LEGISLATIVE FISCAL OFFICE
Fiscal Note

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

Date: October 22, 2020 1:22 PM
Dept./Agy.: Natural Resources / Revenue
Subject: Severance Tax Exemption For Orphaned Wells

Author: DEVILLIER
Analyst: Greg Albrecht

TAX/SEVERANCE-EXEMPTION EN -$10,375,000 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 from any newly drilled well, a completed well undergoing enhancements that require a DNR permit, or an orphan well. The exemption lasts up to the earlier of either payout of well drilling or enhancement costs is achieved, or 12-months for new wells, 6-months for recompleted wells, or 24-months for orphan wells. Available to wells that commence production on or after January 1, 2021 and on or before December 31, 2023. Participating wells are limited to only one exemption per wellhead. If a participating orphaned well is unable to produce in paying quantities, the operator may be reimbursed costs to plug and abandon the well from the Oilfield Site Restoration Fund. The Fund threshold, above which the per barrel and mcf fee is halted is increased to $25 million from $14 million. The Fund's fees are applicable to production participating in the bill's tax exemption. The number of participating wells and exemption cost, as well as the number of orphan wells plugged and reimbursement cost is to be reported by March 1, 2023. Operators violating Statewide Order 29-B are not eligible for the exemptions.

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.	($4,515,000)	($6,484,000)	($10,375,000)	($10,375,000)	($1,345,000)	**($33,094,000)**
Agy. Self-Gen.	$25,000	$81,000	$129,000	$129,000	$0	**$364,000**
Ded./Other	($735,000)	($1,056,000)	($1,689,000)	($1,689,000)	($219,000)	**($5,388,000)**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**($5,225,000)**	**($7,459,000)**	**($11,935,000)**	**($11,935,000)**	**($1,564,000)**	**($38,118,000)**

EXPENDITURE EXPLANATION

Well eligibility is determined by the Dept. of Natural Resources, while the period of exemption is determined by the Dept of Revenue. 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. See page 2

REVENUE EXPLANATION

The estimated severance tax losses resulting from this version of the bill are based on adjustments to the loss estimates of the reengrossed bill. Reengrossed bill loss estimates are explained on the fiscal note for that version of the bill. Those estimates were adjusted downward for this version of the bill in proportion to the different lengths of time this version of the bill allows for exemption (6 months for recompleted wells and 12 months for new wells) relative to the length of time in the reengrossed bill (24 months for all wells). Costs for new wells are such that they will receive a full 12 month exemption. Costs for recompletions are such that they will likely receive a full 6 month exemption, although there may be some of these wells that achieve payout before 6 months. Orphan wells receive a 24 month potential exemption period, but the nature of orphan wells is such that it seems unlikely that orphan wells will significantly participate in the exemption program. By shortening the months of potential exemption from the reengrossed bill, this version of the bill reduces the severance tax loss ramp-up, since wells will come off of exempt status earlier, subjecting their production to tax earlier. This assumes that production from these wells is sustained beyond their exemption period. The FY21 severance tax loss is the same as in the reengrossed bill, since these wells will likely receive at least 6 months of exemption, and only one-half of a year's production was already assumed to be affected in the reengrossed bill. This version of the bill requires participating production to commence by December 31, 2023. This works to terminate exemption for recompletions by the end of FY24, and for new wells by half-way through FY25. By FY26 no exemptions are in effect.

The key components of an estimated severance tax loss are:
(a) FY20 actual new well (55) and recompleted well (160) production, at FY20's $46 per barrel average price, reflect the routine annual baseline of activity that the bill exempts.
(b) The FY20 actual activity was discounted by 25% for FY21 and beyond to acknowledge a weak price outlook.
(c) No additional well activity was assumed, based on empirical findings by LSU's Center for Energy Studies.
(d) This static analysis accounts for aggregate dynamic effects, in that stimulative effects on sales and incomes from drilling sector spending are offset by the contractionary effects on sales and incomes from diminished public sector spending (the state government balanced budget constraint).
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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}

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CONTINUED EXPLANATION from page one:

Continued Revenue Explanation

The dedicated fund reductions in the table above reflect the loss to the parish severance tax allocation and the wetlands fund allocation from the overall loss of state severance tax collections. Some portion of this exempted production may 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 due to the effects of the Covid-19 virus pandemic on economic activity in general and oil prices in particular.

The bill also increases the threshold of the Oilfield Site Restoration Fund per barrel and per mcf fees (from $14 million to $25 million) above which the fee collections are halted. Thus, additional dedicated funding to that special fund is possible, largely dependent upon the volume of oil and gas production in the state; although such fee collections have not achieved those levels in the past.

The Dept of Natural Resources indicates that there will be potentially 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. 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.

The Dept of Natural Resources has expressed concern regarding the provision that provides for reimbursement from the Oilfield Site Restoration Fund to well operators that plug and abandon a well that fails to produce in paying quantities. The program/Fund has limited resources for plugging the existing priorities of orphan wells, and the bill's language may allow wells affected by this bill to draw on the Fund without going through the program's prioritization and bidding process for plugging and abandoning. However, the bill provides the authority to the Secretary of the Dept to approve or deny reimbursement in whole or in part, and to promulgate appropriate rules, in consultation with the office of conservation.

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. DNR does not anticipate the need for additional personnel, but these fees would be available to cover additional administrative costs. However, should there be an influx of applications for various types of recompletions, the Dept may require additional personnel resources to timely process permits. The application fee is $504, generating $129,000 per year in fee revenue to the Dept.

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