

Enhanced Oil Recovery

Section 43 of the Internal Revenue Code provides an enhanced oil recovery (EOR) credit equal to 15 percent of the qualified enhanced oil recovery costs incurred in a tax year. Existing Treasury guidelines for the Section 43 tax credit are very narrow, generally including only expensive EOR processes -- many of which are no longer in use. It excludes, however, many EOR processes that are the result of technological advances now considered common in the industry.

The Petroleum Technology Transfer Council (PTTC) in March 1997 compiled a list of EOR methods that should be included under Section 43. This study was part of an industry effort to expand the EOR definition to include technologies that have proven potential for mitigating well abandonment and increasing oil production and resource recovery.

Anywhere from 30 to 70 percent of oil, and 10 to 20 percent of natural gas, is not recovered in field development. It is estimated that enhanced oil recovery projects, including development of new recovery techniques, could add about 60 billion barrels of oil nationwide through increased use of existing fields.

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Proposal

Have the IRS review and expand the definition of methods qualifying for the EOR tax credit.

Reason for Change

The existing Treasury guidelines are based on 1979-vintage technology. This list has not kept pace with technology. Adding other technologies would encourage producers to expand extraction of existing reservoirs in order to maximize production of existing domestic reserves.

Two additional categories to the EOR list are proposed. Those categories include Enhanced Gravity Drainage (EGD) and Marginally Economic Reservoir Repressurization (MERR). Included under EGD would be horizontal drilling, multilateral well bores and large diameter lateral well bores. Included in MERR would be natural gas injection and waterflooding. Certain qualifiers and limiting factors include economic criteria for approved projects and incremental production limitations on each project.

By redefining the definition of EOR projects to include both EGD and MERR technologies, the EOR tax credit will encourage conservation measures to expand recovery of existing crude oil reservoirs and promote new drilling activity.

Congress needs to consider legislation to implement these definitional changes if the Administration is unwilling to correct the current constrained interpretation of the tax code.

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