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

SPONSOR Larranaga **ORIGINAL DATE** 2/24/07 **LAST UPDATED** **HB** 777

SHORT TITLE Oil and Gas Reclamation Fund Stability **SB**

ANALYST Francis

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY07	**FY08**	**FY09**		
	NFI		Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Energy Minerals and Natural Resources Department (EMNRD)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

House Bill 777 changes the threshold for distributions from the oil and gas reclamation fund to $2.5 million up from $1.15 million. Current law for the oil and gas conservation tax has a variable rate depending on the balance in the oil and gas reclamation fund. If the fund, under current law, is above $1.15 million in any month, the rate is 0.18 percent and otherwise it is 0.19 percent. This law changes that threshold to $2.5 million.

Table 1: Current Law Oil and Gas Conservation Tax Mechanism

	Oil and Gas Conservation Tax	Distribution to General Fund
If Oil and Gas Reclamation Fund is greater than $1,150,000	0.18%	100%
Otherwise	0.19%	95%

FISCAL IMPLICATIONS

According to the Taxation and Revenue Department (TRD), there would be no fiscal impact since the oil and gas reclamation fund is estimated to be below the current threshold for the foreseeable future and so increasing the threshold does not impact the revenue. However, if prices continue to be high and the rate of funding projects from the reclamation fund has not kept up with the growth in value, the cap may be reached. By raising the cap, it means that the fund will be allowed to build up a larger reserve and the tax rate will remain at 0.19 percent.

TRD:

> The stability of the Reclamation Fund is directly related to the volatility of oil and gas prices. Conservation Tax collections and distributions change every month as oil and gas prices change. If stability of allocations to the Reclamation Fund is the objective, a funding requirement formula might be warranted.

SIGNIFICANT ISSUES

Energy Minerals and Natural Resources Department (Oil Conservation Division (OCD)):

> Raising the cap on the reclamation fund will allow the OCD to accumulate a "rainy day fund" to facilitate plugging and reclamation when the need is greatest, decrease the demand for manpower and equipment when the industry demand is greatest, help provide jobs when oil and gas prices fall, and plug abandoned wells and do reclamation work when the cost is lower.
>
> When oil and gas prices are low, weaker operators collapse, increasing the need for the state to plug abandoned wells and remediate abandoned sites. Prices for plugging and remediation are at their lowest, and personnel and equipment are available. However, the reclamation fund will also be at its lowest, because lower prices mean lower tax proceeds and lower distributions to the fund.
>
> When oil and gas prices are high, more taxes are collected and more money is distributed into the reclamation fund. When prices are high, the industry is healthy and there is less need for the state to plug abandoned wells and remediate abandoned sites. But when oil and gas prices are high, the OCD must spend the reclamation fund to stay below the cap. It often finds itself in a bidding war for manpower and equipment that is already fully utilized, driving up the costs of plugging services.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

OCD reports that the number of projects increases when prices are low and without an adequate reserve, it will be difficult to fund projects.

If the reclamation fund balance cap is reached, the oil and gas conservation tax will decline to 0.18 percent on production.

NF/mt