November 28, 2012

The Honorable Dave Camp
Chairman
Committee on Ways and Means
1102 Longworth HOB
Washington, DC 20515

The Honorable Max Baucus
Chairman
Committee on Finance
219 Dirksen SOB
Washington, DC 20510

The Honorable Sander M. Levin
Ranking Member
Committee on Ways and Means
1106 Longworth HOB
Washington, DC 20515

The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
219 Dirksen SOB
Washington, DC 20510

Dear Chairman Camp, Ranking Member Levin, Chairman Baucus and Ranking Member Hatch:

As Congress gathers to address issues for the remainder of this session, of the many items that may be offered are tax increases on American oil and natural gas production. Action that would target a single industry that is so critical to America's economy should not be carelessly wedged into a last minute legislative package. While there are a number of oil and natural gas tax provisions targeted by the Obama Administration, this letter addresses a specific provision that affects small businesses and royalty owners only – repeal of percentage depletion.

Why has the Obama Administration targeted percentage depletion?

Is it one of those provisions that has been in the tax code for a century? Yes – well, almost. While cost depletion has been in the tax code since 1913, percentage depletion was added in 1926 when Congress realized that without value depletion, national resources would be lost because they would become uneconomic. But all minerals are allowed to have percentage depletion and the Administration only seeks repeal of oil and natural gas percentage depletion and coal percentage depletion. So, percentage depletion must not be bad tax policy.

Is it a tax provision that helps the big oil companies that the Administration so often singles out in its rhetoric? No, oil and natural gas percentage depletion is only available for independent producers first 1000 barrels/day of production and for royalty owners – farmers, ranchers, retirees whose families own mineral resources. Oil and natural gas percentage depletion is really a provision that affects small businesses and individuals.

These small producers operate America's marginal oil and natural gas wells. Are these wells important to America's production? You bet. Marginal oil wells account for 20 percent of US production; marginal gas wells account for about 13 percent of US natural gas production. The International Energy Agency has projected that the US could be the world's largest oil producing country by 2020 and North America could become energy independent. These changes have huge implications for America's energy security and its foreign policy. But, marginal oil and natural gas production are an integral part. Loss of percentage depletion puts marginal well production in jeopardy.

Repealing percentage depletion would impact millions of royalty owners across the United States. Royalty owners exist in every state and Congressional District. Often, royalty payments are a major component of a royalty owner's income – particularly for retirees. Elimination of percentage depletion would have the unintended impact of harming these individuals.

So, what is the Administration's rationale for repealing oil and natural gas percentage depletion? Its budget request documents have justified repeal because when the provision "…encourages overproduction of oil and gas, it is detrimental to long-term energy security…." As an Administration that touts the importance of increased American oil and natural gas production, this seems like an oddly inconsistent justification.

What all this really says is that Congress should not make quick, precipitous decisions to change the tax code that could have fundamental negative effects on America's small business oil and natural gas producers and on royalty owners. These are not issues that should be changed in the Lame Duck session of Congress.

Sincerely,

Barry Russell
Independent Petroleum Association of America

Jerry Simmons
National Association of Royalty Owners

Brian Petty
International Association of Drilling Contractors

Kenny Jordan
Association of Energy Service Companies

Kelly Robbins
Arkansas Independent Producers and Royalty Owners

Rock Zierman
California Independent Petroleum Association

Doug Flanders
Colorado Oil and Gas Association

Brad Richards
Illinois Oil & Gas Association

Ed Cross
Kansas Independent Oil & Gas Association

Don Briggs
Louisiana Oil & Gas Association

Frank Mortl
Michigan Oil and Gas Association

Dave Galt
Montana Petroleum Association

Jerry James
Ohio Oil & Gas Association

Mike Terry
Oklahoma Independent Petroleum Association

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Pennsylvania Independent Oil and Gas Association

Bruce Hinchey
Petroleum Association of Wyoming

Alex Mills
Texas Alliance of Energy Producers

Greg Kozera
Virginia Oil and Gas Association

Corky DeMarco
West Virginia Oil and Natural Gas Association

Ben Shepperd
Permian Basin Petroleum Association

Charlie Burd
Independent Oil and Gas Association of West Virginia

Charles Smith
Indiana Oil and Gas Association

Ed Longanecker
Texas Independent Producers and Royalty Owners

CC: The Honorable John A. Boehner
The Honorable Nancy Pelosi
The Honorable Harry Reid
The Honorable Mitch McConnell
The Honorable Eric Cantor
The Honorable Steny Hoyer
The Honorable Richard J. Durbin
The Honorable Jon Kyl
The Honorable Timothy F. Geithner
All Members of the Committee on Ways and Means
All Members of the Committee on Finance