

**Internal Revenue Service**

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Person To Contact:

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PLR-149545-04

Date:

September 30, 2005

**LEGEND:**

Taxpayer:

Reservoir:

Method:

F:

Facility:

A:

B:

C:

Dear :

This letter responds to your letter request for a ruling that, for purposes of § 43 of the Internal Revenue Code, the Method, as applied at the Reservoir, is a qualified tertiary recovery method that is not described in § 1.43-2(e)(2) of the Income Tax Regulations or in a revenue ruling.

The information submitted and the representations made are as follows:

Taxpayer is an accrual method calendar year taxpayer. Taxpayer is the owner of an operating interest in oil and gas property comprising of a nearly saturated Reservoir in State A. Taxpayer intends to implement a project using the Method, and will use injection wells to alternate injection of enriched hydrocarbon gas and water into the Reservoir. The enriched hydrocarbon gas will be manufactured at Facility and is described as having an "Ethane Plus" composition of A percent. The anticipated amount of enriched gas injection is B. The anticipated duration of enriched gas injection is C years.

Taxpayer represents that the injection of enriched hydrocarbon gas alternating with water will affect the Reservoir fluid by swelling the oil and reducing its viscosity. The Method is preferable to the miscible water alternating gas process for the Reservoir.

Taxpayer represents that the Method under consideration changes the properties of the reservoir oil by swelling the oil and reducing its viscosity, a result that cannot be achieved by either waterflooding or gas cycling. The proposed Method also provides the energy necessary to force the oil to the production wells. Taxpayer has represented that the proposed Method is within the United States and first injection will occur after December 31, 1990 as required under § 43(c)(2). Also, Taxpayer has represented that the Method involves the application (in accordance with sound engineering principles) of a recovery method which can reasonably be expected to result in a more than insignificant increase in the amount of oil that will ultimately be recovered.

Section 43(a) provides a credit in an amount equal to 15% of certain costs paid or incurred by a taxpayer in connection with a qualified enhanced oil recovery project.

Section 43(c)(2) defines the term "qualified enhanced oil recovery project" to mean any project that: (1) involves the application (in accordance with sound engineering principles) of one or more qualified tertiary recovery methods (as defined in section 193(b)(3)) that reasonably can be expected to result in a more than insignificant increase in the amount of crude oil that ultimately will be recovered; (2) is located within the United States (within the meaning of section 638(1); and (3) with respect to which the first injection of liquids, gases, or other matter commences after December 31, 1990.

Section 1.43-2(e)(1) of the regulations defines the term "qualified tertiary recovery method" to mean any one or combination of the tertiary recovery methods described in section 1.43-2(e)(2) or a method not described in section 1.43-2(e)(2), which has been determined by revenue ruling to be a "qualified tertiary recovery method." A taxpayer may request a private letter ruling that a method not described in section 1.43-2(e)(2) or in a revenue ruling is a qualified tertiary recovery method. Generally methods identified in revenue rulings or private letter rulings will be limited to those methods that involve the displacement of oil from the reservoir rock by modifying the properties of the fluids in the reservoir or providing the energy and drive mechanism to force the oil to a production well.

Section 1.43-2(e)(3) states the term qualified tertiary recovery method does not include waterflooding and cyclic gas injection. Cyclic gas injection is the increase or maintenance of pressure by injection of hydrocarbon gas into the reservoir from which it was originally produced.

As required by section 1.43-2(e)(1), the Method involves the displacement of oil from the reservoir rock by modifying the properties of the fluids in the reservoir or that provide

the energy and drive mechanism to force the oil to a production well. This Method does both.

The water alternating gas injection resembles cyclic gas injection, an excluded method under § 1.43-2(e)(3), in that in both cases hydrocarbon gas is being injected into the reservoir. Cycling, which is introduced early in the life of the field, is a primary method for recovering condensate from a gas condensate reservoir by maintaining the original pressure of the reservoir to prevent retrograde condensation. This method is introduced early in the life of the field. (See Manual of Oil and Gas Terms, Howard R. Williams and Charles J. Meyers, 1987, Matthew Bender, page 215. Also see § 1.613A-7(k)). In this case, the reservoir is not a condensate reservoir and the gas is not being injected to prevent retrograde condensation.

Based on the information submitted and the representations made, as well as review by Service experts, we conclude that the Method Taxpayer will implement at the Reservoir, is a qualified tertiary recovery method not described in § 1.43-2(e)(2) or in a revenue ruling, and therefore, the project using the method is a qualified tertiary recovery project provided it otherwise meets the requirements of § 43 and the regulations thereunder.

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion whether the project implemented by the Taxpayer otherwise meets the requirements of a qualified enhanced oil recovery project under § 43 and the regulations thereunder.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

**/s/**

Brenda M. Stewart  
Senior Counsel, Branch 7  
(Passthroughs & Special Industries)

PLR-149545-04

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cc: