LEGISLATIVE FISCAL OFFICE
Fiscal Note

Fiscal Note On: **HB 28** HLS 202ES 54
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: September 30, 2020 12:07 PM
Author: DEVILLIER
Dept./Agy.: Revenue
Subject: Severance Tax Exemption - Incapable Well Oil Production
Analyst: Greg Albrecht

TAX/SEVERANCE TAX OR -$2,436,000 GF RV See Note

Reduces the rate of severance tax on oil produced from incapable wells under certain conditions (Item #61)

Current law imposes a severance tax on the production from incapable wells (no more than 25 barrels of oil and at least 50% salt water per producing day) of 6.25% of the value of the oil when severed.

Proposed law reduces the tax rate to 3.125% in any month when the average value is less than $75 per barrel. The Dept of Revenue shall determine the oil value quarterly based on the average New York Mercantile Exchange Price in the prior three months. This exemption is available for nine years, from January 1, 2021 through December 31, 2029.
The bill also requires all production reports be filed timely with the Revenue Dept verifying the average daily production during each month.

EXPENDITURES	**2020-21**	**2021-22**	**2022-23**	**2023-24**	**2024-25**	**5 -YEAR TOTAL**
State Gen. Fd.	SEE BELOW	SEE BELOW	SEE BELOW	SEE BELOW	SEE BELOW	
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						

REVENUES	**2020-21**	**2021-22**	**2022-23**	**2023-24**	**2024-25**	**5 -YEAR TOTAL**
State Gen. Fd.	($1,050,000)	($2,100,000)	($2,100,000)	($2,100,000)	($2,100,000)	**($9,450,000)**
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	($168,000)	($336,000)	($336,000)	($336,000)	($336,000)	**($1,512,000)**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**($1,218,000)**	**($2,436,000)**	**($2,436,000)**	**($2,436,000)**	**($2,436,000)**	**($10,962,000)**

EXPENDITURE EXPLANATION

The Department's current assessment of staff time associated with modifications to the tax processing system to incorporate a new tax return necessary to implement the price-based exemption in this bill is $151,000. Additional staff time costs associated with handling issues with taxpayers resulting from this change may also be incurred. In addition, the Taxpayer Compliance Division and the Field Audit Division each anticipate the need for an additional position to review returns to verify stripper certification, and to administer taxpayer inquiries and compliance ($78,000 FY21, $160,000 FY22).

REVENUE EXPLANATION

Currently, these wells are subject to the incapable rate of 6.25% of value (1/2 the tax of full-rate production). Over the last four years, these wells and have been producing approximately 1.3 million barrels of oil per year, and are being exempted from approximately $4.8 million of severance tax per year (1.3 million barrels and $4.6 million in FY20), relative to the full-rate tax of 12.5% of value.

Oil prices are currently less than $75/bbl, and are not currently expected to exceed that price during the fiscal note horizon. Thus, the bill is expected to exempt these wells from one-half their current level of tax payment, some $2.4 million per year. Modestly rising oil price projections are currently projected, and are assumed to offset modestly declining production over the fiscal note horizon. The price/exemption determination is to be made on a quarterly basis and, under extreme price movements, in some portions of a year this production could be exempt, and in some portions taxable.

On the full-year basis of FY20 actual collections, approximately 86% of annual severance tax reductions will affect the state general fund ($2.1 million), with 11% affecting the parish severance tax allocation ($264,000) and 3% the wetlands fund allocation ($72,000). Half-year effects are assumed for FY21 since the bill's exemption is available beginning with the second half of FY21 (January 1, 2021). Some portion of this exempted production will occur on state lands/waterbottoms, resulting in a small royalty gain offset (less than 1%) to the severance tax losses estimated above. In addition, specific estimates of revenue loss are highly uncertain at this time due to the effects of the Covid-19 virus pandemic on economic activity in general and oil prices in particular.

While a severance tax exemption is similar to a price increase for producers, research by the LSU Center for Energy Studies finds that oil and natural gas production are relatively unresponsive to price changes, and therefore severance tax rates. Specifically, oil production from new wells (one year of age or less) is estimated to increase by 6.2 percent in response to a 10 percent increase in prices in the long run. A statistically significant response of total production to prices in Louisiana is not observed in the long run. A state unilaterally changing severance tax rates may exhibit greater production response, but research on this case still finds the response to be small. This bill targets incapable production in particular, and it seems unlikely that exemption from a relatively low tax rate on relatively low volume wells will elicit material additional or new well drilling and production over a fiscal note horizon.

Senate — Dual Referral Rules

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

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

House

[ ] 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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