FOUR MISCONCEPTIONS ABOUT A SEVERANCE TAX

CLAIM: A SEVERANCE TAX WON'T BRING SUBSTANTIAL REVENUES TO PENNSYLVANIA.

WRONG. A severance tax can bring in substantial and, as natural gas prices rise, growing revenues to help close our budget and investment deficits now and in the future.

Governor Wolf proposed a severance tax as part of his 2018-19 Executive Budget. The tax rate would be tied to the price of natural gas and would therefore increase as the price of natural gas increases. His proposal is projected to bring in over $200 million next year and $400 million and over starting in 2021-22. The funds raised from the severance tax would be in addition to the current impact fee, which would remain in place. The additional funds raised from a severance tax can be used for critical investments in K-12 education, infrastructure, higher education and human services.

CLAIM: DRILLING COMPANIES ALREADY PAY TOO MUCH IN STATE TAXES VIA THE IMPACT FEE AND OTHER CORPORATE TAXES.

WRONG. Oil and gas development companies pay comparatively little in state taxes now.

Even though gas production has more than quadrupled in Pennsylvania since 2011 from 1,065 billion cubic feet to 5,363 in 2017, revenue raised from the impact fee has hovered at around $205 million over the last seven years. Revenue reached its peak in 2013 to $226 million, but dropped as low as $173 million in 2016. Pennsylvania is now the 2nd largest natural gas producer in the nation (behind Texas) but is the only state without a severance tax tied to the amount of gas extracted from within our borders.

Pennsylvania's current impact fee has an effective tax rate (ETR) of 1.6%. This is far below the effective tax rates of most other states with a severance tax (except Ohio). Passing Governor Wolf's severance tax proposal would, combined with the impact fee, put Pennsylvania's effective tax rate at around 4%, which begins to get closer to neighboring West Virginia's rate (5%) and to Oklahoma's (4.8%).

Natural gas drillers pay little to no corporate income tax in Pennsylvania due to federal energy development tax incentives, porous corporate income tax for companies based out of state and many company's status as limited partnerships (or what we call pass-through entities). PBPC's February 2017 analysis found 65% of oil and gas companies were structured as pass-through entities meaning they were paying taxes at the Personal Income Tax rate of 3.07% instead of the higher 9.99% corporate income tax rate. Our most recent estimates show that gas drillers pay somewhere between 7% and 37% less in corporate net income taxes than they did in 2011-2012 at the beginning of the boom.

CLAIM: IF WE INSTITUTE A SEVERANCE TAX, DRILLING COMPANIES WOULD JUST LEAVE PENNSYLVANIA.

WRONG. Every other major gas-producing state has a severance tax, so a severance tax would create no incentive for drilling companies to leave Pennsylvania.

Tax policies make little difference in the decision to extract natural resources in one state over another. Montana, where the first successful horizontal well was drilled, offered tax rates of about half that of neighboring North Dakota. Yet from 2009 to 2016 production of dry natural gas increased by more than eight times in North Dakota and fell in Montana by 52%. Tax incentives cannot overcome geology in determining the best location for production.

What is important to development are gas prices, access to markets, and the relative costs of producing the gas. Pennsylvania's Marcellus/Utica shale play is the largest, lowest-cost gas producing region in the country, so it is very attractive to drillers. It will become more important as new pipelines, already under construction, make investment in Pennsylvania even more attractive.

CLAIM: THE SEVERANCE TAX WOULD BE PASSED ON TO CONSUMERS IN PENNSYLVANIA.

WRONG. Pennsylvania's residential consumers will pay a tiny portion of a severance tax.

Most of the gas produced in Pennsylvania is exported. As a result, according to the Independent Fiscal Office, residents of other states and countries would pay 80% of Pennsylvania's severance tax. Pennsylvania consumers — who already pay severance taxes to other states that ship gas here — will bear less than 20% of the tax burden and will see their gas prices go up by a very small amount.