LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS

Bill Number: SB 100 **50th Legislature, 1st Session, 2011**

Tracking Number: .183279.1

Short Title: Decrease Oil & Gas Severance Tax Rates

Sponsor(s): Senator Mary Jane M. García

Analyst: Peter B. van Moorsel **Date: February 17, 2011**

Bill Summary:

SB 100 amends several sections of law to:

- reduce the severance tax rates pursuant to the *Oil and Gas Severance Tax Act* for FY 12 through FY 14;
- increase the severance tax rates pursuant to the *Oil and Gas Emergency School Tax Act* by an equal amount for FY 12 through FY 14; and
- transfer to the Public School Fund 1.0 percent of the Oil and Gas Emergency School Tax receipts for those fiscal years.

A section-by-section summary of SB 100 follows.

Section 1 amends the *Tax Administration Act* to enumerate the new sections created in this bill.

Section 2 creates a new section of the *Tax Administration Act* to provide that:

- a distribution of Oil and Gas Emergency School Tax receipts be made to the Severance Tax Bonding Fund if the State Board of Finance (BoF) certifies to the Secretary of the Taxation and Revenue Department (TRD) that a distribution is necessary to meet debt service obligations on outstanding severance tax bonds (STBs) and supplemental severance tax bonds (SSTBs) or is necessary to maintain a reserve fund for future debt obligations in order to protect the interest of bondholders; and
- the distribution may not exceed 1.0 percent of Oil and Gas Emergency School Tax revenues for the month in which the distribution is made.

Section 3 creates a new section of the *Tax Administration Act* to provide that:

- a distribution be made to the Public School Fund equal to 1.0 percent of Oil and Gas Emergency School Tax receipts;
- amounts distributed to the Public School Fund not revert to the General Fund; and
- if a distribution to the Severance Tax Bonding Fund is made to service the debt on outstanding STBs or SSTBs or is necessary to maintain a reserve for future debt obligations, the distribution to the Public School Fund be reduced by the amount of that distribution to the Severance Tax Bonding Fund.

Section 4 creates a new section of the *Tax Administration Act* that states:

- the purpose of SB 100 is to temporarily decrease tax rates under the *Oil and Gas Severance Tax Act* and to temporarily increase tax rates under the *Oil and Gas Emergency School Tax Act*;
- the act is not intended to affect the total combined taxes due under those acts; and
- the Secretary of TRD is authorized to adjust tax rates under those acts by rule under certain circumstances.

Section 5 amends the *Severance Tax Bonding Act* to:

- prohibit the BoF from issuing STBs or SSTBs with the expectation that a distribution pursuant to of Oil and Gas Emergency School Tax receipts will be needed to service the debt on either the bonds to be issued or any outstanding STBs or SSTBs; and
- determine the deposits into the Severance Tax Bonding Fund during the preceding fiscal year as follows:

  - in lieu of the actual deposits into the fund in FY 11, the amount used to calculate bonding capacity for FY 12 is to equal the amount distributed to the fund in FY 11 less 1.0 percent of Oil and Gas Severance Tax receipts for FY 11;

  - in lieu of the actual deposits into the fund in FY 14, the amount used to calculate bonding capacity for FY 15 equal the amount distributed to the fund in FY 14 plus 1.0 percent of Oil and Gas Severance Tax receipts for FY 14; and

  - any distributions of Oil and Gas Emergency School Tax Receipts pursuant to the provisions of Section 2 of SB 100 are not considered.

Section 6 amends the *Oil and Gas Severance Tax Act* to lower the severance tax rates for FY 12 through FY 14 from 3.75 percent to 2.75 percent on the taxable value of the following products:

- natural gas severed and sold, except for gas from certified well workover projects and stripper wells;
- oil and on other liquid hydrocarbons removed from natural gas at or near the wellhead, except for oil and other liquids produced from qualified enhanced recovery projects, certified well workover projects, and stripper wells; and
- carbon dioxide, helium, and non-hydrocarbon gases.

Section 7 amends the *Oil and Gas Emergency School Tax Act* to increase the severance tax rates for FY 12 through FY 14 as follows:

- from 3.15 percent to 4.15 percent on oil and on other liquid hydrocarbons removed from natural gas at or near the wellhead, except for oil and other liquids produced from stripper wells;
- from 4.0 percent to 5.0 percent on natural gas, except for gas from stripper wells; and
- from 3.15 percent to 4.15 percent on carbon dioxide, helium and non-hydrocarbon gases.

Section 8 sets a delayed repeal of Sections 2,3, and 4 of SB 100.

Section 9 provides that the distribution to the Public School Fund provided for in SB 100 applies to receipts from the Oil and Gas Emergency School Tax that are attributable to sales made in FY 12 – FY 14.

Section 10 establishes the effective date of the bill as July 1, 2011.

Fiscal Impact:

The TRD analysis of SB 100 estimates the fiscal impact of SB 100, by fiscal year, as follows:

- for FY 12, increase revenue to the Public School Fund (General Fund) by $100 million, while decreasing revenue to the Severance Tax Bonding Fund by $75.0 million;

- for FY 13, increase revenue to the Public School Fund (General Fund) by $106.4 million, while decreasing revenue to the Severance Tax Bonding Fund by $104 million; and

- for FY 14, increase revenue to the Public School Fund (General Fund) by $106.4 million, while decreasing revenue to the Severance Tax Bonding Fund by $106.4 million.

TRD notes that the fiscal impact is based on the consensus revenue estimating group forecast of oil and gas prices and volumes; and furthermore, the revenue changes are shown as "Recurring" despite the sunset provisions because the two taxes are considered part of the recurring revenue base of the two funds.

TRD adds that revenue accrual procedures are different for the General Fund and the Severance Tax Bonding Fund:

- revenues to the General Fund accrue in the sales month of the products; and
- revenues in the Severance Tax Bonding Fund accrue when cash is received, typically three months after the sales month.

The Public School Facilities Authority (PSFA) estimates that the enactment of SB 100 could reduce bonding capacity by $39.0 million for FY 12; and estimates the reduction in SSTBs capacity at $600,000.

Fiscal Issues:

TRD notes that SB 100 would temporarily shift revenue from the state's primary capital program to the General Fund, adding that while this would provide a temporary boost to the General Fund, it might cause investors to question the state's long-term commitment to the bonding program.

PSFA echoes this concern, stating that rating agencies may consider the contemplated tax shift to be a material weakness in the fiscal affairs of the state and assess a rating change to New Mexico's bonds for the perceived increase in risk.

Because proceeds from the sale of SSTBs are the funding source for public school capital outlay, PSFA notes its concern that reduced bonding capacity could adversely affect the condition of New Mexico's public school facilities:

- The average Facility Condition Index (FCI)[1] for all school buildings in New Mexico has been flat at about 36 percent over the past two years, and increased to 37 percent this year.

- The average annual investment in facilities required to keep facilities condition from worsening is about $125 million.

- Current unfunded needs for public school facilities in New Mexico total about $4.05 billion.; and

- Any additional funding burden imposed on the Public School Capital Outlay Fund would have the effect of accelerating FCI levels, meaning that the overall condition of school facilities would worsen.

Related Bills:

HB 222 *Reduce Unequal Treatment of Taxes & Credits*

[1] PSFA provides the following example to illustrate the FCI – if a building costs $100,000 and has an FCI of 37 percent, that building needs $37,000 in repairs; therefore, lower FCIs are better.