



Natural Gas Severance Tax

Testimony of Nathan A. Benefield

Vice President of Policy Analysis, Commonwealth Foundation
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Good afternoon. I want to thank Chairmen Yaw and Yudichak and Chairmen Eichelberger and Blake, along with the members of both committees for the opportunity to testify today.

As we discuss proposals to impose a natural gas extraction tax, I first want to offer some perspective on the current tax structure affecting gas drillers. There is a misconception among the public that gas drillers pay *no or little taxes*, which is as you know, wildly inaccurate.

First of all, gas drillers have paid more than [\\$600 million](#) in impact fee taxes from 2011 to 2013. And despite the name, the impact fee functions as a tax, as funds are used for government projects only tangentially related to gas drilling.

On top of this, gas drillers pay taxes common to every business operating in Pennsylvania, including the corporate income tax, personal income tax, and sales tax.

As a result, Pennsylvania collected [\\$318 million in other state taxes](#) from the gas drilling companies since 2009, while supporting businesses paid another \$1.4 billion in state taxes.

State income tax collections on royalties paid to landowners netted the commonwealth [\\$235 million](#) from 2007-2012, according to the Department of Revenue. That means gas companies paid individuals and families—the true owners of the gas—[about \\$7.7 billion in royalties](#).

And private landowners aren't the only ones that lease gas drilling rights; state and local governments are benefiting as well. Indeed, the state has received [\\$582 million](#) from the lease of state forest land through 2012.

The local impact has been felt in Elk Lake School District in Susquehanna County which collected [almost \\$1.7 million](#) from lease bonuses and royalty payments since 2007. That's enough to pay the average salary and benefits for 25 teachers. Elk Lake is not alone; dozens of schools have signed leases, including [South Butler School District](#), which negotiated a \$628,000 signing bonus in 2011.

Natural gas companies also pay permit fees, fines, and bonds for wells. The Department of Environmental Protection fined drillers [\\$2.5 million](#) during 2013 and raised permit fees in 2014. These are true fees, which cover the cost of inspection and oversight.

It is difficult to claim the industry isn't paying it's "fair share," whatever that really means, but any such argument should at least recognized the burden gas drillers already pay in taxes, fees, and royalties to landowners.

The table below breaks down the tax burden and rates in Pennsylvania compared to other gas producing states. Note that Pennsylvania drillers face one of the highest tax burdens in the country.

Top Natural Gas Producing States 2013	States	Severance Tax on Natural Gas	Exemptions and Incentives for Unconventional Wells	Top Corporate Net Income Tax Rate	State and Local Tax Burden (as a percentage of State income/national rank)
1	Texas	7.5% of market value	Rate reduction appr. 2% for up to 10 years	none	7.5% / 47
2	Pennsylvania	2.1% *		9.99%	10.3% / 10
3	Louisiana	\$0.03-0.13 per MCF	Severance tax suspension on horizontally drilled well for 2 years or until payback	8%	7.6% / 46
4	Oklahoma	7% plus 0.095% excise tax	Exempt from severance tax for 4 years or until gas production pays for the cost of the well	6%	8.5% / 39
5	Wyoming	6% of taxable value	Gas transportation costs subtracted from the taxable value	none	6.9% / 50
6	Colorado	2% - 5% based on gross income	Allows producers to deduct 87.5% of their property taxes paid to gov. from severance tax to state	4.63%	9% / 32
7	New Mexico	3.75%		7.30%	8.6% / 37
8	Arkansas	5%	1.5% on new discovery wells for 24 months and on high cost wells for 36 months (can get extension)	6.50%	10.3% / 12
9	West Virginia	5% + \$0.047 per MCF		6.50%	9.7% / 19
10	Utah	3% - 5%	6 months exemption for development wells	5%	9.4% / 28
11	Alaska	25% - 50% net value	Reduction for all drilling in Cook Inlet basin and when gas in used in state; Limited tax credits for exploration	9.40%	7% / 49
12	Kansas	8% on gross value severed from earth	3.67% tax credit for ad valorem taxes paid, effectively reducing the severance tax to 4.33%	7%	9.4% / 26
13	California	<0.01 per MCF		8.84%	11.4% / 4

*Pennsylvania levies an impact fee (akin to a tax) based chiefly on the number of natural gas horizontal wells. Sources: Energy Information Administration, Independent Fiscal Office, Tax Foundation

The commonwealth's *overall* tax burden is far higher than other drilling states, as well. Pennsylvanians shoulder the 10th highest local and state tax burden in the nation, with the nation's highest effective corporate income tax.

In contrast, there is no corporate income tax or personal income tax in Texas or Wyoming, and the corporate income tax in West Virginia is 6.5%, compared to Pennsylvania's 9.99% rate. In Alaska, taxpayers get refunds from oil and gas drilling.

A majority of states with significant drilling activity include severance tax exemptions. For instance, Texas applies a reduced rate to "high-cost wells" and Louisiana exempts horizontal wells for two years.

While Pennsylvania contains the most lucrative areas of the Marcellus shale, our tax and regulatory burden make us less competitive than other states, and we're losing ground.

In the 2014 [Fraser Institute Global Petroleum Survey](#) the commonwealth ranks 56th (among 156 jurisdictions with drilling) in attractiveness to invest, well below competing states like West Virginia, Texas and Ohio. The Marcellus Shale cannot be moved, but drilling rigs can easily relocate to more than twenty profitable oil and gas fields throughout the United States.

Indeed, we've already seen that low gas prices, the imposition of the impact fee tax, and other factors has resulted in a decline in activity.

Earlier this year, 162 Chevron field and office workers in Moon Township [received layoff notices](#). That's about one fifth of the company's Pennsylvania work force. Up the Interstate, more Pennsylvanians lost their jobs when Universal Well Services [closed their Meadville facility](#).

Months later, Noble Energy announced [220 layoffs](#), including 20 jobs in southwestern Pennsylvania.

Even organized labor is worried about the impact of a severance tax. Dennis Martire, vice president of the Laborers' International Union of North America, [explains](#), "We have already seen a reduction in pipeline man hours over the past two years related to falling gas prices. If you excessively tax the shale industry, you risk hurting employers, workers and communities across this state."

An additional tax on natural gas extraction would result in further decline and threaten job growth.

I included as an attachment to our testimony an economic analysis of Gov. Wolf's proposed tax changes, using the STAMP model developed by the Beacon Hill Institute at Suffolk University. We found that Gov. Wolf's proposal would result in 40,000 fewer private sector jobs by 2016-17.

Enacting the proposed severance tax, with no other tax changes, (this assumes \$1.015 billion in 2016-17) would result in **4,138 fewer private sector jobs** in fiscal year 2017.

In contrast, Gov. Wolf's proposal to reduce the Corporate Net Income Tax to 5.99 percent would, as stand-alone measure, result in **7,532 more private sector jobs** in 2017.

It's clear the proposed 5% tax on production plus \$0.047 cents per thousand cubic feet of gas – with a tax floor of \$2.97 – would hamper investment and job growth, especially under current market conditions.

The industry and related jobs in drilling communities aren't the only ones who would be harmed. All Pennsylvanians would pay the burden of a new extraction tax. Today, [Pennsylvanians benefit](#) from drilling by way of cheaper energy prices. Low natural gas prices helped *poor* families with a \$10 billion-per-year reduction in utility bills, according to a [Mercator Energy analysis](#).

While it is true that consumers in other states would also pay part of the cost of the severance tax—about 80% of the share, according to [the Independent Fiscal Office](#)—the cost to Pennsylvania families would be substantial.

About \$181 million of the severance tax cost would be borne by families earning less than \$100,000, according to the IFO.

Finally, I want to make a few comments on education spending, given the major selling point for a severance tax is that the money would be used for public schools. Even if you ignore the high probability that severance tax revenue would be diverted away from the schools, this sales pitch is based on several myths and half-truths.

Pennsylvania already [spends \\$3,000 more per student](#) than the national average. We rank 10th in spending per student, according to [NCES](#), and 6th in revenue per student according to the [NEA](#). Our state share, as a percentage of the total, is less than most states, but [state funding per student](#) ranks 25th, mirroring the national average.

New annual financial report summaries from the Department of Education—which we will be summarizing in an analysis coming out later this week—show that school district revenue increased by \$213 million in 2013-14 to nearly \$26.2 billion, an all-time high. Spending per student in 2013-14 rose to \$15,091.

And despite tales of cuts, school districts increased funding reserves by \$106 million, to \$4.1 billion in total reserves.

Pennsylvania's education woes stem not from a lack of funding, but from a broken funding system and an ongoing pension crisis. That's a problem new taxes simply cannot fix.

Rather than looking to new and higher taxes to aid public schools, we should work together to fix Pennsylvania's broken funding formula, address pension reform, and relieve school districts of costly mandates.

Simultaneously, lawmakers and the Governor should limit state spending to inflation plus population growth. Such limits would end the cycle of overspending and protect working families from tax increases when the economy sags.

Thank you for the opportunity to testify, and I look forward to any questions you may have.