Colorado Legislative Council Staff

Initiative #70

INITIAL FISCAL IMPACT STATEMENT

Date: November 14, 2017 **Fiscal Analyst:** Larson Silbaugh (303-866-4720)

LCS TITLE: SEVERANCE TAXES ON OIL AND GAS

Fiscal Impact Summary	FY 2018-2019	FY 2019-2020
State Revenue	**$219.4 million**	**$470.8 million**
Cash Funds	$219.4 million	$470.8 million
State Transfers	**$219.4 million**	**$470.8 million**
Department of Natural Resources	3.7 million	51.5 million
Department of Local Affairs	3.7 million	51.5 million
Severance Tax Stabilization Fund	212.0 million	367.8 million
State Expenditures	**$198.5 million**	**$434.1 million**
General Fund	0.2 million	
Cash Funds	$198.3 million	$434.1 million
Perpetual Base Fund (DNR)	1,9 million	25.8 million
Operational Fund (DNR)	1.9 million	25.8 million
Department of Local Affairs	3.7 million	51.5 million
K-12 Education (CDE)	95.4 million	165.5 million
Medical Care (CDPHE)	95.4 million	165.5 million

Note: This *initial* fiscal impact estimate has been prepared for the Title Board. If the initiative is placed on the ballot, Legislative Council Staff will revise this estimate for the Blue Book Voter Guide as new information becomes available.

Summary of Measure

Beginning January 1, 2019, the measure increases the oil and gas severance tax rate by 5 percentage points for all operators, eliminates the existing property tax credit, and halves the threshold for the stripper well exemption. Oil and gas severance taxes under the measure are exempt from the spending limits in the state constitution. Starting in 2019, oil and gas severance tax revenue is allocated to the following funds:

- 22 percent to the Severance Tax Trust fund within the Department of Natural Resources;
- 22 percent to the Local Government Severance Tax Fund within the Department of Local Affairs; and
- 56 percent to a newly created Severance Tax Stabilization Trust Fund which is distributed to the Department of Education and Department of Public Health and Environment.

State Revenue

This measure will increase oil and gas severance tax revenue by $219.4 million in FY 2018-19 and $470.8 million in FY 2019-20, with ongoing increases in future years. The measure begins January 1, 2019, half way through FY 2018-19.

Oil and severance tax revenue. Starting in tax year 2019, the measure increases oil and gas severance tax rates for all oil and gas producers as shown in Table 1.

Table 1: Severance Tax Rates on Oil and Gas Producers Under Initiative 2017-18 #70

Gross Income	Current Law Tax Rate	Proposed Tax Rate
Under $25,000	2%	7%
$25,000 and under $100,000	3%	8%
$100,000 and under $300,000	4%	9%
$300,000 and over	5%	10%

The new tax rates are a 5 percentage point increase for all oil and gas producers, regardless of gross income level.

The measure also eliminates the property tax credit and halves the stripper well exemption starting in 2019. Under current law, oil and gas producers are allowed to claim a credit against their severance tax liability equal to the amount they paid in property taxes to local governments in the prior year. In addition, current law exempts from taxation the value of production from oil and gas wells that produce either fewer than 15 barrels of oil per day or fewer than 90,000 cubic feet of natural gas per day. The measure reduces the threshold for the exemption to 7.5 barrels of oil per day or 45,000 cubic feet of natural gas per day. Table 2 shows the revenue associated with each change in the oil and gas severance tax structure .

Table 2: Change in Revenue Under Initiative 2017-18 #70

	FY 2018-19	FY 2019-20
Current Law Forecast*	**$159.2 million**	**$185.9 million**
New Revenue	**$219.4 million**	**$470.8 million**
Increased Tax Rates	$80.0 million	$186.9 million
Elimination of Ad Valorum Credit	$103.6 million	$210.7 million
Halve Stripper Well Exemption	$35.8 million	$73.2 million
Total Oil and Gas Severance Tax Revenue	**$378.6 million**	**$656.7 million**

**September 2017 Legislative Council Staff Oil and Gas Severance Tax Forecast.*

The revenue impact in this fiscal impact statement is based on the September 2017 Legislative Council Staff oil and gas severance tax forecast. The price of oil and gas is volatile, introducing significant forecast error into the revenue forecast.

State Transfers

The measure changes the distribution of oil and gas revenue to the Department of Natural Resources (DNR) and the Department of Local Affairs (DOLA), and creates an allocation to the new Severance Tax Stabilization Fund starting January 1, 2019. Table 3 shows the current law distributions of oil and gas severance taxes and the distributions under the measure.

Table 3: Distribution of Oil and Gas Severance Tax Revenue Under Initiative 2017-18 #70		
Transfer	**Current Law**	**Initiative #70**
Department of Natural Resources (DNR)	50%	22%
Department of Local Affairs (DOLA)	50%	22%
Severance Tax Stabilization Fund	-	56%
Total	**100%**	**100%**

Table 4 shows the current law transfers of oil and gas severance tax revenue, the transfers under the measure, and the net change for FY 2018-19 and FY 2019-20.

Table 4. Transfers Under Initiative 2017-18 #70			
FY 2018-19			
Transfers	**Current Law**	**Initiative #70**	**Net Change**
Department of Natural Resources	$79,582,495	$83,303,499	$3,721,004
Department of Local Affairs	$79,582,495	$83,303,499	$3,721,004
Severance Tax Stabilization Fund	-	$212,045,271	$212,045,271
TOTAL	**$159,164,990**	**$378,652,269**	**$219,487,279**
FY 2019-20			
Transfers	**Current Law**	**Initiative #70**	**Net Change**
Department of Natural Resources	$92,954,948	$144,477,832	$51,522,884
Department of Local Affairs	$92,954,948	$144,477,832	$51,522,884
Severance Tax Stabilization Fund	-	$367,761,754	$367,761,754
TOTAL	**$185,909,896**	**$656,717,418**	**$470,807,522**

State Expenditures

In FY 2018-19, the measure increases state expenditures by $116,688 and 0.9 FTE from the General Fund for the Department of Revenue to administer the new tax structure, and increases cash fund expenditures by up to $198.3 million. In FY 2019-20, cash fund expenditures will increase by up to $434.0 million. Table 5 summarizes expenditures for each agency under Initiative #70 and more detail is provided below.

Table 5. Expenditures Under Initiative 2017-2018 #70		
Agency	**FY 2018-19**	**FY 2019-20**
Department of Revenue	$116,688	
General Fund Total	**$116,688**	
Department of Natural Resources	$3,721,005	$51,522,884
Department of Local Affairs	$3,721,005	$51,522,884
Department of Education	$95,420,372	$165,492,789
Department of Public Health and Environment	$95,420,372	$165,492,789
Cash Fund Total	**$198,282,754**	**$434,031,346**
TOTAL	**$198,399,442**	**$434,031,346**

Department of Revenue. Department of Revenue General Fund expenditures will increase by $116,688 and 0.9 FTE in FY 2018-19 as shown in Table 6. This amount includes personal costs for additional staff to answer taxpayer questions, postage to notify taxpayers of the change in the severance tax structure, and computer programing.

Table 6. General Fund Expenditures Under Initiative 2017-2018 #70

Cost Components	FY 2018-19	FY 2019-20
Personal Services	$42,819	
FTE	0.9	
Operating Expenses and Capital Outlay Costs	5,088	
Computer Programing (GenTax)	43,927	
Mailing and Postage	13,818	
Centrally Appropriated Costs*	11,036	
TOTAL	**$116,688**	**$0**

** Centrally appropriated costs are not included in the measure's appropriation.*

The measure changes the distribution to the Department of Natural Resources and the Department of Local Affairs, and creates the Severance Tax Stabilization Fund. Money is transferred from the fund to the Colorado Department of Education, the Colorado Department of Public Health and Environment, and a newly created Perpetual Base Account.

Department of Natural Resources (DNR). Statutory transfers and appropriations in DNR will increase by $3.7 million in FY 2018-19 and $51.5 million in FY 2019-20. The measure changes the distribution to DNR so they receive 22 percent of severance taxes on oil and gas starting January 1, 2019. Revenue to DNR is distributed equally between the Severance Tax Perpetual Base Fund and the Operational Fund. The disbursement of revenue from these funds is set in current law.

Department of Local Affairs (DOLA). DOLA's severance tax revenue is credited to the Local Government Severance Tax Fund and distributed to local governments. The measure changes the distribution into the fund starting January 1, 2019, when the fund will receive 22 percent of oil and gas severance tax revenue. DOLA cash fund transfers and expenditures will increase by $3.7 million in FY 2018-19 and $51.5 million in FY 2019-20.

Department of Education (CDE). The measure creates a statutory appropriation to the Colorado Department of Education to expand full-day kindergarten and increase funding for K-12 education. The appropriation is equal to 50 percent of oil and gas severance tax revenue in the newly created Severance Tax Operational account and starts January 1, 2019. The measure is silent about which cash fund within the department will receive the revenue. Cash fund revenue within the Colorado Department of Education will increase by up to $95.4 million in FY 2018-19 and up to $165.5 million in FY 2019-20. Implementing legislation will be needed to specify how this money is used.

Department of Public Health and Environment (CDPHE). The measure creates a statutory appropriation within the Colorado Department of Public Health and Environment starting January 1, 2019 to fund medical care for people suffering negative health impacts caused by oil and gas production. The measure is silent about which fund or program will receive the revenue. Funding and expenditures will increase by up to $95.4 million starting in FY 2018-19 and up to

$165.5 million in FY 2019-20. Implementing legislation will be needed to determine how claims are made, which conditions are caused by oil and gas development, how the revenue is distributed, and to authorize administrative costs for the department.

New perpetual base account. The measure creates a new Perpetual Base, which receives 10 percent of the revenue to the Severance Tax Stabilization Fund. Funds in the account are not appropriated until the Perpetual Base Account exceeds 125 percent of the previous year's operational account expenditures. Perpetual Base Account revenue will total $21.2 million in FY 2018-19 and $36.8 million in FY 2019-20; however, this revenue will not be spent until the balance in the account exceeds 125 percent of operational account expenditures.

Table 7 shows increased cash fund expenditures under Initiative 2017-2018 #70.

Table 7. Cash Fund Expenditures Under Initiative 2017-2018 #70

Fund	FY 2018-19	FY 2019-20
Department of Natural Resources (22%)	$3,721,005	$51,522,884
Perpetual Base Fund (50% of DNR)	1,860,502	25,761,442
Operational Fund (50% of DNR)	1,860,502	25,761,442
Department of Local Affairs (22%)	$3,721,005	$51,522,884
Severance Tax Stabilization Fund (56%)	$212,045,271	$367,761,754
Operational Account (90% of Stabilization Fund)	$190,840,744	$330,985,579
K-12 Education (CDE) (50% of Operational Account)	95,420,372	165,492,789
Medical Care (CDPHE) (50% of Operational Account)	95,420,372	165,492,789
Perpetual Base Account (10% of Stabilization Fund)*	21,204,527	36,776,175
Total Cash Fund Expenditures	**$198,282,754**	**$434,031,347**
TOTAL	**$219,487,281**	**$470,807,522**

* *Money in the Perpetual Base Account is not spent until the balance in the account exceeds 125 percent of operational account expenditures.*

Local Government Impact

Local governments will receive increased local government impact grants administered by DOLA. In addition, some of the new expenditures in the measure may increase revenue to school districts and county health agencies depending on implementing legislation.

Economic Impact

This measure increases severance taxes paid by the oil and gas industry, increasing the cost of oil and gas development in Colorado. The fiscal impact statement does not attempt to estimate a behavioral change from the oil and gas industry in response to the increased oil and gas severance tax.

To the extent that the tax increase decreases oil and gas development in Colorado, there will be less oil and gas employment, less demand for associated services, reduced rent and royalty income to mineral owners, and reduced profits for oil and gas companies. The severance tax rate is only one consideration for the industry when deciding where to develop oil and gas; other factors include the cost of extracting oil and gas, the existence of supporting infrastructure, the ability to market extracted oil and gas, existing business commitments, and prevailing prices.

The new tax revenue will be spent on state and local government services, including K-12 education and the treatment of associated medical conditions. The additional spending may increase access to these services and may reduce the amount of money households need to budget for these services. To the extent that households have more money available in their budgets, they can increase other household purchases, savings, or investments.

Effective Date

If approved by voters, the ballot initiative takes effect upon proclamation of the Governor within 30 days of the official canvas of votes at the 2018 general election. The new tax rates and structure apply starting January 1, 2019.

State and Local Government Contacts

Counties	Education	Local Affairs
Municipalities	Revenue	Natural Resources
Public Health and Environment		

Abstract of Initiative 70: Severance Taxes on Oil and Gas

This initial fiscal estimate, prepared by the nonpartisan Director of Research of the Legislative Council as of November 2017, identifies the following impacts:

The abstract includes estimates of the fiscal impact of the initiative. If this initiative is to be placed on the ballot, Legislative Council Staff will prepare new estimates as part of a fiscal impact statement, which includes an abstract of that information. All fiscal impact statements are available at www.ColoradoBlueBook.com and the abstract will be included in the ballot information booklet that is prepared for the initiative.

State Expenditures. In FY 2018-19, the measure increases state expenditures by $116,688 and 0.9 FTE from the General Fund and increases cash fund expenditures by up to $196.4 million. In FY 2019-20, cash fund expenditures will increase by up to $408.3 million, with ongoing increased cash fund expenditures in future years.

State revenue. This measure will increase oil and gas severance tax revenue by $219.5 million in FY 2018-19, $470.8 million in FY 2019-20, with ongoing increases in future years.

Local government revenue, expenditures, taxes, or fiscal liabilities. Several of the programs that receive additional revenue under the measure increase grants to local government agencies.

Economic impacts. This measure increases severance taxes paid by the oil and gas industry, increasing the cost of oil and gas development in Colorado. To the extent that the tax increase decreases oil and gas development in Colorado, there will be less oil and gas employment, less demand for associated services, reduced rent and royalty income to mineral owners, and reduced profits for oil and gas companies. The new tax revenue will be spent on state and local government services, including K-12 education and treatment of medical conditions. The new tax revenue will be spent on state and local government services, including K-12 education, and the treatment of associated medical conditions. To the extent that households have more money available in their budgets, they can increase other household purchases, savings, or investments.