LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 86TH LEGISLATIVE REGULAR SESSION

April 12, 2019

TO: Honorable Dustin Burrows, Chair, House Committee on Ways & Means

FROM: John McGeady, Assistant Director Sarah Keyton, Assistant Director
Legislative Budget Board

IN RE: **HB2545** by Guillen (relating to franchise tax, oil production tax, and gas production tax incentives for certain desalination facility operations.), **Committee Report 1st House, Substituted**

The fiscal implications of the bill cannot be determined at this time; however the bill could result in a negative fiscal impact depending on the extent of innovation in water desalination technology.

The bill would amend Chapter 171 of the Tax Code, regarding the franchise tax, to provide tax incentives for certain desalination facility operations.

The bill would allow a person who holds all necessary state and federal permits to operate a desalination facility to be eligible for a franchise tax credit based on the total dissolved solids concentration of the source water it treats. The bill would define desalination facility as a facility that treats source water under the jurisdiction of the Texas Commission on Environmental Quality (TCEQ) or Railroad Commission that has a high total dissolved solids concentration to produce fresh water of usable quality and begins initial operations on or after January 1, 2020.

The total amount of credit is equal to: (1) $0.50 for each 1,000 gallons of source water treated that has a total dissolved solids of more than 5,000 milligrams per liter; (2) $1 for each 1,000 gallons where at least 50 percent of the source water treated has a total dissolved solids of more than 30,000 milligrams per liter; and (3) $5 for each 1,000 gallons where at least 50 percent of the source water treated has a total dissolved solids of more than 50,000 milligrams per liter; and (4) $17 for each 1,000 gallons where at least 50 percent of the source water treated has a total dissolved solids of more than 90,000 milligrams per liter. The bill would require that the water be treated by the permit holder during the period on which the franchise tax report is based, and that the resulting fresh water be put to beneficial use in this state.

The bill would allow the permit holder to treat source water with differing total dissolved solids concentrations, and to prorate the credit based on the duration of processing time associated with each level of concentration. The bill would only allow treated water to be counted once in determining the amount of credit, and only one permit holder may claim a credit for the same treated water.

To be eligible for a credit, the permit holder must be a taxable entity and must submit to the TCEQ monthly statements that include certain information about the source water treated and the resulting fresh water. The bill would also require that the permit holder apply to the commission for certification, and establishes that certain information be included with its application. If the permit holder provides the statements, application, and other information required, the commission must issue a certificate of eligibility to the permit holder. The commission must immediately notify the Comptroller's Office if it later determines that the permit holder was or has become ineligible.

The bill would require that a permit holder apply for a credit on or with the report for the period for which the credit is claimed. The permit holder would be required to file a copy of each relevant certificate issued by the commission and any other information required by the Comptroller to demonstrate that the permit holder is eligible for the credit and the amount of the credit.

The total credit claimed for a report, including the amount of any carryforward, could not exceed the amount of franchise tax due for the report after all other applicable tax credits. The bill would allow the permit holder to carry any unused credit forward for not more than five consecutive reports. A credit carryforward from a previous year would be considered used before the current year installment.

The bill also would allow the permit holder that earns a credit to sell or assign all or part of the credit to another entity. The bill specifies that there is no limit to the total number of transactions for the sale or assignment of the credit. The sale or assignment of a credit would not extend the period for which a credit may be used, and does not increase the total amount of the credit that may be claimed.

The bill would allow an entity to which all or a part of the credit is sold or assigned to apply that credit against either the franchise tax, the natural gas production tax, or the oil production tax. The total credit claimed against the natural gas production tax or the oil production tax could not exceed the amount of tax due for a report after all other tax credits are applied, and could be carried forward until used. The bill also includes provisions related to the allocation of credit amongst the partners, members, or shareholders of certain pass-through entities.

Any entity that sells or assigns a credit would jointly submit written notice of the sale or assignment to the Comptroller within 30 days of the sale or assignment. The bill requires that certain information be included on the notice.

The bill would require the Comptroller and the commission to adopt rules necessary to implement the tax credits.

The bill would also allow a taxable entity to exclude from its total revenue any amount received by the entity from the sale of minerals or materials extracted from water by the desalination facility during the desalination process. The bill would require that the entity hold all state and federal permits necessary to operate a desalination facility.

The tax credit and revenue exclusion would expire on December 31, 2024. The expiration would not affect carryforward of a tax credit or credit accrued on source water treated before the expiration date.

The bill would provide tax benefits to entities employing rapidly changing technologies with evolving applications. For example, the Environmental Protection Agency is currently studying new ways to manage and regulate the wastewater generated in the oil and natural gas industry. The extent to which innovation occurs in this sector, as well as how quickly the necessary regulatory framework could be developed to allow new applications that might result in treatment of water eligible to earn credits is not known. If or when desalination of water with the higher concentrations of total dissolved solids becomes feasible, the value of tax credits provided under the bill could be substantial.

The bill would take effect January 1, 2021, and would only apply to reports originally due on or after that date, and before January 1, 2025.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: WP, KK, SD