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DEPARTMENT OF NATURAL RESOURCES

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Division of Oil, Gas and Mining

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March 3, 2020

Notice to Oil and Gas Producers

Re: Severance Tax Credit Applications

This letter is to update taxpayers about the severance tax credit program intended to provide incentive for production enhancement workovers on oil and gas wells in the State of Utah. It also explains changes to the severance tax credit application process and provides information required to submit requests for the tax credit.

Utah House Bill 389, titled Incentive Program Amendments, was approved and signed by Governor Herbert to take effect on May 14, 2019. This bill amended Utah Code Section 59-5-102(7) and thereby made statutory changes to the process of requesting severance tax credits for well workovers and recompletions. Because the H.B. 389 changes to the severance tax application process required certified public accountant (“CPA”) certification that was inconsistent with professional CPA standards, the subject was revisited during the 2019 First Special Session of the legislature and H.B. 1003 was approved on September 23, 2019 to modify the CPA review provisions enacted by H.B. 389.

As was the requirement prior to the recent legislative amendments, a Form 15 (Designation of Workover or Recompletion) must be submitted to the Utah Division of Oil, Gas and Mining (“DOG M”) to claim a workover tax credit. In addition to the Form 15, modifications to the application process made in H.B. 389 and H.B. 1003 now require an independent CPA to report on the accuracy and validity of the expenditure amount eligible for a severance tax credit, and the report prepared by the CPA is to be submitted to DOGM with the Form 15. Preparation of the CPA report is to be in accordance with Agreed-Upon Procedures (AUP) established by DOGM. After reviewing a submitted Form 15 with supporting documents to verify the workover qualifies for tax credit, DOGM will the return reports providing an approved qualifying workover expense amount to the taxpayer.

A copy of the AUP document providing criteria for the required CPA report and a reference copy of the Form 15 created by online application through the DOGM ePermit system are both included as attachments to this letter. The AUP document includes detailed instructions for how oil and gas well operators are to submit the Form 15, and the document provides requirements or reference to requirements for acceptance and approval of the severance tax credit application. A copy of this AUP document will also be made available under “Forms” on the Oil and Gas page of the



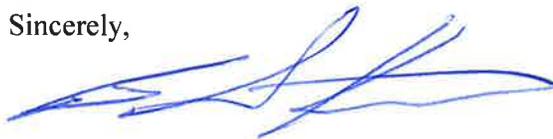
DOGM website. Operators will need to provide a copy of this AUP document to the independent CPA preparing the required report. DOGM received and very much appreciated assistance from the Utah Association of CPAs in preparing the AUP.

Because the bills amending Utah Code Section 59-5-102(7) have retrospective operation to January 1, 2019, DOGM will require a CPA report for any Form 15 submitted for a workover with activity extending into calendar year 2019 and not approved by DOGM before the date H.B. 389 became effective. Operators who have submitted a Form 15 for qualifying work that has not already been approved by UDOGM will be requested to amend that Form 15 submittal to include the now required CPA report. DOGM was able to process and approve all Form 15 applications submitted with acceptable documentation before May 14, 2019, but no Form 15 submissions have been processed since that date.

Applicants who receive an approved Form 15 from DOGM to qualify for the workover tax credit must then obtain a tax credit certificate from the Governor's Office of Energy Development ("OED"). The online application for tax credit certificate can be accessed on the OED website (energy.utah.gov) that will link the user to the application portal website (oed2.fluidreview.com). The DOGM approved Form 15 is to be submitted with the online application to OED as supporting documentation. OED will issue a certificate to the taxpayer that includes the approved workover severance tax credit amount for the taxpayer to submit with other necessary items to the Utah State Tax Commission when they file their severance taxes. OED will also submit a list identifying each taxpayer and the amount of tax credit listed on their respective tax certificates to the Utah State Tax Commission.

While we are pleased about continuation of the severance tax incentive program to encourage production enhancement work on oil and gas wells, we do regret and apologize for the added complexity to the approval process for the tax credits. If you have any questions regarding the information provided with this correspondence, please contact Ellis Peterson by phone at 801-538-5315 or by email at empeterson@utah.gov.

Sincerely,



Bart Kettle, Deputy Director
Utah Division of Oil, Gas and Mining

Agreed-Upon Procedures

Well Workover and Recompletion Severance Tax Credit

Utah Division of Oil, Gas and Mining
January 2020

Purpose and Preamble

These Agreed-Upon Procedures (“AUP”) are to provide criteria for the report prepared by an independent certified public accountant (“CPA”) and submitted by an oil and gas well operator (“taxpayer”) with a Form 15 (Designation of Workover or Recompletion) to the Division of Oil, Gas and Mining (“DOGGM”) as part of the severance tax credit application process. This AUP relates specifically to the Form 15 and required CPA report, and are not intended to describe, mandate, or direct how the severance tax credit application process proceeds beyond the submission of documents to DOGM.

In 2019 the Utah State Legislature amended Utah Code § 59-5-102 (workover and recompletion tax credits for oil and gas operators). The 2019 amendment requires an independent CPA to report on the accuracy and validity of the expenditure amount eligible for a tax credit. To claim a severance tax credit, a taxpayer must prepare a summary of the workover¹ expenditures and an independent CPA must provide a report in accordance with this AUP. After the summary and CPA report are complete, the taxpayer then submits the documents to DOGM for verification of eligible expenditures. After DOGM verifies the expenditures, they issue the taxpayer a report showing the approved eligible workover expenditure amount, the CPA report, and the taxpayer’s summary of expenditures. After receipt of the DOGM report, the taxpayer shall apply to the Utah Governor’s Office of Energy Development (“OED”) for a tax credit certificate that includes the amount of taxpayer’s eligible expenditures during the calendar year and the amount of taxpayer’s tax credit.

The Form 15 must be submitted within 90 days of completing the workover using the DOGM ePermit system, and it must be approved by DOGM before the taxpayer can proceed to request the requisite severance tax credit certificate from OED. Only a properly completed Form 15, submitted through the DOGM ePermit system, will be considered the statutorily required taxpayer’s summary of expenses for a severance tax credit. DOGM will not approve a Form 15 unless the CPA report is prepared in accordance to this AUP and submitted as an attachment to the Form 15 through ePermit.

¹ “Workover” is used throughout this document to denote the term “well recompletion or workover” as referenced in the Oil and Gas Rules. *See* Utah Admin. Code R649-1-1. The oil and gas industry recognizes a recompletion as being a type of workover, and reference to workover is generally used only in association with a well. Therefore, the term “workover” as used herein for brevity is consistent with “well recompletion or workover” as referenced in statute and rules.

Procedures for Taxpayer

An oil and gas well operator must proceed with the fourteen steps as detailed below in order for DOGM to verify and approve the workover expenditures for severance tax credit.

- 1) Review AUP and Utah Administrative Code rules R649-3-23 (Well Workover and Recompletion) and R649-8-17 (Form 15, Designation of Workover or Recompletion) and be compliant with these rules. The referenced rules can be accessed on Oil and Gas page (<https://oilgas.ogm.utah.gov/oilgasweb/>) of the DOGM web site.
- 2) Confirm that a Form 9 or Form 3 providing notice of intention (“NOI”) for the workover was submitted through the DOGM ePermit system and approved by DOGM before workover activity requiring NOI began. The workover tax credit will be denied by DOGM if the required NOI was not properly submitted and approved prior to commencing the workover.
- 3) Confirm that a Form 9 or Form 8 providing subsequent report (“SR”) of the workover was submitted through the DOGM ePermit system within 30 days of completing the workover operations. A report of operations performed daily on the well must be provided with the SR, and that report must provide adequate detail for DOGM to determine specific operations conducted during the workover, relevant depths and intervals of the wellbore affected, and the services and materials required to complete the workover.
- 4) Determine the purpose or type of work for the workover to be selected in Section 10 on the Form 15. The four non-exclusive choices are: production enhancement, recompletion, convert to injection, and repair well. In most cases a workover to replace or repair equipment in a well, or workover activity considered as routine maintenance, is not eligible for a severance tax credit. The only circumstance when costs for repairing a well are acceptable for a severance tax credit is when the workover is to specifically repair damaged casing or liner.
- 5) If unfamiliar with the DOGM Form 15, Designation of Workover or Recompletion, download a sample copy of the Form 15 from the Oil and Gas Report Forms page: (<https://oilgas.ogm.utah.gov/oilgasweb/forms/forms-main.xhtml>)

The sample copy of Form 15 is identical to the form created by the DOGM ePermit system after online entry and submission of the required information. Please note that copies of the Form 15 submitted any way other than through the ePermit system are not accepted by DOGM.

- 6) Establish the dates when the workover commenced and was completed for Section 11 on the Form 15. The date a workover commenced is normally the day when location preparation for the workover began, or when equipment required for the workover was first moved to the well site. The date a workover was completed is ordinarily the later of either the workover rig release date or the day when the well was ready to be reconnected to its production/injection facility. Multiple workovers on the same well should be submitted on separate Form 15 applications and not submitted on one Form 15.
- 7) Compile copies of invoices, accounting reports, payment records, field tickets, or other available information to detail and substantiate costs in the CPA report. This information provided will be used by the CPA for review and preparation of their CPA report. The information related to workover expenditures must include the vendor, service or work dates, details of services and/or equipment provided, and expenditure amounts. The maximum allowed tax credit per taxpayer per well during a calendar year is limited to the lesser of 20% of eligible workover expenditures or \$30,000.

- 8) Categorize and sum the well expenditures eligible for a tax credit by groupings found in Section 12 on the Form 15. Abbreviated and general descriptions of the Section 12 categories are as follows:
- a. Location preparation and cleanup – Costs for services required to accommodate workover equipment on location and then restore site back to previous producing/injecting state after workover. This would include services like rig anchor testing, limited dirt work, and flowline disconnect and reconnect. No other surface equipment replacement or repair costs are allowable.
 - b. Move-in, rig-up, and rig-down – Mobilization and demobilization costs for the workover rig and associated workover equipment including transportation and crane services.
 - c. Rig charges (including fuel) – Costs for the service/workover rig and associated equipment, expendable materials, and personnel.
 - d. Coiled tubing, nitrogen, foam, and other circulating services – Costs for materials, equipment, and other related services providing clean-out and circulating assistance.
 - e. Water and chemicals for workover fluid – Costs for water, water hauling, filtering, disposal, additives, and chemicals for workover/circulating/well-control fluid.
 - f. Equipment purchase – Purchase costs for equipment or materials directly related to the workover, but primarily limited to only expendable items such as bits, drillable plugs, pump-off subs, etc. Costs for repair/replacement of tubing, artificial lift equipment, and surface equipment are generally disallowed from tax credit eligibility. Notable exceptions for tax credit eligible equipment purchases are when tubing is down-sized in a gas well to increase flow capacity, and the purchase of sub-surface equipment for a different type of artificial lift to increase production from an oil or gas well. No expenditures for surface equipment or installations are eligible for the severance tax credit.
 - g. Equipment rental – Costs for all rental equipment related to a workover, including the transportation, personnel, inspection, and repair expenses associated with that equipment. The workover related rental equipment can include items used on surface (BOPE, tanks, pump, power swivel, flow-back equipment, etc.) and sub-surface (work string, casing scraper, mills, fishing tools, packer, etc.).
 - h. Cementing – All cementing service and related costs for equipment, personnel, materials, and transportation.
 - i. Perforating – All costs related to perforating services including equipment and personnel for wireline or pipe conveyed deployment.
 - j. Acidizing – All costs for the acid, additives, diverter materials, haulage, pumping, and any other equipment or services related to pumping acid or similar treatment fluids into a well. When acid is pumped in conjunction with hydraulic fracture stimulation, the acidizing costs can alternatively be included with the fracture stimulation expenses and not separately reported under this acidizing category.
 - k. Fracture stimulation – All costs for hydraulic fracturing materials, haulage, additives, equipment, and services provided by pumping contractors and other suppliers. Acceptable materials costs can include but are not limited to those for proppant, water, additives, chemicals, diverters, and energizing gas. If relatively small volumes of acid are pumped in conjunction with other fracture stimulation fluids, include the total pumping stimulation costs under this category.

- l. Logging and wireline services – Costs for open- and cased-hole logging services and all other wireline services, including but not limited to setting of plugs/packers, pipe recovery and cutting, slick-line, and wireline deployed pressure/temperature surveys.
 - m. Supervision and overhead – Expenses for direct supervision and taxpayer overhead costs for the workover, as allowed by operating agreement and/or relevant COPAS accounting standards, can be included under this category. Workover supervision can be from a contractor or an employee of the taxpayer, and eligible expenses can include those for travel, lodging, and meals incurred by the supervisor as result of the workover.
 - n. Other – Any costs incurred with the workover that cannot reasonably be included in the other specified groupings should be itemized under this category. Expenses included under this other category will need a descriptive label, and additional explanation may be necessary to provide justification for tax credit eligibility.
- 9) Prepare a summary of the workover expenditures with the same or similar format and cost categories as on the Form 15, and with the work commenced and completed dates as to be reported on the Form 15.
 - 10) Engage an independent CPA to: (1) review the taxpayer-prepared summary of workover expenditures and supporting documentation, (2) prepare a report in accordance with this AUP, and (3) then deliver that report to the taxpayer. Provide the CPA with the following information or as otherwise requested by the CPA for this AUP engagement:
 - a. A copy of this AUP.
 - b. Copies of invoices, accounting reports, payment records, field tickets, or other information and details required for reporting on the accuracy and validity of the taxpayer’s workover expenditures.
 - c. Name and 14-digit API number for the well subjected to workover.
 - d. Dates when the workover was commenced and completed.
 - e. A copy of the summary prepared by the taxpayer of the workover expenditures categorized as in Section 12 on the Form 15.
 - 11) Upon receipt of the report prepared by CPA, perform a basic review to check for completeness and obvious errors. Affirm this AUP was followed by the CPA, and rectify any differences between categorized workover expenditure totals in the CPA report and those prepared by taxpayer.
 - 12) Login to the DOGM ePermit system and select “New Tax Credit” option on the ePermit user menu. Select the operator and well completion corresponding to 14-digit API number (*eleventh and twelfth digits are to be correct directional sidetrack codes*) from the pull down tabs, specify new or amend Form 15, and “Yes” to attach a file. You will be directed to choose a file, which must be in PDF format and include the CPA report. Proceed by selecting “Next” and the appearing page will have the well information auto-filled. Check the boxes that apply for the type of work in Section 10, enter work commenced and work completed dates in Section 11 (mm/dd/yyyy date format), and then select “Submit”. On the next page that appears, enter the expenditure totals by category in Section 12 under the “Expenses” column, and add descriptive labels needed for any items included in the “Other” category, then select “Submit.” Be sure that the expense amounts submitted by category on this Form 15 match those in the CPA report. If there are working interest owners of this well who take production in kind and are authorized to share in the requested workover tax credit, enter the name, address, city, state, DOGM account

number, and the net interest percent for those working interest owners in Section 13, then select “Submit.” The next page provides the option to either change the file to attach or to upload the file already selected and continue submission. After selecting the appropriate file upload option and if the entered information was acceptable, the created Form 15 will be shown. Select “Final Submit” to send the created Form 15 to DOGM for approval.

- 13) After DOGM verifies the workover expenses and finishes processing the Form 15, an approved copy of the Form 15 and CPA report will be returned to the taxpayer. The approved Form 15 is the DOGM report required by statute, and the total of expenses listed on the Form 15 under the column labeled “Approved by State” is the amount of approved workover expenses to apply for the severance tax credit.
- 14) Apply for a tax credit certificate from OED using the information on the approved Form 15. The OED application portal can be accessed from the OED website (<https://energy.utah.gov>) or at the link: <https://oed2.fluidreview.com>

After successful submission through the OED application portal, qualifying taxpayers will be issued a written certificate (TC-684B Certificate) that includes the approved severance tax credit amount to submit to the Utah State Tax Commission.

The CPA report submitted to DOGM, and supporting records for that CPA report, are subject to audit and Utah Administrative Code rules R649-2-6 (Access to Records). These documents should be kept on file and available for inspection for a period no less than six years.

Procedures for CPA

The CPA must follow the instructions provided below and prepare their report before the taxpayer can apply for a workover severance tax credit. The objectives of the CPA in conducting an agreed upon procedures engagement are to: 1) apply to the subject matter procedures that are established by the specified parties who are responsible for the sufficiency of the procedures for their purposes, 2) issue a written practitioner’s report that describes the procedures applied and the practitioners finding and, 3) communicate further as required by relevant AT-C sections. To meet DOGM requirements for verifying the accuracy and validity of the taxpayer’s submitted workover cost, the CPA report must include three tables presenting expenditure amounts for the workover. The three tables required by DOGM can be prepared with a pivot table and are described as follows:

Workover Expenditure Detail (Table 1) – Entries for each payment made for workover related costs and providing the vendor paid, cost description, service/purchase date(s), payment amount, and correlating Form 15 expense category, plus the total of all listed workover expenditures.

Workover Expenditure Totals by Category (Table 2) – Sum of workover expenditures by Form 15 expense category and the total of those sub-total amounts.

Workover Expenditure Totals by Vendor (Table 3) – Sum of workover expenditures by the vendor and the total of those sub-total amounts.

These procedures are not intended to comprise terms of engagement, dictate timing, or address other matters subject to agreement between taxpayer and CPA. Copies of the report prepared by the CPA for submission with a Form 15 will be presented to DOGM for their use and may be made available to other Utah State agencies or public if so required.

- 1) Verify the taxpayer has provided:
 - a. A copy of this AUP.

- b. Copies of invoices, accounting reports, payment records, field tickets, or other information and details required to prepare a report as prescribed in this AUP.
 - c. Name and API number for the well subjected to workover.
 - d. Dates when workover was commenced and completed.
 - e. A copy of the summary prepared by the taxpayer of the workover expenditures categorized by the expense group as to be provided on the Form 15.
 - f. Any other information that is required and can be made available by taxpayer for the CPA to use in performing AUP engagement as directed.
- 2) Prepare a report table (Table 1) to present a list of line entries of payments made to the vendors that provided services and/or materials for the workover. If the taxpayer provided this described table to the CPA, then the CPA should compare entries in the provided table to the information provided by the taxpayer to verify table entries agree with the provided payment records. Format and provide information in the table as follows:
- a. Label the table for identification as “Workover Expenditure Detail” and include the well name, well API number, and dates when workover commenced and was completed.
 - b. Prepare the table with no less than five columns organized in order from left to right with labels and content as follows:
 - Column 1: Vendor – Name of the business entity paid for services rendered and/or materials provided for the line entry payment record.
 - Column 2: Cost Description – A name or brief description of the services rendered and/or materials provided by the vendor. This description should be detailed as needed for someone knowledgeable with workover operations to understand the precise services or materials provided for the entered payment record.
 - Column 3: Dates – The date(s) or date interval when the services and/or materials correlating to the payment record were provided.
 - Column 4: Amount – The cost or expenditure amount of the line entry payment record.
 - Column 5: Category – The serial identifier of the Form 15 category for expenditures that this payment record was assigned by the taxpayer or should be assigned per reasoning of the CPA. For example, serial identifier “C” would represent “Rig charges.”
 - c. Enter a single line entry in the table with information conforming to the five columns for each payment that was made by the taxpayer for workover expenses. The payment amounts included in this table are those provided by the taxpayer for severance tax credit and may not include all workover related costs if the taxpayer excluded costs that are ineligible for tax credit.
 - d. Compare the work dates for each line entry cost amount to assure those dates are within the workover commencement and completion time interval. Exclude any cost entries from the table that are not specifically for the worked over well or within the denoted workover time interval.
 - e. Sum all the cost entries in the table to provide a summed total of the taxpayer provided workover costs below the individual line entries.

- 3) Prepare a report table (Table 2) titled “Workover Expenditure Totals by Category” to present the sums of workover expenses corresponding to the Form 15 categories and a grand total of those category sub-total sums. This can be a simple table with two columns, one labeled “Category” and the other labeled “Total”, and a line for each corresponding Form 15 expense category. The grand total value for all table entries will be listed below the line entries and should equal the expenditure totals on the other tables.
- 4) Prepare a report table (Table 3) titled “Workover Expenditure Totals by Vendor” to present the sums of workover expenses corresponding to the different vendors paid for workover services/materials and a grand total of those category sub-total sums. This can be a simple table with two columns, one labeled “Vendor” and the other labeled “Total”, and a line for each different vendor. The grand total value for all table entries will be listed below the line entries and should equal the expenditure totals on the other tables.
- 5) Prepare the CPA report consistent with applicable professional standards of AICPA, including a manual or printed signature of the CPA firm. Include the three tables of workover expenditures prepared according to this AUP in the report and provide explanation as needed for any discrepancies to the taxpayer categorized workover cost sums.
- 6) Present copies of the prepared CPA report to the taxpayer in their specified form and as a PDF file to be included as an attachment to a related Form 15 for electronic submission to DOGM.

This is the end of DOGM specified AUP.

INSTRUCTIONS

Each operator desiring to claim a tax credit for workover or recompletion work performed must submit this form within 90 days after the workover or recompletion work is completed. Upon determination and notification by the division that the described work qualifies for a tax credit, the operator may claim the tax credit on reports submitted to the Utah State Tax Commission during the third quarter after completion of the work.

NOTIFICATION REQUIREMENTS

In accordance with the Utah Oil and Gas Conservation General Rules, a notice of intent to perform the described workover or recompletion must be submitted to and be approved by the division prior to performing the work. A subsequent report giving detail of the actual work performed must be submitted within 30 days of the completion of the workover or recompletion operations. The intent and subsequent reports shall be submitted on Form 9, Sundry Notices and Reports on Wells.

QUALIFYING WORK

A workover is defined as “any downhole operation that is: (i) conducted to sustain, restore, or increase the producibility or serviceability of a well in the geologic intervals in which the well is currently completed; and (ii) approved by the division as a workover. Workover does not include operations that are conducted primarily as routine maintenance or to replace worn or damaged equipment.” A recompletion is defined as “any downhole operation that is: (i) conducted to reestablish the producibility or serviceability of a well in any geologic interval; and (ii) approved by the division as a recompletion.

The following workover and recompletion operations qualify for a tax credit:

- Perforating
- Stimulation (e.g., acid jobs, frac jobs, solvent treatments, nitrogen cleanouts)
- Sand control
- Water control or shut-off
- Wellbore cleanout
- Casing or liner repair
- Well deepening
- Initiation of enhanced recovery for board approved projects (excluding surface equipment and associated costs)
- Change of lift system (excluding surface equipment and associated costs)
- Gas well tubing changes
- Thief zone identification and elimination

The following workover and recompletion operations do not qualify for a tax credit:

- Pump changes
- Rod string fishing and repair/replacement
- Tubing repair/replacement
- Surface equipment installation and repair
- Routine maintenance and repair

EXPENSES

List the expenses incurred as part of the workover or recompletion on the appropriate operation lines of the form. Use the “other” lines for those qualifying expenses not described by any of the other categories. Use separate attachments if necessary to adequately characterize the expenses as “qualifying.” Do not write in the column marked “Approved by State.” Division approval indicates approval of the particular operation and reasonableness of the expenses only. Division approval is conditional subject to audit, and submitted expenses may be disallowed if they are not appropriate workover or recompletion expenses.

WORKING INTEREST OWNERS TAKING PRODUCT IN KIND

List only the working interest owners who take product in kind. Provide name, addresses, and Utah account numbers (account numbers can be obtained by contacting the division). Show the percent of ownership to the seventh decimal place.

SUBMISSION

This is a sample form provided for reference only. Applications for workover tax credits are not accepted on this paper form. All applications must be submitted electronically via the Utah ePermit program, located under the "Electronic Reporting" tab on the Utah DOGM website.

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