HOUSE
RESEARCH
ORGANIZATION bill analysis 5/27/97

SB 1440
Wentworth
(Holzheauser)

SUBJECT: Tax exemptions for low-producing wells

COMMITTEE: Ways and Means — favorable, with amendment

VOTE: 9 ayes — Craddick, Ramsay, Heflin, Holzheauser, Oliveira, Stiles, Telford, Thompson, Williamson

0 nays

1 present, not voting — Horn

1 absent — Grusendorf

SENATE VOTE: On final passage, May 7 — voice vote

WITNESSES: None

BACKGROUND: Oil and gas produced from a well designated by the Railroad Commission (RRC) as a three-year inactive well qualifies for a 10-year severance tax exemption. Oil and gas produced from a well subject to a Texas Experimental Research and Recovery Activity agreement also qualifies for a tax exemption.

DIGEST: SB 1440, as amended, would allow a five-year, 50 percent tax exemption on a oil lease's incremental production in excess of its baseline. Qualifying wells would have a baseline production of no more than seven barrels of oil equivalent per day in a four-month period and demonstrate increased production for four out of five consecutive months after performing an incremental production technique within the lease. The operator of a qualifying lease would have to apply to the RRC for a determination of a lease's incremental ratio before February 11, 1999; the incremental production would have to occur between September 1, 1997, and December 31, 1998.

Operators increasing production by marketing gas from an oil well or lease that had been released into the air for 12 months or more also would be entitled to a five-year 50 percent tax exemption for the life of the well or lease.

SB 1440 would allow for the temporary suspension of the tax credit if the price of crude oil reached $25 per barrel until the price dropped below $25. If an operator paid the tax before the comptroller approved the exemption, the operator would be entitled to a 50 percent tax credit.

The bill would take effect on September 1, 1997.

SUPPORTERS SAY:

SB 1440 would create another incentive for well operators to invest in production-enhancing activities for low-producing wells. The tax break would be justified because lower producing wells have higher production costs and smaller profits. The tax exemption would only be given to leases that showed a sustained increase in production after performing incremental production enhancement techniques at a minimum cost of $5,000. Without the tax exemption, these low-producing wells would likely be plugged, and the state would then receive no economic benefit.

Increased production generates other economic activity and translates into more revenue for the state through sales and property taxes. Increased production also creates more jobs and puts more petroleum and natural gas products on the market, benefitting consumers. Furthermore, state tax measures that induce enhanced petroleum production from low-producing properties increase the value of such properties to local taxing jurisdictions. Although a baseline of no more than seven barrels a day may be arbitrary, the line has to be drawn somewhere.

OPPONENTS SAY:

It is not good policy to grant tax exemptions for special interests. It is unfair to grant tax exemptions based on an arbitrary production level of no more than seven barrels of oil a day.

NOTES:

The committee amendment would delete the section dedicating revenue collected from incremental production of qualifying leases to the Texas Tuition Assistance Grant Program.

A related bill, SB 126 by Bivins, offering a 10-year severance tax exemption for inactive wells brought back into production, was signed by the governor on May 23.