

OIL SEVERANCE FACT CHECK

Assembly Revenue and Taxation Committee:

How Does California's Taxation of Oil Production Compare to Other States?

...California is the only major oil producing state that does not charge a severance tax.

...this Committee asked staff at the Franchise Tax Board and Board of Equalization to calculate the combined tax burden per barrel of oil in both California and Texas. After accounting for regulatory fees, applicable severance taxes, property taxes, and income and franchise taxes, this analysis found that California's combined tax burden on oil production was \$4.22 per barrel in 2008. In Texas, by contrast, the combined tax burden on oil production was more than three times higher at \$14.33 per barrel.

How Will This Bill Impact Consumers? The Legislative Analyst's Office noted in its 2006 report on Proposition 87, which would have imposed a similar severance tax, that market forces could ensure that the oil severance tax would not be passed on to consumers. Because California oil refiners have many options for purchasing crude oil in the global oil market, California oil producers will have to maintain competitive prices to retain their share of the market. Otherwise, oil refiners facing higher-priced oil from California producers could, at some point, find it cost-effective to purchase additional oil from non-California suppliers, whose oil would not be subject to this bill's severance tax.

Committee Analysis February 2010

Severin Borenstein, UC Berkeley Energy Institute:

Oil companies often remind us that the price of oil is set in a world market and they are right when they say that. They are wrong when they say that taxing oil produced in California would raise the price of California oil and, thus, the price of California gasoline.

California already imports more than half the oil we use. The price of oil in California is already set by the cost of importing oil from the world market. Some oil produced in the state has lower production costs, but those producers still sell that oil for the market price. They don't lower their price because they have lower costs any more than you are willing to sell your house for below the market price even though you bought it for a much lower price 20 years ago.

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1. California is the only state without an oil production/severance tax. A severance tax, as proposed in AB X3 9, would be 6% of the sales price of oil. We appear to be the only place in the world which does not collect taxes or royalties on oil production. Other states' rates: Alaska: 12.25%, Louisiana 12.5%, Oklahoma 7%, Kansas 8%, Colorado 5% over a minimum payment, Texas 4.6%, Wyoming 6%, New Mexico 3.75% plus 3.15% for schools.
2. The proposed severance tax would raise over \$900 million, as follows: \$85/barrel at 6% = \$5.10 per barrel, times 190 million barrels = \$969 million. The actual price of oil yesterday was \$95.60 per barrel at Midway-Sunset, but the assumption of the above revenue estimate is that oil prices will settle back to the \$80's. At yesterday's price, the revenue would be \$1.090 billion.
3. Despite oil company claims, California's total taxes on oil are the lowest of any state. Our sales tax on equipment is a comparatively small cost. Our corporation taxes are apportioned, so that when the LAO looked at corporate tax payments, based on FTB data, the apportionment factors of the majors were relatively low and the effective corporate rate on oil was about 3%. And, for property tax purposes, most of the oil in the ground is protected by Proposition 13, at very low values.
4. Why has California not had a severance tax, despite bills offered by Villaraigosa, Klehs, Bates, Burton and Gov. Pat Brown? Aside from the politics, the long-standing claim is that California oil is "heavy and sour" as opposed to "light and sweet". It is more expensive to refine and more expensive to get out of the ground. As a result, the California price of \$95.60 compares to yesterday's West Texas Intermediate, at \$107.90. So the refining premium is already built into the price. The cost of production is higher in California, at an estimated \$20/barrel. This may have been a factor when oil was \$30/barrel, but at \$80-90 it's irrelevant. An addition 6% of the price (\$5/barrel at these prices) in tax per barrel has no impact on production.
5. The Rand Corporation did a study of a 6% oil severance tax and found the following: it cannot be passed on to consumers and it will not affect production. That study was done when oil prices were far lower, but virtually all economists agree that the world market sets the price of oil, and that underlying taxes, whether from Texas, Kuwait or California, are not passed through at the pump.
6. While oil is a declining resource in California, there still are very large reserves of heavy oil. So, at these high oil prices, revenues will continue for a long time.

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