Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Technology, Energy & Communications Committee

HB 2701

Brief Description: Concerning fossil fuel production.

Sponsors: Representative Morris.

Brief Summary of Bill

- Establishes a severance tax on oil and gas production.

Hearing Date: 1/25/08

Staff: Scott Richards (786-7156).

Background:

Recent high prices for crude oil and natural gas have led to oil and natural gas exploration in areas where extraction is more expensive. In recent years, parts of the state have been explored for natural gas reserves, such as the Columbia River Basin. Natural gas exploration companies must drill though thousands of feet of basalt rock to determine whether natural gas is present in marketable amounts. In addition, geological formation in southwest Washington may potentially contain reserves of coalbed methane which is a form of natural gas extracted from coal beds.

Department of Natural Resources
The Department of Natural Resources (DNR), through the Division of Geology and Earth Resources, regulates drilling and related activities under the Oil and Gas Conservation Act and the DNR rules. In the event of a discovery, the DNR would also regulate production to assure equitable distribution of the proceeds.

Energy Freedom Account
In 2006, the Legislature established the Energy Freedom Account in the Washington Department of Agriculture to develop a viable bioenergy industry, to promote public research and development in bioenergy sources and markets, and to support a viable agriculture industry to grow bioenergy crops. In 2007, the Legislature transferred responsibility of the Energy Freedom

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Account to the Department of Community, Trade and Economic Development and created the Green Energy Incentive Account within the Energy Freedom Account. Appropriations made to the Green Energy Incentive Account are dedicated for refueling station development, plug-in hybrid pilot projects, and hydrogen vehicle demonstration projects.

Severance Tax
The state does not assess a severance tax for oil or gas production.

Summary of Bill:

Beginning January 1, 2009, the Department of Revenue (Department) must collect a 12.5 percent severance tax on the removal of oil or gas from any land or water in the state. The measure of the tax is the value of the oil or gas at the time and point of production. The value of the oil and gas is the fair market value of the oil or gas at the time of severance and at the point of production.

The operating producer of oil and gas production is responsible for filing the return with the Department, paying the tax due, and deducting and withholding the rateable share of the tax from payments made to other producers in proportion to their interest.

Oil and gas values that are tax exempt due to federal laws or negotiated compacts with a tribal government are not subject to the severance tax. Likewise, the value of oil or gas that is re-injected for storage is exempt from the severance tax.

Severance taxes collected by the Department must be deposited into two accounts: the Energy Freedom Account and the Local Government Severance Taxation Account. The Energy Freedom Account receives 80 percent of the severance taxes collected by the Department and the Local Government Severance Taxation Account receives 20 percent of the severance taxes collected by the Department.

The Legislature is required to compensate the DNR for regulating oil and gas production. Moneys from the Energy Freedom Account may be appropriated by the Legislature to recover the cost of oil and gas regulation as contained in the budget of the DNR.

Moneys from the Local Government Taxation Account must be used solely for making distributions to those local governments in which impacts from oil and gas production activities occur, after appropriation by the Legislature.

Oil and gas reserves and leases on the rights to develop and operate oil and gas production are exempt from property taxation.

Appropriation: None.

Fiscal Note: Requested on January 16, 2008.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.