



# Appalachian Partnership for Economic Growth

## Testimony to the House Ways and Means Committee House Bill 375

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Good afternoon Chairman Beck and members of the committee. My name is John Molinaro. I am the President and CEO of the Appalachian Partnership for Economic Growth (APEG), the JobsOhio partner for southeast Ohio. We provide economic development and Manufacturing Extension services in 28 Appalachian Ohio counties, including most of the counties with Utica and Marcellus Shale activity. Thank you for the opportunity to offer testimony as an Interested Party on House Bill 375.

As the economic development organization charged with building prosperity of the region where most of the shale play is currently underway, APEG supports a reasonable severance tax on oil and gas extraction and production, so long as a significant portion of the revenues derived are dedicated to mitigating short and long term impacts of the extraction and to building a better economic future for the region.

Over the past 35 years I have had the privilege of working in economic development in rural regions across the U.S. and have direct experience with both oil and gas development and severance tax policies in several states. I have had opportunities to examine the effects of both good and poor policy and practice and would like to share some observations that may help strengthen the proposed legislation.

### **Economic Displacement: “Dutch Disease”**

Virtually every place in the world with an extraction-related economic boom has also experienced a phenomenon called “economic displacement” which later led to a significant

decline in the local economy. This happens when the companies that come in to do the extraction bid up the cost of labor, land, facilities and services.

This bidding-up process squeezes out local activities that are the underpinnings of the economy. Firms that cannot raise their prices enough to pay these increased costs close or move. When the extraction ends, the local economy finds itself with fewer jobs to support its people and less tax revenue to support critical government services.

The bust that comes after the boom often results in the local economy dropping well below pre-extraction levels. This can affect entire regions, states and even nations. Economists often refer to this as “Dutch Disease” after the example of the Netherlands in the 1970’s. When their offshore drilling boom ended, the entire national GDP sank well below pre-drilling levels and took many years to recover.

The bad news is, while we are still very early in the Shale play, we already see signs of economic displacement in eastern Ohio. Current Shale activity has caused workforce shortages for truck drivers and some manufacturing and trades jobs, as well as raising the cost of housing in some areas.

The good news is that a carefully structured severance tax has been shown to be very effective in fighting Dutch Disease.

### **Severance Tax Set-Asides: the IRRRB Experience**

Countries, states and regions that have avoided the worst of Dutch Disease all have one thing in common: they set aside a significant portion of the increased tax revenues from the extraction to mitigate impacts and support the economic revitalization in the area where the extraction occurs. There are many excellent examples of this in the U.S. and abroad, but I would like to highlight one with which I am intimately familiar from a region with many similarities to Appalachian Ohio.

I have more than two-decades experience working in rural development in Minnesota, where a portion of the severance tax on Taconite<sup>1</sup> has been set aside for economic revitalization of the

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<sup>1</sup> Taconite has replaced iron ore as the mineral from which most iron is produced

Northeast Minnesota region where it is mined. Their story is one of the most outstanding success stories for a severance tax set-aside in the U.S.

Seventy-three years ago, the Minnesota Legislature set aside a portion of its Taconite severance tax to mitigate mining impacts and diversify and strengthen the region's economy. The Legislature also founded a regional oversight body, the Iron Range Resource and Rehabilitation Board (IRRRB), to guide the use of these tax revenues.

Prior to the set-aside, Northeast Minnesota was every bit as economically challenged as Appalachian Ohio. Today, as a direct result of the IRRRB's efforts, it is one of the strongest rural regions in Minnesota, with a thriving, diversified economy.

Over its history, IRRRB has provided loans and grants to assist new and existing businesses, creating thousands of new jobs; supported communities with financial assistance for infrastructure development; led efforts to rehabilitate communities and abandoned minelands; supported the region's culture and tourism industry; partnered with K-12, higher education and industry in development of a well-trained workforce; and reinvested in northeastern Minnesota's forest and mining industries.

Some of the strengths of the IRRRB structure include:

- Strong political support statewide for a severance tax that predominantly supports the general operations of state government but also includes a significant set-aside for benefit of the affected region
- A governing board that broadly represents the region and stakeholders including state, county and local interests
- A broad mission that includes both mitigation of impacts and economic revitalization
- Flexibility to use the set aside funds for needs and opportunities as they change over time – with no fixed allocation formula.

## **Proposed Changes to HB375**

Based on the experience of other regions, APEG proposes the following changes to HB375 to address both near and long-term impacts associated with Shale-related extraction:

1. **Set aside a portion of severance tax proceeds to mitigate impacts and build the economy of Appalachian Ohio.** Appalachian Ohio has repeatedly experienced severe economic downturns following periods of intensive resource extraction. As a result, its economy lags far behind the rest of Ohio. Setting aside a significant portion of the severance tax proceeds to mitigate impacts and build a stronger and more diverse economy has proved to be the one effective cure for this type of boom and bust cycle.
2. **Establish a broadly representative oversight board to determine specific uses for set-aside severance tax funds.** Needs and opportunities associated with mitigating impacts of extraction and building a more diverse economy are varied and change over time. A governing board that represents state, regional and local interests has proven to be more effective in addressing impacts and building a more robust economy than a predetermined or exclusively legislative allocation mechanism.

## **Conclusion**

Experience in other regions of the U.S. and around the world shows that a boom of the type we are seeing from shale in Ohio is always accompanied by both immediate impacts and longer term economic displacement. Appalachian Ohio has experienced this repeatedly – with past boom and bust cycles from timber-, oil- and coal-related extraction.

Judicious use of a portion of the severance taxes generated by the current boom, can break the cycle and put Appalachian Ohio on a track to attain long-term economic stability and increased self-sufficiency. With your visionary leadership, we have a one-time opportunity to transform the economy of Appalachian Ohio, and set it on the road to contribute equally with the rest of the state.

APEG strongly supports a reasonable severance tax, on par with other states, with a significant set aside to mitigate impacts of extraction and build a stronger and more diverse economy in the Appalachian Ohio region.

I thank you for your time and attention and welcome any questions.