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Drilling for tax credits

Runaway coalbed methane development doesn't need a tax break

For more than a decade, no form of energy production in the United States has been developed more quickly, or more recklessly, than natural gas found in coal seams, typically called coalbed methane. A negligible energy source prior to 1990, coalbed methane accounted for 57 percent of the growth in U.S. natural gas production between 1990 and 1999, according to the Department of Energy. Nowhere is coalbed methane developing more rapidly, and taking more of a toll on the environment and precious groundwater resources, than in Wyoming's Powder River Basin, where the Bureau of Land Management anticipates a staggering 40,000 new coalbed methane wells will be drilled over the next decade.

The coalbed methane drilling process involves massive dewatering, and each day tens of thousands of gallons of groundwater are summarily spilled across the countryside. Aquifers are depleted, but the dewatering is not merely an appalling waste—the water can inflict heavy damage through soil erosion, and the high water volumes can alter river drainages. The byproduct water is often high in sodium and other dissolved minerals, which can contaminate surface waters, destroy vegetation and wreck wildlife habitat. All that water, and what to do with it, has prompted lawsuits, interstate tensions, bureaucratic buck-passing and hard feelings within impacted communities, and whether coalbed methane developers will be forced to mitigate the environmental impacts of their activities frankly remains to be seen.

There is no doubt, however, that coalbed methane is booming. The last thing the industry needs is a tax break.

Energy legislation in Congress would extend and expand federal “Section 29” tax credits for coalbed methane production.

Currently, section 29 tax credits apply only to wells drilled between 1979 and 1993, and to production from those wells through 2002. The tax portion of the energy bill would apply the benefit to new wells and extend it until 2007. Supporters say the credits are necessary to encourage continued production. But coalbed methane drilling needs no congressional encouragement.

Powder River Basin coalbed methane production		
Year	Producing wells	Production (mcf)
1987	7	403,740
1988	15	706,634
1989	22	987,792
1990	32	1,097,392
1991	48	966,239
1992	47	783,151
<i>Section 29 tax credits apply only to wells drilled prior to 1993</i>		
1993	113	1,101,700
1994	118	2,429,529
1995	158	4,769,933
1996	178	8,567,705
1997	360	14,048,488
1998	652	30,667,606
1999	1,683	58,188,601
2000	4,506	150,757,549
2001	8,188	254,227,800
2002	10,718	326,983,794

Source: Wyoming Oil and Gas Conservation Commission

- In 1992, when the Section 29 tax credits still applied to new wells, about 50 coalbed methane wells produced 783,000 mcf (thousand cubic feet) of gas in the Powder River Basin. Over the next ten years, more than 10,000 wells were drilled in the basin, and production skyrocketed to 327 million mcf—*without the benefit of the Section 29 credits*.
- In 2000, the Wyoming Legislature recognized the maturity of the coalbed methane industry, and repealed state severance tax incentives. Coalbed methane from wells drilled after April 1, 2000 is now subject to the same state severance tax rate as traditional natural gas producers.
- Although the Section 29 credits have not applied to new wells for a decade, and eligibility on production from those wells expired as scheduled at the end of 2002, some of the country's biggest energy companies—Phillips Petroleum, Texaco, USX, Williams—have been spending hundreds of millions of dollars to acquire coalbed methane properties. As the Department of Energy observed in 2001, “Ongoing coalbed methane projects and recent acquisitions indicate a continuing interest in coalbed methane by the majors even if eligibility for Section 29 credits expires.”
- The Section 29 tax credit is absurdly generous. During the 1990s, the credit averaged \$1.02 per mcf. The wellhead price for gas averaged roughly \$3 per mcf over the same period. Equaling one-third the wellhead price, the monetary value of Section 29 credits conceivably could add more to a company's bottom line than the net revenues from actually selling the gas.
- In 1999, more than 1.3 trillion cubic feet of coalbed methane was produced in the United States, according to the Department of Energy. The tax credit proposal in the energy bill would vastly expand Section 29 tax credits to that production. The Joint Committee on Taxation has estimated the credit would cost \$2.47 billion through 2007. But the coalbed methane boom has outstripped expectations thus far, and the cost could easily outpace today's estimates. No matter what the ultimate cost of the credit, it amounts to a needless gift to an already booming industry.

***If Section 29 provisions are expanded and extended,
energy companies won't be drilling for natural gas.***

They'll be drilling for tax credits.

Sources

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