LEGISLATIVE FISCAL OFFICE
Fiscal Note

Fiscal Note On: **HB 29** HLS 202ES 4
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: October 1, 2020 6:10 PM
Author: DEVILLIER
Dept./Agy.: Natural Resources / Revenue
Subject: Severance Tax Exemption For New or Enhanced Wells
Analyst: Greg Albrecht

TAX/SEVERANCE-EXEMPTION OR -$36,000,000 GF RV See Note
Suspends severance taxes on production from certain oil wells (Items #26 and 61)

Proposed law provides an exemption from severance taxes on oil production occurring on or after October 1, 2020 from any newly drilled well or from a completed well undergoing enhancements that require a DNR permit, such as re-entries, workovers, or plug-backs. The exemption lasts for 24-months or until payout of well drilling costs or enhancement costs is achieved, whichever occurs first, as determined by the Dept. of Natural Resources. The availability of the exemption extends through December 31, 2025.

Effective upon governor's signature.

The fiscal note assumes that the bill does not intend to provide its tax exemption to oil condensate produced by natural gas wells.

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.	($4,520,000)	($22,580,000)	($36,120,000)	($36,120,000)	($36,120,000)	**($135,460,000)**
Agy. Self-Gen.	$25,000	$81,000	$129,000	$129,000	$129,000	**$493,000**
Ded./Other	($740,000)	($3,680,000)	($5,880,000)	($5,880,000)	($5,880,000)	**($22,060,000)**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**($5,235,000)**	**($26,179,000)**	**($41,871,000)**	**($41,871,000)**	**($41,871,000)**	**($157,027,000)**

EXPENDITURE EXPLANATION

The Department of Revenue's current assessment of staff time associated with modifications to the tax processing system to incorporate a new tax return necessary to implement the payout-based exemption in this bill is $151,000. Although necessary determinations are required of the Dept of Natural Resources, the exemption is against severance tax administered by the Dept of Revenue, and additional personnel in the Dept of Revenue may be necessary.
Continued on page 2

REVENUE EXPLANATION

Using FY20 as an initial model for a baseline of activity affected by the bill, the Dept of Natural Resources indicates that there were some 55 new wells (735,000 barrels) and 160 recompletion wells (4.2 million barrels) brought into production. The severance tax value of this production at an FY20 oil price of $46.42/bbl is approximately $28 million per year. This accounts for the different tax rates applied to the wells based on their daily volumes (12.5% full-rate, 6.25% incapable, 3.125% stripper). Well costs (new and recompletion) can vary considerably across wells, but the relatively low severance tax value per well (at most $420,000, at least $363) suggests that nearly all affected wells are likely to receive a 24-month exemption. Thus, the FY20 proxy generates a first full year effect of the bill of some $28 million of severance tax revenue loss. The second full year of revenue loss is double at $56 million; the second 12-months of exemption for the first year's participating wells plus the first 12-months of exemption for the second year's participating wells. Revenue losses stabilize at that level through FY27 before falling off as the last wells entering the program in 2025 exhaust their 24-months of exemption. The period of FY21 is roughly half a one-year effect, depending on how fast program participation ramps up.

This is a simple model of the potential revenue loss from the bill. More realistic losses are likely less than this due to the major factors of a somewhat lower oil price outlook, probably fewer wells involved than in FY20, and the possibility that some wells may achieve the payout equivalent of their severance tax exemption in less than 24-months. However, if oil prices strengthen over time, these dampening factors would be less significant or even reversed. That said, an adjustment of the FY20 model results by as much as 25%, still results in first full year revenue losses of $21 million and subsequent full years of $42 million. Annual losses are likely to ramp up to these full year effects because the bill starts one-quarter of the way into FY21, and wells will come in production over the course of year. There is no precise way to estimate the phase-in of the exemption effect. To reflect this ramp-up, it is assumed that 1/4 of a full year effect occurs in FY21, and one-half of first and second year effects accumulate over FY22 and beyond. Allocation of revenue loss is approximately 86% to the general fund and 14% to the dedicated funds {wetlands fund (3%) and parish allocations (11%)}. 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. Continued on page 2

Senate	Dual Referral Rules	House
☐	13.5.1 >= $100,000 Annual Fiscal Cost {S & H}	☐ 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}
☒	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}

Christopher A. Keaton
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CONTINUED EXPLANATION from page one:

Continued Revenue Explanation

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. Thus, the bill is likely to result in revenue losses.

Continued Expenditure Explanation

The Revenue Dept Taxpayer Compliance Division and the Field Audit Division each anticipate the need for an additional position to review returns to verify proper certification, and to administer taxpayer inquiries and compliance ($78,000 FY21, $160,000 FY22).

Since the bill relies on existing DNR permitting, administrative costs of the Dept may not be materially effected. The Dept indicates that there will be potentially an additional 500 hours of work time associated with processing approximately 255 applications per year for the required certifications ("Application for Severance Tax Relief - Well Status Determination") each year. The application fee is $504, generating $129,000 per year in fee revenue to the Dept. DNR does not anticipate the need for additional personnel, but these fees would be available to cover additional administrative costs. The fee revenue would be deposited to the Oil and Gas Regulatory Fund statutory dedication, but is depicted on the table on page one as self-generated revenue to distinguish it from the revenue loss components of the bill. This fee revenue is depicted as ramping up at the same pace as the total revenue loss estimates. However, should there be an influx of applications for various types of recompletions, the Dept may require additional resources to timely process permits.

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☐	13.5.1 >= $100,000 Annual Fiscal Cost {S & H}	☐ 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}
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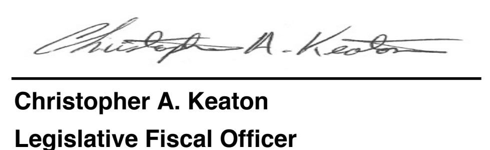

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