F I S C A L I M P A C T R E P O R T

SPONSOR: Rawson DATE TYPED: 02/12/02 HB

SHORT TITLE: Well Workover Projects SB 345

ANALYST: Smith

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY02	FY03			
	($165.0)	($330.0)		Severance Tax Bonding Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files
Energy, Minerals & Natural Resources
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 345 amends the Natural Gas and Crude Oil Production Incentive Act so that an operator may be entitled to a reduction in the severance tax rate (from 3.75% to 2.4%) if the operator installs equipment that is "intended to substantially increase the life of the well." In order to qualify, any such equipment must be approved and certified by the Oil Conservation Division of the Energy, Minerals and Natural Resources Department. Before an operator would qualify, the division would have to determine that the equipment would "substantially" reduce operating costs thereby increasing the life of the well and recoverable reserves attributable to the well. The division would also have to determine that the installation of the equipment is not routine maintenance.

Significant Issues

Crude oil and natural gas prices are significantly lower than they were only one year ago. The drop in prices means that wells that were marginally economic to produce a year ago are becoming unprofitable. The bill provides an incentive to encourage continued production from these wells by reducing the overall tax burden. The bill does this by expanding the definition of a "well workover project" to include installation of equipment on a crude oil or natural gas well that is intended to "substantially" increase the life of the well (the Production Incentive Act currently permits a tax rate reduction when workover equipment is installed that "increases" production from the well). Crude oil and natural gas wells become uneconomic to produce before all the crude oil or natural gas is removed; all wells encounter this economic limit --- it is the time when the costs of producing the commodity exceed the amount for which it can be sold. The bill would increase the time a well is economically capable of producing at a profit, and would thereby increase the ultimate recovery of crude oil and natural gas.

FISCAL IMPLICATIONS

The Revenue table reflects estimates from TRD. The Energy, Minerals & Nat. Resources Department notes the following fiscal impact:

Direct revenue from oil and gas taxes would decrease to some degree if the bill became law. However, a study of the Interstate Oil and Gas Compact Commission and the Energy Council, "Against the Wind: The Economic Impact of Incentives During the Oil Price Collapse," by David M. Garlick and Patricia Cleary Leo, suggests that the impact of any reduction may be mitigated by economic benefits and resulting revenue. The authors analyzed the impact of existing well workover incentives in New Mexico and found that while they reduce annual direct tax revenue by $309,845 (oil and gas), the incentives produced economic activity that netted state and local governments an additional $5,121,337 in other taxes and revenue.

OTHER SUBSTANTIVE ISSUES

The bill would aid in preventing premature plugging and abandonment of wells due to low production, low prices and other causes. Without the bill there would be no production from the prematurely plugged and abandoned wells and therefore no accompanying taxes and royalties from the production benefiting the state.

SS/sb:ar