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

SPONSOR Adair **DATE TYPED** 03/08/05 **HB**

SHORT TITLE Reduce Natural Gas Severance Tax Rate **SB** 764

ANALYST Padilla-Jackson

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY06	FY07			
($50,500.0)	($48,400.0)	Similar	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to House Bill 644 and House Bill 1086

SOURCES OF INFORMATION

LFC Files

Responses Received From
New Mexico Public Education Department (PED)

SUMMARY

Synopsis of Bill

Senate Bill 764 proposes to decrease the tax rate on the severance of natural gas to the same rate currently imposed on the severance of crude oil. Specifically, the bill would decrease the Emergency School Tax rate on natural gas from 4 percent of taxable value to 3.15 percent.

The effective date of the provisions of this bill is July 1, 2005.

Significant Issues

The tax increase would equalize the rate paid by both natural gas and crude oil producers, placing them on equal footing. That said, current tax rate differentials between natural gas and crude oil producers could likely represent differences in profitability.

The NM PED commented that revenue generated from the severing of oil and gas and other natural resources from New Mexico lands is a major source of revenue for the state coffers and contributes directly and indirectly to available funding levels for school districts. They caution that a reduction in the tax rate for any of these services would lower available funding for the school districts.

PERFORMANCE IMPLICATIONS

NM PED provided the following comments:

The Public School Capital Outlay Council (PSCOC) is responsible for the administration of school-related construction projects throughout the state. According to current estimates released by the PSCOC, approximately $2.3 million is required for school capital needs to meet minimum school building adequacy standards. The current primary funding source for Supplemental Severance Tax Bonds (SSTB) and a portion of the Senior Severance Tax Bonds are the revenues generated under 7-31-4. SSTB are bonds issued by the State Board of Finance (SBF) and paid by revenue derived from the taxes levied upon the natural resource products severed and saved from the soil and other sources.

Current studies from the Public School Capital Outlay Task Force conclude that the state should continue to rely on SSTB as a permanent revenue stream for PSCOC projects based on current estimates of supplemental severance bonding capacity. The task force has concluded that for the foreseeable future these revenues should be sufficient to address the adequacy needs to provide for significant improvements in the condition of school facilities. Reducing the tax rate will decrease the bonding capacity and will decrease the available revenues dedicated for public school construction. In order to guarantee a minimum annual permanent revenue stream level of $125,000.0 for funding PSCOC projects, a reduction in current tax rates should be avoided. Without a permanent funding source, the PSCOC will not be guaranteed a level of support that it can distribute each year, which is a requirement mandated by the courts under the Zuni lawsuit, which claimed inequitable distributions of state capital outlay funds to school districts.

A reduction in available funding for capital outlay projects will also increase the timeframe for all school buildings to meet established minimum adequacy standards.

FISCAL IMPLICATIONS

The total fiscal impact of this bill is -$50.5 million for FY06 to the General Fund. The fiscal impact is calculated by comparing the product of the gas taxable value estimate and the proposed new rate of 3.15 percent versus the product of the gas taxable value estimate and the existing rate of 4 percent. The assumed taxable value is based on the most up to date consensus oil and gas revenue estimates for FY06 and FY07. The fiscal impact could change based on changes in natural gas prices, which have tended to be fairly volatile in recent years.

ADMINISTRATIVE IMPLICATIONS

Minimal impact to TRD.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

House Bill 644 also reduces the tax rate on the severance of natural gas to 3.15 percent, the same rate currently imposed on the severance of crude oil. However, House Bill 644 also proposes to reduce the stripper well incentive rates to be in the same proportion to 3.15 percent as the old rates were to 4 percent. House Bill 1086 proposes to increase the tax rate on the severance of crude oil from 3.15 percent to 4 percent.

TECHNICAL ISSUES

In a similarly drafted bill dealing with crude oil, the Energy, Minerals & Natural Resources Department pointed out that the bill does not include a corresponding change in the tax rate imposed on natural gas removed from a stripper well property. They believe that those rates would have to be addressed also in order to completely equalize the oil and gas tax rates.

OPJ/lg:yr