LEGISLATIVE FISCAL OFFICE
Fiscal Note

Louisiana Legislative Fiscal Office — Fiscal Notes

Fiscal Note On: **HB 661** HLS 21RS 844
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: May 2, 2021 2:15 PM
Author: COUSSAN
Dept./Agy.: Natural Resources / Revenue
Subject: Severance Tax Exemption For Newly Drilled Wells
Analyst: Greg Albrecht

TAX/SEVERANCE-EXEMPTION OR -$2,411,000 GF RV See Note
Exempts oil production of certain newly drilled wells from severance tax

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 that full-rate (incapable wells, 6.25%). Wells producing less than 10 barrels per day pay one-quarter the full-rate (stripper wells, 3.125%).

Proposed law provides a severance tax exemption for oil production from newly drilled wells, excluding horizontally drilled wells. The exemption period is the earlier of months to payout of well costs or 12-months. Available to wells that commence production on or after January 1, 2022 and on or before December 31, 2024. Only one exemption is allowed per wellhead.

Effective upon governor's signature.

EXPENDITURES	**2021-22**	**2022-23**	**2023-24**	**2024-25**	**2025-26**	**5 -YEAR TOTAL**
State Gen. Fd.	INCREASE	INCREASE	INCREASE	INCREASE	INCREASE	
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	**2021-22**	**2022-23**	**2023-24**	**2024-25**	**2025-26**	**5 -YEAR TOTAL**
State Gen. Fd.	($2,411,000)	($15,853,000)	($18,263,000)	($15,686,000)	($1,809,000)	**($54,022,000)**
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	($181,000)	($1,193,000)	($1,375,000)	($1,181,000)	($136,000)	**($4,066,000)**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**($2,592,000)**	**($17,046,000)**	**($19,638,000)**	**($16,867,000)**	**($1,945,000)**	**($58,088,000)**

EXPENDITURE EXPLANATION

The Dept. of Natural Resources indicates no additional administrative expenses. The Dept. of Revenue has indicated $77,000 of staff time to modify tax processing systems to incorporate similar exemptions provided in other bills, as well as 2 additional positions (Compliance Division and Field Audit Division) at roughly $160,000 per year; one-half of one position in FY22 plus setup costs, and 2 positions annually through the life of the program. This bill involves fewer participating wells but the exemption is based on a time to payout concept or a fixed time period, varying the exempt period per well.

REVENUE EXPLANATION

The LSU Center for Energy Studies (CES) analyzed bills involving new and enhanced wells combined, and enhanced wells separately. The difference between these results was taken as an estimate of this bill involving new wells only. CES consulted with private energy firms and consultants, other LSU economists, and economists from DNR and the Legislative Fiscal Office (LFO). That analysis was based on an existing baseline of 187 new wells per year in the state, modeled well types (full-rate, incapable, and stripper), accounted for production decline rates, the number of tax exempt months provided by the bill, the differing severance tax rates based on well production volumes, and the current official REC forecasts of oil prices. The resulting baseline severance tax losses were estimated at $2.6M in FY22, $17.0M FY23, $19.6M FY24, $16.9M FY25, and $1.9M FY26; totaling $58.1M over five years. Approximately 7% of these losses will accrue to the parish severance tax allocation, with the balance accruing to the state general fund. These losses are based on the bill's full 12-month exemption period for new wells. Loss estimates that were roughly 19% smaller over the five year horizon were made, as well, based on a 9-month exemption period for new wells. However, this shorter exemption period does not seem consistent with likely new well costs, payout of which will actually determine the length of the exemption period. A broad aggregate approach, averaging within well types, utilized by DNR and the LFO, resulted in $87.8M of baseline severance tax loss, with much of the difference with CES being in the first year and due to no accounting for well production decline rates.

CES also estimated possible effects on inducing additional oil drilling, and the associated economy-wide impacts. This analysis was based on the effect on the internal rate of return of wells from the oil price change equivalent of the severance tax exemption, and earlier CES estimates of the long-run responsiveness of oil production to oil price changes. The results were 29 additional wells producing over a five year period. Production from these wells could offset losses by somewhat less than 8.4% over five years, with state royalty gains providing somewhat less than an additional 2.5% of offset (if all were on state land/waters). General economy-wide tax receipts attributable to the spending associated with these induced wells provides somewhat less than another 7.3% offset. Total positive offsets to the baseline severance tax losses would be somewhat less than 18.2%. To complete the analysis, the state's balanced budget constraint was recognized, requiring governmental spending reductions or compensating tax increases matching the severance tax losses. The analysis reduced state government spending through various sectors of the economy, proportional to the state budget, negating somewhat less than 24% of the positive offsets (generously reducing spending after positive offsets and not accounting for federal match consequences of health care spending cuts). Complete results reduced the baseline severance tax loss by somewhat less than 13.8%. This offset is as large as it is because the bill affects an industry with a long presence and well-developed supplier linkages in the state economy. Other incentive programs may not provide similar effects. While this type of analysis can provide interesting results, and the CES analysis is quite thorough and involved considerable hours of work, various aspects of analysis such as this in general are subject to increased levels of uncertainty, and are less reliable for budgeting purposes.

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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