Approved On: ________________

Minutes of the House Committee on Assessment and Taxation. The meeting was called to order by E. C. Rolfs, Chairman, at 9:00 a.m. on March 4, 1986 in room 519 South at the Capitol of the State of Kansas.

All members of the Committee were present.

Committee staff present:

Tom Severn, Legislative Research
Melinda Hanson, Legislative Research
Don Hayward, Reviser of Statutes
Millie Foose, Committee Secretary

Mr. Harley Duncan, Secretary Kansas Department of Revenue. discussed HB-3069, an act relating to taxes and fees imposed on oil and gas production, providing requirements for filing returns and payment of such taxes and fees. (Attachment 1) Under the bill, a taxpayer would be required to file only one report and make payment to the Department of Revenue, who would then be responsible for distributing the appropriate fees to the KCC and the Department of Health and Environment.

Mr. Don Schnacke, representing Kansas Independent Oil & Gas Association, said his organization has no objection to this bill, but hopes that its passage would not interfere with the possible passage of HB-3078 which would transfer the entire oil and gas regulatory program that now lies in KDH&E to the KCC which has the vast majority of the oil and gas regulatory program. (Attachment 2) The members of the committee questioned him concerning the amount of money that is now in the fund and concerning HB-3078. This concluded the public hearing on HB-3069.

Representative R. D. Miller discussed HB-2934. an act relating to taxation; concerning the rates of the state retailers sales and compensating taxes. He said that this bill is needed to help preserve the oil industry. He said the low price of oil has resulted in unemployment, loss of sales, and loss of income tax revenue.

Mr. Schnacke also discussed HB-2934. He said that KIOGA considers this bill a "safety net" legislation for the oil producing industry in Kansas, which is the #2 industry in Kansas. He said the dramatic decline in the price of oil since January 1 has resulted in large lay-offs, shut-down in production, increased plugging of wells, and bankruptcies and reorganizational activity. (Attachment 3) His presentation included charts showing the effect of 8% severance tax on stripper well economic life and percent of stripper wells abandoned. He also provided tables showing the national impact of decreasing oil prices on stripper wells and the impact in Kansas. He also submitted a schedule showing the impact of a $1.00 decrease in the crude oil price in selected states.

Mr. Schnacke indicated from an independent report that a drop of only $1.00 could result in 2000 jobs lost and eight million dollars in taxes. He said a bill is being developed in the Senate that would modernize exemptions, basing them on gross value instead of the number of barrels. This concluded the public hearing on HB-2934.

Chairman Rolfs announced that all property tax exemptions would be considered as amendments to SB-400 and SB-450.

The minutes of March 3 were approved.

There being no further business, the chairman adjourned the meeting.

Ed C. Rolfs, Chairman

MEMORANDUM

TO: The Honorable Ed C. Rolfs, Chairman
House Committee on Assessment and Taxation

FROM: Harley T. Duncan, Secretary
Kansas Deparment of Revenue

RE: House Bill 3069

DATE: March 4, 1986

Thank you for the opportunity to appear before you on House Bill 3069. The Department of Revenue supports this measure.

House Bill 3069 consolidates the reporting and remittance procedures and requirements for the severance tax on oil and gas as well as the oil and gas conservation fees assessed by the Kansas Corporation Commission and the environmental fees assessed by the Kansas Department of Health and Environment. Under the bill, a taxpayer would be required to file only one report and make one payment to the Department of Revenue. Under an interagency agreement, we would then be responsible for distributing the appropriate fees to the KCC and the Department of Health and Environment.

To insure that information is available when necessary but that a financial burden is not imposed on any taxpayer, the bill requires that all oil and gas production (including such information as price, exempt status, and property description) **be reported** to the Department by the last day of the month following the end of the month in which the oil or gas is severed and removed from the lease or production unit. **Actual payment** of the taxes and fees would not be required until the 20th day of the second month following the month in which the oil or gas is severed and removed which is the same as is required for payment of the severance tax presently. This compares to the current situation in which KCC oil reports are due by the 15th of the month following the report month, KCC gas

Attachment 1 3/04/86
Hs. A&T

reports by the 10th, and KDHE reports by the 20th. To insure that all parties have sufficient time to adjust to these new procedures, we recommend a January 1, 1987 effective date.

HB 3069 also provides that a severance tax exemption will be denied if the operator of that lease does not have a valid operator license from the KCC. We believe that to be registered and licensed properly with the appropriate authority should be a prerequisite to a severance tax exemption. It will also improve our ability to verify exemptions.

We believe that HB 3069 will make matters simpler for the oil and gas industry. The information required for the payment of any and all of these taxes and fees is essentially the same. Yet under the current arrangement it is being reported to three different agencies in slightly different formats at three different times. We also believe that it will simplify matters for state government as well as improving the accuracy and timeliness of data submitted to it. This bill was developed jointly with the KCC and KDHE. Both agencies support the measure. We also sought the input of the industry in developing the bill.

Thank you for this opportunity. I would be glad to attempt to answer any questions.

KIOGA
KANSAS INDEPENDENT OIL & GAS ASSOCIATION
500 BROADWAY PLAZA • WICHITA, KANSAS 67202 • (316) 263-7297

March 4, 1986

TO: House Committee on Assessment & Taxation

RE: HB 3069 - Severance Tax Collection

We have no objection to HB 3069. As a matter of fact, we wanted this included in the severance tax passed in 1983, if for no other reason than to indicate that a minor severance tax had been in place for years, that amounts to nearly $4 million annually and that there is extensive regulation of the industry. That money is being used to regulate our industry in Kansas.

We also believe HB 3069 will put into procedure a discipline in collecting the severance tax designated for the KCC and KDH&E. Up to now, these agencies have only hoped the assessments would come in, and, if they don't, they just merely raise the levy. It is possible, through an increase in collections, the levy by the two agencies could be reduced.

We would hope that passage of HB 3069 would not prejudice the possible passage of HB 3078 which is recommended by the Organizational Sub-committee of the "Blue Ribbon" Committee appointed by KCC Chairman Lennen and KDH&E Secretary Sabol, which would transfer the entire oil and gas regulatory program that now lies in KDH&E (about a $500,000 effort) to the KCC which has the vast majority of the oil and gas regulatory program (about a $3.5 million effort).

We suggest you look at the citations on lines 217-220, KSA 55-609(c) and KSA 55-711(c). These citations are incorrect. The (c) should be dropped in both cases.

Donald P. Schnacke

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Attachment 2 3/04/86
Hs. A&T

KIOGA

KANSAS INDEPENDENT OIL & GAS ASSOCIATION

500 BROADWAY PLAZA • WICHITA, KANSAS 67202 • (316) 263-7297

March 4, 1986

TO: House Assessment & Taxation Committee

RE: HB 2934 - Severance Tax Revisions

KIOGA considers HB 2934 "safety net" legislation for the oil producing industry in Kansas. Repr. Miller is to be commended for sponsoring this legislation. It was introduced without knowledge of our Association. We are very appreciative of your Committee conducting hearings on HB 2934 and considering what the Legislature can do to help an existing Kansas industry that at the present time is in very bad financial shape and is faced with thousands of marginal wells being shut-in or plugged.

With all the talk of economic development in Kansas, very little official concern has been focused on the number two industry in Kansas and what is happening as prices have fallen dramatically. Dr. Anthony Redwood's preliminary report to the Legislature made a brief mention that the Kansas oil industry is in trouble, but made no recommendations. We do, however, expect that his final report will reflect more concern for the fate of our industry.

The Kansas oil industry does not just touch the producers in Kansas - numbering 4,700 plus. The rippling effect through the economy of Kansas is dramatic. The dramatic decline of the price of oil since January 1st, only 60 days ago, has been from $27 to $15 - nearly 40% of the total lost in the Kansas economy.

Already we have heard of large lay-offs in our industry; shut-in production; increased plugging of wells; and bankruptcies and reorganizational activity. First hit are the drilling and service and supply companies. The rig count in 1981-82 was at 224 in Kansas and it is below 50 today and going down. When there is no drilling, the service and supply companies suffer. Lay-offs follow. You can expect this last 60 day drop to be reflected among many Kansas banks. Our industry is spread through all 105 counties and production is found in 90 counties. Main street businessmen are all feeling this dramatic decline in prices. The collections of severance tax drop as the price of oil drops. The rippling effect on the collections of income and sales taxes will soon be seen. The ad valorem taxes to the counties will drop dramatically.

The IOCC, of which Kansas is a member, commissioned the RAM Group, Ltd. to do a study of the impact of decreasing oil prices on stripper wells, wells that produce less than 10 barrels of oil daily (BOD). Most Kansas production (90%) is stripper production. The average stripper well in Kansas is 3.5 BOD. We have a lot of production below 1 BOD - some 200 operators produce 0.2 BOD, or 8 gallons a day. We do not mirror the public image of oil producers found in the TV shows like "Dallas" or "Dynasty". I enclose the RAM Group study for your consideration.

Attachment 3 3/04/86 Hs. A&T

For you that do not understand how a severance tax accelerates the plugging of a well, I'm enclosing a graph that shows that a severance tax is another level of cost, imposed by government, which moves forward the day the well is plugged.

The reason we fought the severance tax so bitterly in 1983 was that Kansas was going to tax oil and gas much higher than it was in other comparable states. For instance, Oklahoma is at 7%, but without an ad valorem tax. Texas is at 5%, but without an income tax. Kansas has both the ad valorem tax ($125 million) and the income tax ($100 million). The severance tax had been netting around $110 million annually before prices started to drop.

Your action recently recognizing the impact on intra-state natural gas producers in Kansas was commendable. I hope that bill will make it through the legislature this year. It could stimulate a segment of our industry in the intra-state gas market.

Most producing states are looking at various schemes to relieve their oil producers from the economic plight in which they find themselves. The dream of $50, $60, or $100 oil in 1983 did not develop. Our concern in 1983 that our industry is cyclic and that the bottom can drop out, is being fulfilled. Reliance on a severance tax for state government is very risky. HB 2934 would simply say that after the price of oil drops below $20, a 1/4¢ sales tax replaces the suspended severance tax on oil production. Many Kansas newspapers have hailed this idea as practical by instilling stability in the tax collections for the state, while helping a basic industry and the economy of Kansas.

There is another proposal that is being worked on currently that would modernize the oil exemptions found in the severance tax act. That bill is being developed in the Senate at the direction of the Chairman of the Senate Assessment and Taxation Committee, in cooperation with the State Geological Survey and the Secretary of Revenue. I would expect a bill to be developed reflecting yet another "safety net" approach that is designed to help keep the industry from prematurely shutting in and plugging wells in Kansas. It would replace the per barrel exemptions that now exist with a gross value exemption for crude oil. You'll be hearing more about that proposal soon.

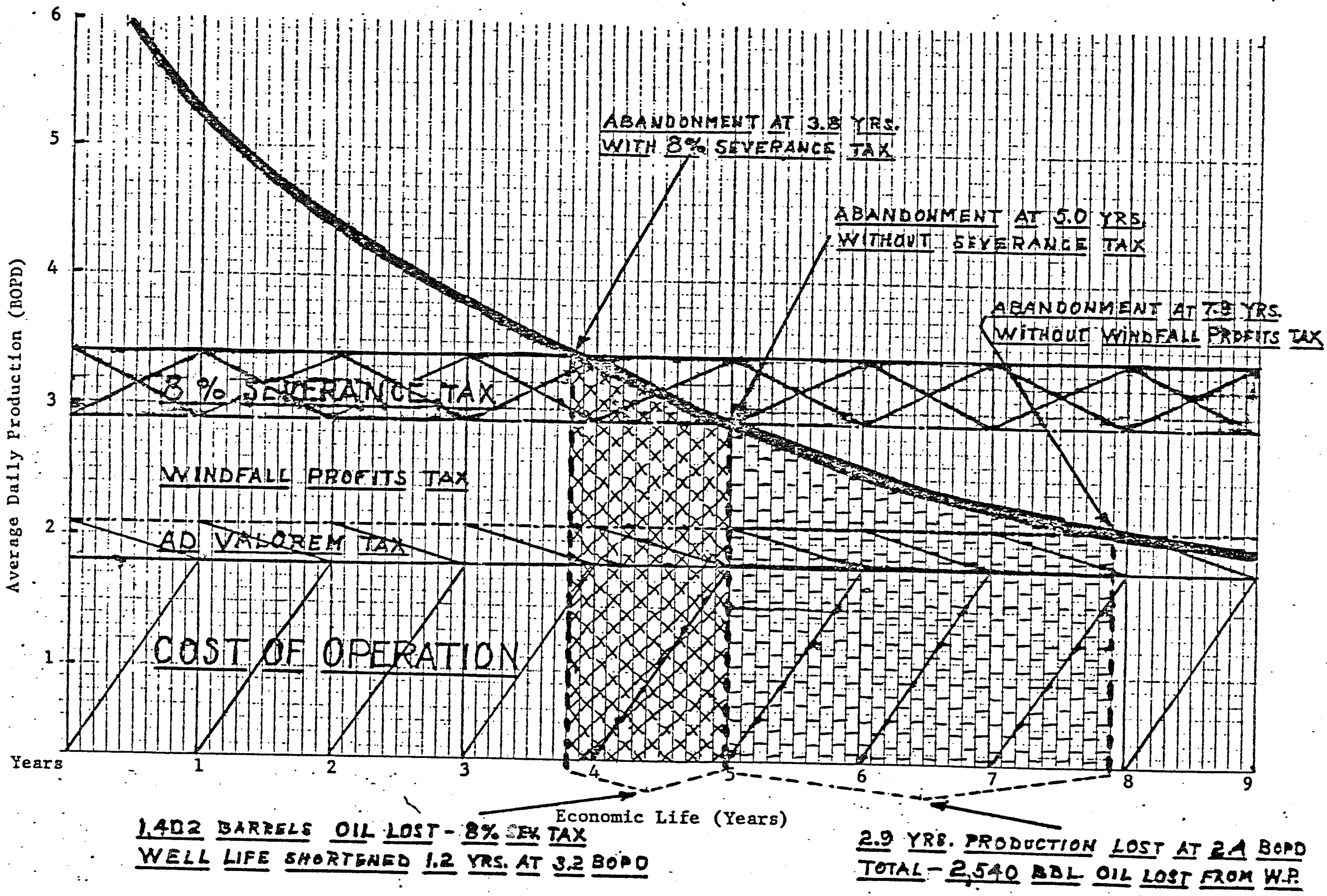
We would urge serious consideration of the passage of legislation along this line as an expression of assistance to a major industry attempting to continue to do business in Kansas.

Donald P. Schnacke

DPS:pp
Attch

EFFECT OF 8% SEVERANCE TAX ON

STRIPPER WELL ECONOMIC LIFE



Impact of Decreasing Crude Oil Prices on Stripper Oil Wells, Production and Reserves

Introduction

This study examines the impact of decreasing crude oil prices on stripper oil wells, which are wells producing less than 10 barrels per day. Because of their low production rates, stripper well economics are often marginal and very sensitive to changes in the price of crude oil.

In 1984, stripper wells accounted for approximately 15% of the nation's total oil production, and about 70% of the total number of U.S. oil wells. That year, stripper wells produced 463,459,000 barrels of oil. As of January 1, 1985, there were 452,543 stripper wells in the United States, with average production of 2.8 barrels per well daily.

Projected Impact

As shown on Chart 1, as the price of crude oil declines, the percentage of stripper wells abandoned as uneconomic increases. For example if the domestic crude oil price stabilizes at $18 per barrel, 15.6% of all stripper wells are forecast to become unprofitable and would thus be abandoned. At $15 per barrel, the nation is projected to lose 22.5% of its stripper wells. At $10 per barrel, 41% of the nation's stripper wells would be abandoned.

Table 1 shows the projected impact on stripper wells at various oil prices. At $15 per barrel, an estimated 101,958 stripper wells would be abandoned. This would result in a loss of oil production during the first year of 254,901 barrels per day, valued at $1,396,000,000 for that year. In addition, 976,000,000 barrels of crude oil reserves attributable to the abandoned wells would be lost.

The impact of the forecast stripper well abandonments would be relatively greater in Texas, Oklahoma and Kansas, which together account for 56% of the nation's stripper oil production. The impact in these states are shown on Tables 2-4.

The loss would be greatest in Texas, where an estimated 28,433 stripper wells would be abandoned at $15 per barrel, resulting in lost production of 84,033 barrels per day during the first year.

In Oklahoma, the loss would be very significant because stripper wells account for nearly 60% of the State's oil production. At $15 per barrel, Oklahoma would lose 18,572 stripper wells producing 51,737 barrels per day, or nearly 12% of the State's total oil production from all wells.

In Kansas, an estimated 10,307 stripper wells would be abandoned at $15 per barrel, costing the state's oil production 26,781 barrels per day.

The projected impacts for 19 other states with significant stripper oil production are shown on Tables 5-23.

PERCENT OF STRIPPER WELLS ABANDONED

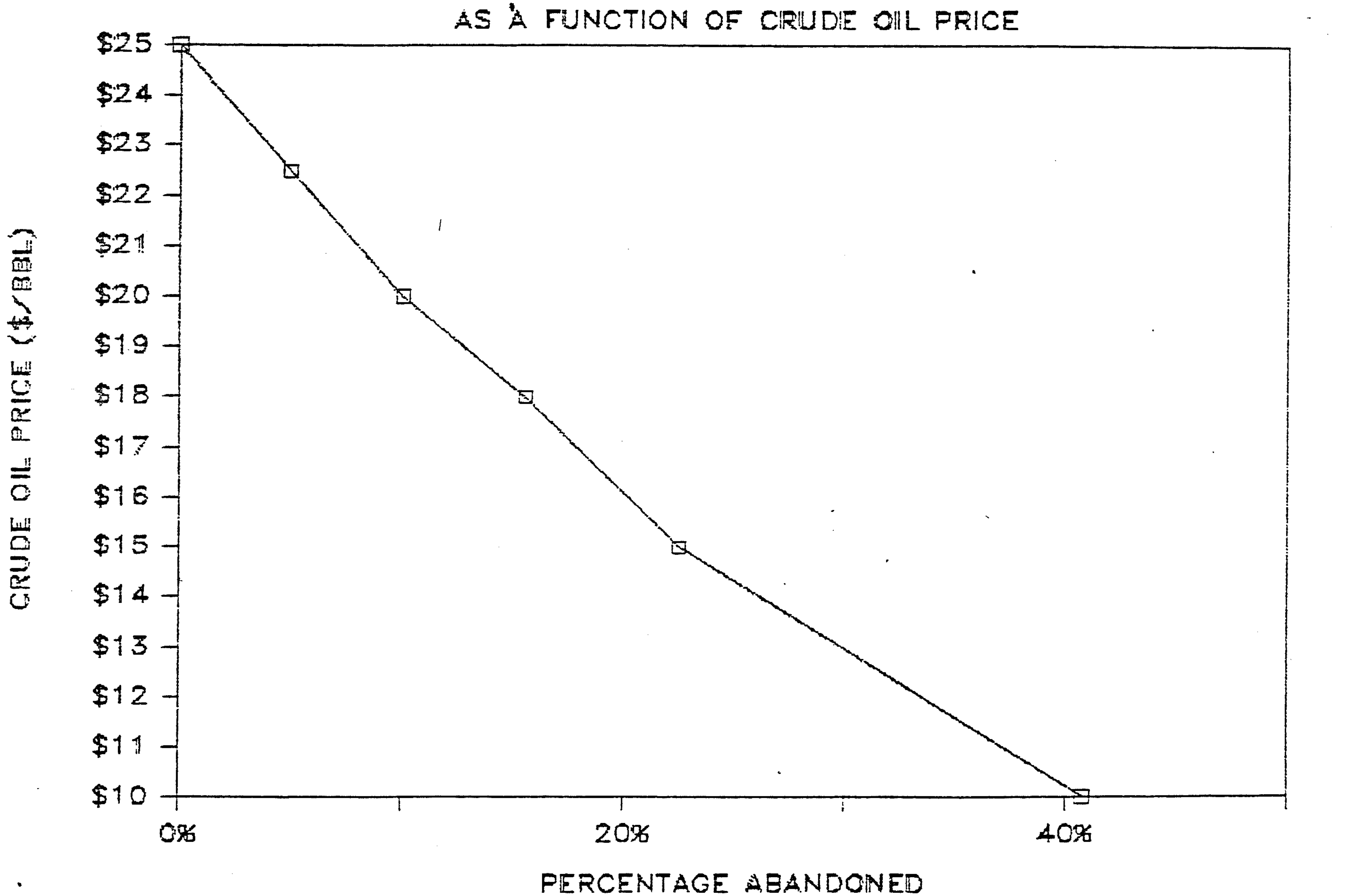


TABLE 1

NATIONAL
IMPACT OF DECREASING CRUDE OIL PRICES
ON STRIPPER WELLS

OIL PRICE	PERCENTAGE OF STRIPPER WELLS ABANDONED	NUMBER OF STRIPPER WELLS ABANDONED	PRODUCTION LOST FIRST YEAR (BPD)	VALUE OF PRODUCTION LOST FIRST YEAR ($ MILLION)	TOTAL RESERVES LOST (MM BBLS)
$10	40.8%	184,547	638,046	$2,328.869	2,610.880
$15	22.5%	101,958	277,090	$1,517.065	733.812
$18	15.6%	70,370	175,746	$1,154.654	278.490
$20	10.0%	45,390	106,586	$778.077	92.783
$23	5.0%	22,446	49,756	$408.618	16.862
$25	0.0%	0	0	$0.000	0.000

NOTE:

STRIPPER WELLS AS OF 1/1/85	452,543	WELLS
AVERAGE STRIPPER WELL PRODUCTION	2.8	BPD

TABLE 4

KANSAS
IMPACT OF DECREASING CRUDE OIL PRICES
ON STRIPPER WELLS

OIL PRICE	PERCENTAGE OF STRIPPER WELLS ABANDONED	NUMBER OF STRIPPER WELLS ABANDONED	PRODUCTION LOST FIRST YEAR (BPD)	VALUE OF PRODUCTION LOST FIRST YEAR ($ MILLION)	TOTAL RESERVES LOST (MM BBLS)
$10	40.8%	18,656	67,036	$244.682	274.311
$15	22.5%	10,307	29,112	$159.390	77.098
$18	15.6%	7,114	18,465	$121.313	29.259
$20	10.0%	4,589	11,198	$81.748	9.748
$23	5.0%	2,269	5,228	$42.931	1.772
$25	0.0%	0	0	$0.000	0.000

NOTE:

STRIPPER WELLS AS OF 1/1/85	45,749	WELLS
AVERAGE STRIPPER WELL PRODUCTION	2.91	BPD

Interstate Oil Compact Commission
Impact of $1.00 Decrease in Crude Oil Price, Selected States

nterstate Oil Compact Commissi
Decrease in Crude Oil Price,

	Annual vol. Crude Oil	Est. NG Liquids	Total	%of U.S.	Lost Jobs	GSP	Taxes
Arkansas	17,618	909	18,527	0.49	390.49	46,858,995	1,561,966
Kansas	75,723	20,928	96,651	2.54	2,037.10	244,452,351	8,148,412
Louisiana	449,545	155,194	604,739	15.92	12,746.02	1,529,522,406	50,984,080
Mississippi	31,879	1,666	33,545	0.88	707.02	84,842,931	2,828,098
New Mexico	75,532	54,534	130,066	3.42	2,741.39	328,966,482	10,965,549
North Dakota	52,654	6,028	58,682	1.54	1,236.83	148,420,118	4,947,337
Oklahoma	153,250	54,262	207,512	5.46	4,373.71	524,845,022	17,494,834
Texas	856,085	330,048	1,186,133	31.22	25,000.00	3,000,000,000	100,000,000
Wyoming	127,763	15,657	143,420	3.77	3,022.85	362,741,784	12,091,393