

## Section 38.—General Business Credit

The definition of the term "qualified tertiary injectant expenses" includes expenditures related to the use of a tertiary injectant as well as expenditures related to the acquisition of the tertiary injectant. Costs that would have been paid or incurred in the development or operation of a mineral property if an enhanced oil recovery project had not been implemented are not "qualified tertiary injectant expenses." Costs that are related to the use of a tertiary injectant and that also are related to other activities must be reasonably allocated among the tertiary injectant and the other activities. See Rev. Rul. 2003-82, page 125.

## Section 43.—Enhanced Oil Recovery Credit

26 CFR 1.43-4: *Qualified enhanced oil recovery costs.*  
(Also §§ 38, 193.)

**Tertiary injectant expenses.** This ruling clarifies whether only the costs of acquiring tertiary injectants are eligible for the enhanced oil recovery credit provided in section 43 of the Code or whether the costs of using tertiary injectants also are eligible for the credit.

## Rev. Rul. 2003-82

### ISSUE

For purposes of § 43(c)(1)(C) of the Internal Revenue Code, what expenditures are included in the term "qualified tertiary injectant expenses" under § 193(b)?

### FACTS

X, a domestic producer of oil, owns operating interests in numerous mineral properties located within the United States. Subsequent to December 31, 1990, X began the injection of liquids and gases into oil reservoirs in connection with enhanced oil recovery (EOR) projects X had implemented with respect to the mineral properties. All of the EOR projects that had been implemented by X qualify for the enhanced oil recovery credit provided in § 43.

In some cases, X purchased liquids and gases to inject into the reservoirs in connection with the EOR projects. In other cases, X produced tertiary injectants (for

example, X burned natural gas to fuel boilers that produced steam for use as an injectant) rather than purchasing them.

X paid or incurred costs either to acquire or produce the liquids and gases used as tertiary injectants in X's EOR projects. In addition to the costs of acquiring or producing the tertiary injectants, X also incurred costs to inject, recover, and reinject the purchased and produced tertiary injectants.

### LAW AND ANALYSIS

Section 43(a) provides that, for purposes of § 38, the enhanced oil recovery credit for any taxable year is an amount equal to 15 percent of the taxpayer's qualified enhanced oil recovery costs for the taxable year.

Section 43(c)(1) provides that the term "qualified enhanced oil recovery costs" means any of the following:

(A) Any amount paid or incurred during the taxable year for tangible property

(i) which is an integral part of a qualified enhanced oil recovery project, and

(ii) with respect to which depreciation (or amortization in lieu of depreciation) is allowable under chapter 1;

(B) Any intangible drilling and development costs

(i) which are paid or incurred in connection with a qualified enhanced oil recovery project, and

(ii) with respect to which the taxpayer may make an election under § 263(c) for the taxable year.

(C) Any qualified tertiary injectant expenses (as defined in § 193(b)) which are paid or incurred in connection with a qualified enhanced oil recovery project and for which a deduction is allowable for the taxable year.

Section 193(a) allows as a deduction for the taxable year an amount equal to the qualified tertiary injectant expenses of the taxpayer for tertiary injectants injected during the taxable year.

Section 193(b)(1) provides that the term "qualified tertiary injectant expenses" means any cost paid or incurred (whether or not chargeable to capital account) for any tertiary injectant (other than

a hydrocarbon injectant which is recoverable) which is used as a part of a tertiary recovery method.

Section 193(c) provides that no deduction shall be allowed under § 193(a) with respect to any expenditure

(1) with respect to which the taxpayer has made an election under § 263(c), or

(2) with respect to which a deduction is allowed or allowable to the taxpayer under any other provision of chapter 1.

Section 43 was enacted as part of the Omnibus Revenue Reconciliation Act of 1990, Pub. L. 101-508, 104 Stat. 1388. As it was originally enacted, § 43(c)(1)(C) defined the term "qualified enhanced oil recovery costs" to include any qualified tertiary injectant expenses that are paid or incurred in connection with a qualified enhanced oil recovery project and for which a deduction is allowable under § 193 for the taxable year.

Section 317(a)(1)-(2) of the Community Renewal Tax Relief Act of 2000, Pub. L. 106-554, 114 Stat. 2673A-587, amended § 43(c)(1)(C) to provide that the term "qualified enhanced oil recovery costs" means any qualified tertiary injectant expenses (as defined in § 193(b)) that are paid or incurred in connection with a qualified enhanced oil recovery project and for which a deduction is allowable for the taxable year. The amendment was to take effect as if included in § 43 as it was originally enacted under the Revenue Reconciliation Act of 1990.

Consequently, the term "qualified tertiary injectant expenses" for purposes of § 43(c)(1)(C), as amended, has the same meaning as that term has for purposes of § 193(b).

The legislative history underlying § 193 indicates that tertiary injectant expenses include costs related to the use of a tertiary injectant, for example, "costs related to injecting a substance with a transitory effect on production" and "costs of producing and reinjecting gas or hydrocarbon liquids utilized in a recycling process." See S. Rep. No. 394, 96<sup>th</sup> Cong., 1<sup>st</sup> Sess. 97 (1979), 1980-3 C.B. 131, 215. The legislative history further states that the purpose of § 193 is "to encourage the use of expensive tertiary enhanced oil recovery processes." *Id.* 1980-3 C.B. 131, 216. Neither § 193 nor its legislative history,

however, indicates that the term “qualified tertiary injectant expenses” was intended to include costs a taxpayer would have paid or incurred in the development or operation of a mineral property if an enhanced oil recovery project had not been implemented with respect to the property, for example, costs paid or incurred to plug and abandon wells.

Accordingly, for purposes of § 43(c)(1)(C), X’s costs paid or incurred to either acquire or produce the liquids and gases used as tertiary injectants in X’s EOR projects are “qualified tertiary injectant expenses” as defined in § 193(b). The term “qualified tertiary injectant expenses” also includes X’s costs to inject, recover, and reinject the purchased and produced tertiary injectants.

## HOLDING

For purposes of § 43(c)(1)(C), the definition of the term “qualified tertiary injectant expenses” includes expenditures related to the use of a tertiary injectant as well as expenditures related to the acquisition (whether produced or acquired by purchase) of the tertiary injectant. The term “qualified tertiary injectant expenses”, however, does not include costs a taxpayer would have paid or incurred in the development or operation of a mineral property if an enhanced oil recovery project had not been implemented with respect to the property. Costs that are related to the use of a tertiary injectant and that also are related to other activities (for example, primary or secondary recovery) must be reasonably allocated among the tertiary injectant and the other activities to determine the amount of tertiary injectant expenses paid or incurred by the taxpayer for the taxable year.

## DRAFTING INFORMATION

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