ipaa
America's Oil & Gas Producers

Barry Russell
President & CEO

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The Honorable John Boehner
Speaker
U.S. House of Representatives
Washington, DC

The Honorable Harry Reid
Majority Leader
U.S. Senate
Washington, DC

The Honorable Nancy Pelosi
Minority Leader
U.S. House of Representatives
Washington, DC

The Honorable Mitch McConnell
Minority Leader
U.S. Senate
Washington, DC

Dear Speaker Boehner, Majority Leader Reid, Minority Leader Pelosi, Minority Leader McConnell:

Much has been said about the elements of a compromise to address the forthcoming expiration of the statutory debt ceiling and the challenges of reducing the federal deficit. Among the issues that have been raised are targeted tax increases on specific industries. President Obama targeted the oil and natural gas exploration and production industry in many of his recent statements. As the most active advocate for America's independent producers, the Independent Petroleum Association of America (IPAA) requests that these proposals to target a specific industry for tax increases be rejected.

Massive, billion dollar tax increases will put thousands of jobs in jeopardy and deepen our nation's dependence on unstable regions of the world to fuel our economic recovery and future growth. Such a change would have an adverse effect on America's independent oil and natural gas producers' ability to invest in new, American energy production – which also means fewer jobs and less economic growth.

Some key facts about America's 18,000 independent natural gas and oil businesses:

- ✓ **SMALL BUSINESSES:** On average, independent producers employ only 12 workers.
- ✓ **JOBS:** In 2010, almost 4 million direct, indirect and induced jobs were supported by the onshore independents' business ecosystem, accounting for over 3% of all US jobs.
- ✓ **THE ECONOMY:** The onshore independents' business ecosystem contributed $579 billion (4.0%) of US GDP in 2010.
- ✓ **TAXES:** In 2010, onshore independents' (upstream) activity generated $30.7 billion in income taxes (federal and state), sales tax and excise taxes. Additionally, independents' upstream activity led to $38.4 billion in corporate taxes, severance taxes and federal royalty payments in 2010. The entire direct/indirect/induced ecosystem of the independents generated $131 billion of federal and state taxes in 2010, a figure that will increase to $189 billion by 2020.
- ✓ **ENERGY CONTRIBUTION:** Independents - onshore and offshore - collectively develop 95% of America's oil and natural gas wells; producing 54% of domestic oil and 85% of America's natural gas, accounting for 67% of total U.S. oil and natural gas production.
- ✓ **PROPOSED TAX INCREASES:** Projected to result in 25-35% reduction in capital expenditures. While the Administration believes such a change will increase federal revenues, IPAA's assessment concludes that lost federal revenues from reduced investment would actually be *triple* the Administration's calculated increase – and state revenues would suffer as well.

Political rhetoric describes tax provisions related to oil and natural gas production as “loopholes” or “subsidies.” Two key issues that affect independent producers relate to drilling costs and percentage depletion. These are neither loopholes nor subsidies. They are mechanisms – like depreciation – that provide for capital recovery. Independent producers historically have reinvested as much as 150 percent of their American cash flow back into new American projects. Changes that limit this capital will affect the 4 million jobs associated with just America’s independent onshore investments.

For example, adopting the Obama Administration proposal to change the depreciation of drilling costs would reduce independents’ capital expenditure budgets by about 25 percent. A second, targeted oil and natural gas tax provision is the availability of percentage depletion. All mineral resources are allowed a deduction for percentage depletion. However, oil and natural gas percentage depletion is severely limited under current tax law. Only the first 1000 barrels per day of an independent’s production or a royalty owner’s is eligible for the percentage depletion deduction.

Consequently, oil and natural gas percentage depletion is a small business and landowner tax issue. Many royalty owners are farmers, ranchers and retirees who rely on their royalties for essential supplement income. Most small business independent producers are operators of America’s marginal wells – wells that produce about 20 percent of US oil and about 12 percent of US natural gas. Percentage depletion can be essential to keep these wells operating.

There are other less well known oil and natural gas production tax issues also targeted by the Administration that provide a safety net for America’s marginal wells, encourage investment with small business producers and support enhanced oil recovery.

All of these provisions need to be well understood and thoughtfully addressed in a broad tax reform debate. They should not be revised in a highly charged, rapidly thrown together legislative compromise to resolve the debt limit ceiling in the next few weeks.

Clearly, the concept of tax reform poses the potential for broad changes to tax policy. But, in such a deliberation, Congress would hopefully consider the long term implications of each change to tax policy. Making changes in the short time frame before the debt limit ceiling is addressed does not allow for appropriate consideration.

IPAA looks forward to participation in a future deliberation on tax policy that is well reasoned and fully considered.

Sincerely,

Barry Russell
President and CEO