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Falling Oil Prices Help Consumers, Hurt States.

The price of oil has dropped by 40 percent over the past few months. Most oil states have money saved in permanent funds, but the drop in revenues is causing shortfalls already.

It's been nice for drivers to fill up their tanks at the lowest cost in years. But a 40 percent decline in oil prices over the last half of the year is bad news for energy-producing states.

In New Mexico, for example, every dollar drop in the price of a barrel of oil means $7.5 million less for the state's general fund. "It adds up pretty quick," said David Abbey, who directs the Legislative Finance Committee. "When prices are falling like a brick, we can't lower our estimates fast enough."

Abbey notes that his state – along with other oil and gas states such as North Dakota and Texas – devotes most of its oil revenues to permanent funds, which have billions of dollars in reserves. Capital outlays may be delayed and there could be less money for education or debt service, but money socked away when things were flush will keep those states from having to impose deep cuts right away. "They can weather these short term swings easily," said Norton Francis, a state tax policy expert at the Urban Institute. "The problem comes when this price stays low for a long time."

Some state officials are hopeful that the drop in gas prices – coming just in time for the holiday shopping season – will put more money in consumers' pockets and thus give a boost to sales tax revenues. Greg Albrecht, the chief economist for Louisiana's Legislative Fiscal Office, noted that mineral taxes account for a much smaller share of state revenues than sales taxes, which have run ahead of forecasts this year. Mineral taxes account for 13 percent of Louisiana's general fund revenues, compared with 29 percent from sales taxes.

Still, each dollar-per-barrel drop in oil cuts state revenue by $12 million. Declining oil revenues are the cause of more than half of Louisiana's $171 billion budget shortfall, which has already led to spending freezes and the elimination of state jobs. The situation is worse in Alaska. The state depends on oil for more than 90 percent of its general fund revenues and forecast the highest oil prices of any state when it set its budget. Oil revenues were already going to drop due to a tax cut, but the steep fall in prices has saddled the state with a $3.5 billion shortfall.

The situation is nowhere near as dire in other states, but oil dropping below $60 per barrel doesn't help states' bottom lines. Aside from a decline in severance taxes and royalty payments, low prices hurt oil state economies. Production is already being cut, with field workers being laid off. And the few states that link their gas taxes to the prices of oil, such as Kentucky and Pennsylvania, can count on a drop in fuel tax collections, noted Michael Streepey of the National Association of State Budget Officers. Kentucky, for example, can count on $129 million less in gas and diesel tax collections in 2015.

Diminished oil revenues are thus compounding budget problems that persist in many states, despite the overall economic recovery. Kansas is projecting $1 billion in shortfalls during the current fiscal year and next. "In Kansas, that's another $5 million that they don't have," said Francis, referring to the state's losses with every dollar drop in oil prices.

He said states like Kansas might ultimately be hurt the most. The major oil states such as Texas have been socking away billions in permanent or rainy day funds for years, if not generations. (Alaska had $14.7 billion in its reserve funds at the end of November.) They can ride out the price drop, which is expected to persist through 2015. It's the states that get a little extra help from oil that haven't saved as much and therefore are going to miss the money that's not coming in that much more. "Swings make them more vulnerable," Francis said. "If they're already in a precarious position like Kansas, even a small swing in oil money causes problems."

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