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HOUSE OF REPRESENTATIVES

HOUSE FINANCE COMMITTEE HEARING

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1:08 P.M.

PRESENTATION ON HOUSE BILL 10

BEFORE:

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HONORABLE BRIAN L. ELLIS
HONORABLE FLORINDO J. FABRIZIO
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I N D E X

TESTIFIERS

P R O C E E D I N G S

CHAIRMAN LEVDANSKY: Good afternoon. The subject of today's committee meeting is House Bill 10, legislation that pertains to the assessment of property and whether or not it should include the value of the minerals that underlie the surface and surface structures. The issue had been brought to the floor by a 2002 State Supreme Court ruling in a case brought in Fayette County, whereby the Court determined that the oil and gas rights were not to be included as taxable and included in the assessed valuation of property.

That court decision has had an impact on the various taxing bodies throughout the Commonwealth, taxing bodies being counties, school districts and local governments. And in response to that, that court decision, Representative Bill DeWeese has introduced House Bill 10, Printer's Number 904, to address this particular issue. And I would like to invite Representative DeWeese to take a few moments and share with us his concerns regarding this issue.

REPRESENTATIVE DEWEESE: Thank you, Mr. Chairman.

My name is not Bill Kortz, and I am focused entirely upon this issue for the afternoon. The fact is that historically, in settings like Greene County and

Fayette County -- and my good friends from IOGA will at least nod in some affirmation -- my friends from the coal industry, we have had at least the ability for some revivification in our rural townships and boroughs and schools districts because coal has been valued as an underground mineral resource in school districts like West Greene or Southeastern Greene or Central Greene and innumerable other school districts within the Commonwealth where the beneficiaries of coal is being valued at a certain assessment level.

The history of the natural gas world being assessed before 2002 will probably be brought out later in the hearing, but certainly it was advantageous for Henry Clay Township or Wharton Township or rural townships in Fayette County to be benefitted from the revenue stream that would be forthcoming.

I've said again and again -- and I'll contain my remarks to three or four minutes here, but the metal excreta of the coal industry, whether it was LTV or Bethlehem Steel or other entities leaving Greene County specifically or their sister and brother counterparts in Lackawanna and Luzerne and Schuylkill and the devastation that was brought in the late 19th and throughout the 20th century to our rivers and streams and stream banks and the calm piles and the brick buildings and the perpetual settings of dilapidation when industry would get up and skedaddle, hither, yither and yawn -- I am not going to mix the severance tax dialog with the assessment dialogue, but I will say they are fundamentally in a nexus because these rural settings have been so devastated historically.

And yet in my home area, thanks to the coal industry, the wonderfully advantageous community of interest that the coal folks in my 50th Legislative District in particular and in southwestern Pennsylvania have offered over the past many years, whether it's the assessments that the county commissioners are collecting or whether it's the baseball fields that the young girls can play on that have been contributed to are vital.

And I think that there is a way for this committee, Honorable Chairman Ledvansky, Honorable Chairman Rohrer and my colleagues, to work a very, very reasonable reconstruction of the statute that existed prior to 2002 and also, on a related subject, to look at a very, very modest severance tax like almost a score of what other states have throughout the U.S. This is a phenomenal opportunity for us relative to the Marcellus Shale dynamic.

And my closing observations would be that if we are prudent -- and even my good friend Chairman Ellis, I think, will potentially be motivated in the final construction of a statute -- we can realize a very modest stream of revenue from these assessments and hopefully some day from a severance tax. But if we lose this opportunity like legislators in the 1890's or 19-teens or 1930's or 1950's or, indeed, in the 1970's, when Joe Jerzack (ph) of the United Mine Workers -- and Mr. Ellis smiles in assent. He and I introduced a severance tax on coal. We did not only not arrive at first base, I don't think we got out of the batter's box.

But the assessment, in conclusion, the assessment is so much of an opportunity for us to realize revenue in small rural counties, townships, boroughs, school districts. And if we don't go too far and we just focus on a very reasonable level of taxation, like Chairman Rohrer has discussed in so many other settings, I think this committee's work can be one of the most invaluable efforts that we realize between now and November 30.

Thank you very much, Mr. Chairman, for the opportunity to have eight minutes at the microphone.

CHAIRMAN LEVDANSKY: Thank you, Representative DeWeese.

Before I call the first panel to testify, let me start by having members of the Committee identify themselves by the record starting to my left with Chairman Rohrer.

REPRESENTATIVE ROHRER: Representative Rohrer, Berks County.

REPRESENTATIVE HARRIS: Representative Adam Harris; Juniata, Mifflin and Snyder.

REPRESENTATIVE ELLIS: Representative Brian Ellis, Butler County.

REPRESENTATIVE PEIFER: Representative Mike Peifer; 139th District, which is Wayne, Pike and Monroe Counties.

REPRESENTATIVE FABRIZIO: Flo Fabrizio, Erie County.

REPRESENTATIVE MIRABITO: Rick Mirabito, Lycoming County.

REPRESENTATIVE KESSLER: Dave Kessler, Berks County.

REPRESENTATIVE SAINATO: Chris Sainato, Lawrence and a small section of Beaver County.

REPRESENTATIVE YUDICHAK: John Yudichak, Luzerne County.

REPRESENTATIVE SEIP: Tim Seip, representing part of Berks and part of Schuylkill County, including Pine Grove, home of Grover the Groundhog, who tells us we will have six more weeks of winter.

CHAIRMAN LEVDANSKY: Thank you on that wonderful thought.

The first panel are panel people from local government. Let me call up to the front to offer testimony Mr. Doug Hill, the Executive Director of the County Commissioners Association of Pennsylvania; Elam Herr, the Assistant Executive Director of the Pennsylvania State Association of Township Supervisors; and Ed Troxell, the Director of Government Affairs for the Pennsylvania State Association of Boroughs.

Welcome, gentlemen.

MR. HILL: Thank you, Mr. Chairman, members of the Committee, and Representative DeWeese, prime sponsor of today's legislation. I'm Doug Hill, Executive Director of the County Commissioners Association.

And, Mr. Chairman, you introduced the other members of the panel. I presume we'll each present some remarks, and then we'll all be happy to take your questions. I represent the County Commissioners Association of Pennsylvania, which is a nonprofit, nonpartisan association that provides legislative training, insurance, technology, research and other programs on behalf of all the Commonwealth's 67 counties.

And it is a pleasure to appear before you today to talk about House Bill 10, which would restore the assessability of oil and gas. And I want to say at the outset that our testimony is not about the severance tax. It is not about a new tax or fee. It is not about a separate tax or fee. It's not about all the other issues related to Marcellus, including economic development, infrastructure, environment, emergency preparedness and others. But rather what our testimony is about is simple equity, and it is about restoration of equity.

As was indicated in Representative DeWeese's opening remarks, what occasions this bill is the 2002 decision of the Pennsylvania Supreme Court in Independent Oil and Gas et al. versus Fayette County Board of Assessment, in which the Court ruled that counties did not have authority to assess oil and gas for property tax purposes.

And I should say at the outset, counties are the ones responsible for maintenance of the assessment system on behalf of county, municipal and school governments. The basis of the Court's decision was simply that it wasn't enumerated in law, and that's despite the very clear language in the general county assessment law that everything is assessable unless specifically exempted by the General Assembly.

I think it's also important to note that the Court's decision was not on a constitutional issue or an equity issue, but, again, based exclusively on the point that there was not clear enumeration in law. And so that's what House Bill 10 intends to do. By amending the fourththrough eighth-class county assessment law with appropriate reference to the other classes of counties as well, it would restore that assessability and restore that equity.

I should mention as well, even though we are having this hearing in the context and in the era, if you will, of the Marcellus Exploration, our interest in the restoration and assessability predates that, the Marcellus play. We actually have been seeking this legislation since the original court decision in 2002. So I also need to say clearly that our membership views the industry as an important industry and that it represents tremendous opportunities for economic development locally and jobs and potential growth in the time of an economic downturn.

But the benefits are also no different from what other small businesses and large businesses and industries bring to the community. What is different is that all of those businesses are paying their fair share of the local property tax. The oil and gas industry, because of the court decision, is not. And so what our intent is is to restore that assessability, restore that equity and that parody compared to other businesses and industries.

The thing that's important to note is that any time one segment of the community is exempted from taxes, that doesn't mean that we reduce services. We don't have the luxury of reducing services. Those of you that have served in local government know that very well. At the county level, Children and Youth case load doesn't decrease just because you don't have the revenues to pay for it. The criminal case load doesn't decrease because we don't have the budget capacity. So instead what happens when any class is exempted from taxation, that means that tax burden is borne by everyone else.

And so this is a matter of equity, not just -- this is a matter of equity for all the other property taxpayers. And I should also emphasize it's a matter of equity for the other mineral interests as well. Currently under Pennsylvania law, coal, limestone, sand, any other mineral is assessed for property tax purposes and is paying its fair share. So what we are looking for is a restoration.

Now, I have to emphasize as well that there is a differentiation between the producer's interest and the landowner's interest because the question we often get is who does this fall back against. When a property goes into production, or for that matter, when a lease is executed to provide a right to assess that property for production, that either, by the lease or by an actual transfer of deed, severs the right for the mineral interest; and that mineral interest then gains a value because it is now accessible for extraction.

And so a property right attends to the lease or the transfer, and a value attends to that as well, an increase in the value of the property. When the property assessment roll is done, there is a value assessed to the surface rights of the property, and that's the landowner, the traditional landowner. And then there's a separate parcel, if you will, created for the subsurface rights. And that is assessed separately, and whoever controls those subsurface rights is the person or entity who gets the property tax bill.

Now, the industry has called property tax assessment unnecessary and that the industry has no impact on local government or nominal impact. I think you all can understand very easily when you see 40 trucks moving frac water that there is very clearly an impact on municipal roads, and my colleagues will testify about that more later. But there's also an impact at the county level, and, in fact, in many ways it's peculiar to this industry because a lot of the workforce until now and, for that matter, in the foreseeable future, is drawn from out of state.

And what we are seeing at the county level is, in addition to the effects on our county bridges, we're also seeing impacts on our social services and human services systems. We see -- and by the way, I don't mean to imply that these out-of-state workers are any different from the regular population, that they're any worse or they're a different kind of person or anything like that, but rather proportionally, people coming in from out of state also have their share of people who have problems that they bring with them.

We have already seen Children and Youth issues, Domestic Relation issues, criminal justice issues. And in fact, for that matter, what we're finding now is if they come in from out of state and they're on probation or patrol, under the interstate agreements, they fall into county and state probation and patrol systems, and we pick up that responsibility.

There are other effects at the county level as well. Counties are responsible for emergency management, both response and for planning, and emergency management planning means, for example, we're assigning discreet addresses to each of these well sites; so that if there's an incident, we know from our locator systems how to respond. Similarly, we're responsible at the county level for doing hazardous materials emergency response plans.

And whether you classify frac water as a hazardous material or not, any type of industrial use requires us to at least take it into account as a part of our hazardous materials planning. Even in the Recorder of

Deeds office, we're seeing an impact. And in particular, if you look at some of our smaller counties in the northeast, northeastern part of state, they've extended office hours; they've hired in new employees. We even have a couple counties who have given a handful of trusted attorneys extra keys to the courthouse, so, you know, just do your deed search until you're finished and then lock the door when you leave.

So there are a number of impacts other than the ones we see very easily on the impacts of the roads. But all that aside, the fundamental basis of a property tax system is that everyone who owns property, whether that's an individual, a store, a mineral producer, a power plant or a factory, has some obligation, is a member of the community and has some obligation to help support that community.

So a property tax is not a service fee, per se, but rather a property tax is imposed without regard to the level of service use, but rather recognizes that we're all part of a community together and this is one means of apportioning the share of the cost of providing services to everyone in the community. A couple other points to make, industries argued that few counties were assessing oil and gas prior to the 2002 decision.

In fact, the ability to do so exists we know from case law, at least going back to the early 1900's, if not before. The reason it was not significant on the books around the turn of this century is that most of our oil and gas wells were, I won't say depleted, but at least were producing it at moderate levels or on the down side of their production scale. And so the amounts were not significant, and more to the point, we didn't have clear technologies on how we would do that assessment.

However, in the last couple decades of 1900's, we developed some newer methodologies, very much akin to what we do for coal and other minerals, that we were beginning to apply to the oil and gas wells. And that resulted in higher values for those properties, but it was a fair value because it's based on potential income. And similarly -- and we think, in fact, that might be part of the reason that spurred the original litigation that led to the court decision.

At the time of the litigation, about half the counties had implemented these new technologies, and most of the remainder were in the process of doing so. And so while it is accurate to say the amount of revenue, the amount of assessed value for these properties were relatively nominal prior to the court decision, that's true; but moving forward, we are putting in place much better means to determine the values.

I should also mention, property assessment has a number of different components. The easiest methodology that everyone, at least the one that people understand the easiest is comparable sales. So if you have a residential property and it sells for this and most of the houses in your neighborhood sell for that, then that's a fair means of assessing the value for your property.

However, not every property fits easily into that categorization. So under Pennsylvania law, the other two methodologies that we use are replacement costs or what's called the income approach. And so if you look at oil and gas, you don't have comparable sales; you don't have a replacement value, but you do have an income approach. And the income approach is what's most typically used for commercial facilities, and it is what is used for all of the other mineral types of production.

In practice, the way the assessment is done is to develop a table of potential value of the resource, and then it's done actually as a depreciation table because we know value's going to decline over time as the resource is extracted. Typically, we do a five- to ten-year table, and then that's renewed every five to ten years after that. So there is a discrete value attached, but it does take into account the probable declining value of the property, or of the resource rather.

The industry has also suggested that just doing the evaluation is an expensive process. And it can be because, as I said, this isn't just a simple comparison of comparable sales, but rather it does involve some calculation. It does involve development of tables and all the rest, and so it can be a little bit more expensive. However, you've never given us the discretion before to say, well, this particular class of properties is hard or expensive to assess and so you don't have to do it.

Instead, we have to go out and hire the special assessors we might need. For example, most counties can do an assessment of residential real estate. Most counties can do assessment of open space. I don't know of many, if any counties that have someone on staff who can do a professional assessment of a power generation station, and so we hire someone in to do that.

We would be doing a similar thing for oil and gas assessment, and that's primarily -- most of that cost, like a full scale reassessment, most of that cost is the up-front cost the first time you do it. Maintenance of the value after that is much less expensive. The other concern that's been raised is that if we put in place this -- if we restore assessability, that we're going to drive the industry away.

And I think a fair comparison is to take a look at other industries we try to attract. If you're trying to attract an automobile manufacturing plant, well, yeah, certainly they're going to take a look at the tax incentives that are available and they're going to compare that in an open marketplace to the tax incentives available in North Carolina or Tennessee or whatever and they're going to make a decision on that basis.

The difference here is the gas is fixed to that property, and so ultimately if they want the resource, they aren't going to go to a neighboring state and throw a horizontal well clear into Pennsylvania to do that. This is -- it's fixed here, and so the industry will make access to that resource. It may be a little bit slower over time, but ultimately, the value of the resource is still there.

And, in fact, from everything we've seen, their interest in assessing a resource is much more based on what the market value is of the gas itself rather than the incidental costs, particularly like the costs that restoration of property tax assessability would add. We've also heard arguments by the industry that they pay taxes already, and, in fact, they even claim -- well, they claim the corporate taxes justifiably, but they're even claiming, well, our employees pay the local income tax.

Well, that may be true, but that's also true of any other industry in Pennsylvania. The difference is all those other industries also pay the property tax as well. In fact, there are a couple unique issues with this industry. I mentioned earlier the number of out-of-state employees that the industry relies upon. If the home state of those employees has a reciprocity agreement with Pennsylvania, then the local income tax goes to their home municipality. It's not paid locally.

So even that is less. And then one other point for that matter, because of the number of out-of-state employees -- and this is particularly an issue in the northern tier -- the companies have leased hotels, motels for a long term. And if you recall, under Pennsylvania law, neither the state nor the county receives a hotel tax if a stay is more than 30 days. It's no longer considered a transient rental, and so it's exempted from the hotel tax. So we're even losing revenue from that perspective, and as our tourism industry, we're also losing available beds to bring the tourists through with all the other economic opportunity that comes with them. I do want to turn just briefly to the separate issue of severance tax. I know that's been a matter of discussion of this committee, and you've moved the legislation already on that point.

I want to emphasize for the record that our association does not have a position on the severance tax per se, that is, whether it should be levied or not. The only position that we do have is that if it is levied, that there should be some share for county and municipal government as well as for other appropriate environmental purposes, including conservation districts, the Environmental Stewardship Fund and Growing Greener. With that, I think I will turn the microphones over to my colleagues to make a few remarks, and then we'll be pleased to take your questions.

MR. HERR: Thank you, Mr. Chairman, and Representative Rohrer.

My name is Elam Herr. I'm Assistant Executive Director for Township Supervisors Association. And you have a copy of my testimony in front of you, so I will paraphrase. And what I will say today will be even cut shorter because a lot of what Doug has already said, we go along with wholeheartedly.

Just so you know, my membership represents about 90 percent of the land mass in Pennsylvania, so the majority of wells are in my members' townships. So we are here to stipulate and state clearly that we are in support of House Bill 10. I will also say at this time, our position differs a little bit than Doug on the severance tax in that we do support a severance tax, but that is separate for another day, and I will not discuss that issue here today.

What I want to reinforce, again, following up with what Doug had said, is that we're looking at equity in restoring some fairness to the property tax system. Realize that we do not do assessments on property. That is the county's function. What we do is place our millage on that assessment that is levied, so we're not going to get into the actual comments about how minerals are assessed.

But we do feel that since coal and other minerals are presently being assessed for property tax purposes, that counties should have that ability to place those assessments on it and we should have the ability to levy millage on that figure. Again, it's a fairness issue. We have been taxing coal and other minerals for years. It's only been with the court case that Doug referenced back in 2002 that the taxing of gas and oil has been removed from our abilities.

Realize one of the other things that Doug did say, that -- actually two things that Doug did say was that if you take any entity out of the tax mix, somebody else is picking up the cost. Our municipalities, counties have some fixed costs that have to be paid on a monthly basis the same as everyone else. We have to raise the revenues. If one entity is removed, then the rest of the taxpayers in that municipality are going to pay higher taxes.

And, again, you get back to the fairness issue.

The other thing that Doug did bring out is that literally with this industry -- and, again, it goes beyond with the Marcellus Shale. But that's where we're seeing now the biggest effects on our municipalities, is that local, the governments are not seeing any taxes or revenues coming in from that employment. Doug mentioned some of the effects that we see. We have one municipality in the northern tier in one day had over 300 trucks carrying water to the site.

Our townships have taken the position that this is a viable activity. They support the gas drilling operations within the Commonwealth, but with that being said, they also say that their citizens should not have to foot the bill for this activity to take place. Think about this right now: We have been told that, from just the Marcellus Shale, that it's $10 to $20 billion over several years. The latest report says that it's approaching over $1 trillion that potentially will come out of the ground.

And if you think about it, recently Exxon, Mobile has gotten into the realm of participating. That is a company that would not have come into this activity if they did not see a viable end result or return on their investments. So with that being said, if there is that type of activity going on, citizens within the township, citizens within the boroughs and the counties should be able to receive some of the benefits from it.

Some of the problems need to be addressed, and, again, with Marcellus Shale, we're seeing the biggest problem. It's things that you see very easily, damage to roads that are out there and activity that has to be taken care of. Again, I will say today that the entities that are out there have been working with our members to repair the damage that they are doing, but it's still a major problem. And if this industry takes off as the economy improves, the potential damage will go even higher.

Water well contamination and environmental damage, again, this is something that our members are seeing and hearing from their constituents that they are concerned that with the potential for increase in drilling, that environmental problems will result. And, again, if you're living on a well, which a lot of rural Pennsylvania is, you do not want something to happen that's going to take away your water supply. Presently, laws say that the entity that destroys a well must supply you with potable water.

The problem is, how long do you want to go with water buffalos sitting in your driveway until a municipality will end up having to put in some type of water system? Treatment of waste water, that is an issue that has to be addressed because, again, if the waste water is not properly taken care of, there will be a potential problem of water getting back into the ground water, which results back into the drinking water supplies. And finally, one of the issues that you have to take into consideration -- and, again, Doug brought this up -- emergency management.

Although our volunteers out there on emergency management are not going to be called in to take care of well fires or anything like this -- and heaven help us, I hope we never have a well fire in Pennsylvania -- they will be responsible for doing other types of activities. Funding needs to be provided so they can take care of those responsibilities. There is a lot of other information within the testimony that I've given, that I've presented to you. You know, we'll be able to answer any questions you have.

All I would like to end up with is following up with what Doug said is that this is an equity issue. We feel that this industry, as well as the other mineral industries, should be paying their fair share so that the citizens of our communities are not burdened with the end result of this activity. And thank you.

CHAIRMAN LEVDANSKY: Thank you.

Mr. Troxell?

MR. TROXELL: Yes. Good afternoon, chairman Ledvansky, Chairman Rohrer, and members of the Committee. Thanks so much for having us up here to speak with you a little bit about House Bill 10 that we're looking at today. I'm Ed Troxell. I'm the Director of Government Affairs with the Boroughs Association. We represent over 950-plus borough communities throughout the Commonwealth.

I'm just going to skim over my testimony, even ad lib a bit from it because I want to thank my esteemed colleagues here who really covered a lot of the bases. And I'm sure questions are probably what the Committee has, so I'm going to work through it real quick and so we can get to some questions. Basically though what I'd like to put out there is that the Boroughs Association is in support of House Bill 10.

We do see it as an equity issue. We actually participated in the press conference, the media event with Representative DeWeese many months ago supporting the bill. However, also as Elam alluded to, we do support a severance tax in the Association. And what we would like to see is an ideal way to distribute revenues to communities that are impacted and those who are within the region. We understand that the assessment aspect that we're looking at in 10 deals more or less on a focus basis.

We're looking at something a little more regional that would manifest itself preferably to a severance tax. Also, some of the things that my folks have to deal with are the trucks that come through our communities, are the emergency services that our fire and our police have to respond to, a lot of the things that the townships have already spoken to you about.

But I guess what I'd really like to close with -- and I guess it will really probably raise some flags in the room, but I'm just going to have to share it with you, is I have a little borough who suffered at the hands of another energy king, when coal was king. And to this day, Centralia Borough is still facing the impacts of what took place at that time.

So what we want to do as an association is protect our communities, protect our residents, not leave a heritage behind that would damage them, but leave a heritage to them that would actually be a blessing to the folks that live within those communities and throughout the Commonwealth. Thank you.

CHAIRMAN LEVDANSKY: Thank you, Mr. Troxell.

Before I ask members for questions, I just want to note the presence of Representative John Pallone from Westmoreland and Armstrong Counties and Jim Cox from Berks County. Thanks for being here.

Before I turn to the members for questions, let me just make it clear the severance tax issue. I've been involved in that. I've had discussions with all of you and others in the room, and that is an issue that we'll deal with at another point in time. But I'd just appreciate it if we could keep our focus on House Bill 10.

And to that extent, Mr. Troxell, your first three paragraphs in your written presentation really do a really good job of summarizing the key issue of how the law was being implemented prior to the court case of 2002 and what the court case has meant relative to the application of the property tax system since then.

So, you know, I would appreciate it if members could, you know, if we could get back to House Bill 10, and the contents and questions should reflect that legislation, not the broader issue of the severance tax. If we did that, trust me, we would be here more than just this afternoon. We'd be here for a couple more days having a hearing on all those issues. So not that I don't think and recognize it's important, but I'd like to try to keep the focus to House Bill 10.

With that, any questions from the members?

Representative Ellis?

REPRESENTATIVE ELLIS: Thank you, Chairman Levdansky, and if I could just ask a real quick question of Mr. Herr. In your testimony -- obviously we are at what many people in Pennsylvania are very excited at the beginning of an industry. And I'm not going to ask about the severance tax, but it does play into this piece of legislation. But I just want you to clear up a few things for me. You suggested that the concerns were water well contamination and emergency management and the damage to roads and road bonding.

Obviously, those are all things that I believe the industry is mindful of. Can you give me specific townships where these instances were not -- either they did occur and weren't rectified and this assessment would have created a different scenario where these problems wouldn't have occurred?

MR. HERR: This legislation wouldn't have changed potential problems that would have happened, but it would have given municipalities some additional revenue to address some of the issues. We had a board meeting last week. A board member from Bradford County has said that -- it was either November or December of 2009 -- over 400 incidents happened within the county, Bradford, that ranged from traffic accidents to other types of incidents with potential drilling that are related to gas production.

REPRESENTATIVE ELLIS: Were any of those specifically water well contamination or environmental damage because I'm just trying to understand because I have not heard of this mass water well contamination or environmental damage? And I just wanted to be sure because we are experiencing some drilling and some permitting in Butler County, and, you know, certainly it's an important issue to me back west where we're just at the start. We're not at the Bradford levels, but eventually we hope to get somewhere into that level where the jobs are coming freely into Butler County as well.

MR. HERR: As far as water well contamination, I have not heard of any specific yet where they -- but the concern has been raised because of some leaks either during the drilling process or after with the waste water that has come out. There have been some environmental degradation. I can get you that information from our board member from Bradford County with a list.

REPRESENTATIVE ELLIS: I would appreciate that, and then just specifically too, have you seen an incidence where the roads were damaged and there was not adequate bonding to repair them and the industry didn't work with the local municipalities to make sure that they were doing the right thing?

MR. HERR: At the present time, the industry is very cooperative with our municipalities. The industry, at the present time, also would rather enter into agreements to try to correct any damage that's done. In the cases that we have heard, they have fulfilled those obligations. Our concern is, as this industry takes off, others will get into the operation and may not be as financially well off as the industry that's there today and we will need something to take care of the bonding.

Bonding, right now, if you have a dirt road, the max you can bond the road for is $6 thousand. If it's hard covered, which in most cases in our townships, it would be blacktop, you can get 12,500. A road that was done in Blair County, 2008, which the industry did supply the money for, was $126 thousand to redo the road. What we're saying is, you know, if a municipality even gets the bond without additional revenues that they're taking out of their general fund, they can't repair the roads to what their citizens are looking for.

MR. HILL: If I could respond briefly as well, from the county perspective, this is an issue that, while the roads are an issue for the counties, bridges are, this is an issue that we've discussed with the industry as well. Anecdotally, at least from my members, they said that the industry has been very cooperative with them, and to a degree, has been willing to step forward, put additional money in.

And my members tell me -- now, the industry might have a different perspective, but what my members tell me is, in their discussions with the industry, they've said, well, number one, we had anticipated some local taxation in our business models and we get here and we find there isn't any, so that --

REPRESENTATIVE ELLIS: Which specific companies asked you, said that they anticipated a tax in their business model?

MR. HILL: I would have to find out from --

REPRESENTATIVE ELLIS: If you could find that out for me, I'd greatly appreciate it.

MR. HILL: I'd be happy to do that, but the bottom line for our folks is that while that goodwill does exist and they have good working relationships now, if you get a company like Exxon -- and I'm not casting aspersions, but a larger company that might not have the same community interest or might not have the same business model, you really don't want to rely on an ad hoc system of some kind to prepare for the long term needs. REPRESENTATIVE ELLIS: Thank you very much, Mr. Chairman.

CHAIRMAN LEVDANSKY: Thank you.

Representative Peifer?

REPRESENTATIVE PEIFER: Thank you, Mr. Chairman.

Mr. Hill, I'm just trying to get my arms around House Bill 10 and the way the law was read before 2002. You would go and assess the property, a well head, and we don't have -- you know, we don't use comparable sales; we don't use replacement value. We actually use income approach, which tends me to believe it's similar to a severance tax, correct, because that's the income approach on a severance tax?

MR. HILL: No, it's not. It's not the same thing. The income approach is, as I mention in my testimony, the income approach is what we would typically use, what we now typically use in something like a commercial facility or an industrial facility where you don't have comparable sales, you don't have a replacement value. And so we use statistical information that's furnished by the company, information that's available from the lease and other sources.

We develop a depreciation table on what might be expected to be derived from the income on that well head and then develop the table which shows the assessed value. That -- and as I say, that is comparable to what we do with commercial properties.

If you have two strip malls, two strip shopping centers, and this one has higher-end retailers and this one has lower-end retailers, the assessed value is going to be higher over here because of the income that's derived compared to this one. And the notion is the same. When you have a resource that can be extracted and you have projections of what that extraction can be, then you can attach a value, an income value to that.

REPRESENTATIVE PEIFER: So determining an assessed value in your mind isn't that difficult basically. I mean, it is -- I mean, in my eyes, it seems very difficult to do what you're saying. I mean, you could argue, yes, we have name retail stores or we don't have name retail stores; I have a well that's producing or I have a well that's not producing. I mean, it just seems very difficult to determine that assessed value.

MR. HILL: Number one, it's not impossible to do. I, as I suggested in my testimony, most of the time, a county would be required to bring in an outside consultant to get the system set up and to attach the initial values. Once it's in place, it's something that we'd be able to do largely in-house; second -- this is probably the most important -- the methodology that we are using is the same methodology that's used in other states where they use, have assessed values for the oil and gas. Texas is one; West Virginia's another.

REPRESENTATIVE PEIFER: My second question then has to do with the way the millage is split then. Would the millage be split the way it is existing in that county now?

MR. HILL: I have to be very clear. This is not a separate tax. This is simply to add them to the assessment roll the same as the shopping center is, the same as the farm, the same as the residential property is. So there's not a separate millage. There's nothing else there, so --

REPRESENTATIVE PEIFER: So the county, the school and township or borough splits would be the same that's actually there existing now?

MR. HILL: They just get an assessment bill along with all the other properties with the millage attached based on assessed value.

REPRESENTATIVE PEIFER: With the same distribution of millage?

MR. HILL: Right, because we can't levy a different millage against the different class of property. They go onto a single assessment roll, and that's the millage that's levied against them.

REPRESENTATIVE PEIFER: What about the Commonwealth? Would the Commonwealth receive any of this money?

MR. HILL: No. The Commonwealth doesn't have a property tax.

REPRESENTATIVE PEIFER: Okay. Thank you.

Thank you, Mr. Chairman.

CHAIRMAN LEVDANSKY: Thank you.

Representative Cox?

REPRESENTATIVE COX: Thank you, Mr. Chairman.

Kind of in honor of the prime sponsor of this bill, I'd like to start off with, that which we call a rose by any other name would smell as sweet. I look at this, and I call this a severance tax. I know the Chairman said we're not talking about a severance tax, but everything I'm looking at here is saying this is a severance tax. And yet we're trying to say, we're trying to call it anything other than a severance tax just to avoid the political flurry that might follow.

I guess regardless of what we call it, I have a couple of questions that I'd really like to get a handle on, and that is the nature of what we're trying to tax here. I'm not an expert in these areas, but my understanding of it is that natural gas can flow pretty freely from one area to another depending on the geologic formations that surround it. So there's a fluid nature of it.

It may move from one parcel of land to another. It may move small distances or large distances depending on what it's up against. So that's one aspect of it, and the other aspect of it is just the fluid nature of the market. Gas may be worth, you know, a set amount one day and greatly increase or decrease the following day or the following weeks, and yet we're going to tax a solid -- you know, we're going to put a tax on here and say this is what is going to be taxed. How are we going to account for both the fluid nature of the gas itself and also the fluid nature of the market? How are we going to make sure that, if this were to go through, that we're taxing fairly?

MR. HILL: Sure. And, actually, I guess there's three different questions to respond to. The first is a tax by any other name. This is not a severance tax, but rather -- I mean, to call this a severance tax would be the same as calling an income-based approach valuation of a commercial property an income tax. It's not, but rather it's the property has an intended value because of what it's capable of producing.

So when we develop the depreciation tables, it's not based on the actual extractions, but rather based on the available resource and the value that that has if it were to be sold on the market, either sold by extraction or sold to another company that wants to be able to extract. So it is different than a severance tax very distinctly.

Second, if I can use Representative DeWeese's phrase, the term you're talking about, migration, is called fugacious. It can migrate from property to property. Pennsylvania though -- and the industry can give you a little more clarity on this when they testify, but

Pennsylvania's what's called an extraction state. And so the value is based on the piece of property from which you extract it rather than what it underlies.

Now, given that this is a little bit different from coal because it is, as you say, a little bit more movable, my understanding is the industry has been doing more diligence in securing leases on adjacent properties where the horizontal border might be so that they lessen -- and give additional value to those so they'd lessen the question of whose guess is it anyway.

But the bottom line is, the fact that the tax, the assessment goes against the holder of the mineral value means, from a property tax perspective, it doesn't matter whose property it underlies. It's the entity that has the right to the extraction, so fugacious really has no meaning in this particular point. And then last, the depreciation tables do take into account the availability of resource.

So if the resource has been extracted, there is less value to that property and then, hence, the assessed value goes down. That can be affected by the market, and when that depreciation table is recalculated -- as I mentioned, they're recalculated every five to ten years -- that's very similar to what would happen in a commercial property. If you had a commercial property where you had all high-end stores and then we have a economic bust and all those stores close, that property can apply for a reassessment and does because there is less value of the property because no income's being generated there.

MR. HERR: If I may, Representative Cox, to add kind of, what Doug's explaining to counties, it's great theoretically, and it took me a while to get my mind around the whole concept. And I tried to boil it down to more or less what we saw taking place was we're creating another parcel. Those leases basically are another parcel that's assessed, and it's treated similar to something like that.

So that's the way that, I guess, I helped understand that, okay, this is how you can tax something that's under the ground, something that's relatively stable. Also, the question out there about the fugacious nature, because that's the language that the Court kicked around in its decision in 2002, really when you look at the nature really though of the natural gas locked up in the shale, I would have to argue, is it truly fugacious?

I mean, because it is more or less stable, something similar to coal. Coal was always about being able to operate your coal, meaning being able to get to it to mine it and take advantage of it and use it as an energy source. Now, here we have the gas, which is actually locked up within the shale, and we notice we have to frac the shale in order to get to that gas so then it can take on its fugacious nature. So it's kind of transitory like that.

So that kind of, like, is the way I try to piece this together in the early portions of my testimony, is that we're basically -- and I had to share this with my membership -- that we're creating another parcel that needs to be assessed for its value, and as Doug explained, that it's depreciated according to its depletion, what the reserves have the potential to yield and the very technical nature of it. So I don't know if that helps, but it helped me, I found out, throughout the process.

REPRESENTATIVE COX: Okay. Just one quick follow-up, if I may, Mr. Chairman.

You had said the reassessment, the request for reassessment, five to ten years is kind of the automatic thing, or if there's an economic downturn, some of these commercial properties seek reassessment when the stores leave or whatever the case may be?

MR. HERR: Yeah, any property that ceases value -- you add on to your house or your house burns down, your assessed value's going to change up or down.

REPRESENTATIVE COX: Under this scenario, would these property holders be able to do the same thing? They're not going to be treated any differently?

MR. HERR: That's correct because, as I said, initially we do a depreciation table typically five years, sometimes ten. But if the market turns, then, yes, the same as any other property owner, they have rights of appeal under the law.

REPRESENTATIVE COX: Thank you.

Thank you, Mr. Chairman.

CHAIRMAN LEVDANSKY: Thank you.

Representative Seip?

REPRESENTATIVE SEIP: Thank you, Mr. Chairman.

Thank you all for your testimony today. Some of the remarks by Mr. Hill particularly captured my attention. We've had many prior discussions about the nuances associated with property tax assessments, and I guess we won't get into those today. But I'm always cognizant of the demands of human service delivery and the costs appreciated by the counties, and I certainly appreciate your comments because I hadn't thought about that.

There are more people, just a higher percentage of people seeking services from Children and Youth Services or drug and alcohol or some of those county human service systems that people typically don't consider. We're talking about drillers and businesses and business tax and those kinds of things, and we're really not always concentrating on those human service delivery costs. So I appreciate your comments, and I just wanted to highlight that for the record so that that doesn't get lost.

And certainly the emergency management piece, those folks are very, very taxed. I certainly appreciate the work that they do. They have to try and address all different kinds of possible scenarios, and I'm sure there's a big cost in situations like this to them as well. So I just wanted to say I appreciate your comments on that, and thank goodness they didn't get lost in all the other important discussion that's going on.

MR. HILL: Thank you, and if I could expand on that just a little bit. I mentioned in my testimony that a transient population isn't any better or worse than our resident population. But one of the things that we find in human sources particularly, is for our resident population, at least they have family and other local supports, and the transient population often does not. And that actually increases the cost of service delivery for the same types of services. Thank you. I appreciate that.

REPRESENTATIVE SEIP: Excellent point. Thank you.

Thank you, Mr. Chairman.

CHAIRMAN LEVDANSKY: Thank you, Representative Seip.

Representative Kessler?

REPRESENTATIVE KESSLER: Thank you.

I just want to make sure I understand House Bill 10. The township I live in, we have a quarry. And the trucks exit the quarry onto a township road, and it takes quite a beating. So we have to repair and pave that road a lot more often than a road that cars may be exiting onto from a development. The quarry is assessed based on commercial use and on a quarry, so it brings in ample enough money for us to be able to take care of that section of road.

Now, in this situation where you have a gas drill, you could have the same amount of trucks leaving that property, but that county, that local municipality is only collecting the assessed value on the person that owns the land, not based on its use. Is that --

MR. HILL: That's correct.

REPRESENTATIVE KESSLER: -- correct? So, therefore, you do need to bring in more revenues, just like with the quarry, as far as the wear and tear on the road in order to prepare that road for that type of traffic, where the money coming in on that land because it's leased doesn't come close to covering that.

MR. HILL: That's right.

REPRESENTATIVE KESSLER: Thank you.

MR. TROXELL: If I may add as well, Representative Kessler, is that the ironic part of this is that the improved roads, because of the nature of the industry, traveling and drilling and once they're done, they don't need to move heavy equipment into that area, a lot of times, our communities have, now have these wonderful improved roads that they didn't necessarily need at that point. They may have been fine with a gravel road whose drainage was fine, whose technology deployed was able to take care of the water and the runoff and things like that.

Now all of a sudden, a community may find itself with a system of improved roads having to deal with the infrastructure that services those improved roads. So you may have to put curbing in; you're going to have to channel that water and its runoff, what type of streams it may impact, things like that. You know, you wouldn't think of these, but as you start to peel this onion, there are some issues.

REPRESENTATIVE KESSLER: Absolutely, because the comparison of what I used as far as the quarry and versus that, the moneys are not coming in and you have the same amount of truck traffic; you have the same problems. Thank you.

CHAIRMAN LEVDANSKY: Representative Mirabito?

REPRESENTATIVE MIRABITO: Thank you.

A couple questions, do you have any numbers of the folks on probation?

MR. HILL: I don't have any, no.

REPRESENTATIVE MIRABITO: Are the counties collecting that information?

MR. HILL: I don't know if they are, but I could expect we could find out.

REPRESENTATIVE MIRABITO: I think that'd be helpful. The other thing is the hotel tax, the numbers of folks who are staying beyond the 30 days so that we're no longer collecting the hotel tax. Just by way of analogy, the folks who actually own the land, the farmer or the family that owns the land, they know they have gas under it and they don't do anything to develop it, they're not going to be subject to this, correct?

MR. HILL: That's correct.

REPRESENTATIVE MIRABITO: So it's really no different than if I own a piece of land and it's assessed low because it's vacant, but I decide to invest some money and put a million dollar building on it and now this million dollar building changes the assessment because I've changed the nature of the use of the land.

MR. HILL: That's correct.

REPRESENTATIVE MIRABITO: Here, instead of putting up a building, we're investing $500 thousand in drilling equipment and we're changing it. So it's really, in that sense, that's the equity that you're talking about?

MR. HILL: That's correct. Yes.

REPRESENTATIVE MIRABITO: Okay.

MR. HILL: Very well stated.

REPRESENTATIVE MIRABITO: I think that's all I have. Thanks.

MR. HERR: Thank you.

CHAIRMAN LEVDANSKY: Thank you, Representative. Representative Pallone?

REPRESENTATIVE PALLONE: Thank you, Mr. Chairman.

And I'm not exactly clear on what direction we were going, but I think -- I don't remember which one of you said it -- that the gas is fairly stable and not, whatever, fugacious. That's assuming that all the gas is Marcellus Shale. This House Bill 10 pertains to all gas, correct, not just Marcellus Shale? It includes coal methane and oil, which aren't stable. So I don't know if what you said is accurate. It isn't a stable mineral.

MR. HILL: It may be accurate for shale properties, but you're correct. This applies to any type of --

REPRESENTATIVE PALLONE: All four types of minerals.

MR. HILL: Right. But, again, returning to the original point, the assessment is against the individual or the company that has the equitable interest, regardless of the property that it underlies. It's based on extraction, and so the bill goes to that individual, not to the -- it has no effect on the surface owners, so it doesn't matter what properties it underlies or the fact that it's movable. They have --

REPRESENTATIVE PALLONE: Well, I think Representative Kessler clarified it for me. This is a, kind of a value added kind of situation -- or Mirabito -- I'm sorry -- where you tax the real estate and then the improvement. This is considered another improvement on the property.

MR. HILL: That's correct.

REPRESENTATIVE PALLONE: The issue though -- and I got a couple of questions going down that road, but what we're talking about is gas, oil and coal methane which are being extracted by private companies. We also have at least two or more private water companies in Pennsylvania that are drilling water wells all over Pennsylvania to provide water utilities throughout the Commonwealth.

Many water plants are, or water systems are municipal authorities and owned by the community and whatever, but many are also private. Does House Bill 10 pertain to the extraction of what I'm going to call very generically the water mineral relative to private developers and private water companies, not just private gas, oil and coal methane extractors?

MR. HILL: Well, the House Bill 10, the only change in language relates to coal, oil -- I'm sorry -- to oil, gas and coal methane, and so there is no effect on water. Now, water to the extent it would be taxable, it would be taxable as it always has been. And for the purposes particularly as a public utility, that's not an issue.

I candidly don't know the answer if -- for example, in the eastern part of the state, we have a couple that make major extractions for the purpose of dye works or major extractions for the purpose of resale of the water, bottled water. And I'll be candid with you, I don't know how that applies, but I can find out for you.

REPRESENTATIVE PALLONE: And I wonder if we have maybe a constitutional issue, that we're treating one group of private companies that extract the mineral differently than a different group of companies that extract another type of a mineral, which is the H20.

MR. HILL: Well, the H20, I think, is a different matter because it's been treated as a utility. In this case, if you want to turn that constitutional argument a different way, we are now taxing coal and limestone and others, and we're not taxing oil and gas.

REPRESENTATIVE PALLONE: I'm just curious as to the balance on that. That's all.

MR. HERR: Yeah. And if I could, I appreciate the remark about the smaller facilities. And that's something that I had in my written testimony, but didn't mention in the oral testimony. We do recognize, and particularly in the western part of the state, there are many of the older wells, you know, the smaller vertical wells and others that are commonly called stripper wells that really do operate on the margin.

And we understand that issue. Other states, I know Texas notably and I think some others, do provide some differentiation, if you will, between types of wells so that the ones that operate on a marginal basis aren't affected or aren't affected as greatly by the assessability.

REPRESENTATIVE PALLONE: And do you know whether or not this is going to cause, again, an additional mandated reaction by the county's assessment offices to go back out throughout the county and reassess a number of properties that have existing wells that already have been there for a decade or more and may be producing a little bit or a lot, but at least enough to provide that particular homeowner or small business with the allocated

CF's (ph) that they get because of their local lease or whatever?

Is that going to create another level or burden? Because it's easy to say, well, this is the new well. They're going to come in and -- but how about all these old ones? And I can tell you, my counties, Westmoreland and Armstrong, we got, not dozens, hundreds of them.

MR. HERR: I see. I know that.

REPRESENTATIVE PALLONE: And I'm looking at both of my counties that are financially strapped like everywhere else. Is that going to cause another problem for them to go out searching for these well heads?

MR. HERR: Well, again, as we say in the testimony, we concede that point for the industry on those older wells and those more marginal facilities. And we'd welcome the opportunity to find a way to minimize the impact on them. For any county that adds or adjusts the values for these properties on their assessment rolls, constitutionally, they will be obliged, if they look at one, they have to look at all before they can put it in place for any of them.

So if the county is satisfied with how all its wells are treated, then it doesn't have to do another thing, if they believe they're in comportment with the law. But if they decide we're going to have to go -- you know, we have a lot of new wells that aren't assessed and we need to assess them, so we're going to have to look at the value of the older wells.

REPRESENTATIVE PALLONE: And lastly, I can see that there's a marginal value, if nothing else, because in the southern tier of Armstrong County that I represent, there were a number of surface gas wells drilled in the last four or five years. And those townships and boroughs really took a beating on the roads, and it cost them money that they didn't otherwise have.

But then when you start balancing that out, you know, I wonder if the owners of those properties would have been so appreciative if we ended up putting an additional assessment on their land because of the wells that they drilled. So we're going to have a serious balance there that we have to deal with.

The last issue or the last question I have is the test, if you will, or the taxing on the roads. What we did learn or what we do know is that beating of the road only occurs during that period of drilling, and then it doesn't happen anymore.

But yet, I don't see that as a limitation on the additional assessment to say, okay, we're going to assess you one way during the time you're abusing our roads, but then when you quit abusing our roads, we're still going to assess you. So I think I have an issue with that as well. I don't know that that's equitable maybe to the company, although I'm sure the township or the borough or the city would enjoy that very well.

MR. HERR: And that's a fair point. And, again, returning to the testimony, a property tax is not a fee for service. We've raised these examples just to show that there are community impacts from any kind of, anyone who's a member of the community, but a property tax is based on value of property rather than services derived. And so, for example, Wal-Mart might move into a township, and they're added to the assessment roll.

And that's irrespective of whether Wal-Mart has required the two-lane road to become six lanes now or stay as it is or whether, whatever other impacts it might be. We value them and we're happy to have them as a part of the community, but they pay a fair share based on an assessed value of the real estate, not based on the specific services that they might derive from the community.

REPRESENTATIVE PALLONE: And I certainly understand that, and I appreciate that because I know that in my legislative district, a number of the communities have done analyses and came back and said that for every residential dollar that they collected cost them $1.40; for every commercial property dollar that they collect only cost them .60. They would naturally rather have a community full of commercial buildings than houses.

I guess we're getting to a point now where we'd rather have a community full of gas wells and oil wells and methane coal wells than businesses because that tax dollar might only cost them .20 because there's no people to protect; there's no streetlight needed; there's no fire hydrants; there's no water and sewer and all that that goes with it. So I understand that. And I fully appreciate it, and most communities will.

But I was just concerned though that when we're looking at it and we look at the infrastructure impact, while it's an improvement to the land arguably, it doesn't create a permanent tax on the services that the community generally provides as a commercial or a residential community would.

MR. TROXELL: That's why, I guess, as Elam shared earlier, why there needs to be some look at how we do posting and bonding currently because it's just not keeping up with the impacts that are taking place. And it's that temporary time when the exploration, when the wells are coming, heavy equipment is coming in. It's just that temporary time, and then after that, you know, we don't have the --

REPRESENTATIVE PALLONE: And then my last point, and it doesn't require an answer. It's just a comment that, you know, I think it goes off what Representative Seip said with the inconsistency with property tax assessments throughout the Commonwealth.

When I look at my two counties that I represent, you know, one has a 1998 assessment value; the other has a 1968 assessment value. I think that creates an issue that maybe exacerbates what we're trying to do or what you might be trying to accomplish with this. And I thank you for your testimony today.

Thank you, Mr. Chairman.

MR. HILL: We look forward to working with the Committee on the assessment issue in a separate context. Thank you.

CHAIRMAN LEVDANSKY: Chairman Rohrer?

REPRESENTATIVE ROHRER: Thank you, Chairman Levdansky.

I appreciate the testimony. I got just a couple of questions. I think a lot of these things have been covered quite well. I was thinking more along the lines of the public policy aspect, and I think Representative Pallone actually picked up on several things I'm thinking about here. One is this: The consistency of the application by bringing in the oil and gas to what is already existing under coal. Now, are they, in your minds, the application here, the same? Is the assessment the same? Is the valuation the same? I mean, is all of that the same as you look at these two components in your mind?

MR. HERR: If House Bill 10 were law, yes. There's a value to the resource. There's a value upon extraction.

REPRESENTATIVE ROHRER: Both assessed the same way?

MR. HERR: And the methodology's comparable, yes.

REPRESENTATIVE ROHRER: Okay. All right. That would be 1. Number 2, in the testimony at the beginning -- well, I'll just follow up on that one other thing. If -- and I had thought about the water as an example. If something else were to be found -- for instance, a lease may be put in place for gas. Okay. And you may know that there's a value of a certain amount of gas in the ground.

A few years from now, they may find oil. Okay. What happens then? Is it automatically reassessed? Is it changed at that point, or how is that treated? Or suppose something else comes up down the road, could be like water or something new that it has not yet been discovered, and all of a sudden, it has value. What's the mechanism, and is this thing being done in such a way that everything would be treated equally known or unknown, or are we talking about specifically treating things as we'd know it once something is determined to have value?

MR. HERR: The notion with mineral extraction is that there's an intent for that mineral to be extracted before it has a value. So most of you, given the state we live in, may probably have minerals under your property, but we're not going to assess you for that because you're not going to dig a big hole and pull it out.

And so to answer the specific notion, if you're going down for natural gas and you find liquid oil and that's not what you're there to extract unless you change your intent to extract that, which obviously means bringing in different kinds of equipment and whole different processes, then, no, that wouldn't immediately add to your assessed value. At the point at which you turn your operation toward extraction of the oil, then it would.

REPRESENTATIVE ROHRER: So it's a whole different set of permits?

MR. HERR: That's correct. It's a different set of permits.

REPRESENTATIVE ROHRER: So an action for allowing the recovery at that point would be a trigger at that point? All right. Another question if I could just follow up. In the testimony, a lot of what you talked about was tied to local impact, correctional, whatever. So to some extent, the -- I mean, not that this becomes an impact fee, but in some respects, some of what was being discussed almost sounds a little bit like an impact fee type of a circumstance. Now, you mentioned that the industry has been working very, very well to make sure that impacts are, in fact, taken care of.

In your mind, is this -- are you really going after the inability to address impacts, and if the industry addresses the impacts, is the need therefore now met; or are we really, in truth, looking for more revenue because others, perhaps, have gone down or whatever?

And I think, to me, it's a little bit -- I'd just like to hear a further exploration of that because I think, you know, obviously everybody's becoming very creative on wanting to tap into what appears to be some potential new revenue.

And if everybody is successful in tapping into it, there won't be any revenue left. So within that balance of knowing impact and what's logical, what is the primary, what's the primary goal here in this, recovery of impacts and costs or a desire for some, the future revenue?

MR. HERR: Sure. The primary issue is equity and its equity of the property tax system. We believe we had that equity relative to these minerals prior to the court decision. We believe we lost it with the court decision. To give you two points in support of that argument; first, we've been seeking this legislation since before widespread knowledge of the Marcellus play, and it was simply restore the law the way it had been and it would have effected primarily the existing wells and the ones that were being developed under the old regimen.

Second, we actually have included in the legislation an anti-windfall provision, so that if in the year a county implements the new assessed value system, a new system of assessing oil and gas wells, if the revenue increases and property tax revenue's projected to increase in the following year, then every taxing jurisdiction has to reduce its millage rate to what it was in the prior year and then treat any other millage increase as a separate vote. It's very much akin to what happens in the year following a full-scale reassessment. So, again, I think it addresses the issue of are we in this for revenue or not.

MR. HILL: Mr. Chairman, the way I kind of understood your question was, to me, is more or less this assessment language being put out there to deal with impacts. And I guess what I did in my mind is just return back to what exactly is an assessment. An assessment is when we place a valuation on a piece of property or a parcel because of what that property can deliver, what type of impact that that piece, or parcel of property actually has on the economic nature of its community and other things like that. So when you can more or less say, yes, the assessment is to deal with the impact, but aren't all assessments dealing with impacts of some type?

MR. HERR: Another point to add in that respect is that while the companies by and large are very cooperative now, that's no guarantee for the future, number one; number two, I don't think any of us wants an ad hoc system of local taxation where we barter property-by-property-by-property-by-class of property for this is what your fair share should be; this is what your fair share should be.

And so valuing it using accepted market value approaches and adding it to the assessment roll and then the taxes apply blindly and uniformly on a millage basis against all of them, we think makes the most equitable sense. I think one other point to raise too is that we're also mindful of the future.

You know, it's one thing to fix the road right now because that's where the direct immediate impact has been, but even looking out in the longest term, we see historically, if you look at a picture of Warren County from around 1900, 1910, you see your denuded hillsides where we first came through and took all the hardwood and then we put up all the oil wells and then that was gone and then saw a period of many decades of decline across the whole northern tier.

I think we also need to have some ability to generate revenue now to invest in our infrastructure, to invest in -- and not just our hardscape infrastructure, but also in community and economic development; so that once these industries face their inevitable decline, that we still have vibrant communities going forward.

REPRESENTATIVE ROHRER: All right. Thanks so much. I appreciate it.

CHAIRMAN LEVDANSKY: Thank you.

We've also been joined by Representative Dan Frankel from Allegheny County.

I just got a couple of quick questions -- I hope quick because I'd like to get back to the agenda. We're significantly behind schedule. Just for, I think for Mr. Hill, has any comprehensive assessment been done relative to -- you know, prior to 2002, obviously counties were legally entitled to include the value of oil and gas and coal bed methane in the assessed valuation.

Do you have any aggregate data or even county-by-county data as to what the total assessment of the mineral rights minus coal or prior to 2002 and any estimates on what it could be if House Bill 10 were law?

MR. HILL: We don't, no. And the reason for that is -- well, yes and no. We can do comparative data based on the wells that are in place in the period immediately prior to the decision --

CHAIRMAN LEVDANSKY: Prior to 2002?

MR. HILL: -- based on the changes in methodology. Going forward, we can't because you need a certain amount of statistical data on the leases and on the value of the lease and on the available mineral resource and so on to be able to do the calculations, and we don't have that. And absent the law, we have no means to get that data.

CHAIRMAN LEVDANSKY: Okay. So based on the income capitalization approach, you can put together, on a county-by-county basis, the assessed value prior to 2002?

MR. HILL: Right.

CHAIRMAN LEVDANSKY: And I'd appreciate it if you could provide me with that as a follow-up. Okay? Secondly, based on that evaluation then prior to 2002, if us could even indicate the amount of property tax revenue generated for both county, school district and municipalities based on that assessment prior to 2002.

MR. HILL: That latter point might be a little bit tougher because I have to go back and apply millage rates to every jurisdiction against those values, but we can get you to an order -- it would still be valid to do a percentage comparison.

CHAIRMAN LEVDANSKY: Okay. Thank you. And one final thing, I think for either or both Elam and Ed. I'm going to deviate just a little bit from House Bill 10, I mean, because you mention in your testimony the whole thing about wage tax collection. You know, the increased drilling in Pennsylvania has resulted in a lot of new workers coming from out of state.

I mean, to be honest with you, these are very -- a lot of these positions are really technology specific skill to the drilling industry, and the people who have historically done that are from Texas, Oklahoma, Louisiana, Arkansas, places like that. Do you -- you pointed out the issue of collection of wage taxes.

Do we have to have reciprocal agreements in place between Pennsylvania and these other states in order for our municipalities to collect the wage tax, or can the local governments levy and collect the wage, local wage tax independent of anything else?

MR. HERR: I'll go first. I just actually looked this up yesterday due to some comments that were being made. Act 511 is fairly specific with in-state workers and out-of-state workers, and without the reciprocal agreement that would be up there, municipalities would lose the ability to tax nonresident workers. If you're a resident worker, or resident of Pennsylvania and you go out of state and work, it's very specific about giving credit to that person.

If you're from out of state and come in without a reciprocal agreement, you may levy the tax, but the possibility and probability of getting that tax from them, you wouldn't receive because it will go back to their home state. And I had the citation. I forget what it is off the top of my head right now, but I can get that to you out of 511.

CHAIRMAN LEVDANSKY: Okay. Mr. Troxell?

MR. TROXELL: Yeah, I did see -- it's funny you brought that up because I did read yesterday over the wires -- it came from, like, the Observer Reporter, I think, that's out in Washington County, or out in western PA, and there was a tax collector there who was saying that you could collect a nonresident.

There's a few -- I mean, it was an editorial into the paper there speaking about the ability to levy that, levy a wage tax or an earned income tax because it all goes back to, you know, what we did a few months ago, weeks ago, years ago, but basically that you may be able to levy provided you had a nonresident.

So if there is some cloudy area there, we have our staff looking actually at the language in 511 at this point to where, you know, a nonresident would stand in something like that. So that's something we need to get settled because, you know, we're very interested in that when it comes to basically, you know, those revenues that could be --

CHAIRMAN LEVDANSKY: Yeah, because in a lot of cases, I think, the workers that come from out of state are here for well over the majority portion of the days in a year, and chances are, I mean, I think this industry is going to continue to grow and boom in Pennsylvania. So I think we're going to have to take a look at that issue.

MR. TROXELL: And it also points to something that we're going to have to give to our folks in the tax collection committees. You know, we did Act 32 and the earned income tax collection like that. That's something that we're going to be talking to our municipalities when we're putting these RFPs together for those collectors; you better look into that aspect of 511 to see whether they can collect that.

CHAIRMAN LEVDANSKY: But the problem there is the residents could be a lot of motels and hotels.

MR. HERR: Yeah, because they're still listed as living in Texas, so they're not full-time residents in Pennsylvania.

MR. HILL: Right. The real answer would be to reinvest in our workforce development programs so that we bring the jobs here too.

CHAIRMAN LEVDANSKY: Yeah, long term, that's obviously -- okay. Gentlemen, thank you very much for your testimony and for your tolerance in answering a lot of questions.

MR. HILL: Our pleasure. Thank you.

CHAIRMAN LEVDANSKY: Next, I'd like to call Mr. Lou D'Amico. Mr. D'Amico is the Executive Director of the Independent Oil and Gas Association of Pennsylvania, otherwise known as IOGA. Also, before Mr. D'Amico gets started, we've been joined by Representative Dave Reed from Indiana and Armstrong Counties.

Mr. D'Amico?

MR. D'AMICO: Good afternoon, Chairman Levdansky, Chairman Rohrer, committee members, and Representative DeWeese -- I don't know if he's still here or not -- also to you. Rather than go through the testimony and read it verbatim since we've already been here for quite some time, I'm going to kind of summarize as I go through with some of these things and give you an opportunity to question some of the things that we've heard already, and I'd be more than happy to deal with those.

First of all, let me tell you, I hate to take blame for anything, but I guess I individually am the reason why we're today. I was the one who encouraged our organization to file the suit back, I guess it was 1998 when we started the process that led to the Supreme Court decision in 2002. Obviously, you know, both IOGA and the Pennsylvania Oil and Gas Association, who I'm also representing here today, are opposed to House Bill 10.

And we went through great effort to have this overturned, and the primary reason for it was the very methodology that was discussed and how we approach assessment of oil and gas properties. When the Supreme Court ruled the overwhelming majority -- you know, it was a unanimous decision, and they all concurred that the language in the tax authorization did not include natural gas and oil.

Two of the justices, Justice Saylor and Justice Nigro, actually went a step further and said that, indeed, the very nature of natural gas makes it inappropriate to tax as real estate because it doesn't have the same qualities as real estate, and what he's referring to is the fugacious nature -- I almost hate that word, but the ability of it to flow across boundaries.

The problem with fugacious nature is not only in where the gas is actually coming out of. From an assessment status, that makes no difference. It's actually assessed at the well which it would come out. But where it makes a difference is as additional oils are drilled, we have a dramatic change, a potential for dramatic change in the flow rates within a reservoir. I'm not a tax expert. I can't sit here and tell you the ins and outs of how a severance tax might work, how a wage tax might work or some of these other things.

I am a petroleum engineer, and I do know how natural gas flows and the problems with assessing values to natural gas. That was the key issue here, that as we change -- and the industry has changed so much. We've gone from an era where natural gas prices were extremely stable in the early part of my career, to a time now where from day to day, we're not sure where natural gas prices are going to be headed.

In the early days of the development of this Marcellus play when it first started drilling wells, we started doing some county outreaches to explain to people what this all meant. And I was very excited to tell them, you know, we're getting $13.70 in mcf of gas, and even I fell for the dream that this was going to be the do-all and save-all for Pennsylvania with huge numbers because people were just going to be dying to get that kind of revenue back.

Well, today, I haven't seen this morning's numbers, but our numbers are down about $5.40 and falling here in the middle of winter. I think we're going to see, as the year progresses, the prices are going to continue downward, not upward. And this is happening on a year-to-year basis. The idea that you're going to be able to set a schedule that's going to last five or ten years what the property value's going to be is, for this industry is ludicrous.

It's not like a house where, you know, the house is either doing one or two things; it's going to stay the same, or it's, in most cases, going to appreciate. Our value's going to be all over the place, and we're going to have to come back every year to seek modifications of the assessment on this value. This is not a cheap process.

What led us in the case of Fayette County originally was that the cost to assess the properties in Fayette County was actually going to exceed the amount of money that Fayette County was going to get back from our gas prices at that time, and it did just not make economic sense for the county. It did not make economic sense for us to go through all these consistently bringing more and more information to fight every year over what this assessment might be.

You know, I think that these are key issues. I think if we go back to the Supreme Court -- if House Bill

10 passed tomorrow, was concurred in the Senate and we would go back to the Supreme Court again on the same issue, I think we would win the case because I think the difference, the flow of natural gas and the fact that it will change the value so much, I think we would win.

The roads issue is certainly where we're going to have the greatest impact. It's already where we're having the greatest impact. We are stepping to the plate as an industry and repairing those roads. Not only are we repairing those roads, in most cases, we're actually approving the standards of the roads because, for our own purposes, we cannot go back to a two-lane goat path, which is some of the areas we're operating in is basically what we have. These roads were designed to no more than handle a school bus once a day during the school year and an occasional milk truck.

They were not meant to handle the kind of truck traffic we bring out to it. So it's like -- it's the pottery barn rule for us; we break it, we fix it, and it's as simple as that. Are there cases out there where somebody has not in the past done that? I'm sure there are. And there are legal abilities for the townships or counties to address that and get their funding back.

I think on some of the other issues that were raised, I kind of scratched my head. I think one of the points were made about Child and Youth Services and the impact all these transient workers were bringing in. I guess I'd have to actually see some numbers to get that because most of the people I see coming in on a drilling rig aren't bringing their wives, families and girlfriends with them. They're bringing their pick-up truck and a suitcase and living out of the motel.

Up until today, I was kind of shocked. I didn't realize that there was a law that said that if you were in a hotel room for more than 30 days, you were no longer subject to that tax. That's certainly not our fault, and I would actually encourage the General Assembly to fix that in the case because I think that is going to be an issue.

I do take some exception, Representative Levdansky, about all these guys who are coming in from the southwest because as a native here, I've worked all my career in Pennsylvania. We have the third most active drilling state in the country for about the last seven or eight years. We have a lot of people already employed in this industry who didn't come from Texas and Oklahoma, and we're very proud of that.

And we are also very eager to see the percentage increased dramatically. Many of the companies that are coming in have actually built into their contracts that any contractor that they bring in from out of the state is required, after a period of six to nine months, to have a significant presence of Pennsylvania employees on their staff, which I certainly strongly encourage. Again, as a native, I'm not interested in creating jobs for Texans. I'm interested in creating jobs here.

Some of the other costs -- excuse me. I was kind of shocked to hear Mr. Troxell's comment about improving the roads, that that was a problem. I actually thought we were supplying a benefit by improving, and I think that is the case in most cases. And I think the damages that are done for the most part will be those damages that will be done on township roads.

There will be some traffic in boroughs and cities, and that will have to be recognized and dealt with and repaired. As far as whether we can expect the same kind of people to be operating in this industry in the future, I think it's very clear that that is the case. I'm not concerned about seeing a fly-by-night outfit coming in here to try to operate at the cost of drilling the horizontal Marcellus Shale well.

This is not for the weak-hearted or faint-hearted. These are folks that have serious investment and serious taste for risk to undertake these efforts. You know, I think even some of the people who I have traditionally represented in our industry are not going to be able to pursue Marcellus Shale for that very reason, so I think the funding issue where these things are is not necessarily a legitimate issue. You know, again -- and I think it was Representative Pallone raised the issue about the timing of how long this activity is going to be.

During the drilling phase is when all the truck traffic's going to be. It's going to be when all the personnel are going to be swarming into an area, and that is a short-term issue. After that point, then the people who are left are going to be the people who are actually doing the production, who are involved as welltenders and are permanent employees of that area.

Representative Reed has already left, but Representative Pallone, if you have Armstrong and Westmoreland, you're familiar with that right now. You have those people in your counties, as Representative Reed does, and there are some in Representative Ellis's district also.

So I think the long run, the impact on the state is going to be minimal for what we are not paying for flat out. And I guess at this point, probably rather than sitting here and talking any longer, it would behoove me to turn it over to you all and let you ask the questions and let me address them as best I can.

CHAIRMAN LEVDANSKY: Thank you, Mr. D'Amico.

Any questions from members?

Representative Mirabito?

REPRESENTATIVE MIRABITO: Thank you.

You made the statement that real estate will stay the same or appreciate as an example of the difficulty of trying to reassess, but if we've learned anything in this recession, real estate has crashed; commercial real estate, rental real estate. You know, values for rents have gone down and a question of whether landlords go back and get reassessments, so I kind of think that that's not a fair argument for saying that it's difficult.

MR. D'AMICO: Well, let me address that if I can. I think that you're absolutely right. I mean, particularly, not necessarily in Pennsylvania because I think fortunately, we have not been hammered quite as bad in the real estate market as some of the other areas of the country; but the reality is, those are unusual events and unusual occurrences compared to virtually monthly changes and weekly changes and daily changes in price and value of natural gas and oil.

We're affected by so many things beyond our control. We're affected by industrial demand. In the midst of a recession, you know, obviously there's not as much industrial demand, which is a big part of what makes the natural gas industry work. We're also affected as oil prices rise and fall because natural gas is, in many cases, used as a replacement for fuel oil. Political instability in other parts of the world has affected us because of the oil prices.

Every time that Accuweather says there might be a hurricane blowing into the Gulf of Mexico, our pricing goes crazy here in Pennsylvania because of the off-shore platforms and all the productions within 20, 30 miles of the Gulf in the southwest. So these things happen to us on almost a daily basis. It's not something that's really an ongoing everyday event for other real estate.

REPRESENTATIVE MIRABITO: You know, one of the issues that resonates with me is the question of equity, and you mentioned that in the most active drilling phase -- I'm sorry -- in the drilling phase is when you have the trucks and so forth, and then after that, you said you'll have people involved in production.

And I guess the question I would ask is part of -- or the sole purpose of this is what the gentleman before you testified about was the concept of community, that taxes support communities. So whether you work in the production phase or you work in the drilling phase, you're a member of a community. And I guess I just don't know how to explain to the mom and pop person who has a barber shop who's paying an assessed value on their barber shop that's higher than their neighbor's building because they generate income that they're subject to this assessment, but a very large entity that drills gas or oil is not. And I guess I'd like you to try to, if you could, just address the idea of community.

MR. D'AMICO: Well, I think the idea of community is certainly -- again, as I indicated earlier, I'm a native here and certainly feel the impacts of that. I also live in a natural gas producing area. I live in Crawford County surrounded by gas wells, which is how I got there in the first place. As far as what the support of community is, every nickel that we are spending in those communities actually goes back to that barber shop or the restaurant or the bar or the grocery store or the local Ford dealer who we're buying trucks of off.

So, you know, there is a large financial investment going into that community that there is benefit to. In the long run as the producing phase of these wells go in, then those are actually the people who are living members of that community. They actually live there; they own property there; their children go to school there. That's the only difference of what I'm referring to.

REPRESENTATIVE MIRABITO: I mean, for example, I have a business, right? I collect rents; I reinvest money in the community. I hire people to put a roof on; I hire people to put a boiler in, but I'm still subject, my real estate is still subject to the tax. And I guess what I just don't understand of how to explain to people is you take a group of people and make them subject to it, but then you carve out one group. And I understand the argument you made in the beginning about the fugacious nature of it, and I think that that's something to be looked at.

MR. D'AMICO: And that's really the key issue to me that I raised with the Supreme Court originally, is that by the very nature of natural gas, it's not real estate; whereas, coal has a discreet property on a farm or a parcel of land that is x-feet thick, so many acre foot, so many tons return from that. You can get a pretty accurate estimate, not only to how much is there, but where it's actually coming from.

It's not going to decline. That coal's not going to move over to the next property and be extracted there. It's actually going to come from that property. And that is the difference with the natural gas. The other issue too is, I think part of the temptation, I would say -- and I think somebody mentioned it earlier, the temptation from everybody to want a piece of the action with this Marcellus Shale that's being developed is we're not the only ones who are impacted on this, the industry.

When there is a severance, we're getting, at most, seven-eighths of that gas. One-eighth still remains with the mineral owner who, in most cases, is also the surface owner. So you're also impacting that individual over and above what they're already paying in their real estate taxes.

In the case of the Marcellus Shale where these royalties are considerably higher than the normal one-eighth that you find in the shallow zones, that impact is going to be pretty hefty on these folks, and it's going to be something that's going to be broad based across the state.

We're not talking about one small discreet area where there's coal. The natural gas with the Marcellus Shale, we're looking at something that's going to be from Greene County all the way to Wayne County, and those property owners are going to be impacted by that.

REPRESENTATIVE MIRABITO: Last question for you, on your tax returns at the federal level, are you able to depreciate the value of the natural gas against the income earned?

MR. D'AMICO: I'm going to have to tell you, as they said earlier, I'm not sure what tax advantages there are. I do know there are deductions for depreciation and depletion for corporations here in Pennsylvania on

Pennsylvania taxes. I do know that partnerships do not have those benefits. The partnerships do not get any deduction on that in Pennsylvania.

REPRESENTATIVE MIRABITO: I guess what I'm suggesting is the fact that these things are subject to federal depreciation on the federal level suggests that there isn't a way to assess the value to them and that it makes it legitimate for assessing the value in HB 10.

MR. D'AMICO: Well, I would also say that, again, we as an industry, for our own purposes, are required to -- for public companies, we're doing this every year. We're re-evaluating the reserves, and sometimes that stings pretty heavy for companies when they find that their stock prices are declining dramatically because they've taken a write-down in their reserves.

CHAIRMAN LEVDANSKY: Thank you, Representative Mirabito.

Chairman Rohrer?

REPRESENTATIVE ROHRER: I got a question here just following up on this. The question that was asked there ties into it. In trying to determine value, we do -- it seems that it flips really close to income or value of that kind of a thing as measured, and even federal deduction would be tied into it and income, where you're tieing it to the value that's coming out of the ground at the point that it is rather than an assessed type of a value.

But that being said, is there -- I mean, you can see what the testimony was and what the desire here on the parts of those who've testified. Is there a model that exists somewhere else in the country, or is there anything that the industry would say is better than a consideration of this as real estate that is a better way to go, or is there really no real way to go?

MR. D'AMICO: I'm going to struggle a little bit with that, but let me think about that for a second. I think, first of all, every state in the union that has oil and gas reserves do something different. Some have no corporate tax; some have severance taxes; some have real estate, some don't. It's all over the place. And one of the toughest things that we've tried to do is, over the years, compare the various states and what the level of tax burden is.

A model, from my standpoint, the model that needs to be taken in any case of assessing is some sort of a profit or income tax type structure. I think one of the fallacies of this approach is you have the difficulty in doing assessed value, but we know how much comes out of the property in any given year.

The difference between that and a severance tax, which is also, you know, one of the things we're hearing proposed all over the state, is a severance tax. The money is not income based. The state takes its chunk before there's any profit to be made. You know, and I know that's not the direction we want to be talking about today, but for a quick example, at $7.50 -- I ran some numbers here a year ago when those prices were common -- that last year's proposal of a severance tax amounted to a 33 percent net income tax over and above what shallow producers were already paying.

I've never done that calculation for the Marcellus, but I think an income approach is probably a fairer approach rather than doing that. But I think the question in my mind that needs to be addressed is what money is needed where and how it gets there and in addition to how it's calculated and the need and the impact it's going to have on the industry.

One of the things we're hoping is to attract the jobs that I've talked about earlier, and to do that, we have to have a viable industry here in Pennsylvania. The Marcellus Shale has a huge promise we think, but the reality is we have very few wells on production. There's some question about what their decline rates are going to be.

A lot of people made huge investments in leases, in drilling. There are folks out there every day making huge investments in pipeline infrastructure. At one point is this industry actually going to make a profit? I have my questions on that. I have predicted it's going to be three to five years before Marcellus producers actually turn a real profit in Pennsylvania. That's a roundabout -- I'm not sure if I answered your question.

REPRESENTATIVE ROHRER: No, that answered my question quite well, and I think the point that you're saying is that something that's tied to value as determined at the point it's taken out of the ground is more realistic than a value that's assessed at any one point in time, particularly with all the viability that's there. That's basically what you're saying?

MR. D'AMICO: Yes.

REPRESENTATIVE ROHRER: All right. Thanks very much.

CHAIRMAN LEVDANSKY: Representative DeWeese has a question he'd like to ask.

Bill?

REPRESENTATIVE DEWEESE: Not a question, I just want the record to show that Lou and the people he represents have been excellent neighbors to those of us in the 50th District, and my motivation for introducing the bill has nothing to do with the warm feelings that he's generated among the townships, the boroughs, the school districts and the county governments back home.

And I just wanted to the record to show that because this is not antagonistic. This is just a way when our revenue yields are so questionable and so paltry, this was something I thought to revivify what we had in 2001 and 2000 and 1999 backward. But, again, Lou and his friends in the industry in Greene County in the 50th District have been wonderful neighbors. Thank you.

CHAIRMAN LEVDANSKY: Okay. Thank you.

Mr. D'Amico, I have a few questions. Relative to the court decision, it seems as though the central issue is the fugaciousness or lack thereof of particular minerals, and correct me if I'm wrong.

So the decision is that because oil and gas are, by their very nature, fugacious materials and difficult then to say how much there is under a particular tract or parcel of property, that it should be exempt as compared to -- you know, it should be exempt from property taxation or included in the assessed value as compared to, say, for example, coal or limestone, which are deposits that clearly don't move?

MR. D'AMICO: Right.

CHAIRMAN LEVDANSKY: It just seems to me that -- I don't know -- there are minerals, and determining whether or not they're fugacious or not, to determine whether or not they're taxed or not just would seem to place some inequity on those individuals and businesses that own minerals that aren't fugacious. Could you see where there'd be, like, an inherent in equity in that?

MR. D'AMICO: Again, it's whether it's a mineral or some other item, whether -- and I'm trying to think how to best describe this. The issue is whether or not the, by its nature, natural gas sits on a property and is appropriate as real estate. That's the question that two justices agreed with us outright that that was not the case. The other ones did not address the issue.

CHAIRMAN LEVDANSKY: Okay. The amount of drilling that has gone on in the state, say, for the last ten years, exclusive of about the last two years when there's been tremendous interest because of Marcellus, what's been going on? In terms of the drilling, has it been stable? Has it been getting less prior to Marcellus when the permits really started ticking up about two years ago?

MR. D'AMICO: Yeah. Natural gases prices had started to head up where they reached that $13.70. Yes, the activity level across the country had increased, and Pennsylvania was a beneficiary in that. One of the -- the big difference between drilling in Pennsylvania versus drilling in most of these other states is the productivity of the wells. Even though we were the third most active drilling state in the country, we were a distant 15th in production. Our wells for the most part prior to Marcellus were shallow marginal wells with very low productivity. We made money by keeping our cost at an absolute minimum, and as prices rose and fell, our activity levels rose and fell.

CHAIRMAN LEVDANSKY: So it's the price that affects a business's decision to whether or not we're going to drill or not. It's the price of the product that is the predominant factor.

MR. D'AMICO: It's the overall economic decision. If you come into Pennsylvania and drill a shallow well with virtually a 99 percent success ratio, the risk is a little bit lower; and if the gas price covers your cost, then we'll attract drilling.

CHAIRMAN LEVDANSKY: Okay. So prior to 2002, oil and gas were subject to property taxation, and then after 2002, it wasn't. Did we see a growth in drilling or a drilling boom created because we no longer taxed it?

MR. D'AMICO: No. We saw a drilling boom because overall cost versus price, the price had gotten to the point where it made a lot of sense to drill in Pennsylvania. I have never, we have never as an industry claimed that the real estate tax was going to drive people completely out of the state or any such claim as that. Does it have an overall impact on our cost structure and how much money we can attract to drill wells? Of course it does, but we've never made the claim that we're going to leave the state because we have a real estate tax.

CHAIRMAN LEVDANSKY: Okay. So if House Bill 10 were to become law, that would likely have a negligible impact on whether or not, you know, on the amount of drilling that's going on in the state especially compared to the price volatility of gas?

MR. D'AMICO: Again, it depends largely on our total cost versus price. It's an example of the cost of operating in Pennsylvania versus drilling -- let's talk about the Marcellus for a minute. It's more expensive to drill a Marcellus well in Pennsylvania than it is to drill a similar well of Barnett Shale in Texas, regulatorywise, drainwise, highwaywise.

So the total cost will be considered. If our reserves are bigger in the Marcellus than the Barnett, yet the Barnett is considerably cheaper to operate, a company says, we'll put our money into the Barnett Shale rather than here. They might put it in the Haynesville Shale in Fayetteville. Somebody mentioned early, and I don't recall which speaker, talked about the gas is always going to be here, so there will be development.

Although that is the case -- it's not like we're going to move a plant. But the reality is, if I, as an operator, have the option of going into the Haynesville shale and my overall economics is better in that area in northern Louisiana than it is to go into Bradford County, Pennsylvania, I'll be in Louisiana.

CHAIRMAN LEVDANSKY: So it's really the spread between the cost of operation and the price you could charge, the market price versus the cost of operation. That differential is what really affects the investment decision making?

MR. D'AMICO: That's correct. It's overall cost.

CHAIRMAN LEVDANSKY: Okay. And correct me if I'm wrong. Vis-a-vis the Barnett and the other gas shale formations down in the south central part of the state, one thing, one advantage we do have isn't just the fact that we have the supply, but the market is right here as well, isn't it? I mean, isn't about 40 to 45 percent of the cost of gas tied up in transportation? And that being so, I'm just going to --

MR. D'AMICO: That's not entirely correct. A good portion of that is transportation, but it's the local distribution company level. Whether we're drilling it in Pennsylvania or I'm drilling it and bringing it up from

Texas, it's going to have the same impact. We're seeing, we've seen over the last two decades a dramatic decrease in the price impact of the transportation rate, the long lines, the interstate lines coming up from Texas. We got another line that just came in from the Rocky Mountains, the Rocky Mountain Express, which is dramatically impacting our prices here because there's additional supply coming in from the Rocky Mountains that didn't exist before here.

CHAIRMAN LEVDANSKY: Right. Well, but, I mean, the fact is they've got to build those pipelines; they've got to build the compressor stations. They've got to maintain them. They've got to pump that gas pretty far away to get to the northeast corridor, vis-a-vis Pennsylvania, we'll be able to pump it a couple hundred miles compared to 12 hundred.

MR. D'AMICO: And that's, in the long run, we're hoping that is a significant benefit. It's going to be something we're looking for in the future. Right now, there's not that much of a difference.

CHAIRMAN LEVDANSKY: Okay. One other quick question, from your perspective in the industry and as an engineer, a natural gas well that produces, say, 60 thousand mcf's a day; pretty big well, average?

MR. D'AMICO: For Pennsylvania, no, that actually is a pretty good well. For the rest of the country, that's a pretty bad well. I think the numbers that the IRS uses for a stripper well, which is a marginal benefit well, is 90 mcf a day. And by the 90 mcf-a-day ruling, probably 97 to 99 percent of the wells in Pennsylvania are marginal wells.

CHAIRMAN LEVDANSKY: And just for information, House Bill 1489, the other bill that is not the subject of this committee hearing, it exempts every, it exempts stripper wells that produce 60 thousand mcf per day. You know, I presume you're aware of that.

You know, you pointed out before that a severance tax would impact the industry, but the reality is that it would exempt that portion of the industry that has historic stripper wells producing, you know, less than 60 thousand mcf a day.

MR. D'AMICO: Yeah. Again, I guess, like you said earlier, I would comment more on the severance tax when you have more hearings on that.

CHAIRMAN LEVDANSKY: Yeah. I'd like to get to that. Trust me. And now just a point I want to make, and you can react to it or not, just pointing out that it's really about the price of gas that really affects the decision to invest in drilling or not. Range resources, we have a citation on this. It basically said that they could make money at $2.50 an mcf, so whenever the prices hit rock bottom in Pennsylvania in the latter part of last year, at $2.50, they were still able to make a profit.

I'm not saying a lot, but they did say that. So any time -- so when you see price go significantly higher than $2.50, I think it attests to the fact that their cost structure is such that if you could make money at 2.50, it would seem to me that you could not only make money at prices higher than that, but you could probably well afford to make money and pay a severance tax at the same time when prices are higher than that.

And just one final thing, and, again, you can react to all this if you want to or not. I hear a lot about all the taxes that the gas industry and drillers already pay. Just let me point out a couple of things. Wage taxes, wage taxes may or may not be paid by the employees. You know, we heard the difficulty in collecting those, but, again, those are wage taxes paid by employees, not by the corporation.

Property taxes, you know, thanks to the court decision now, the oil and gas industry doesn't pay property taxes. You don't pay a severance tax unlike every other, nearly every other state that produces gas with the exception of one or two. And you have the, in terms of the sales tax, you have the manufacturer's exemption, so a lot of the materials that you use in your drilling processes are exempt from the state sales tax.

And on top of this, two-thirds of the wells drilled last year in Pennsylvania were by companies who had LLCs, who had subsidiaries that were LLC, and thus, they were subject to the personal income tax and not the corporate net income tax. One could make the argument, I think pretty strongly, that the industry isn't paying their fair share of taxes vis-a-vis other businesses in the state and individuals for that matter.

So if at the end of the day -- I'll end with a question, and you can react if you want to or not. If at the end of the day your choice is a property tax or a gas severance -- I know it's cod liver oil -- which is your choice?

MR. D'AMICO: Neither. No, I think that a question that Representative Rohrer asked earlier is how -- you know, I think the best process is some sort of an income-type tax or revenue-based tax that is not off the top for anybody who makes a profit or not something that requires some great calculation to figure out.

CHAIRMAN LEVDANSKY: Like a gross receipts tax like Ohio has?

MR. D'AMICO: I'm not familiar with Ohio.

CHAIRMAN LEVDANSKY: Okay.

MR. D'AMICO: Again, I'm an engineer. I'm not an accountant, so I don't have a clue to how -- you're asking an engineer to come up with a solution that good accounting tax people haven't figured out in years.

CHAIRMAN LEVDANSKY: Well, listen, I appreciate your testimony and your frank honest answers to our questions even though they're a little pointed from time to time, but there is one final question by Representative Kessler.

REPRESENTATIVE KESSLER: With horizontal technology, you had mentioned that once the well is drilled, the majority of the traffic is gone. When you drill that well, do you fracture north, east, south and west; or do you just fracture one, pull the gas out, then come back in and fracture again? Because my understanding is that you need a couple million gallons of water to do that, and so that would be probably truck traffic then.

MR. D'AMICO: Absolutely. Any time we are fracing or drilling a well, there's truck traffic involved. What I was talking about is after that initial period when that property is developed and we're now on production for the wells on that pad, then all that activity is pretty much died away.

REPRESENTATIVE KESSLER: So if you need -- and I have numbers of 3 million gallons. I mean, what kind of size tanker trucks are you bringing in carrying water?

MR. D'AMICO: Most of the trucks coming in are hundred-barrel trucks.

REPRESENTATIVE KESSLER: Okay. So fracturing can go on after the well's drilled, six months later on, a year, two years?

MR. D'AMICO: No, we're not talking about six months. It's usually within less than a month after the well's drilled is when you fracture. You want to go in and complete the well as quickly as possible. After you spend all that money, you want to try to get some kind of return on it.

REPRESENTATIVE KESSLER: But is there some point down the road you come in and try to fracture again then?

MR. D'AMICO: No, not normally.

REPRESENTATIVE KESSLER: Okay. Once it's fractured --

MR. D'AMICO: That's something we have not experienced in Pennsylvania, refracturing wells. Now, whether that's something that comes up on the Marcellus, I have no idea, but I don't expect it.

REPRESENTATIVE KESSLER: And then a typical well, how many employees are you talking about at the site?

MR. D'AMICO: On the site at any given time?

REPRESENTATIVE KESSLER: Yeah.

MR. D'AMICO: During the drilling operations or --

REPRESENTATIVE KESSLER: After the drilling.

MR. D'AMICO: Afterwards. You know, one individual, one well tender can probably take care of multiple wells. There might be 20 to 25 wells, Marcellus wells. That's the well tender, but then you have compressor operators and you have some other associated jobs. There's a real good list that Penn College of Technology put together of what percentage of jobs are going to be at every level during the development of this. It makes a very good reading.

REPRESENTATIVE KESSLER: So once the drilling's done, are we looking at one, five, ten employees there, or how many on average?

MR. D'AMICO: In a township you mean, or --

REPRESENTATIVE KESSLER: No, I mean on the well site itself.

MR. D'AMICO: Well, at any given time, you're probably going to see one person on an individual well site. But there's people who are looking after that during the course of a day, and all the subsidiary production operations go with it, like compression, all the other things that are involved. You could probably assume one to two people per well are involved in an area.

REPRESENTATIVE KESSLER: Okay. Thank you.

CHAIRMAN LEVDANSKY: Thank you, Mr. D'Amico. I appreciate your attendance here today.

MR. D'AMICO: And I apologize for having to fight my voice here.

CHAIRMAN LEVDANSKY: I understand.

MR. D'AMICO: I hope somebody could hear me.

CHAIRMAN LEVDANSKY: Sure.

Finally, let me call on Mr. Daniel Fisher, the Superintendent of the Bald Eagle Area School District.

Mr. Fisher, is yours the PowerPoint presentation?

MR. FISHER: Yes, it is.

CHAIRMAN LEVDANSKY: Okay.

MR. FISHER: Good afternoon, Chairman Levdansky, Chairman Rohrer, and members of the House Finance Committee. I am the Superintendent of the Bald Eagle Area School District, and I represent many school districts here today, many school districts, I'm sure, just like the ones where you folks represent. Let me say right from the get-go that our school districts, Pennsylvania School Board Association strongly, strongly supports House Bill 10.

We feel that taking that part of our tax base from us, as was done with the Fayette County and IOGA decision in 2002, was a great injustice. And I have been superintendent long enough and business manager before that to recall when we had the tax revenue coming in from, at that time, it was Eastern States Exploration. So I lived through it budgetarily for the past essentially 20 years.

And I would like to not read the -- first of all, I can't see the print on it to read it even if I wanted to. I know you've had the testimony. I would like to make one correction. We wish we had oil wells in our district, but we don't. But we do have quite a number of gas wells.

Would there be any objection to my standing?

Here we can see the Marcellus Shale deposit just in Pennsylvania. It does extend south and northsouth. As you can see, there are many, many school districts -- in fact, 207 of the 225 or 250 school districts that are below the median resource level, 207 according to PSBA information, 207 of them lie under the footprint of the Marcellus Shale.

Now, keep in mind, when the decision was made in 2002, when we keep talking about fugacious -- and I can't help wonder how it can be more fugacious in Pennsylvania than it is in all the other states that have natural gas. But when we talk about fugacious, we were talking at that time not about the Marcellus Shale, but we are talking about the shallow wells. And we have essentially, right now, somewhere in the vicinity of 10 thousand shallow wells in the Commonwealth of Pennsylvania, 10 thousand, and yet we hear this referred to as a nascent industry.

I'd like to, first of all, locate -- Bald Eagle Area's right there in Centre County. It's actually in the northern part of Centre County. You can see the Marcellus well permits there. You can also see the shallow well permits. And as you look, in 2009, there were 6,233 permits. Of those, 4,249 were shallow wells; 1,984 were the Marcellus Shale wells.

That is a huge, a huge number of the gas industry in Pennsylvania, and this isn't just something that started. This has been going on for a hundred years. It was fairly new to Centre County. It has not gone on in Centre County for a hundred years, but I have heard of gas wells as early as the '30's in Centre County. Drilling in wells that were given by January 4, 2010, you can see a total of 9 wells drilled; 19 well pads sited; 25 permitted, but not drilled; wells and planning, 97, Centre County.

Centre County is not a huge state right now -- or excuse me -- is not a huge county where there's a lot of drilling going on compared to other counties in the Commonwealth. There you can see the wells that are actually, the Marcellus wells that are actually in our district. You can see Snowshoe Township. Most of them are in Burnside Township, and we'll get to Burnside Township a little bit later.

Certainly and, again, not as much activity as there is elsewhere in Pennsylvania, but it's a lot of activity. Just as I left the parking lot today, I think I saw four or five trucks carrying well drilling equipment right past the parking lot. We see that very, very frequently. Here we are. You can see our school district in Centre County. We are the largest school district in Centre County. We cover about 340 acres. Most of our municipalities do not have gas.

They do not have Marcellus Shale gas. Most of the Marcellus Shale gas in Pennsylvania is located here in Burnside and Snowshoe Township, and this is part of the Phillipsburg Area School District, Rush Township. And there are quite a few permits issued, and there's a lot of drilling going on in Keystone Central School District. And earlier -- I wonder if I could turn the light on so we can see, please.

Earlier, I passed out our district newsletter, Eagle Pride. We publish this twice a year, and I'm sure that many of your districts publish the same thing. And in our community and in many rural communities, the school district is actually the community. We have construction people working on our school right now. They're working on our middle and high school, and they said they'd never worked on a school like this; it never closes.

It's closed mostly on Sunday mornings, but I think we often forget how important schools are as parts of the community. How we finance those schools is another big challenge, and in the next few years, it's going to be a huge challenge. 45 of the 50 poorest schools in the district also lie under the Marcellus Shale deposit. All of our school districts, Bald Eagle included, throughout the state have huge pension increases coming.

All of our school districts have huge healthcare increases coming. And as we look beyond this coming year, and I suspect this budgetary year will be difficult too -- as we look beyond that, we have to look at all resources, all tax revenue, all potential tax revenue if, in fact, we're going to find any way to balance those budgets, any way essentially to not cut programs, any way to provide the services that all school districts are required to provide.

Back in 2002, Bald Eagle Area collected $65 thousand from natural gas tax. There you see Burnside Township. It's one of our three townships that had gas wells back in 2002, and you see essentially three wells there, 65 thousand. And at that point, if you look at our tax records, there were pages, pages of tax bills, some of them very small because some of them didn't produce much.

But there were pages of tax bills that were paid by Eastern States Exploration.

None of those tax bills, none of those tax bills on the mineral assessment, none of those were paid by the property owners. They were paid by the people who own the rights to drill for that gas. We go ahead to 2006. And, again, we're looking at Burnside Township, and we're looking at the number of wells in Burnside Township. Now, we heard earlier that the reason there are more wells is because the price of gas went up, and I suspect that's it.

But our revenue in 2006 was zero because of the Fayette County IOGA decision. It was zero. I calculated, just extrapolating for the number of wells that we see there, that our revenue, had that not happened, our revenue would be somewhere around a million-and-a-half dollars from those wells. So essentially, Bald Eagle Area School District and I'm going to guess hundreds of schools districts, or at least a hundred other school districts lost tax revenue, property tax revenue because of that decision.

Now, IOGA, in their quarterly newsletter at that point, said Christmas came early this year, and, in fact, you can look at the quarterly newsletter. It's on the web. What we would be receiving now, my estimate with the Marcellus Shale, is somewhere around 2 million a year. So what happens to that 2 million a year? That 2 million a year then gets downloaded to people much less capable of paying that bill. Our property taxes have gone up with the index every year.

They'll go up with the index again this year, and that's going to happen throughout the Commonwealth. It's going to happen -- it's going to be particularly difficult for poor school districts such as ours and poor school districts such as the 200 that I mentioned earlier that lie within this Marcellus footprint. House Bill 10 -- I don't know if Representative DeWeese is still here, but that bill will serve to correct this.

And that bill will serve to prevent a calamity in at least half of the poor school districts across the state. I know that the House Finance Committee has struggled with local property tax reform for years, maybe decades. Here's an opportunity for real reform, real reform in at least most of the districts and counties in Pennsylvania.

I feel like I'm talking to my -- I taught history for nine years. I feel like I'm talking to my ninth period class here, but thank you. Thank you so much for your attention and for having us here to talk about it. Are there any questions?

CHAIRMAN LEVDANSKY: Thank you, Mr. Fisher.

There's not a lot of members to recognize for questions except Representative Mirabito.

Rick?

REPRESENTATIVE MIRABITO: You know I could probably ask a question.

Do you have any other numbers? I mean, I think that's, what you said is very significant about the $2 million being passed on to other taxpayers. Do you or does the School Board Association have a breakdown county-by-county or school district-by-school district?

MR. FISHER: I don't have the breakdown other than what I gave you for the Bald Eagle Area School District. I'm sure that our folks at PSBA could provide that, and we can ask them to get that to you.

REPRESENTATIVE MIRABITO: That'd be helpful. Thank you.

CHAIRMAN LEVDANSKY: All right. Okay. Mr. Fisher, just curious, Burnside Township, where is that relative to Rush Township?

MR. FISHER: It's north of it and essentially west of it a little. Take a look at it. Burnside would be here, and Rush would be here.

CHAIRMAN LEVDANSKY: So Rush is in the Phillipsburg School District?

MR. FISHER: Yes.

CHAIRMAN LEVDANSKY: Okay. There has been an uptick in obviously drilling in your school district and your county. I mean, has the school district had any increased costs relative to more kids coming, more kids enrolled in your school district because of drilling activity? Could you point to any fiscal impact of the drilling?

MR. FISHER: In my presentation, I did point to the different areas throughout the country, in Texas, in Arkansas, where they had as much as a 131 percent increase. We have not seen that increase as of yet. I suspect we will. What we're seeing right now for the most part, as was mentioned earlier, people who are living in hotels and their families are remaining in Texas or wherever they're from.

But I think as this develops, I think that's -- if you look at the increases in population -- and I have some of those, if you'd like to take a look at them, on the PowerPoint, but they're very, very pronounced. I think the other thing that sort of fits together is sort of a syndetic relationship between the counties and the municipalities. Particularly for the Marcellus Shale, they need a lot of water, and they also need treatment facilities.

And frankly, most of our rural areas, our rural school districts need both of those too. We need water lines extended, and we need treatment facilities. One of the things that precludes development in Bald Eagle Area and in many rural districts is they don't have on-site sewage or water. And we have right next to us, right over the ridge where both State College and Bellefonte have those available.

We see vibrant developments going on there. Those same developments can't go on in our rural municipalities, and it can't go on in many of them throughout the state because of the lack of the sewage and water availability. But I think this is an opportune time where those two goals could be pursued in our rural communities.

CHAIRMAN LEVDANSKY: All right. Okay. Seeing no other members with questions, I appreciate your testimony and your traveling here to testify today and your written presentation as well. I'm familiar with your neck of the woods up there. I've stepped --

MR. FISHER: I saw you were. You're a Penn State grad.

CHAIRMAN LEVDANSKY: A Penn State grad and spent more than a couple days fishing on Bald Eagle Creek, not too far from the Windgate Elementary School down there.

MR. FISHER: You're welcome back any time.

CHAIRMAN LEVDANSKY: Beautiful country up there.

MR. FISHER: Thank you very much.

CHAIRMAN LEVDANSKY: This concludes today's Finance Committee meeting on House Bill 10. Thank you.

(The hearing was concluded at 3:35 p.m.)

I hereby certify that the proceedings and evidence are contained fully and accurately to the best of my ability in the notes taken by me on the within proceedings, and that this copy is a correct transcript of the same.

Jennifer L. Sirois, Court Reporter,
Notary Public

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NOTARIAL SEAL
JENNIFER L. SIROIS, Notary Public
East Pennsboro Twp., Cumberland County
My Commission Expires June 2, 2013