,266,818	$543,670,833	$423,003,864
Total General Fund Revenue	$1,227,668,013	$973,282,589	$804,337,303
Other State Funds:			
Severance Tax Permanent Fund	$567,447,973	$378,141,950	$390,701,713
Land Grant Permanent Fund	463,728,275	460,886,122	322,227,921
Total Other State Funds	$1,031,176,248	$839,028,072	$712,929,634
Total State of New Mexico Revenue	$2,258,844,261	$1,812,310,661	$1,517,266,937
Local Government Revenue:			
Ad Valorem Production Tax	$124,655,359	$114,646,409	$106,628,000
Production Equipment Tax	26,084,111	28,219,389	34,800,000
Total Local Government Revenue	$150,739,470	$142,865,798	$141,428,000
Grand Total State and Local Revenue	$2,409,583,731	$1,955,176,459	$1,658,694,937

Note: Revenue do not include interest revenue on permanent funds, gross receipts taxes, corporate income tax, personal income tax, or employment taxes.

* 2010 Estimated values, subject to change
Source: NMTRD/NMDFA/LFC