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PENNSYLVANIA STATE ASSOCIATION OF TOWNSHIP SUPERVISORS

TESTIMONY BY THE PENNSYLVANIA STATE ASSOCIATION OF TOWNSHIP SUPERVISORS

BEFORE THE HOUSE FINANCE COMMITTEE

CONCERNING

HOUSE BILL 2443

PRESENTED BY

JAMES DECKER, TOWNSHIP SUPERVISOR
STROUD TOWNSHIP, MONROE COUNTY

MAY 13, 2010

SHAWNEE ON DELAWARE, PA

Chairman Levdansky and members of the House Finance Committee:

Good afternoon. My name is James Decker and I am a township supervisor in Stroud Township, Monroe County. With me today is Elam Herr, assistant executive director for the Association. Thank you for the opportunity to appear before you today on behalf of the 1,455 townships in Pennsylvania represented by the Association. We appreciate this opportunity to participate today on this issue that is so important to our members.

Townships comprise 95 percent of the commonwealth's land area and are home to more than 5.4 million Pennsylvanians — nearly 42 percent of the state's population. These townships are very diverse, ranging from rural communities with fewer than 200 residents to more populated communities with populations approaching 70,000 residents.

The Marcellus Shale formation covers two-thirds of the commonwealth, from Greene County in the southwest to Wayne County in the northeast, and is estimated to hold hundreds of trillions of cubic feet of natural gas. In fact, estimated evaluations of the value of Pennsylvania's resources have increased from $10 to $20 billion several years ago to closer to $1 trillion today. While the natural resource in this area has the potential to economically benefit many communities, drilling is not without an impact on townships and their residents.

The Association supports a severance tax on natural gas, provided that at least 25 percent of this tax comes back to the local governments that are affected by the activity. While we believe that House Bill 2443 *(PN 3607)* is a step in the right direction with its inclusion of a local government share of 20 percent, we believe that some improvements need to be made to the bill before it should move forward, particularly concerning how the municipal share is distributed.

Townships are excellent fiscal stewards and are generally among the last to advocate for increasing taxes. We have done more with less for a very long time and pride ourselves in finding efficiencies and economies of scale to benefit our taxpayers. We believe that a natural gas severance tax is not a tax *on* Pennsylvanians, but rather a tax *for* Pennsylvanians that will result in property tax relief. In fact, such a tax would not increase the cost of gas to consumers in Pennsylvania, because we are already paying such taxes on gas imported from other states. Instead, a severance tax would make sure that out-of-state customers are paying the tax to benefit the communities in Pennsylvania where the extraction is taking place. Otherwise, these communities would need to raise property taxes to cover the costs associated with industry impacts.

Over the past several years, we've heard numerous concerns from our members about gas well drilling. It is clearly impacting communities across the Marcellus Shale region, both with economic opportunity, and with the many negative impacts associated with it. Our Association is supportive of economic development and opportunities, provided that drilling activities are conducted in an environmentally responsible manner and that the impacts on the community and the environment are mitigated to the extent

possible. Keep in mind that once a healthy environment is damaged, it can take decades, if not centuries, to recover.

In support of the local share, it is the local communities, and particularly the host municipalities, that bear the brunt of the burden from the industry through destruction of roads and potential environmental disasters. While many of these companies are working well with their local communities, the affected municipalities receive little in terms of local tax revenues from these companies. Other than the local services tax for employees primarily employed in a particular municipality and property taxes on any physical facilities, the industry pays next to nothing to the host communities. In fact, many industry employees are out-of-state residents and are not subject to the local earned income tax.

In addition, while other natural resources in Pennsylvania are assessed as real estate and subject to the property tax, including coal deposits, natural gas and coal bed methane reserves have been exempt since 2002, when the Pennsylvania Supreme Court ruled in *Independent Oil and Gas Association of Pennsylvania v. the Board of Assessment Appeals of Fayette County* that assessing and levying property taxes on oil and gas wells was not explicitly authorized under the law.

Keep in mind that Pennsylvania is only one of three natural gas producing states, including New York and Iowa, that does not levy a severance or similar impact tax on the industry. New York, which has had a moratorium on natural gas drilling permits due to concerns with the potential negative environmental consequences of the industry, has plans to levy a severance tax, as well as to impose stringent environmental regulations, once the moratorium is lifted. Many natural gas drilling companies currently working in Northern Pennsylvania have plans to move into New York as well once the moratorium is lifted.

HB 2443 would impose a severance tax of 25 cents per thousand cubic feet on producing gas wells, which would be placed into a separate fund in the state treasury and, after administrative expenses are deducted, 45 percent would be deposited into the state's General Fund, 20 percent would be placed into a Local Government Services Fund, and the rest would be deposited into a number of special state accounts.

While we are not experts on severance tax rates, we must ask whether 25 cents per thousand cubic feet of natural gas is sufficient. We understand that this particular model is based on Louisiana. However, West Virginia may be a better model based on similarities in climate, topography, and geology. It is worth noting that New York is considering a 3 percent extraction tax when the moratorium on drilling permits is lifted and that Texas imposes a 7.5 percent tax on the market value of oil and gas that has amounted to billions of dollars in the last several years.

Of the monies deposited into the Local Government Services Fund, 30 percent would be allocated to counties with severed wells *(6% of total tax)*; 60 percent to municipalities in counties with severed wells *(12% of total tax)*; and 10 percent to the

Pennsylvania Emergency Management Agency for distribution to volunteer fire and ambulance services in counties where natural gas is severed *(2% of total tax.)* While the bill appropriately allocates funding for emergency first responders in the affected counties, we contend that this funding should come out of the state's share of the tax.

Our primary concern with the bill is the manner in which the municipal share would be divided. Specifically, each municipality in each county where at least one well is severed would receive 1 credit. Each host municipality would receive 2 credits per severed well.

Under this formula, host municipalities would receive a greatly reduced proportional share of the pie because of the need to share with all of the municipalities in the county. Take, for instance, a county with only one severed well. The host municipality will receive 2 credits while every other municipality in the county would receive one credit, regardless of their location or impact. If a county has 40 municipalities, then the host would receive 2 credits worth of funds while the remaining 39 municipalities would receive one credit each. Therefore, the non-host municipalities would receive, as a group, 19.5 times *more* funds than the host municipality that bears most of the impacts associated with the well. We believe this formula needs to be revisited to make sure that the affected municipalities are receiving a share of the funding that is proportional to their impact.

In addition, each non-host municipality receives one credit *regardless* of whether one or 300 wells are severed in that county. This is going to greatly inflate the funds received by municipalities in the county with only one well, but will decrease what municipalities receive in a county with 300 wells. Instead, we contend that this allocation should be made on a county, not a statewide, basis.

Because the severance tax is such a major issue for our members, we have actively worked with the County Commissioners Association of Pennsylvania to draft a severance tax proposal. We offer our distribution formula as an alternative to HB 2443.

Our proposal would distribute 9 percent of the total tax to host municipalities proportionately based on the number of severed wells statewide. In addition, 5 percent of the total tax would be allocated to municipalities that are located in a county in which at least one well has been severed. This pot would first be divided proportionately by county based on the number of wells severed statewide and then distributed to all of the municipalities in each respective county through the liquid fuels formula, which is 50 percent based on population and 50 percent based on road miles. In addition, 8 percent would be allocated to counties on a pro rata basis determined by the number of wells severed and 3 percent of the total tax would be distributed to the county conservation districts, for a total local share of 25 percent of the total tax. While the local share in HB 2443 is close to our proposal, our municipal distribution formula is very different from the bill.

Finally, in addition to levying a severance tax with a 25 percent local share, we believe that the General Assembly should take several actions to help communities better manage their infrastructure and face the influx of oil and gas well drilling in the Marcellus Shale region. These changes would cost the Commonwealth little, if anything, but would create a major benefit for *all* townships across the state, and includes requiring PennDOT to increase the maximum road bonding amounts from the current $6,000 per mile for unpaved roads and $12,500 per mile for paved roads and enacting legislation to increase the required advertising and bidding amount from $10,000 to $25,000, with an annual cost of living increase.

In closing, our Association supports a severance tax as a means of easing future property tax burdens caused by the impacts of this industry and believes that this proposal is a step in the right direction. However, changes need to be made to provide a fair means of distributing these funds to the affected municipalities.

Thank you for the opportunity to comment today on this issue that is of such importance to townships across the state.