



LEGISLATIVE FISCAL OFFICE
Fiscal Note

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

Date: April 14, 2014 6:04 PM	Author: GREENE
Dept./Agy.: Revenue	Analyst: Greg Albrecht
Subject: Severance Tax Refunds	

TAX/SEVERANCE TAX EG -\$28,500,000 GF RV See Note Page 1 of 1

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 effectively states that the severance tax shall not be required to be paid during the suspension period. The well operator must file preliminary applications and directional surveys prior to first production, and complete application for exempt status within 270 days of first production. Effective January 1, 2015.

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.	(\$28,500,000)	(\$47,000,000)	(\$30,900,000)	(\$12,350,000)	DECREASE	(\$118,750,000)
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	(\$1,500,000)	(\$2,500,000)	(\$1,600,000)	(\$650,000)	\$0	(\$6,250,000)
Annual Total	(\$30,000,000)	(\$49,500,000)	(\$32,500,000)	(\$13,000,000)		(\$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, 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 in mid-FY15, there would still likely be refund payments made for overpayments in early- FY15, FY14, FY13, and even FY12 and possibly 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. If started July 1, 2014, rough estimates of this cost 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). Delaying the start of the bill until January 1, 2015 does not change the total transition cost, but only shifts it back by six months and blends the calendar year components of the estimates above into a different fiscal year allocation that sums to the same total transition cost: \$30 million in FY15, \$49.5 million in FY16 (1/2 FY15 above + 1/2 FY16 above), \$32.5 million in FY17 (1/2 FY16 above + 1/2 FY17 above), and \$13 million in FY18 (1/2 FY17 above). Diminishing losses may also occur in FY19, as well.

These costs would be shared between the state and local governments receiving constitutional severance tax allocations in approximate shares of 95% from the state and 5% from local governments. This shared transition cost is what is shown in the table above.

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| <u>Senate</u> | <u>Dual Referral Rules</u> | <u>House</u> |
| <input type="checkbox"/> 13.5.1 >= \$100,000 Annual Fiscal Cost {S&H} | <input type="checkbox"/> 6.8(F)(1) >= \$100,000 SGF Fiscal Cost {H & S} | <input checked="" type="checkbox"/> 6.8(F)(2) >= \$500,000 State Rev. Reduc. {H & S} |
| <input checked="" type="checkbox"/> 13.5.2 >= \$500,000 Annual Tax or Fee Change {S&H} | <input type="checkbox"/> 6.8(G) >= \$500,000 Tax or Fee Increase or a Net Fee Decrease {S} | |

John D. Carpenter
 Legislative Fiscal Officer