

# Bill Levine Talks Severance Tax

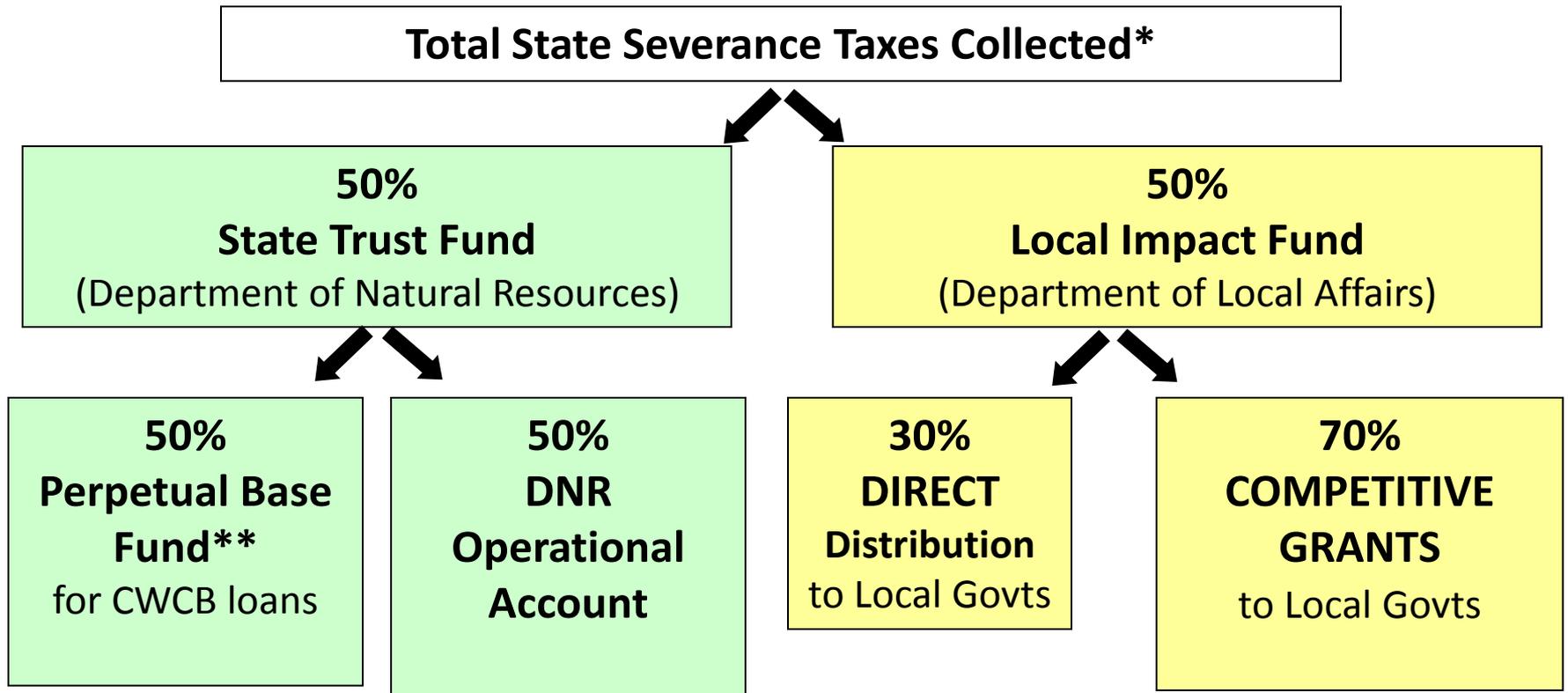
## August 2016



# What is Severance Tax?

- Severance Tax is a tax on nonrenewable minerals as they are “severed” from the earth.
- There are separate severance taxes on oil and gas, coal, metals, and oil shale
- By statute, the General Assembly intends that a portion of severance tax be used for public purposes, a portion be held in perpetual trust, and a portion be made available to local governments to offset the impacts of resource development

# How is Severance Tax Distributed?



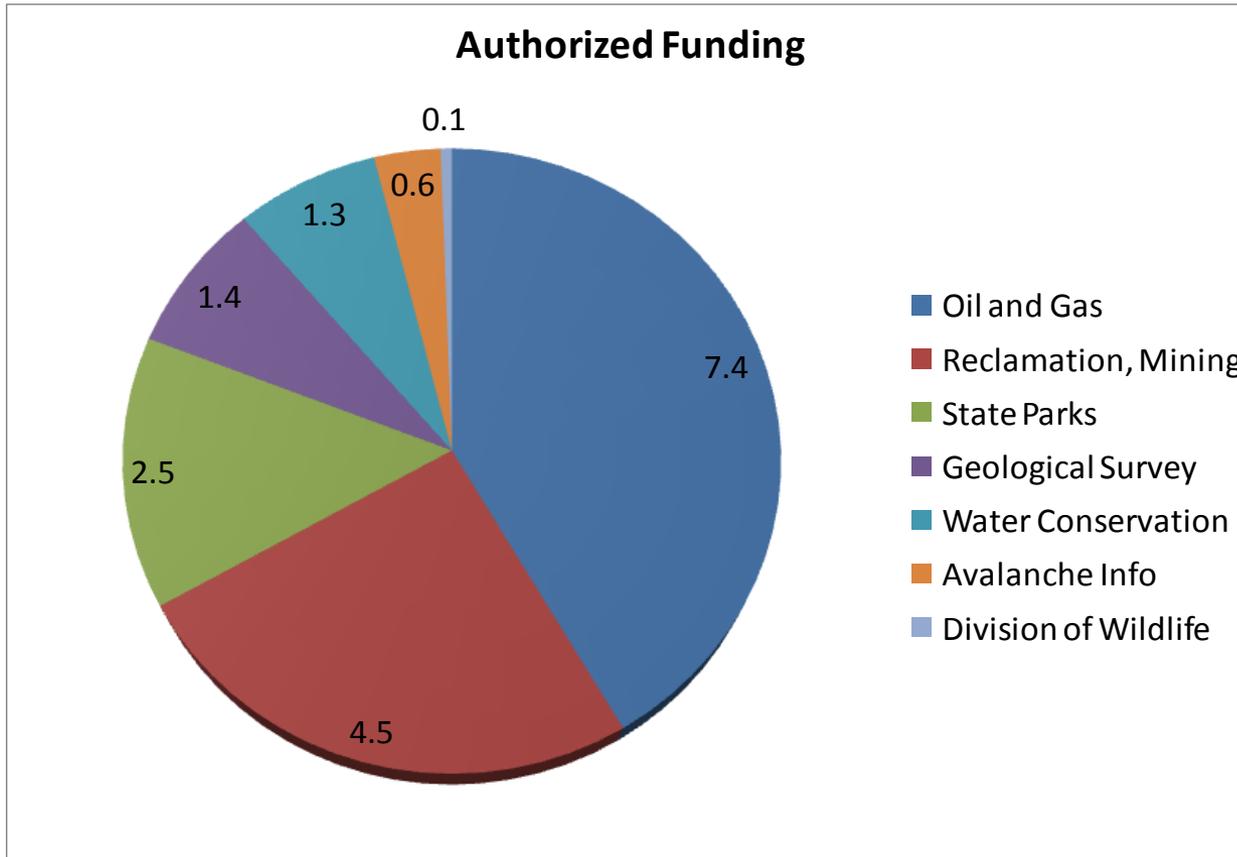
\* \$1.5 Million of severance tax is taken "off-the-top" and deposited into the Innovative Energy Fund

\*\* If Perpetual Base Account revenues exceed \$50M; next \$10M flows to CDPHE's Small Communities Water and Wastewater Grant Fund.)

# Perpetual Base Fund

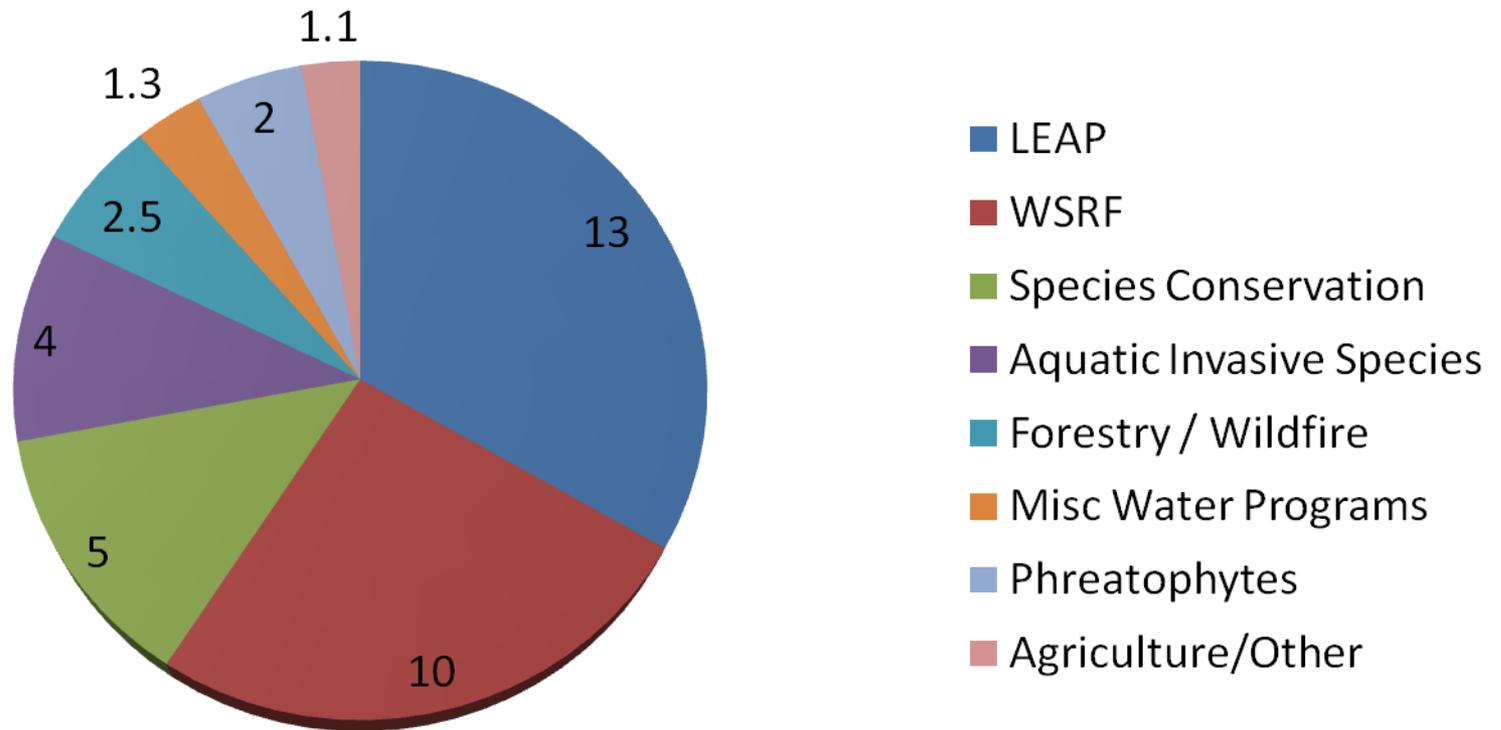
- Very roughly speaking, the Perpetual Base Fund is a \$380 million fund (although most of that amount is loan receivables) that plays a major role in supporting the CWCB Loan Program and helping build water supply infrastructure in Colorado.
- In an average year, there might be \$50 million in new revenues available for new projects.

# Operational Fund -Tier 1 program authorizations in FY 2016-17



# Operational Fund -Tier 2 program authorizations in FY 2016-17

Authorized Funding

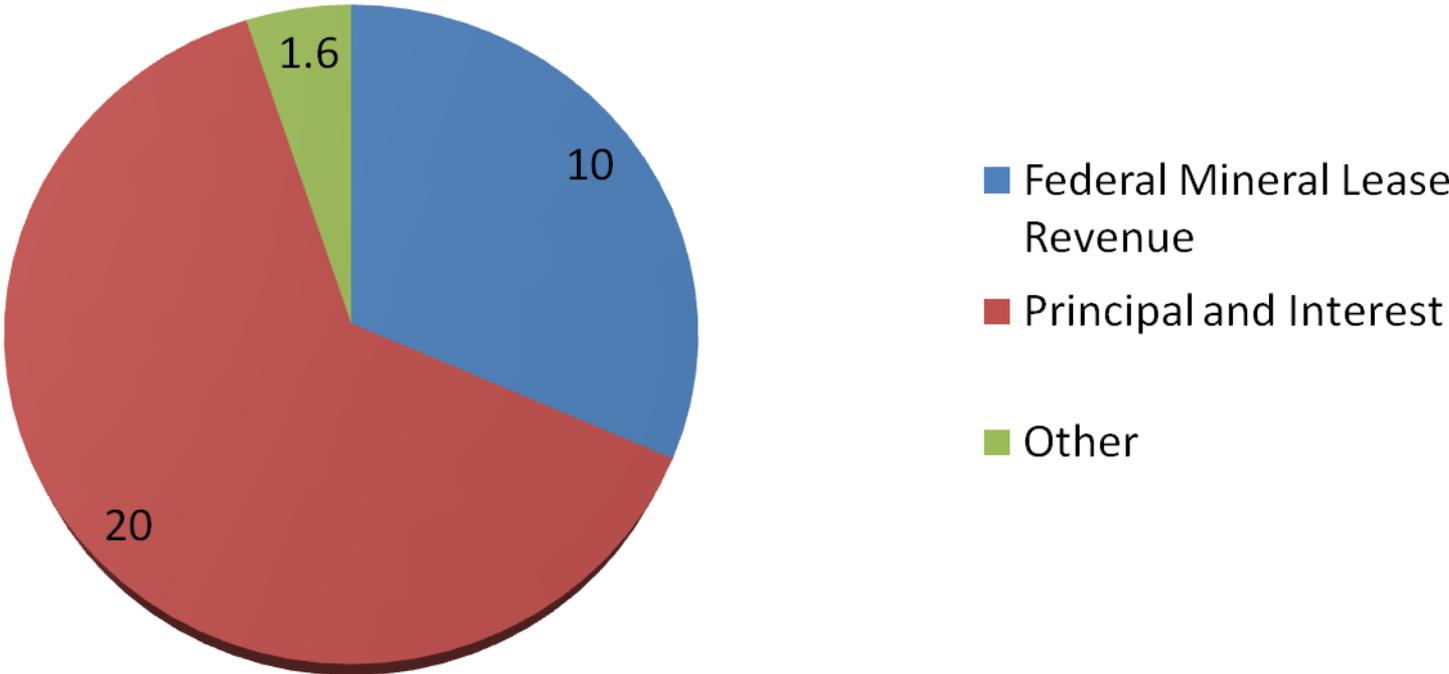


# CWCB Construction Fund

- Very roughly speaking, the Construction Fund is a \$500 million fund (although most of that amount is loan receivables) that plays a major role in funding the basic operations of the Colorado Water Conservation Board as well as funding non-reimbursable expenses and water project loans.
- In an average year, there might be \$50 million in new revenues available for new projects.

# CWCB Construction Fund

Revenue Sources for FY 2016-17

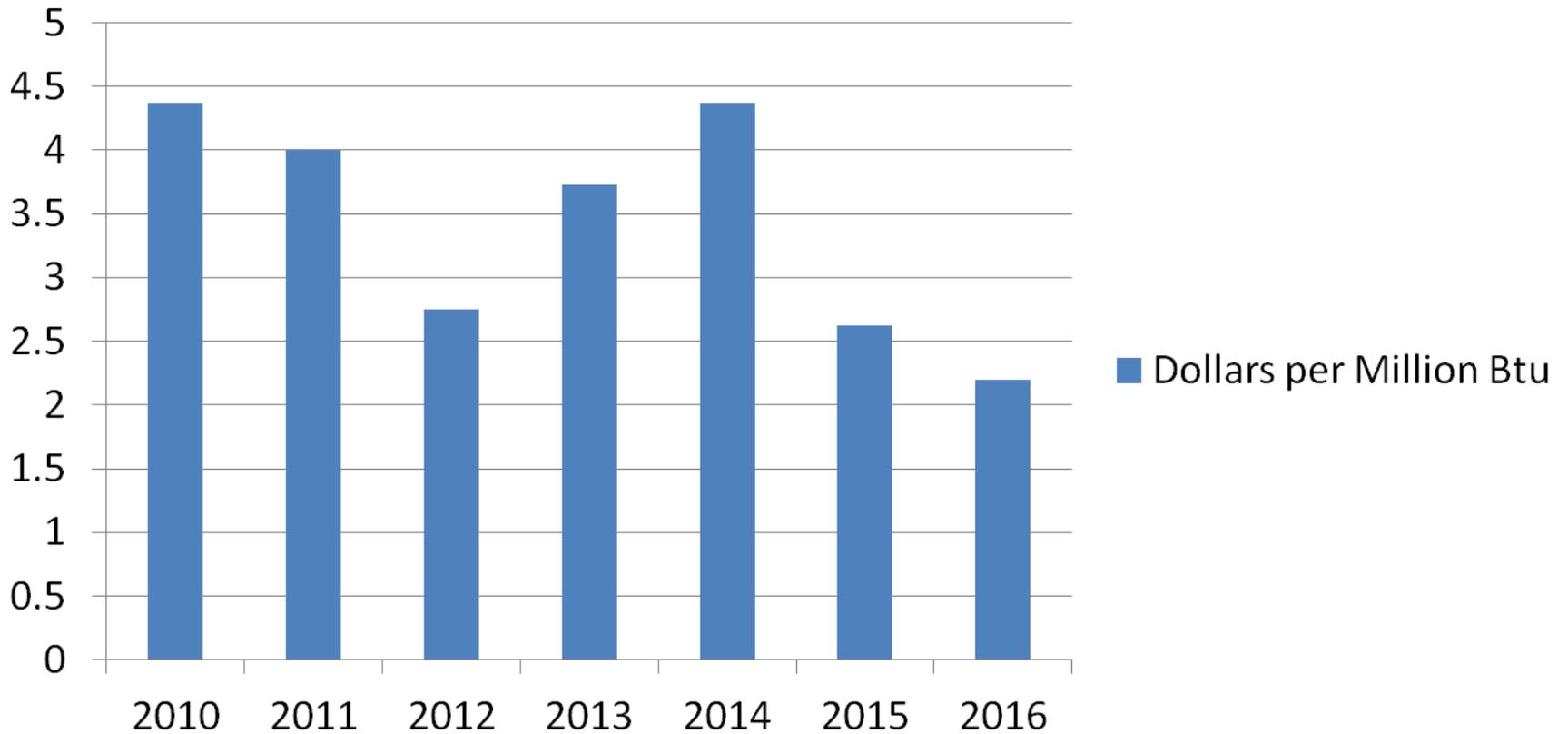


# Severance Tax Update

What's Happening with Severance  
Tax and Tier 2 Programs?

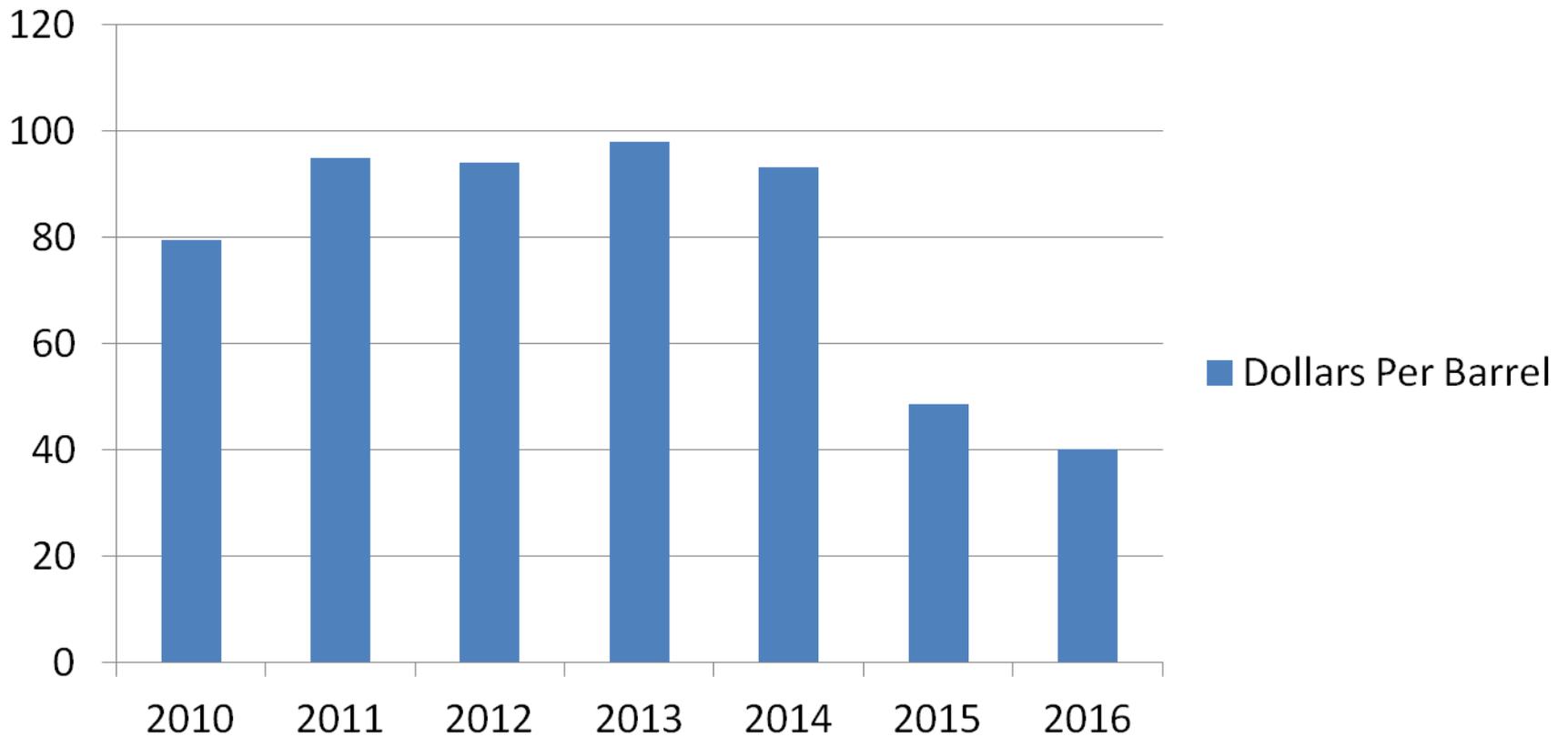
# Henry Hub Spot Natural Gas Prices

Spot Prices at Henry Hub



# Spot Prices for Crude Oil

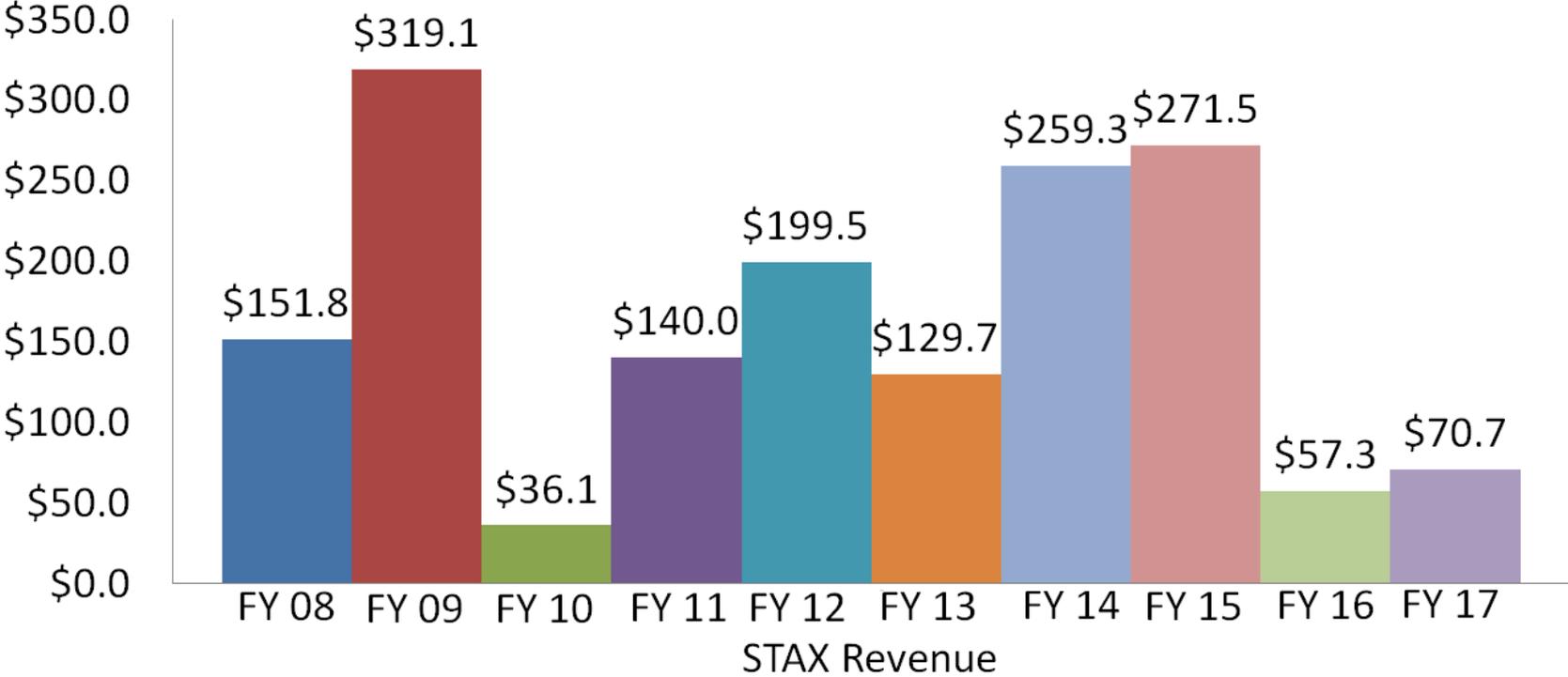
## WTI Crude Oil Prices



So if Energy Prices Got Cut in Half, Did  
Severance Tax Revenue Go Down by Half?



# History of State's Severance Tax Revenue



# Impact of the Ad Valorem Offset

- Colorado law provides a credit equal to 87.5% of the ad valorem taxes may be applied to oil & gas related severance tax liabilities.
- The ad valorem offset is reflective of conditions two years ago. In this regard, the ad valorem offset increase revenue volatility.



# Not Just Volatile, But Unpredictable

## Recent Revenue Forecasts by OSPB

	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	AVG
Dec Forecast	\$64	\$145	\$198	\$115	\$219	\$350	\$182
Actual Revenue	\$48	\$149	\$208	\$139	\$269	\$280	\$182
Variance (\$)	(\$16)	\$4	\$10	\$24	\$50	(\$70)	\$29*
Variance (%)	(25%)	3%	5%	21%	23%	(20%)	16%*

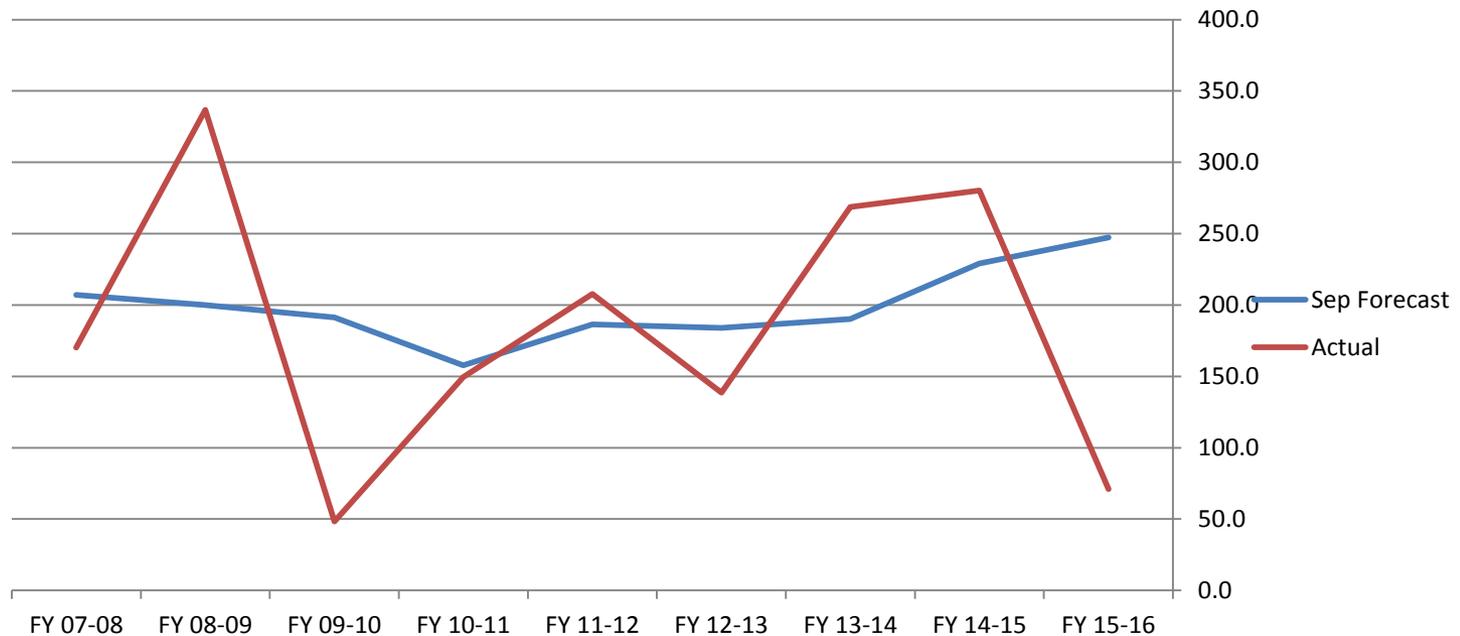
# Not Just Volatile, But Unpredictable

## Recent Revenue Forecasts by LCS

	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	AVG
Dec Forecast	\$85	\$177	\$171	\$122	\$182	\$312	\$175
Actual Revenue	\$48	\$149	\$208	\$139	\$269	\$280	\$182
Variance (\$)	(\$37)	(\$27)	\$37	\$16	\$86	(\$31)	\$30*
Variance (%)	(44%)	(15%)	22%	13%	47%	(10%)	20%*

# Lag Factor

- Though Severance Tax revenue is both volatile and unpredictable, there are patterns to the unpredictability. One of these is a lag factor



# BP America v. CO Dept. of Revenue



# Cost of Supreme Court Decision

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Refund Owed to British Petroleum:	<b>\$2.4 million</b>
Similar ROI-Related Conferee Cases:	<b>\$6.8 million</b>
Amended Tax Returns Related to ROI:	<b>\$2.0 million</b>
<u>Other NERF Deductions Likely Allowable:</u>	<u><b>\$9.0 million</b></u>
<b>Total Known Refunds:</b>	<b>\$20.2 million</b>

Likely Allowable NERF Deductions include: (1) chemicals, lubricants, and supplies used on site; (2) insurance, and; (3) Non-Capitalized repairs.

# Cost of Supreme Court Decision

In addition to the \$20.2 million of known refunds, there are three more potential costs:

- (1) Additional Refunds That Might Still be Filed
- (2) The Cost of ROI Deductions Going Forward
- (3) Additional NERF Deductions

# S.B. 16-218

- Creates a mechanism for paying severance tax refunds in FY 2016-17. Any refund in excess of 15 percent of gross monthly severance tax collections will be paid from the General Fund.
- Restricts DNR's Operational Fund by \$10.0 million
- Restrictions CWCB's Perpetual Base Fund by \$19.1 million

# Perpetual Base Fund Outlook

- The \$19.1 million obligation in S.B. 16-218 was intended to freeze the unobligated cash balance in the Perpetual Base Fund at the end of FY 2015-16.
- For FY 2016-17, the Fund will earn \$23 million in revenue. Of this amount, \$10.2 million will be needed for various projected approved in the CWCB Projects Bill (S.B. 16-174).

# Severance Tax Operational Fund Outlook

- The Severance Tax Operational Fund is projected to have finished FY 2015-16 with a \$19 million fund balance and a \$10 million restriction per S.B. 16-218. This restriction effectively freezes \$4.3 million sitting in the Tier 2 reserve and \$5.7 million sitting in the Tier 1 reserve.
- Tier 1 programs should be funded at 100% in FY 2016-17

# Severance Tax Operational Fund Outlook (Continued)

- Tier 2 programs are currently estimated to be funded at 0% in FY 2016-17 and 50% in FY 2017-18.
- If the \$10 million restriction is lifted, Tier 2 programs would be funded at 11% in FY 2016-17 and 70% in FY 2017-18.

# Water Supply Reserve Fund

## (Tier 2 Transfer = \$10.0 Million Per Year )

- Program Description: The Water Supply Reserve Fund is utilized by the nine basin roundtables to address water supply gaps in the respective basins. Roundtables approve grants from basin and statewide accounts and then pass them along to the Colorado Water Conservation Board for final approval. This is the primary source of funding for Basin Implementation Plans as well as efforts to achieve goals and objectives of Colorado's Water Plan at the basin level.
- FY 2016-17 Programmatic Impacts: At this point, roundtables and stakeholders are being warned that the WSRF account will likely receive no additional revenue for FY 2016-17. Basin accounts do have available balances, which vary by basin. The statewide account has an unobligated balance of roughly \$2.3 million. Requests for statewide grants will be considered in September of 2016.

# Water Supply Reserve Fund

## (Tier 2 Transfer = \$10.0 Million Per Year )

- FY 2016-17 Programmatic Impacts (Continued): Roundtables have begun a rigorous process of additional prioritization and assessment of grant applications in response to this projected revenue shortfall.
- Looking Beyond FY 2016-17: Likely reductions in funding will affect basin roundtables adversely as they work to implement projects that will meet goals and objectives identified in Basin Implementation Plans. Current basin balances will help fund projects which have already been approved, but revenue shortfalls will slow the ability to approve new projects. CWCB has directed staff to evaluate funding for CWCB and the roundtables over the next five years. The Interbasin Compact Committee is also evaluating additional revenue sources for implementation of water projects. However, at this point in time, funding for these types of projects is dependent on Tier 2 transfers.

# Species Conservation Trust Fund (Tier 2 Transfer = \$5.0 Million Per Year )

Program Description: The Species Conservation Trust Fund supports a wide range of research and projects to protect and recover threatened and endangered species – and species that are at risk of such listing – by protecting both species and their habitats. Funded activities and projects aim to minimize Endangered Species Act requirements and restrictions on existing and future land and water use. The program also aims to promote the restoration, recovery, sustainability, and resiliency of endangered, threatened, and imperiled wildlife. Protecting aquatic and riparian dependent species and plants is one of the long-term goals identified in Colorado’s Water Plan.

# Species Conservation Trust Fund

## (Tier 2 Transfer = \$5.0 Million Per Year )

Program	FY 2016-17 Base	FY 2016-17 Adjusted
Native Terrestrial Wildlife Conservation	\$778,135	\$277,985
Native Aquatic Wildlife Conservation	\$321,865	\$172,015
Native Species Management, Monitoring, and Propagation	\$700,000	\$450,000
Gunnison River Basin Selenium Management Plan	\$250,000	\$100,000
Upper Colorado River Recovery Program	\$550,000	\$100,000
Grand Valley Power Plant Repair and Improvement	\$400,000	\$400,000
<b>Grand Total SCTF Spending</b>	<b>\$3,000,000</b>	<b>\$1,500,000</b>

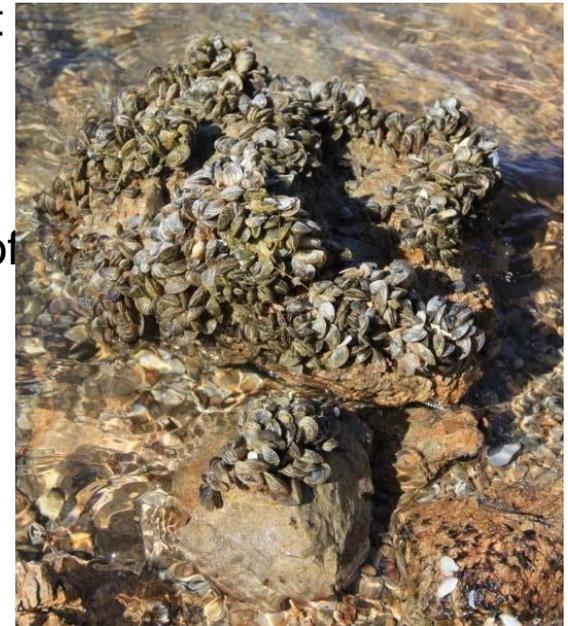
# Species Conservation Trust Fund (Tier 2 Transfer = \$5.0 Million Per Year )

- Looking beyond FY 2016-17, spending on Species Conservation Trust Fund projects is likely to remain below the \$5.0 million continuation level so long as severance tax revenues remain low.
- Colorado Parks and Wildlife will prioritize spending on: (1) continuing ongoing management projects to prevent future listings, and; (2) ongoing research studies (for example, previous investments in a study looking at long-term population trends might be damaged if CPW were to stop collecting population data during this revenue downturn).

# Aquatic Nuisance Species (Tier 2 Transfer = \$4.0 Million Per Year)

## Aquatic Nuisance Species (ANS)

- What gets done: Over 425,000 watercraft inspections and decontaminations (WID) at 71 reservoirs to prevent infestation of mussels and other detrimental aquatic invaders. Monitoring of 200 sites for established ANS.
- Funding cut impacts: Elimination of WID at majority of reservoirs, and substantial reduction to education, monitoring, and coordinated regional program.
- Why it matters: Greater risk of invasion and establishment of detrimental aquatic species, including zebra and quagga mussels, resulting in potential infrastructure damage, disruption of reservoir fisheries, and decrease in water-based recreation.



# Species Conservation Trust Fund

## Impacts of Tier 2 funding cuts

### Aquatic Nuisance Species (ANS) – FY 2017-18 and Beyond:

- Over the longer term, reduced program revenue will lead to less watercraft inspections and decontaminations.
- Without an inspection program, some private waters may become closed to boating recreation.
- Colorado Parks and Wildlife may seek new revenue streams so that a sufficient watercraft inspection and decontamination program may be sustained and public impacts related to aquatic nuisance species can be minimized.

