

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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date: June 23, 2014

to: Alfredo Valdespino
Acting Chief, Excise Tax Program

from: Michael H. Beker
Acting Senior Technician Reviewer, Branch 7
(Passthroughs & Special Industries)

subject: Oil Spill Liability Trust Fund Tax and Bakken Oil

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUE

Whether the Oil Spill Liability Trust Fund tax imposed by § 4611 (OSLTF tax) of the Internal Revenue Code (Code) applies to oil extracted from the Bakken formation (Bakken).

CONCLUSIONS

The OSLTF tax applies to oil extracted from Bakken.

FACTS

Bakken is a geological formation located in the subsurface of the Williston Basin, underlying parts of Montana and North Dakota in the United States, and Saskatchewan and Manitoba in Canada. Bakken is an oil reserve in which the oil is contained in the shale of the formation. The oil in Bakken is commonly referred to as “oil shale”¹, but is more accurately referred to as “tight oil”. To avoid confusion, we will refer to Bakken oil shale as tight oil.

¹ The tight oil in Bakken is sometimes, but inaccurately, called “shale oil”. Shale oil is a sedimentary rock that contains kerogen, a fossil organic material, and is geologically distinct from Bakken tight oil. Petroleum from shale oil cannot be extracted using the same techniques or methods used for Bakken tight oil.

Tight oil is ordinary, light crude oil that has similar characteristics as West Texas Intermediate crude oil, a benchmark petroleum standard. A technique known as “fracking” is combined with the use of horizontal wells to extract tight oil from Bakken. Using these methods, tight oil is pumped from the ground and transported to refineries. Tight oil does not require any pre-processing or chemical conversion to make it usable by refineries; it is refined in the same way as other types of well-pumped crude oil.

LAW AND ANALYSIS

Section 4611(a) imposes a tax on crude oil received at a United States refinery, and petroleum products entered into the United States for consumption, use, or warehousing.

Section 4611(b)(1) provides that if any domestic crude oil is used in or exported from the United States, and before such use or exportation, no tax was imposed on such crude oil under § 4611(a), then tax is imposed on such crude oil. However, § 4611(b)(2) exempts from tax any use of crude oil for extracting oil or natural gas on the premises where such crude oil was produced.

Section 4612(a)(1) defines the term “crude oil” to include crude oil condensates and natural gasoline. Section 4612(a)(2) defines the term “domestic crude oil” to mean any crude oil produced from a well located in the United States. Section 4612(a)(3) defines the term “petroleum product” to include crude oil.

Tight oil is a type of crude oil. Therefore, based on the plain language of the Code, tight oil from Bakken that is received at a refinery in the United States or entered into the United States for consumption, use, or warehousing, is taxable under § 4611(a).

Further, tight oil is crude oil produced from a well. Therefore, tight oil extracted from the part of Bakken that is located in the United States is domestic crude oil as defined in § 4612(a)(2). As a result, if no tax was imposed on tight oil from Bakken under § 4611(a), the tight oil is taxable under § 4611(b) if it is used (except for extracting oil or natural gas on the premises where such tight oil was produced) in or exported from the United States.

You have informed us that some taxpayers argue that the legislative history to the OSLTF tax supports their position that the OSLTF tax does not apply to Bakken tight oil. Specifically, these taxpayers cite language from the legislative history to §§ 4611 and 4612, which were added to the Code by the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) (Pub. L. 96-510, 94 Stat. 2767). In House Report 96-1016(II) to CERCLA (H.R. Rep. 96-1016(II), 1980 U.S.C.C.A.N. 6151, 6154), the House Ways and Means Committee explains that the term “crude oil,” as used in §§ 4611 and 4612, does not include synthetic petroleum. Thus, the Committee explains, “crude oil” does not include shale oil, liquids from coal, tar sands, or biomass, or refined oil. The taxpayers argue that the phrase “shale oil” in the Committee report

evidences Congress's intent to exempt Bakken tight oil from the OSLTF tax. We disagree.

First, the words of statutes should be interpreted where possible in their ordinary, everyday sense. Crane v. Comm'r, 331 U.S. 1, 6 (1947). Only when the words of a statute are ambiguous do we look to evidence external to the Code, such as legislative history, to clarify the ambiguity so that our interpretation of a particular provision conforms to the intent of Congress. As stated above, in the case of Bakken tight oil, the plain language of §§ 4611 and 4612 is unambiguous; the only reasonable conclusion based on that language is that the OSLTF tax applies to Bakken tight oil. Thus, under the rules of statutory construction, it is unnecessary to investigate the legislative history of §§ 4611 and 4612.

Second, the taxpayers' argument is wrong as a matter of fact. Bakken is composed of oil shale, not shale oil; these are two distinct petroleum sources that require different extraction techniques and methods.

Third, the phrase "shale oil" in the legislative history is used to describe "synthetic petroleum". Synthetic petroleum is an intermediate petroleum product produced through an upgrading process. The upgrading process is required to make shale oil usable by refineries. Bakken tight oil is not synthetic petroleum, nor does it require upgrading before being refined. Bakken tight oil is crude oil that is usable by refineries immediately upon extraction. It is clear that Bakken tight oil is not the type of product that the legislative history to §§ 4611 and 4612 indicates should be exempt from tax. In sum, the taxpayers' position is not supported by the facts related to Bakken tight oil, nor is it supported by the plain language of §§ 4611 and 4612 or legislative history to those sections.

Please call (202) 317-6855 if you have any further questions.