SENATE TAXATION
EXHIBIT NO. 13
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BILL NO. SB-561

Letter of Testimony
SB 561

I have been in the business of producing oil and gas since 1983 when I graduated from Montana Tech as a Petroleum Engineer. After ten years working in other states, I was fortunate enough to make it back to Billings where my wife and I are raising our family. During my career, my job has been to make investment decisions for the drilling of oil and gas wells to evaluate acquisition opportunities. I am writing in opposition to SB 561. I think it is important to recognize that the business of producing oil and gas is a very complex business – bills such as SB 561 might appear to be a good idea, but the effects can be far reaching due to the complexities of the business.

My first concern with the SB 561 is it shows that Montana does not have a stable tax environment with which to attract investment. Since the severance tax simplification which MPA spearheaded in 1999, the oil and gas industry has come to the forefront and delivered on their promise to invest in Montana. Results of this can be seen in the increased oil and gas production from which the State of Montana has benefited. In addition to all of the drilling in Northern Montana gas country, a world class oil discovery was made in Richland County, Montana. This oil discovery was not with out economic pain as most of the early wells drilled by Lyco were uneconomic. However, due to the tax incentives, Lyco continued testing and working on their concept that the area contained a huge resource play. Headington Oil and Gas joined in the play and results improved until the point that it became economic. Since then several operators, numerous landowners, the surrounding communities, and the State of Montana have benefited economically – now is not the time to change the rules and add price triggers.

My second point is the cost of drilling and completing the wells. I anticipate that you will hear testimony from the industry that shows costs to drill, complete and equip a well has doubled in the last two to three years – this means an incremental $2,000,000 on the deeper horizontal wells such as the Richland County Bakken play. Obviously, this additional expense increases the payout time and reduces many other economic parameters including the Rate of Return which is a benchmark for most companies. Approval of SB 561 will further erode the economics and result in risking that the development will be stopped due to high tax rates, high drilling costs and low oil prices / increased differentials. Operators define differentials as the difference between the NYMEX oil price (which is referred to in the paper and on television) and the actual oil price received at the wellhead. As you recall, last winter, a few operators were shut-in as oil pipelines were full and there was no place to sell their oil – this resulted in other producers taking higher deducts / differentials in order to sell their oil. This is still an issue today and is due in part to increased production from the Tar sands in Canada, some of which is being trucked across the border and filling the pipeline from Eastern Montana to Clearbrook, Minnesota. Current differentials for Eastern Montana light sweet crude are $5 to $10 off NYMEX. A price trigger of $38 for WTI does not take into account the differentials for Montana crude oil.

My final example deals with the acquisition business. Acquisitions are somewhat unique because they deal with the future. When one oil company buys another company's assets, they estimate how many wells they will drill in the future. This analysis includes determining oil and gas rates and reserves, an anticipated cost to drill, a cost to operate, future oil and gas prices, and last, but not least - severance taxes. Therefore, any company that has purchased oil and gas properties in the State of Montana within the last several years (Encore, Enerplus, Nance, Devon, etc.), has modeled the severance tax rates for any planned new drilling well at the incentive rates. Changing these rates effective 12/1/2007 as outlined in SB 561 will obviously affect the results of the individual company's acquisitions. Therefore, SB 561 in effect penalizes the exact group of company's which had faith in the legislature to retain a stable tax environment and invest in the State of Montana. As a tax payer and an interested citizen in the State of Montana, that is not the message I want to send.

Respectfully submitted,

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