# LEGISLATIVE FISCAL OFFICE
## Fiscal Note

Fiscal Note On: **HB 713** HLS 14RS 1471
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

| | | | |
|---|---|---|---|
| **Date:** | March 28, 2014 10:45 AM | **Author:** | GREENE |
| **Dept./Agy.:** | Revenue | | |
| **Subject:** | Severance Tax Refunds | **Analyst:** | Greg Albrecht |

TAX/SEVERANCE TAX OR -$60,000,000 GF RV See Note 

Provides that severance taxes do not have to be paid during the period of a suspension or exemption from severance tax when the well operator holds a certificate of good standing

Current law suspends the severance tax the production of oil & gas from horizontally drilled wells and wells drilled to a true vertical depth of 15,000 feet or more. The suspension is for 100% of the tax for the earlier of 24-months or until well cost payout. Effectively, the suspension is for 24-months of production. In practice, producers tend to pay the severance tax on production until at least final certifications by DNR and possibly longer, and realize the suspension benefit via refund claims on future returns. Those refunds are paid with judicial interest applied (currently 4% through 2014, and since 2011).

Proposed law states that the severance tax shall not be required to be paid during the suspension period when the operator is in good standing with the Depts. of Revenue and Natural Resources, and has qualified for the suspension prior to the beginning of production.
Effective upon governor's signature.

| **EXPENDITURES** | **2014-15** | **2015-16** | **2016-17** | **2017-18** | **2018-19** | **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** | **2014-15** | **2015-16** | **2016-17** | **2017-18** | **2018-19** | **5 -YEAR TOTAL** |
|---|---|---|---|---|---|---|
| State Gen. Fd. | ($60,000,000) | ($39,000,000) | ($26,000,000) | DECREASE | DECREASE | **($125,000,000)** |
| 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** | **($60,000,000)** | **($39,000,000)** | **($26,000,000)** | | | **($125,000,000)** |

**EXPENDITURE EXPLANATION**

There is no anticipated direct material effect on governmental expenditures as a result of this measure. The Departments of Revenue and Natural Resources will issue certificates of good standing to eligible producers/operators. Any associated costs should be minimal.

**REVENUE EXPLANATION**

With the ramp up of major severance tax suspension programs over the past several years, including the horizontal drilling and deep well programs addressed in this bill, severance tax refunds have increased dramatically. Refunds jumped up sharply starting in the fall of 2009, peaked in the fall of 2011, and have stabilized at an average of $7.8 million per month since April of 2012. The Revenue Dept. estimates 81% of this monthly average is estimated to be associated with the horizontal drilling and deep well programs, or $6.3 million per month. That figure is taken as a proxy for the monthly amount of severance tax overpayments that this bill is encouraging taxpayers to not pay; with $75.6 million the annual amount. Without regard to the timing of overpayments and associated refunds, the bill has no fiscal impact. Under current practice, overpayments are refunded back to taxpayers, with no net effect on the state fisc. Under this bill, potentially no overpayments are received simply because a well is participating in either of these two programs, and no associated refunds occur, as well. The effect is the same on the state fisc.

However, there is likely a transition cost to accomplishing the bill's goal. The Revenue Dept. looked at a few recent months of refunds with respect to the overpayment periods the refund amounts were associated with (after adjusting for payments due to audit). Substantial amounts of refund in any month (and year) can be associated with overpayments made one, two, or even three or more years prior. This review suggests 20% of refunds are for overpayments in the same year, 34% for the immediate prior year, 18% for the second prior year, and 28% for the third prior year. This limited review is generally consistent with analysis done when the refunds increased sharply in the fall of 2009. Thus, if all overpayments targeted by the bill were to cease for FY15, there would still likely be refund payments made for overpayments in FY14, FY13, and even FY12 and earlier, but offsetting overpayments in the current period would not be received. This would result in a net loss of revenue collections each year going forward until all overpayments made in all prior years are finally refunded. Rough estimates of this loss would be $60 million in FY15 (80% of $75.6 million for 3 prior years), $39 million in FY16 (52% of $75.6 million for 2 prior years), and $26 million in FY17 (34% of $75.6 million for 1 prior year). Diminishing losses may also occur in FY18 and FY19, as well.

These rough estimates assume full compliance with the bill's goals; that is, no overpayments of tax simply associated with participation in these two tax suspension programs. To the extent producers/operators continue to overpay their severance tax obligations and claim future refunds for exempt production, these estimates represent rough estimates of the state's loss exposure during the transition period, and actual losses may be materially less than these estimates.

Senate | Dual Referral Rules | House

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

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

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

☒ 6.8(F)(2) >= $500,000 State Rev. Reduc. {H & S}

☐ 6.8(G) >= $500,000 Tax or Fee Increase or a Net Fee Decrease {S}

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