LEGISLATIVE FISCAL OFFICE
Fiscal Note

Fiscal Note On: **HB 474** HLS 13RS 1050
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: April 22, 2013 4:30 PM
Author: BISHOP, STUART
Dept./Agy.: Natural Resources / Revenue
Subject: Inactive Well Severance Tax Exemption Program
Analyst: Greg Albrecht

ENERGY/DRILLING OR +$40,700,000 GF RV See Note
Provides relative to the exemption from severance tax for inactive wells

Current law provides a five-year 100% exemption from severance tax to oil & gas production from wells re-entered after two years of inactivity. Applications were last accepted for the program June 30, 2010, and severance tax exemption can occur essentially through the end of FY15 ("from the date production begins or 90-days from the date of the application, whichever occurs first").

Proposed law subjects this production to a tax rate of 6.25% of value for a period of ten years. After that production would be subject to the normal rate of 12.5%.

EXPENDITURES	2013-14	2014-15	2015-16	2016-17	2017-18	5 -YEAR TOTAL
State Gen. Fd.	$0	$0	$0	$0	$0	**$0**
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	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**

REVENUES	2013-14	2014-15	2015-16	2016-17	2017-18	5 -YEAR TOTAL
State Gen. Fd.	$40,700,000	$38,700,000	($35,100,000)	($36,100,000)	($35,500,000)	**($27,300,000)**
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	**$40,700,000**	**$38,700,000**	**($35,100,000)**	**($36,100,000)**	**($35,500,000)**	**($27,300,000)**

EXPENDITURE EXPLANATION

The Department of Revenue will incur some marginal costs to modify the tax processing system of handle the modifications to this program.

REVENUE EXPLANATION

Both the Department of Revenue (LDR) and the Department of Natural Resources (DNR) interpret the bill as imposing tax on the production of wells that are currently benefiting from full exemption. Thus, severance tax receipts increase for FY14 and FY15 as this production goes from a 0% tax rate to a 6.25% tax. DNR estimated the current law tax exemption total based on the current 9% share of total state oil production coming from inactive wells, and their projections of total oil production and price over the next five years (a 2.6% total production decline and a $10/bbl price decline over the next five years). Current law revenue expected to be foregone in FY14 and FY15 is $81.4 million and $77.5 million, respectively. Consequently, under proposed law this production would bring one-half the foregone amount or, $40.7 million and $38.7 million in FY14 and FY15, respectively. LDR estimated $49.5 million per year would be gained. In the subsequent years of FY16 - FY18, state revenue would be lost. In those years, current law would subject this production to a 12.5% tax rate, while proposed law would impose a 6.25% tax rate. Revenue losses are estimated by DNR at $37.1 million, $36.1 million, and $35.5 million in each year, respectively. LDR estimated $43.5 million per year would be lost.

It is possible that, under current law, some production would be fully exempt into FY16. Thus, under proposed law, there could be some revenue gain in FY16 to help offset the gross loss in that year. However, this extension of the current exemption program can only be for 90 days into FY16 since the five-year exemption period started "from the date production begins or 90-days from the date of the application, whichever occurs first", and applications could not be accepted after June 20, 2010. DNR estimated that 90-day effect at about $2 million. Even if all production received a 90-day longer exemption period under current law, the bill would still result in a net revenue loss to FY16 of $27.8 million (rather than $37.1 million).

Neither DNR or LDR included gas production in their estimates, although the bill establishes a 6.25% tax rate for gas production. Gas has been small in the program, and that rate applied to gas imposes a tax that is substantially higher than the full rate tax on gas, which does not seem consistent with the intent of the bill. Finally, it seems unlikely that a 6.25% tax rate will elicit additional production that would not otherwise occur (even when compared to a 12.5% rate now). Only about 43% of wells still qualified in the program have been re-entered or are producing, even though oil prices have been very high historically over much of the latest five-year exemption period and a 100% tax exemption could have been received.

Senate — Dual Referral Rules — House

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

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