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Why Oil & Gas Tax Treatments Are Not Unique or "Subsidies"

Contrary to what some in politics and the media have said, the oil and natural gas industry currently enjoys no unique tax credits or deductions. Since its inception, the US tax code has allowed corporate tax payers the ability to recover costs and to be taxed only on net income. These cost recovery mechanisms, also known in policy circles as "tax expenditures", should in no way be confused with "subsidies", i.e., direct government spending.

Intangible Drilling Costs (IDCs)

- The IDC deduction is a mechanism that allows for the accelerated deduction of drilling costs, such as labor costs, associated with exploration activities (approx 60-80% of the cost of the well).
- Exploration and production companies can claim a deduction equal to 100% of these costs in the year spent. Integrated companies – "Big Oil" – can only deduct 70% with the remainder recovered over 5 years.
- This is a deduction, not a credit or government spending outlay and is *no different* than the policy behind and treatment of R&D costs vis-à-vis the R&D deduction available for other industries.

Foreign Tax Credit – Dual Capacity Rules

- The dual capacity regulations are not and never have been considered a tax expenditure or "subsidy" by the government.
- They represent additional rules placed on oil and gas companies to prove that the credit used to offset payments to foreign countries are indeed income tax payments and nothing else.
- Repeal of the rules generates revenue solely because it would impose double taxation on US based companies.

Domestic Manufacturer's Deduction – Section 199

- A deduction (not a credit) equal to 9% of income earned from manufacturing, producing, growing or extracting in the United States, is available to every single taxpayer who qualifies in the U.S.
- The oil and gas industry, and only the oil and gas industry, is limited to a 6% deduction.

Percentage Depletion

- The percentage depletion deduction is a cost recovery method that allows taxpayers to recover their lease investment in a mineral interest through a percentage of gross income from a well.
- This is available to all extractive industries (gold, iron, clay, etc) in the US and is in no way unique to the oil and gas industry.
- In fact, this depletion method is limited for the oil and gas industry. It is *not* available to companies that produce oil as well as refine and market it – i.e. "Big Oil".

LIFO Repeal

- Taxpayers that hold an inventory are required by law to track inventory costs – it is simply an accounting method and nothing else.
- Repealing LIFO deems a sale of inventory to occur and generating a significant tax gain. Therefore there is an assumed tax bill without any corresponding cash gain being generated.

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Expensing of Tertiary Injectants

- Tertiary injectants refers to items injected into older reservoirs to help continue production.
- The cost of the injectants are expensed similar to materials and supplies because they are generally used up in the production process.
- Without this provision, it is unclear how such operating costs would be recovered. This could easily increase the costs of operating these older fields.

Geological and Geophysical Costs

- G&G costs are the expenses associated with exploring for oil and gas.
- Currently, independent producers are allowed to recover domestic G&G costs over two years, and the proposal would increase that period to seven.
- "Big Oil" is not impacted, as the largest integrated oil companies already recover the costs over 7 years.

EOR and Marginal Well Credits

- These tax credits are designed to support continued domestic oil production when oil prices are so low that it may otherwise be un-economical. The credit phase out when the price of oil is above a certain amount
- *These credits have not been applicable for taxpayers in the oil and gas industry for years*, and in order to be even the least bit useful, the price of a barrel of oil must be at $42 (EOR credit) or $27 (marginal well).