



TRANSFORMING OHIO FOR GROWTH

TAX CUTS. EDUCATION & WORKFORCE.
ENERGY. MANAGEMENT EFFICIENCY.

Income Tax Cut

THE KASICH INCOME TAX CUT: \$900 Million to \$1 Billion in Tax Cuts Over 5 years

Ohio's High Income Taxes Are a Barrier to Job Creation: Ohio has among the highest income tax burdens in the country. According to the Tax Foundation, Ohio's combined state and local tax burden ranks in nearly the top third in the nation. This limits Ohioans' personal economic power and, therefore, our state's economic recovery. These higher taxes also make Ohio unattractive to out-of-state job creators looking for new places to grow. Reducing Ohio's income tax burden is essential to creating the jobs-friendly climate that will help get Ohio back on track.

More than \$800 Million in Tax Cuts So Far: Ohio's Constitution mandates that the state balance its budget every year. Unlike the federal government, Ohio cannot run a budget deficit by spending more than it takes in or by cutting taxes without equal spending reductions or growth in revenue.

Under Gov. John Kasich's leadership, Ohio has cut taxes by more than \$800 million by following through with previously-promised income tax cuts and by eliminating the Death Tax¹. Restraining spending and saving money through overdue reforms to programs made these tax cuts possible. New income tax cuts will build on past savings and leverage growing economic activity.

\$900 Million to \$1 Billion² in Total New Income Tax Cuts Will Benefit All Taxpayers: New revenue from Ohio's shale oil and gas production should go to Ohio taxpayers, not government. Every cent—100 percent—of new tax revenue from the high-volume horizontal wells like those used in Ohio's Utica and Marcellus shale formations will be used to reduce income taxes the following year. Each of Ohio's nine tax brackets will be reduced to ensure that taxpayers of every income level receive a tax cut. The revenue from new, high-volume horizontal wells will allow Ohioans' income taxes to be cut by an estimated \$900 million to \$1 billion when Ohio reaches peak production in approximately 5 years. As this oil and gas production increases so will the income tax cut for Ohioans.

Modernizing Ohio's Oil and Gas Tax System: Ohio hasn't been a major oil and gas producer in the past century, so our state's 40-year-old tax system for oil and gas production—the "severance" tax—has never been comprehensively modernized. Ohio's current severance tax is only 20 cents on a \$107 barrel of oil³ and 3 cents on a \$2.62 MCF unit of natural gas⁴. There is no separate tax on valuable natural gas liquids.

Just as Ohio is updating its environmental, health and safety regulations to keep pace with new technologies for high-volume horizontal oil and gas wells in Ohio's shale formations, Ohio's severance tax policies need to be updated as well. Updates to Ohio's severance tax policies will keep rates competitive with other oil and gas-producing states while generating new revenue that will go directly to Ohio taxpayers, not government.

¹ The final installment of the four, 4.2 percent income tax cuts enacted in 2006 was not implemented by the previous administration, resulting in an effective tax increase. Finally implemented under Gov. Kasich, it cut income taxes approximately \$450 million, according to the Ohio Department of Taxation. In FY 2011, the Estate Tax generated \$374.2 million.

² Based on production estimates from the Shale Coalition report released Feb. 28, 2012.

³ According to the Feb. 29, 2012 closing price for crude oil on the NYMEX futures exchange.

⁴ According to the Feb. 29, 2012 closing price for natural gas on the NYMEX futures exchange.

BOTTOM LINE: Reducing Ohio's high income taxes helps create the jobs-friendly climate that will get our state back on track. Modernizing Ohio's severance tax system to keep up with new oil and gas production will generate new revenue while still keeping Ohio competitive with other states. All new revenue will go entirely to Ohio taxpayers in the form of income tax cuts.

HOW IT WILL WORK

Ohio Taxpayers Will Receive a \$900 Million to \$1 Billion Total Income Tax Cut: Ohio taxpayers will receive an estimated \$900 million to \$1 billion total income tax cut over the next five years as a result of new severance tax rates for the crude oil and natural gas liquids produced by the high-volume horizontal wells like those used in Ohio's Utica and Marcellus shale formations. When Ohio reaches peak production, income tax cuts could reach \$500 million annually.

- **All new revenue will be returned to Ohio taxpayers through income tax cuts:** Ohio's current severance tax rates will calculate an amount that will help pay for regulatory costs, and all new revenue will go to Ohio taxpayers in the form of an income tax cut. No new revenue will be kept by government.
- **Every Ohio taxpayer will benefit:** New revenue will be deposited in a special income tax reduction fund and be used to reduce all Ohio income tax brackets the following tax year. As oil and gas production and prices increase, so will the amount of the income tax cut for Ohioans. The opposite is, of course, also true. Production from high-volume horizontal wells is expected to ramp up gradually, generating modest revenue initially, but then increase dramatically in the following years to produce significant income tax cuts.

Ohio Will Be Competitive with Other Oil and Gas States: Modernized severance tax policies will generate enough new revenue to cut income taxes for every Ohioan while still being low enough to keep Ohio competitive with other oil and gas-producing states.

- **Taxes Will Be Eliminated On Small Gas Producers:** Small natural gas wells producing less than 10 MCF per day will no longer pay any severance taxes on natural gas production. This eliminates taxes for approximately 90 percent (44,500) of Ohio's conventional natural gas wells. For conventional natural gas wells producing above this level, the new 1 percent rate will apply, with a cap of 3 cents per MCF.
- **Oil & Gas Producers Can Recover Costs First:** High-volume horizontal wells will enjoy a low initial severance tax rate of 1.5 percent⁵ or both natural gas liquids and crude oil. This rate would apply for the first year to allow producers to recoup their drilling costs, which can range from \$6 to \$12 million per well, and can be extended for one additional year if drilling costs haven't yet been recovered in the first year. After the initial cost-recovery period expires, the standard rate of 4 percent will go into effect for both natural gas liquids and crude oil.
- **Natural Gas Severance Tax Rates Will Be Cut for High-Volume Horizontal Wells:** Severance tax rates for natural gas produced by high-volume horizontal wells will be changed from the current 3 cents per MCF to 1 percent (price x production volume). At the current natural gas price (approximately \$2.60/MCF), this represents a tax cut for producers.
- **Severance Taxes Will Remain Unchanged for Conventional Crude Oil Production:** Severance tax rates for crude oil from conventional wells will remain unchanged at the current 20 cents per barrel rate.
- **Severance Tax Will Not Be Applied to Natural Gas Liquids from Conventional Wells:** Ohio currently does not apply a separate severance tax on natural gas liquids produced by conventional wells. That won't change. No separate tax will be applied to natural gas liquids produced by conventional wells.

⁵ Producers will remit taxes quarterly based on this calculation: (Quarterly Production Volume) X (Quarterly average price) X (Taxation Percentage).

SEVERANCE TAX MODERNIZATION		
Product	Conventional Wells	High-Volume Horizontal Wells ("Shale" Wells)
Crude Oil	20 cents per barrel <i>(unchanged)</i>	1.5% for first year, 4% following years <i>(Initial 1.5% rate can be extended for one additional year only if initial costs to drill the well are not yet recovered.)</i>
Natural Gas	0 for wells <10MCF/day, 1% for wells >10MCF/day capped at 3 cents/MCF	1%
Natural Gas Liquids	0 <i>(Currently no separate tax is applied, and that will remain)</i>	1.5% for first year, 4% <i>(Initial 1.5% rate can be extended for one additional year only if initial costs to drill the well are not yet recovered.)</i>

BACKGROUND

Current Rates: Currently Ohio's severance tax rates are 20 cents per barrel of oil and 3 cents per MCF for natural gas.

Ohio Currently Has No Tax on Gas Liquids: Ohio currently has no separate severance tax on "gas liquids," the valuable, highly-sought hydrocarbons which are the feedstock for plastics and other advanced polymers and which are found in Ohio's shale formations.

Ohio's Oil & Gas Taxes Are Currently Among the Lowest, and Will Remain Among the Lowest: Ohio's current severance tax rates are among the lowest in the country. Other oil and gas states have much higher severance tax rates:

SEVERANCE TAX RATES IN OTHER OIL AND GAS STATES		
STATE	CRUDE OIL	NATURAL GAS
Michigan	6.6 percent	5 percent
North Dakota	7 percent	9 cents/MCF
Texas	4.6 percent	7.5 percent ⁶
West Virginia	5 percent	5 percent

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⁶ Lower rate is applied to certain high-cost gas wells until well construction costs have been recovered.