

BILL ANALYSIS

Senate Research Center
86R8200 SMT-F

S.B. 1417
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Finance
3/18/2019
As Filed

AUTHOR'S / SPONSOR'S STATEMENT OF INTENT

In 1989 the Texas Legislature created the "Temporary Exemption or Tax Reduction for Certain High-Cost Gas." This high cost gas tax reduction ("HCGTR") tax break reduced or eliminated the severance tax with respect to qualifying "high cost" gas wells, as the term was then defined by federal law: wells having a completion depth of more than 15,000 feet and being located in either geopressured brine, coal seams, or Devonian shale.

Originally intended to be temporary, the legislature renewed the HCGTR tax break in 1995 and 1999, and made it permanent in 2003.

Since then, the advent of hydraulic fracturing technology has made these "high cost" wells some of the cheapest to drill. The federal government accordingly repealed its 1970s-era "high cost" well definitions. Yet 30 years after the HCGTR tax break was enacted in Texas, it continues to reduce and exempt from taxation wells which are anything but high cost, and which, not incidentally, are among the most productive and profitable on Earth.

Under the Railroad Commission of Texas' interpretation of the statute, all of the wells drilled within the Barnett Shale and the Eagle Ford Shale qualify as a "high-cost" gas wells, regardless of their actual drilling costs. Wells with drilling and completion costs as low as \$24,000 have qualified as "high-cost" and received the severance tax break.

The result is a significant loss to the state and unwarranted distortion of the natural gas market. According to estimates by the comptroller of public accounts of the State of Texas, the HCGTR tax break costs the state over \$200,000,000 in severance tax revenue per year. Moreover, and as noted in the Legislative Budget Board's 2013 report, the HCGTR tax break distorts the natural gas market by providing preferential tax treatment to one form of production over others. Finally, it favors producers in certain regions over producers in other regions.

S.B. 1417 effectuates a gradual phase-out of the HCGTR tax break, by ending new applications as of September 1, 2019. Previously granted applications for the tax break last for up to 10 years; S.B. 1417 will not affect them. Year by year, previously-granted applications will expire, and the phase-out will be complete within a decade.

Ending the market-distorting tax break for the state's most profitable gas wells is highly unlikely to affect drilling activity. Drilling activity responds primarily to market forces, such as fluctuations in the global price of oil and gas, cost effects of continuing technological innovation, and the ability to transport and sell gas on the global market, all of which have far greater effect on investment returns.

The new revenue realized by closing the anachronistic HCGTR tax break will fund critical state needs, being split among the State Highway Fund, the Foundation School Fund, and the Economic Stabilization Fund.

As proposed, S.B. 1417 amends current law relating to phasing out the tax reduction for certain high-cost gas.

RULEMAKING AUTHORITY

This bill does not expressly grant any additional rulemaking authority to a state officer, institution, or agency.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Section 201.057(f), Tax Code, as follows:

(f) Requires the application for temporary exemption or tax reduction for high-cost gas, notwithstanding any other provision of this section (Temporary Exemption for Certain High-Cost Gas), to be filed with the comptroller of public accounts of the State of Texas (comptroller) before September 1, 2019. Requires an application to the comptroller for certification according to Subsection (a)(2) (relating to defining "high-cost gas"), notwithstanding any other provision of this section, to be filed with the comptroller before September 1, 2019, and at the later of the 180th day after the date of first production or the 45th day after the date of approval by the Railroad Commission of Texas (railroad commission), rather than filed with the comptroller at the later of the 180th day after the date of first production or the 45th day after the date of approval by the railroad commission. Provides that the tax reduction, if the application is not filed by the applicable deadline to obtain the maximum tax reduction but is filed before September 1, 2019, rather than if the application is not filed by the applicable deadline, is reduced by 10 percent for the period beginning on the 180th day after the first day of production and ending on the date on which the application is filed with the comptroller.

SECTION 2. Provides that the change in law made by this Act does not affect tax liability accruing before the effective date of this Act. Provides that such liability continues in effect as if this Act had not been enacted, and the former law is continued in effect for the collection of taxes due and for civil and criminal enforcement of the liability for those taxes.

SECTION 3. Effective date: upon passage or September 1, 2019.