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FISCAL IMPACT REPORT

ORIGINAL DATE 2/5/06
 SPONSOR Grubestic LAST UPDATED 2/6/06 HB _____
 SHORT TITLE Oil & Gas Severance Surtax & Fund SB 468
 ANALYST Francis

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Non-Rec	Fund Affected
FY06	FY07		
	155,500.0	Recurring	Severance Tax Permanent Fund

(Parenthesis () Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY06	FY07	FY08		
	155,500.0	\$303,700.0	Recurring	Severance Tax Permanent Fund
	155,500.0	303,700.0	Recurring	Community Energy Security Fund

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files
 Consensus Revenue Group

Responses Received From

Higher Education Department (HED)
 Energy Minerals and Natural Resources (EMNRD)
 Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 468 creates a new fund called the “Community Energy Security Fund,” imposes a surtax on oil and gas severance receipts, and distributes the proceeds of the surtax to the created fund.

The community energy security fund will be used first for making grants to municipalities, counties and public institutions of higher education to conduct studies on the economic impact of high energy costs. For municipalities and counties, the study will include how many households in the government’s boundaries have heating cost in excess of 6 percent of that household’s income, which locally owned businesses are most vulnerable to high energy costs with an estimate of energy cost burdens for a sample of businesses, and the municipality or county’s energy costs. For a higher education institution, the study will assess the institution’s total energy costs.

An eligible entity who has conducted the study can apply for a grant to implement energy cost saving measures. In the case of municipalities or counties, the types of projects should be aimed at assisting those households and businesses identified as vulnerable and the government’s own energy costs. For a higher education institution, the purpose will be for installing and utilizing energy conservation measures.

The fund will receive revenues from the oil and gas severance tax surtax. This surtax is pegged to the taxable value price of natural gas and oil in the previous year:

Price of Oil per Barrel		Price of Natural Gas per Thousand Cubic Feet		Surtax Imposed
More Than	But Less Than	More Than	But Less Than	
\$ -	\$ 22.00	\$ -	\$ 2.70	0%
22.00	27.00	2.70	4.20	1%
27.00	32.00	4.20	5.70	2%
32.00	37.00	5.70	7.20	3%
37.00	42.00	7.20	8.70	4%
42.00	47.00	8.70	10.20	5%
47.00	52.00	10.20	11.70	6%
52.00		11.70		7%

* Price is the effective price based on taxable value

The effective date is February 1, 2007.

FISCAL IMPLICATIONS

The effective date of SB468 is February 1, 2007, so only five months of oil and gas activity is included in the estimate. For FY07, the consensus revenue group has forecast the prices of oil and gas as \$55/barrel and \$6.10 per thousand cubic feet (MCF) respectively. For FY08, those prices are \$53/barrel and \$5.80/MCF. With deductions from taxable value (historically 9 percent of value for oil and 17 percent of value for natural gas), the taxable value prices which are used to establish the surtax are shown in table one.

In FY07, the surtax is estimated to increase severance tax revenues by \$155.5 million and in FY08 the increased revenue is \$303.7 million.

The appropriation to the community energy security fund of \$155.5 million in FY07 and \$307.3 million in FY08 contained in this bill is a recurring expense to the severance tax permanent fund. Any unexpended or unencumbered balance remaining at the end of each fiscal year shall not revert.

Consensus Forecast

	Price*	Volume	Value** (\$M)	Taxable Value Price	Surtax Imposed	Surtax (\$M)
Oil						
FY07***	\$ 54.00	25.67	1,258.49	49.03	7%	88.09
FY08	51.00	59.50	2,755.33	46.31	6%	165.32
Natural Gas						
FY07***	\$ 6.50	626.67	3,368.65	5.38	2%	67.37
FY08	5.65	1,481.00	6,920.05	4.67	2%	138.40

* Calendar year price is average of consensus group fiscal year prices.

** Typical deductions have been accounted for.

*** Effective date of February 1, 2007 means only five months are included in FY07.

This bill creates a new fund and provides for continuing appropriations. The LFC has concerns with including continuing appropriation language in the statutory provisions for newly created funds, as earmarking reduces the ability of the legislature to establish spending priorities.

SIGNIFICANT ISSUES

This is a major tax increase on the oil and gas industry. Even though it may be designed for windfall profits due to recent high prices, the current forecast for oil and gas prices mean that the surtax will likely stay above 4 percent for oil and 2 percent for natural gas. The surtax may add to the volatility of production in New Mexico as exploration and drilling will contract when prices are lower than they have been.

TECHNICAL ISSUES

EMNRD:

The project qualifications criteria in the bill are complex and do not necessarily result in selection of a cost effective project. A good return on investment on specific projects should be a major part of the selection criteria. A return on investment greater than what the state gets on its overall investments would be a good measure.

It is difficult to obtain new or current energy consumption data from the utility on household energy consumption. The information may not be available because the utility companies consider it private information. A county with households that spend more than 6% on their utility bill would be eligible. Census data or other typical sources of general information would not be useful because they do not consider the increase in energy costs that occurred in the last 12 months.

There are two definitions of “Department”. In the tax section, the bill refers to the Taxation and Revenue Department. In the new material section, it refers to the Department of Finance and Administration. The definitions should clarify this issue.

Amendment: Add “biobased energy related systems and equipment” under energy conservation measures. HB995 – Biomass-Related Equipment tax Deduction passed by the 2005 Legislative session has specific definitions.

ALTERNATIVES

EMNRD proposes the following amendment:

Section 6. E. (2) (k) Remove: ~~or~~

Section 6. E. (2) (l) Add: or

Section 6. E. (2) “ (m) biomass-related equipment used to produce energy from biobased products, biofuels and biomass materials that is useful to operate facilities, motor vehicles or equipment.”

The following are specific definitions in the law that could be included.

(1) "biobased products" means products created from plant- or crop-based resources such as agricultural crops and crop residues, forestry, pastures and rangelands that are normally made from petroleum;

(2) "biofuels" means biomass converted to liquid or gaseous fuels such as ethanol, methanol, methane and hydrogen;

(3) "biomass material" means organic material that is available on a renewable or recurring basis, including:

(a) forest-related materials, including mill residues, logging residues, forest thinnings, slash, brush, low commercial value materials or undesirable species, salt cedar and other phreatophyte or woody vegetation removed from river basins or watersheds and woody material harvested for the purpose of forest fire fuel reduction or forest health and watershed improvement;

(b) agricultural-related materials, including orchard trees, vineyard, grain or crop residues, including straws and stover, aquatic plants and agricultural processed co-products and waste products, including fats, oils, greases, whey and lactose;

(c) animal waste, including manure and slaughterhouse and other processing waste;

(d) solid woody waste materials, including landscape or right-of-way tree trimmings, range land maintenance residues, waste pallets, crates and manufacturing, construction and demolition wood wastes, excluding pressure-treated, chemically treated or painted wood wastes and wood contaminated with plastic;

(e) crops and trees planted for the purpose of being used to produce energy;

(f) landfill gas, wastewater treatment gas and biosolids, including organic waste byproducts generated during the wastewater treatment process; and

(g) segregated municipal solid waste, excluding tires and medical and hazardous waste; and

(4) "biopower" means biomass converted to produce electrical and thermal energy."

POSSIBLE QUESTIONS

1. There will be hundreds of millions of dollars going into this fund over the next several years at forecast oil and gas prices. How much does it typically cost to weatherize a house?

NF/yr