



Dangers of a Natural Gas Severance Tax

Given the fiscal challenges facing the state, many advocacy groups are calling for new taxes on natural gas. However, lawmakers should be aware that a severance tax will make Pennsylvania less attractive for gas drillers. Tax increases will not solve the long-term fiscal problems facing our state, with budgetary drivers like pension costs and welfare growing faster than our economy. Finally, this tax increase will victimize Pennsylvania landowners who will see their royalty checks shrink and small business owners who provide products and services to gas drillers.

A Severance Tax will End Pennsylvania's Competitive Edge

The [Independent Fiscal Office \(IFO\) report](#) on a severance tax found that a 5 percent severance tax would place Pennsylvania's tax rate slightly above other states' effective tax rate, but only if one excludes other tax burdens and regulatory costs.

The IFO report mentions, but fails to quantify those other taxes that gas drillers pay in Pennsylvania. This includes the highest effective corporate income tax in the country at 9.9 percent. Several drilling states, including Texas and Wyoming, don't even have a corporate income tax.

Lawmakers should also be aware that 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. In other words, the effective severance tax rate is far less than a flat 5 percent.

In some cases, severance taxes are used to off-set other spending, not increase overall revenue. [Ohio is considering a severance tax](#) in order to reduce state income taxes. You cannot compare the competitiveness of states by looking at severance taxes alone.

In addition to impact fees, corporate taxes and income taxes, drilling companies are subject to sales tax, permit fees, fines, and bonds for wells. Natural gas companies have paid an [estimated \\$2.1 billion in taxes](#) since 2008. The industry also pays millions in permit fees each year. A recently approved permit increase will result in an additional \$5 million for Department of Environmental Protection (DEP) inspections. In addition, DEP fined drillers [\\$2.5 million](#) during 2013.

Pennsylvania is already losing ground to other states. In the newest 2013 [Fraser Institute's Global Petroleum Survey](#) the commonwealth **dropped 24 spots** to 58th in attractiveness to invest. The Marcellus Shale cannot be moved, but drilling rigs can relocate to more than twenty profitable oil and gas fields throughout the United States.

A Severance Tax won't Solve our Chronic Budget Shortfall Problem

There is no guarantee that the revenue collected from a severance tax would meet future desired levels of spending. In 2013, a severance tax would have generated \$230 million more than the impact fee. This is about what **state government spends in one day**. In fact, a 5 percent severance tax, if it had been in

place in 2011 and 2012, would have generated **less money** than the impact fee.

A severance tax doesn't solve the problems of runaway welfare costs, which are growing faster than state revenue, or our \$50 billion pension liability which would require an additional \$3 billion in payments each year for the next 30 years. Pennsylvania already maintains the [10th highest state and local tax burden](#), which hurts our ability to compete. If lawmakers do not address these cost drivers, a severance tax will be just one of many tax hikes necessary to prop up spending as the state's economy languishes.

Another danger of a severance tax is divorcing the revenue from local impacts, creating a slush fund for unrelated programs. The impact fee requires 60 percent of the revenue to stay in the local communities facing impacts from resource extraction. Transitioning to a severance tax removes the very rationale for the impact fee: to allow local governments to deal with costs related to the impact of drilling.

A Severance Tax will Harm Local Landowners, Schools and Business Owners

The impact fee is already reducing investment in Pennsylvania. Drilling companies such as Talisman and Anadarko chose to fill in or plug uncompleted [wells rather than pay an impact fee](#) for sites that were not producing gas.

Less investment means fewer royalty checks for landowners like [Shawn Georgetti](#). Shawn was a farmer living paycheck to paycheck and worked with 30-year-old equipment. Thanks to royalty checks, he purchased a new tractor. Royalties to landowners totaled an [\\$810 million](#) in 2013.

A severance tax would further increase the cost of drilling, meaning fewer wells will be drilled and fewer landowners will have the opportunity to collect royalty payments. When West Virginia increased their severance tax the number of drilling rigs declined, [according to Pennsylvania Independent Oil and Gas Association](#).

Schools districts could also lose income with a severance tax. Elk Lake School District in Susquehanna County has 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.

Higher taxes will also hurt small businessmen that are offering quality local jobs. New Pig Energy in Blair County specializes in well pad containment products. According to vice president Beth Powell, "Marcellus Shale is 100 percent of our business. Our [employment has more than doubled](#) since we started. We are up to 23 employees." But if drilling expenses increase and rigs diminish, New Pig's employees could lose their jobs.

Whether it is landowners, children or small business owners, a severance tax will harm Pennsylvanians by shifting resources from the local community to Harrisburg's coffers.

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