LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 82ND LEGISLATIVE REGULAR SESSION

May 5, 2011

TO: Honorable David Dewhurst, Lieutenant Governor, Senate

FROM: John S O'Brien, Director, Legislative Budget Board

IN RE: **SB655** by Hegar (Relating to the continuation, functions, and name of the Railroad Commission of Texas.), **As Passed 2nd House**

Estimated Two-year Net Impact to General Revenue Related Funds for SB655, As Passed 2nd House: a positive impact of $51,241,691 through the biennium ending August 31, 2013.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2012	$25,613,453
2013	$25,628,238
2014	$25,628,238
2015	$25,628,238
2016	$25,628,238

All Funds, Five-Year Impact:

Fiscal Year	Probable Savings/ (Cost) from *General Revenue Fund* 1	Probable Revenue Gain/(Loss) from *General Revenue Fund* 1	Probable Savings/ (Cost) from *Oil-field Cleanup Acct* 145	Probable Revenue Gain/(Loss) from *Oil-field Cleanup Acct* 145
2012	$21,213,453	$4,400,000	$27,500,000	($55,201,000)
2013	$21,728,238	$3,900,000	$27,500,000	($25,111,000)
2014	$21,728,238	$3,900,000	$27,500,000	($25,268,000)
2015	$21,728,238	$3,900,000	$27,500,000	($25,483,000)
2016	$21,728,238	$3,900,000	$27,500,000	($25,696,000)

Fiscal Year	Probable Savings/ (Cost) from *New Other--Oil and Gas Regulation and Cleanup*	Probable Revenue Gain/(Loss) from *New Other--Oil and Gas Regualtion and Cleanup*	Probable Savings/ (Cost) from *Alter Fuels Research Acct* 101	Probable Revenue Gain/(Loss) from *Alter Fuels Research Acct* 101
2012	($52,519,054)	$82,719,054	$1,700,000	($2,600,000)
2013	($52,190,639)	$52,190,639	$1,700,000	($2,100,000)
2014	($52,044,281)	$52,044,281	$1,700,000	($2,100,000)
2015	($52,044,281)	$52,044,281	$1,700,000	($2,100,000)
2016	($52,044,281)	$52,044,281	$1,700,000	($2,100,000)

Fiscal Year	Change in Number of State Employees from FY 2011
2012	28.0
2013	28.0
2014	28.0
2015	28.0
2016	28.0

Fiscal Analysis

The bill renames the Railroad Commission the Texas Oil and Gas Commission, retains the three, statewide elected Commissioners and continues the agency for twelve (12) years.

The bill would eliminate the requirement that the agency employ a chief engineer and a chief petroleum engineer, as well as an administrative chief, i.e., the Executive Director.

The bill maintains, but renames the Oil Field Cleanup Fund Advisory Committee as the Oil and Gas Regulation and Cleanup Fund Advisory Committee, but deletes the requirement that the Committee meet quarterly. Under the provisions of the bill, the Commission retains the authority to conduct hearings on enforcement and gas utility contested cases.

The bill would create the Oil and Gas Regulation and Cleanup (OGRC) Fund as a special fund in the treasury outside of the General Revenue Fund. The OGRC would replace the existing General Revenue-Dedicated Oil Field Cleanup (OFCU) Account No. 145, with all balances in that account transferring to the OGRC Fund, and all current revenue streams to the OFCU Account No. 145, except penalties, accruing to the OGRC Fund. Penalties would be deposited to the credit of the General Revenue Fund. The bill would authorize surcharges on the agency's existing fees to provide that the OGRC Fund cover all of the agency's costs related to the regulation of oil and gas development. The bill would provide a specific methodology for the OGC to determine the amount of such surcharges. In addition, the bill would require that the Comptroller notify the OGC when the OGRC Fund has an unexpended balance of $20.0 million or greater, at which point the agency would cease collecting oil-field cleanup regulatory fees, until the unexpended balance of the OGRC Fund falls to $10.0 million.

The bill would require the OGC to establish specific performance goals for oil and gas regulation through the appropriations process for: the number of orphaned wells plugged with the use of state funds; the number of abandoned sites to be investigated, assessed, or cleaned up; and the number of surface locations to be remediated. The OGC would also be required to submit quarterly reports to the Legislative Budget Board on OGRC Fund revenues and expenditures and progress towards the performance goals. Annually, the OGC would be required to report to the Legislature a review of the effectiveness of money provided in the OGRC Fund at enabling the agency to better protect the environment.

The bill would abolish the Alternative Fuels Research and Education (AFRED) program and the General Revenue-Dedicated AFRED Account No. 101. Funds remaining in the AFRED Account No. 101 would be transferred to the undedicated portion of the General Revenue Fund.

The bill would add a requirement for the OGC to post certain certificates related to severance tax exemptions, rate reductions, or credits electronically. It would also require the OGC to regulate through the issuance of permits the treatment and disposal of oil field fluids and oil and gas wastes. In addition, the bill would require the OGC to adopt rules requiring oil and gas companies to provide information on the estimated amount and location of groundwater used in oil and gas exploration and for the OGC to notify the Texas Water Development Board (TWDB) of certain groundwater information.

The bill would provide a procedure to entities to obtain an exception to the OGC's gas well spacing requirements, and would authorize persons to request hearings on applications for wells in the Barnett Shale area. These hearings could be conducted by teleconference.

The bill would give the OGC jurisdiction over pipelines used to transport saltwater oil and gas waste.

Entities operating such pipelines would be required to register with the OGC. The OGC would be required to adopt safety regulations relating to applicable pipelines and related facilities. The bill would provide that saltwater pipeline facilities could be installed, maintained, or operated through, under, along, across, or over a state highway if the facilities comply with OGC promulgated safety regulations, and applicable Federal regulations, and any rules adopted by the Texas Transportation Commission (TTC).

The bill would expand the applicability of the pipeline safety fee to include gas utility regulatory functions.

The bill would require operators to report to the OGC on their use of hydraulic fracturing and the use of fluids, additives, and chemicals, and the OGC would be required to make annual reports on hydraulic fracturing to the Legislature. The bill would require the OGC to conduct a study of tracer substances and a study of the costs, benefits, and feasibility of regulating hydraulic fracturing.

The bill would create the Alternative Fuels Fund in the state treasury to fund certain OGC functions related to alternative fuels. The Fund would consist of gifts, grants, and other assistance. The OGC would be authorized to adopt rules to establish a consumer rebate program related to vehicles, appliances, and equipment fueled by alternative fuels.

The bill would require the OGC to conduct a study of the treatment of tax expenses for the purpose of computing gas utility rates. In addition, the bill would require the OGC to conduct a study of odorization of natural gas transported in gathering and transmission lines located in populated areas.

Methodology

This estimate assumes that the cost of changing the name of the agency could be absorbed using existing agency resources.

Regarding the creation of the OGRC Fund, this estimate assumes that all balances in the OFCU Account No. 145 as of August 31, 2011 as reported in the Comptroller's Biennial Revenue Estimate (BRE) for 2012-13 of $30.2 million would transfer to the new special fund and effectively be a loss to the General Revenue Fund. Current revenues to the OFCU Account No. 145, estimated at approximately $25 million per year based on the Comptroller's BRE, minus an estimated $2.5 million in penalties, or $22.5 million per year, would begin to accrue to the new OGRC Fund, and is shown in the table above as a revenue gain, while a loss of $25.0 million per fiscal year is shown to the OFCU Account No. 145. The $2.5 million per year in penalty revenues is shown in the table above as a gain to the General Revenue Fund.

The bill would require the OGC to cover all costs of oil and gas-related activities. Currently in the 2012-13 biennium, $18.9 million in annual expenditures for oil- and gas-related strategies are being paid out of the General Revenue Fund, along with an estimated $3.9 million in associated employee benefits, for a total of $22.8 million. This amount is shown as a savings to the General Revenue Fund in the table above.

Based on the agency's 2012-13 Legislative Appropriations Request, the Railroad Commission's costs in 2010-11 out of the OFCU No. 145 of $27.5 million exceed revenues by $2.5 million, including benefits costs. Upon passage of the bill, $2.5 million in penalties would no longer be available, increasing that deficit to $5.0 million per year. This estimate assumes that the agency would have to set fees sufficient to cover that deficit, along with the $22.8 million amount to replace current General Revenue appropriations. It is therefore estimated that the OGC would have to set surcharges sufficient to raise $27.8 million in new revenue per fiscal year. Because the agency would spend all of the new revenue stream plus amounts covered by revenues to the OFCU Account No. 145 ($22.5 million per fiscal year that would transfer to the new OGRC Fund), the OGRC would have total annual estimated costs of $50.3 million. As shown in the table above, this estimate assumes that revenue to the new OGRC Fund would be equal to total costs out of the Fund. It should be noted that the amounts included in the total costs and revenues for the OGCR Fund also include costs added by the bill for saltwater pipeline regulation and additional contested case hearings in the Barnett Shale area, as described below.

The elimination of the AFRED program would result in balances in the AFRED Account No. 101 being deposited to the General Revenue Fund. Although the Comptroller's Biennial Revenue Estimate for 2012-13 reports a projected balance in the account of $10.0 million on September 1, 2011, the Railroad Commission reports that the majority of these cash balances will, in fact, be spent prior to the end of fiscal year 2011. Therefore, this estimate assumes only $500,000 in AFRED Account No. 101 balances will actually move to the General Revenue Fund. In addition, $2.1 million in annual revenues to the AFRED Account No. 101 will be lost, partially offset by an estimated $1.7 million in annual expenditures, based on 2010-11 expenditure levels. Elimination of the marketing and education program would also result in 10.0 fewer FTEs being needed, as compared to 2010-11.
Because the bill deletes the requirement of an administrative chief at the OGC, this estimate assumes that the new agency would begin operations without an executive director. The elimination of the executive director is estimated to result in a savings of $163,751 per fiscal year out of the General Revenue Fund and a reduction of 1.0 FTE. This estimate assumes that the agency would continue to require a chief engineer and chief petroleum officer or the equivalent. Thus, no additional savings are estimated as a result of the elimination of the requirement of those positions.

Costs to the agency to electronically post tax exemptions, tax rates, and reduction or tax information on the OGC's website are not expected to be significant. Likewise, costs from the bill's requirement that the agency regulate the treatment and disposal of oil field fluids and oil and gas wastes are not expected to be significant. The requirement that the agency collect information on groundwater and report information to the TWDB is also not expected to result in significant costs to the agency.
The bill's requirement for contested case hearings in the Barnett Shale area is expected to result in an additional 60 hearings per fiscal year. It is estimated that the Railroad Commission would require 5.0 additional FTEs and $508,768 in additional costs. This estimate assumes that these costs would be offset by an increase in revenues to the OGRC Fund created by the bill.

The bill's provisions requiring the OGC to regulate saltwater pipelines are expected to result in the need for 16.0 additional FTEs at a cost of $1,710,286 in fiscal year 2012, $1,381,871in fiscal year 2013, and $1,235,513 in future years. This assumes that the OGC would establish standards and testing requirements, including reporting and recordkeeping, and regulate 140,000 miles of pipeline throughout the state. Because the regulation of saltwater pipelines relates to oil and gas-related activities, this estimate assumes that such costs would be offset by an increase in revenues to the OGRC Fund.

Provisions in the bill relating to the safety of saltwater pipelines are expected to result in 18.0 additional FTEs and related costs of $1,750,298 in fiscal year 2012 and $1,240,088 in future years to the General Revenue Fund. These costs are a result of the agency needing to assess all pipelines located in state highway rights-of-way and reflect the assumption that 2.0 additional FTEs would be needed in each of the agency's nine regional offices to inspect saltwater pipelines and enforce requirements that would be adopted by the OGC.

The bill's expansion of the pipeline safety fee to include gas utility regulatory functions would enable the agency to recover costs associated with the agency's gas utility regulation activities in Strategy A.2.1, Gas Utility Compliance, which currently receives approximately $1.5 million in General Revenue that is not fee supported, plus related benefits costs. This estimate assumes that the agency would raise the pipeline safety fee to the maximum rate under current law of $1 per line, as compared to $0.70 currently in place by agency rule. Raising the fee to the maximum rate would generate a total of $1.4 million per year to the General Revenue Fund. Because the bill's provisions relating to saltwater pipeline safety would require 18.0 FTEs and $1.7 million in 2012 and $1.2 million in future fiscal years, and because the costs of that new program would also be eligible to be paid out of the proceeds of the pipeline safety fee, this estimate assumes that the additional fee revenue to the General Revenue Fund, which is included in the table above, would be used to cover the costs of the new saltwater pipeline safety program, with no additional capacity within the statutory fee cap to pay for utility regulation.

The bill's reporting requirements relating to hydraulic fracturing and the bill's requirement that the OGC conduct a study of tracer substances and a study of the costs, benefits, and feasibility of regulating hydraulic fracturing are expected to be absorbed using existing agency resources.

Although the creation of the Alternative Fuels Fund in the state treasury could result in revenues to the Fund resulting from gifts and grants, which could be used by the OGC to fund an alternative fuels consumer rebate program if the funds were appropriated by the Legislature, this estimate does not assume that the revenue stream would be significant; thus no estimated revenues or expenditures from the Alternative Fuels Fund are included in the table above.

The bill's requirements for a study of the treatment of tax expenses for the purpose of computing gas utility rates and for a study of odorization of natural gas transported in gathering and transmission lines located in populated areas are expected to be completed using existing agency resources.

Technology

The bill's requirement that the OGC regulate saltwater pipelines will result in the need for a new system to track complaints, damage, and other events similar to the agency's existing Damage Prevention and Reporting system. The cost is estimated at $622,800 and is expected to be spread over fiscal years 2012 and 2013.

Local Government Impact

No significant fiscal implication to units of local government is anticipated.

Source Agencies: 116 Sunset Advisory Commission, 360 State Office of Administrative Hearings, 455 Railroad Commission, 304 Comptroller of Public Accounts

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