

October 24, 2017

The Honorable Mike Turzai, Speaker
PA House of Representatives
139 Main Capitol
Harrisburg, PA 17120

The Honorable Dave Reed, Majority Leader
PA House of Representatives
110 Main Capitol
Harrisburg, PA 17120

The Honorable Frank Dermody, Democratic Leader
PA House of Representatives
423 Main Capitol
Harrisburg, PA 17120

Members of the PA House of Representatives

Dear Representatives:

It's well past the time for an honest discussion about a Pennsylvania severance tax.

A little over a week ago at an event in Erie, Governor Wolf urged the legislature to come back to Harrisburg to complete the budget process by passing a severance tax and funding the state-related universities, stating that the "fairest and simplest solution to the current budget challenge is a severance tax on natural gas production." The governor also said that he's "not sure what it is that people don't like about this tax."

Now that severance tax supporters are closer than ever to getting their wish in the form of HB 1401, it's time to be honest about why this is the case – simply to fulfill the governor's signature campaign promise and help to get him reelected.

What people don't like about a Pennsylvania severance tax is simple, for those who want to listen. First and foremost, it's based upon what are nicely called false premises:

- During his campaign, the governor asserted that natural gas drillers were not paying their "fair share" of Pennsylvania taxes, and this assertion has continued to be one of the primary "sound bites" used by severance tax supporters.

False – Natural gas drillers pay the taxes other businesses pay, PLUS the impact "fee" that NO OTHER businesses pay, **so natural gas drillers are paying MORE than their fair share.**

- During his campaign, the governor asserted that Governor Tom Corbett drastically “cut” state education funding.

False – Governor Ed Rendell, for whom Governor Wolf worked, cut state education funding and used federal “stimulus” money to replace the cuts. **Governor Corbett INCREASED state education funding each year of his term, to the highest level ever - \$10.5 billion – at the time he left office.**

- Severance tax supporters continue to say that “we’re” not getting a fair share of the benefits of “our” natural gas.

False – Most of the natural gas produced in Pennsylvania is from privately owned resources and so does not belong to “us.” **The public IS being fairly compensated for the natural gas produced from publicly owned resources through bonus and rental payments and royalties** via leases with DCNR (state forests and parks), Game Commission (state game lands), DGS (State System of Higher Education & other state agencies), Fish and Boat Commission, and local governments (municipally owned parks, school property). **Any failure of the public to get its fair share of these publicly owned resources is because of Governor Rendell’s October 2010 moratorium on new leasing of resources under lands owned and managed by DCNR after using the proceeds to help balance a few State budgets, and because of the reinstatement of that moratorium by Governor Wolf in January 2015.**

- Severance tax supporters continue to say that most (80%) of the severance tax would be paid by out-of-state consumers because 80% of the gas produced is exported out of Pennsylvania.

False – **The severance tax would NOT be a gross receipts tax paid by consumers, but would be levied on - and paid by - Pennsylvania producers.** As explained in the next bullet, Pennsylvania producers are “price takers,” not “price makers” who can include the cost of an additional tax in the price they receive. Any additional tax on natural gas producers will reduce the amount of money available for continued private investments in exploration and development that will provide more tax revenues at all levels of government through growth.

- A state representative recently said that the price of natural gas to the customer in every state is set by an international market that has already factored in a reasonable severance tax because every other state has one.

False – **Natural gas prices in the Appalachian region are NOT set by international markets, but rather by gas-on-gas competition among Appalachian producers that bid against each other to sell gas at the lowest price.** Gas produced in the Appalachian Basin is priced at a severe discount to the prices received for gas produced in other regions of the country and the world due to insufficient pipelines and infrastructure to transport our gas to those regions.

- During that recent event in Erie, a state representative said that “Our gas is currently being used tax-free by other citizens in various states, while Pennsylvanians are paying taxes that help build roads and schools in states like Texas.”

False – This statement is a variation of the false statements above. **It is the equivalent of saying that**, before Pennsylvania was producing 5 times more natural gas than we are consuming and therefore imported gas from other states, **Pennsylvania consumers paid these other states’ severance and other taxes that helped to build roads and schools in these states.**

- Another primary “sound bite” used by severance tax supporters is “the gas is here so the drillers won’t leave.”

False – The natural gas is indeed here, but it’s also in many other states that have more business-friendly, predictable and consistent tax structures and regulations. Those states also do not target the industry with uneven enforcement of constantly changing regulatory rules and policies and subject the industry to lengthy permitting delays in violation of clear statutory deadlines. The initial wave of shale resource development activity in Pennsylvania will not reoccur if the current anti-business approach – including the enactment of an additional tax targeting only our industry – continues. **Industry investment capital will move to these other states, even though they have severance taxes, because of their overall more predictable and reasonable regulations and taxation of the industry.**

- Perhaps the “sound bite” most overused by severance tax supporters is “Pennsylvania is the only gas-producing state without a severance tax.”

While this is true in the most narrow sense, it is also an objectively false comparison. True if the impact fee is not viewed as a severance tax, but **false as an honest comparison of state tax structures.** Severance tax supporters repeatedly use the words “fair” and “reasonable” and “commonsense” but what is fair, reasonable and commonsense about focusing on only one aspect of other states’ tax structures? Nothing. Texas and Wyoming have no state corporate or individual income taxes, while Alaska has no state individual income tax. Should Pennsylvania also get rid of its state corporate and individual income taxes to better level the playing field with those states? Of course not, because we have our historical state and local tax structures, just as other states do, and **picking one aspect of another state’s tax structure while ignoring the whole structure is the ultimate false comparison that provides no support for adopting that one aspect.**

But the impact “fee” is, in operation and use, a TAX, and one that for its first 6 years of existence has averaged about 5% of the wellhead value of gas in PA, which is comparable to other states that impose a severance tax and exceeds the effective

severance tax rate charged for unconventional wells in Texas – Pennsylvania's No. 1 competitor for natural gas markets.

- And finally, just last week, a caller to a PCN *Call-in Program* stated that Texas collected enough money from taxing its shale production “in one year as we need to balance our budget,” and in response a state senator said “is an economic argument to be made on taxing Marcellus Shale.”

The caller's statement was true in the broadest sense, but is another objectively false comparison. It is true that the combined Texas severance tax revenue from oil and natural gas in 2016 was nearly \$2.3 billion, **but only 25% of this revenue was derived from natural gas, with the balance from crude oil.** And lest this give severance tax supporters the idea to include crude oil in the tax, Pennsylvania is not in the same category as Texas in oil production. While Texas natural gas production exceeded Pennsylvania's production in 2016 by only 22%, the big difference was in crude oil production – 1.18 billion barrels for Texas; but only 0.006 billion barrels for Pennsylvania. In terms of the total wellhead value of combined oil and gas production in 2016, Texas's was \$59 billion compared to Pennsylvania's \$5 billion.

As for another valid comparison, **last year our impact “fee” raised more (\$173.3 million) than the severance tax revenues of Ohio (\$36.67 million), West Virginia (\$69 million), Colorado (\$26 million) and Arkansas (\$38.2 million) combined (\$169.87 million).** Also, states that rely upon severance taxes to fund their budgets have suffered dramatically reductions in collections over the last few years as natural gas prices have declined. (Texas - ↓ 50%; N Dakota - ↓ 49%; WV - ↓ 47; Oklahoma - ↓ 44%).

The senator is, of course, entitled to his opinion, but not to his own facts. As shown above, the economic argument for taxing Marcellus Shale natural gas production is based on false premises.

Moreover, the Southeast delegation was very quick to complain about the proposed warehouse and hotel taxes that, in their view, would have hurt their constituents. But they have no qualms about hurting rural Western Pennsylvania by going that area's ox, even though their constituents have benefitted from shale production through lower energy prices and avoided refinery shut-downs and even impact fees even though there is no production anywhere near them.

The other fundamental reason people don't like the idea of imposing a severance tax on one industry that risked its capital on American ingenuity and technological innovation to bring jobs and the benefit of lower cost energy to Pennsylvania is that it's bad economic policy and sends the wrong message to businesses – if you help our economy and people, we'll tax you more and more to address a state budget mess your business had nothing to do with creating. Targeting for even more taxes an industry that is already *in fact* paying more than its fair share of taxes is a short-sighted and misguided way of helping that industry succeed.

The Pennsylvania Chamber of Business and Industry has been leading a diverse coalition representing thousands of businesses across a wide spectrum of industrial sectors throughout the Commonwealth that are opposed to a severance tax. As this coalition has stated, rather than continually looking to the oil and natural gas industry as a source of additional tax revenue, the focus should be on maximizing the economic opportunities that this industry represents. Pennsylvania has the real potential to cement its role as a world-class energy leader, but that will only happen if the General Assembly and Governor Wolf implement policies that support the responsible growth of the industry – such as the vital build out of pipelines and infrastructure to get the gas to market, along with a predictable permitting process that follows the law.

Only then will Pennsylvania realize its potential as **The Keystone to America's Energy Future.**

Sincerely,

A handwritten signature in black ink, appearing to read "Dan Weaver", with a long, sweeping horizontal line extending from the end of the name.

Dan Weaver
President & Executive Director