LEGISLATIVE FISCAL OFFICE
Fiscal Note

Louisiana Legislative Fiscal Office Fiscal Notes

Fiscal Note On: **HB 506** HLS 20RS 332

Bill Text Version: **ENGROSSED**

Opp. Chamb. Action:

Proposed Amd.:

Sub. Bill For.:

Date: May 12, 2020 2:59 PM

Author: DEVILLIER

Dept./Agy.: Revenue

Subject: Reduce Oil Severance Tax Rate

Analyst: Greg Albrecht

TAX/SEVERANCE TAX EG DECREASE GF RV See Note

Reduces the severance tax rate for oil over a certain period of time and clarifies the severance tax rate for oil produced from certain incapable wells

Present law imposes a severance tax rate on most oil produced in the state at 12.5% of value. Wells producing less than 25 barrels per day and at least 50% salt water per day pay one-half the tax rate (incapable wells, 6.25%). Wells producing less than 10 barrels per day pay one-quarter the tax rate (stripper wells, 3.125%).

Proposed law reduces the full-rate from 12.5% to 8.5% in one-half percent increments by July 1, 2028 (starting in FY22). The tax rate will be 12% for FY22, 11.5% for FY23, 11% for FY24, 10.5% FY25, 10% for FY26, 9.5% for FY27, 9% for FY28, and 8.5% for FY29 and thereafter. The current tax rates on incapable and stripper well production are retained at 6.25% and 3.125%, respectively. In addition, the bill provides oil and natural gas price triggers during FY21, such that at any time oil falls below $30/bbl the oil severance tax rate shall be 2%; when natural gas prices fall below $1.90/mcf the gas severance tax rate shall be reduced by 80%. Effective upon governor's signature.

EXPENDITURES	2020-21	2021-22	2022-23	2023-24	2024-25	5 -YEAR TOTAL
State Gen. Fd.	$575,000	$476,000	$483,000	$490,000	$497,000	**$2,521,000**
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	$0	$0	$0	$0	$0	**$0**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**$575,000**	**$476,000**	**$483,000**	**$490,000**	**$497,000**	**$2,521,000**

REVENUES	2020-21	2021-22	2022-23	2023-24	2024-25	5 -YEAR TOTAL
State Gen. Fd.	DECREASE	($8,800,000)	($20,600,000)	($32,500,000)	($43,200,000)	**($105,100,000)**
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	DECREASE	($400,000)	($1,300,000)	($2,400,000)	($3,400,000)	**($7,500,000)**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total		**($9,200,000)**	**($21,900,000)**	**($34,900,000)**	**($46,600,000)**	**($112,600,000)**

EXPENDITURE EXPLANATION

The Dept. of Revenue estimates that it will incur some $208,000 of staff time cost to initially modify the tax administration system to incorporate the provisions of the bill, with additional costs each year of $103,000 as the tax rate changes annually. Such costs are typically absorbed by the Dept. initially, but become a component of budget funding as legislative changes accumulate. The bill provides no guidance as to what price concepts are associated with the triggers, and tt is not clear how the Dept. will administer the price trigger provisions of FY21. Continued on page 2

REVENUE EXPLANATION

Based on the May 11, 2020 official REC forecasts of mineral revenue, and the FY19 share of severance tax attributable to oil (61%), the phase-down of the full-rate 12.5% tax rate, as provided in the bill, results in state severance tax revenue losses of some $9 million in FY22, growing to $47 million by FY25, and further growing to $94 million by FY29 when the tax rate phase-down is complete. This revenue loss would be shared with local parish governments through the constitutional parish severance tax allocation. Parish severance tax allocation losses are estimated at $412,000 in FY22, growing to $3.4 million by FY25, and further growing to $6.9 million by FY29. The balance of the total severance tax revenue loss and the parish severance tax allocation loss is the state general fund severance tax loss; ranging from some $9 million in FY22, and growing to $43 million by FY25, and further growing to $87 million by FY29.

The bill also includes price triggers that could reduce revenue collections during FY21. At any time during FY21 that the oil price falls below $30/bbl the oil severance tax rate shall be 2%; at any time during FY21 that natural gas prices fall below $1.90/mcf the gas severance tax rate shall be reduced by 80%. The gas tax rate for FY21 has been established at 9.34/ mcf. The current official forecast includes an average oil price of $32.17/bbl in FY21, and $2.40/mcf gas price average. Both exceed the trigger prices in the bill. However, oil and gas prices are volatile and highly uncertain, and the bill triggers tax rate reductions "at any time" the price falls below the triggers. Thus, it is possible that prices will be lower than the triggers during some portion of FY21, and that revenue collections during FY21 wold be reduced by some uncertain amount.

However, specific estimates of state general fund loss and dedicated parish allocation losses provided in the table above are highly uncertain at this time because the bill's effect follows a period of unprecedented volatility of uncertain duration in the world oil market as a result of global demand weakness from the Covid-19 virus pandemic, and a global supply glut resulting from a market share competition between Saudi Arabia and Russia. Total state mineral revenue receipts and constitutional parish allocations will be substantially impacted by these events for the foreseeable future. However, the bill can only result in a significant loss of state severance tax receipts and parish allocation amounts from what would otherwise be the case. The estimates above reflect the current forecasts of this uncertain event. Continued on page 2

Senate / Dual Referral Rules

[x] 13.5.1 >= $100,000 Annual Fiscal Cost {S & H}

[x] 13.5.2 >= $500,000 Annual Tax or Fee Change {S & H}

House

[x] 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}

[ ] 6.8(G) >= $500,000 Tax or Fee Increase or a Net Fee Decrease {S}

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CONTINUED EXPLANATION from page one:

CONTINUED EXPENDITURE EXPLANATION

Price fluctuations around the $30.00/bbl and $1.90/mcf triggers could conceivably change tax rates repeatedly through the fiscal year, requiring considerable taxpayer oversight and guidance. The additional uncertainty of the price triggers in FY21 and the annually changing tax rates in subsequent years may also require additional auditor resources. The Dept. indicates the likely need for 4 additional tax auditor positions and associated expenses (FY21: $367,000 personnel and travel, growing to $393,000 by FY25).

CONTINUED REVENUE EXPLANATION

Since production on state lands and waterbottoms pays severance tax as well, and state royalty receipts are adjusted for their share of the severance tax, the bill's severance tax reduction results in a relatively small gain in state royalty receipts, shared with parish governments through the constitutional parish royalty allocation (10% of royalties attributable to production with each parish). State general fund royalty gains are estimated at some $61,000 in FY22, growing to $311,000 by FY25, and further growing to $623,000 by FY29. Parish royalty allocation gains are estimated at some $7,000 in FY22, growing to $35,000 by FY25, and further growing to $69,000 by FY29.

Over the fiscal note horizon, the net effect to the state general fund and the dedicated parish allocations is shown in the table above. By FY29, net state general fund losses are $86.3 million, and net dedicated parish allocation losses are $6.8 million.

Senate	Dual Referral Rules	House
[x]	13.5.1 >= $100,000 Annual Fiscal Cost {S & H}	[x] 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}
[x]	13.5.2 >= $500,000 Annual Tax or Fee Change {S & H}	[ ] 6.8(G) >= $500,000 Tax or Fee Increase or a Net Fee Decrease {S}

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