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Shale Gas Impact Fee Revenue Continues to Slide

Summary: Pennsylvania enacted an impact fee on any natural gas well drilled in the state's shale formations in 2012. Since then it has brought $1.216 billion in revenue. Thus far the money has benefitted counties and municipalities across the Commonwealth, various state agencies, and a legacy fund designed to help with environmental concerns. Annual impact fee revenue has declined significantly since 2013 primarily due to weakness in the price of natural gas.

In mid-June, the Pennsylvania Public Utility Commission (PUC) released data on 2016 revenue generated by the state's impact fee. A total of $173.26 million was collected based on 8,121 unconventional wells (those drilled in the shale formations using the fracturing method). This represents the lowest annual revenue since collection of the impact fee began in 2012. In the years since the impact fee was enacted, it has generated a total of $1.216 billion in revenue.

Peak annual impact fee revenue occurred for the 2013 reporting year when collections reached $225.75 million. In that year just 6,550 wells were subject to the fee. Since 2013, revenue has fallen steadily despite increases in the number of wells eligible to pay the fee. The $173.26 million figure for 2016 is 23 percent below the high set in 2013.

Act 13 of 2012 authorized the impact fee for each operating well using a schedule based on the natural gas trading price from the New York Mercantile Exchange and the age of the well. Thus, the three year decline in impact fee collections since 2013 reflects three major factors. First, the major drop in the price of natural gas due to the glut of gas in the market brought about, in large part, by the substantial rise in production from Marcellus and Utica Shale. Second, the number of new wells has been trending lower. And third, because the impact fee is lowered as wells age and with each passing year the average age has risen owing to the fact that the number of aging wells is significantly greater than the number of new wells.

Not only has the slide in market prices led to lower impact fee revenue, it has been a contributing factor in the significant decline in drilling activity. Since 2011 when there were 1,956 wells started, the new well count has fallen in every year except 2014 to stand

at 504 new wells started in 2016. In total, 3,878 new wells were started in the four years 2013 through 2016. However, as indicated above, the total number of eligible well rose by only 1,571. That means roughly 2,300 new or existing wells were capped or taken out of production.

The impact fee is divided among a handful of state agencies, a Marcellus Shale legacy fund, and the municipalities and counties across the Commonwealth.

Thus far state agencies have benefitted greatly from the impact fee since its first collections in 2012. The Department of Environmental Protection ($36M) has received the largest sum since collections began. Other agencies receiving money include the PUC, the Fish and Boat Commission, and the Department of Transportation ($6 million each). The State Conservation Commission has received $37.7 million which it in turn has distributed funds to County Conservation Districts across the state. In total, the state agencies have received $120.68 million since the impact fee collections commenced.

The Marcellus Shale legacy fund has received a total of $438.49 million from the fee. This fund is used to provide financing for: (1) for highway and bridge improvements ($109.6M), (2) water and sewer projects through two different state authorities (PA Infrastructure Investment Authority and the Commonwealth Financing Authority—$54.8 million each), (3) the Commonwealth Financing Authority ($87.7M for environmental items such as acid mine drainage or well abandonment), (4) an environmental stewardship fund ($43.8), and (5) a county rehabilitation of greenways program ($65.8M). The intent is to help offset the negative impacts natural gas drilling may have on the communities in which they occur.

Through the first six years of collections, counties and municipalities have shared $292.65 million generated by the impact fee. One of the goals for imposing the impact fee is to return money to the municipalities and counties that are most affected by the activity. However, all counties receive money whether or not any drilling takes place within their borders. Counties with drilling activity shared $248.57 million while those without activity have split over $44 million. The latter's allotment is based on population. Thus Philadelphia County, the largest in the Commonwealth (by population) has received over $7.9 million since the impact fee has been imposed. Even the smallest counties receive at least $25,000 per year.

In the Southwest corner of the state, Washington County has received $32.8 million from impact fee revenue, statewide, second only to Bradford County's $38.4 million. Allegheny County has received $7.8 million, Westmoreland $8.7 million and Butler $9.6 million. The impact fee has greatly benefitted many local governments as well as many statewide programs.

However, absent a major uptick in gas prices, new drilling activity and production are likely to be far from robust for some time, at least until pipelines are completed that open up more markets and boost demand for Pennsylvania gas.

The impact fee has accomplished what it set out to do; impose a tax on the shale gas industry in order to: (1) provide revenue to counties and municipalities most impacted by the activity, (2) finance a legacy fund that addresses environmental issues, and (3) to help fund several state agencies. More than $1.2 billion in impact fee revenue has been collected thus far.

Unfortunately, since the current Governor took office, there has been talk that an impact fee is not enough and there has been a renewed push for a severance tax to close a large gap in the state's budget. Currently, a bill has passed the State Senate that includes a severance tax. Act 13 of 2012 that created the impact fee contains a provision (§2318) that requires elimination of the impact fee if a severance tax is enacted. Will that stipulation be overturned leaving the industry saddled with both the impact fee and a severance tax, as well as the corporate income tax and all the other fees and taxes the gas companies pay? Would that not be reneging on a commitment made to the industry when the impact fee was enacted?

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