Joint Statement on Ohio's Shale Severance Tax

Ohio's existing severance tax on oil and gas production is among the lowest of all oil and gas producing states, but local expenses related to drilling are high. Ohio has experienced rapid development of oil and gas extraction from hydrofracturing or fracking over the past four years. The state's well production is the highest it has been in 100 years.[1]

Shale development comes with escalating costs—increased road maintenance needs, new demands for emergency services, rapid escalation of housing costs, greater need for oversight and regulation of the industry, and negative effects on air and water quality, among other issues.[2] Residents of effected communities also complain of increased traffic, destruction of the landscape and concern over potential lasting damage to their water supply.

Despite these many costs, Ohio's lucrative oil and gas industry pays a mere dime per barrel of oil in severance taxes and 2.5 cents per thousand cubic feet of natural gas (MCF) plus a small conservation fee of ten cents per barrel of oil and half-cent per natural gas MCF.

Ohio lags behind other Midwestern states in its oil and gas severance tax rates. Our sister state of West Virginia has a fair severance tax rate of 5% on oil and gas. The more mature shale producing regions, like North Dakota, Texas and Wyoming, have even higher rates (i.e. North Dakota has a severance tax rate of 10%). Ohio's effective severance tax rate is less than 1%.[3] Despite significantly higher severance tax rates in other oil and gas producing states, industry development has flourished in those states, running counter to industry claims that increasing the severance tax rate will suppress shale development.

While prices for oil and gas have recently fallen, they are predicted to grow over the long term.[4] Even if Ohio's shale development sees a temporary lull, as other states have recently experienced, these resources will be extracted in the future. Smart states plan for the long term. Ohio should be a smart state and prepare for the future.

The Ohio General Assembly recently created an "Ohio 2020 Tax Policy Study Commission" in the new state budget bill (HB 64). This commission aims to review the state's tax structure and policies and to make recommendations to the legislature. The first charge of this commission is to address "how to reform Ohio's severance tax in a way that maximizes competitiveness and enhances the general welfare of the state." By the end of October 2015, the commission plans to publish an initial set of findings and recommendations.

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[1] Bob Downing, "Ohio's Utica Shale continues to set state oil, natural gas production records," Akron Beacon Journal, August 27, 2015.
[2] http://www.policymattersohio.org/governors-mar2014#sthash.rKeN5aJz.dpuf
[3] Ohio's effective severance tax rate over the past decade has been .07 percent of the total value of oil (7/100 of 1%), and .39 percent (almost 4/10th of 1%) of the value of natural gas – this is based on data from the 2013 Summary of Ohio's Oil and Gas.
[4] U.S. Energy Information Administration, Annual Energy Outlook, 2015.

Given the condensed time frame for the formation of the Tax Policy Study Commission and the apparent lack of opportunity for public input and review of this issue so far, a number of Ohio-based organizations have come together to offer the following high-level policy recommendations for a fair and common sense severance tax on shale wells in Ohio.

Policy Recommendations

While there are benefits to shale development, it also comes with costs. We recommend increasing the severance tax and investing a fair share of proceeds toward minimizing costs. At a 5% rate – without tax breaks - almost $100 million could have been collected in 2014. A 5% severance tax rate is fair, and necessary. Increased revenue from a reasonable severance tax can and should be used to cover the shale gas price tag:

Addressing negative effects on local communities
A portion of Ohio's severance tax on shale oil and gas should help make communities whole from the negative impacts experienced due to the shale boom in Appalachia. At least $170 million in immediate needs have been presented by local community leaders in testimony to state legislators. These needs include infrastructure (water, sewer, roads and bridges), emergency response needs, affordable housing, and planning to ameliorate expected negative effects, and protect public health and safety. The Ohio Shale Country Listening Project identified the top three concerns of nearly 800 local residents in the Utica Shale region as water contamination, damage to farmland and ecosystems, and increased truck traffic.

Concern over water is particularly pressing. Operational mishaps and illegal dumping have contaminated land and streams in Ohio. Ongoing shale development continues to pose serious risks to both surface and drinking water. Drilling pads, pipelines, and wastewater pits alter the landscape, including the flow of water. Massive water withdrawals for fracking compete with water needs of communities and other industries. Funds need to be dedicated to investing in regional watershed restoration and management to protect local tourism and recreation and safeguard drinking water.

Covering costs of adequate regulatory oversight of the shale industry
A portion of Ohio's severance tax on shale oil and gas should cover the regulatory oversight of all activities related to the exploration, production, transportation, and processing of oil and gas resources, including permitting, inspection, enforcement, and remediation of negative effects. Sufficient revenue should be allocated for regulatory, enforcement and emergency management activities by both the Ohio Department of Natural Resources and Ohio Environmental Protection Agency.

Ameliorating the boom/bust cycle seen in extraction-based economies
Several states with significant natural resources established "permanent funds" or "legacy funds," investing proceeds in education, workforce and economic development in order to transform the regional economy. This funding ameliorates the natural boom and bust cycle of resource extraction by underwriting long-term investments to strengthen and diversify local economies dependent on resource extraction. When production meets a certain point or earnings rise by a certain percentage, an additional fee should be established to start building a "legacy fund" in Ohio.