Myth vs. Fact – Oil & Gas Subsidies

- **MYTH:** Eliminating subsidies to the oil and gas industry will raise gas prices.
  - **FACT:** Variations in gas prices are driven by the world market, and are not dependent on U.S. government policies. This includes the existing subsidies for the oil and gas industry according to multiple studies that have found that repealing oil and gas subsidies would have only a marginal impact on gas prices. Assistant Secretary of the Treasury Alan Krueger estimated in 2009 that “eliminating [oil and gas subsidies] would have an insignificant effect on world oil prices.” Analysis by the think tank Resources for the Future arrived at a similar conclusion, finding that eliminating oil and gas tax preferences would increase the world oil price by just 10 cents per barrel in 2030. This minimal increase in cost would translate to an extra expenditure of $2.17 per year on petroleum products for the average U.S. consumer. At the same time, the U.S. government – by eliminating unnecessary subsidies for oil and gas - would be saving on the order of $10 billion per year that could be invested in other national priorities like defense, transportation, or alternative energy. A Congressional Research Service report corroborates these findings. Gilbert Metcalf, Deputy Assistant Secretary for Environment and Energy at the U.S. Department of Treasury, also has said that removing U.S. tax subsidies for oil and companies will have an “imperceptible” effect on world oil supply.

The reason why eliminating subsidies would not raise gas prices is simple – the U.S. produces only a small portion of world oil, so any change in U.S. oil production would have an insignificant effect on the world oil market, which drives oil prices and therefore gasoline prices.

- **MYTH:** Eliminating subsidies to the oil and gas industry will hamstring domestic oil production.
  - **FACT:** As explained above, eliminating subsidies will have little effect on the world supply and price of oil. Consequently, consumer demand for petroleum products, like

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3 Id.
4 This value includes savings from repealing the nine subsidies specific to oil and gas (enhanced oil recovery, production from marginal wells, intangible drilling costs, tertiary injectants, passive loss limitations, percentage depletion for oil and gas wells, domestic manufacturing, geological and geophysical amortization, and refinery expensing) as well as two subsidies exploited mostly by oil and gas companies (foreign tax credits for dual-capacity taxpayers and last-in, first-out (“LIFO”) accounting).
gasoline, would not change. On the supply side, removing oil and gas subsidies is estimated to increase costs of finding and producing oil by less than 2 percent.\footnote{Testimony to Senate Committee on Finance, Subcommittee on Energy, Natural Resources, and Infrastructure. 10 Sept. 2009. Page 6. http://finance.senate.gov/imo/media/doc/091009aktest.pdf.}

- **MYTH:** The government takes in $86 million from oil and gas every day – far more than from any other business.

  Furthermore, how much the oil and gas companies pay in taxes in no way justifies the continued existence of unnecessary subsidies. Actually, the very fact that companies pay so much in taxes shows just how profitable the industry is and, consequently, how little it needs subsidies. And, as discussed below, actual domestic income tax rates paid by U.S. oil and gas corporations are far lower than commonly stated.

- **MYTH:** Oil companies pay a 43% income tax rate.
  - **FACT:** The defenders of oil and gas subsidies like to claim that oil and gas companies already pay far more than their fair share of taxes. As in all things, but especially when discussing taxes and tax rates, the devil is in the details. The standard federal corporate income tax rate is 35%, and oil and gas companies tend to pay much less than that, not more. Those that cite numbers like 43% are including taxes that these companies pay to other countries. Not only are they not paying these taxes to the U.S. government, they are also deducting these taxes via tax credits which lowers the taxes they do pay to the government. The majority of income taxes paid by oil and gas companies go overseas, so, once you subtract that amount, and the amount they’ve deducted, their domestic federal income tax rate is far less than even the standard 35% federal corporate income tax rate.\footnote{Hargreaves, Steve. “Parsing Exxon’s tax bill.” CNN. 4 May 2011. http://money.cnn.com/2011/05/04/news/companies/exxon_oil_taxes/index.htm} According to data from the U.S. Energy Information Administration, major oil and gas corporations\footnote{For a full list of companies, see http://www.eia.gov/emeu/finance/page1b.html.} paid an average federal income tax rate of 25% between 2007...
and 2009, the most recent year for which data for the whole sector is available.

Looking at individual companies makes this case even more clear. In 2010 Exxon Mobil paid a domestic federal income tax rate of just 17%, based on their U.S. pre-tax income of $7.5 billion. Literally half the standard corporate tax rate. Worse yet, in 2009, Exxon Mobil paid no U.S. federal income taxes. That’s right, 0%. This is because they took advantage of the federal subsidy that allows them to take foreign tax credits on royalties disguised as income taxes. These royalties are not taxes but are in exchange for the right to produce oil. And they paid so much in royalties to foreign governments that year that the U.S. government was left with nothing, far less than the 43% they imply they pay in taxes. Over the years 2008 to 2010, Exxon Mobil’s domestic federal income tax rate averaged just 14.2%. Other large oil companies paid similarly-low domestic federal income tax rates over that period. Chevron’s rate was 24.8%, ConocoPhillips’s was 26.9%, Apache’s was 0.6%, and Marathon Oil’s was 15.8%. None were anywhere near 43% or even close to the standard rate of 35%.

Data from the U.S. Energy Information Administration clearly shows why oil and gas companies pay such low federal income tax rates — huge tax credits including one for foreign levies. In 2009, major oil and gas companies received a $6.6 billion tax refund from the U.S. government thanks to a $23 billion write-off of foreign tax credits. Previous years tell a similar story — while major U.S. oil and gas companies paid $99.4 and $87.2 billion worldwide in income taxes in 2008 and 2007, respectively, their U.S. federal income taxes were much less - $23.3 and $28.1 billion - thanks to write-offs of

12 Pre-tax income was calculated by summing annual pre-tax income for U.S. petroleum and downstream natural gas segments and operating income for U.S. electric power segment (as pre-tax income was not provided) from Tables T-5, T-6, and T-7. Combined actual U.S. federal tax provisions for 2007, 2008 and 2009 (Table T-12: Income Taxes) were then divided by combined pre-tax income to calculate the average 2007-2009 income tax rate. Source: U.S. Energy Information Administration. “Performance Profiles of Major Energy Producers 2009.” 2009. http://205.254.135.7/finance/performanceprofiles/


18 Id. Page 50-52.


foreign tax credits of $43.5 billion and $34.4 billion, respectively.\(^{21}\) So they use these foreign payments – payments other governments charge them – to both inflate their image as taxpayers and lower their U.S. tax bills, at the same time.

Thus, a recent Wall Street Journal editorial was technically correct when it claimed, “[t]he federal Energy Information Administration reports that the industry paid some $35.7 billion in corporate income taxes in 2009.”\(^{22}\) However, the $35.7 billion in corporate income taxes\(^{23}\) were paid worldwide, and none of that amount was paid to the U.S. federal government.

Not only do oil and gas companies pay far more in foreign than domestic income taxes, their foreign income tax rates are much higher as well. According to data compiled by Citizens for Tax Justice, for the years 2008 to 2010, Exxon Mobil, ConocoPhillips, Marathon Oil, Occidental Petroleum, and Chevron all had a lower domestic income tax rate than foreign income tax rate.\(^{24}\) For instance, Exxon Mobil from 2008 to 2010 had a domestic income tax rate of just 14.2%, whereas its foreign income tax rate was 45.3%, or more than triple its domestic tax rate.\(^{25}\) ConocoPhillips’s domestic income tax rate was less than half of its foreign income tax rate between 2008 and 2010.\(^{26}\)

It’s also important to note that oil companies have a bad habit of counting taxes that they don’t actually pay, like sales taxes that we pay at the pump.\(^{27}\) Exxon Mobil, for instance, claims its 2010 total tax expense in the U.S. was $9.8 billion,\(^{28}\) but only $1.6 billion (or 1/6) of that was in actual U.S. income taxes - $1.3 billion in federal income taxes and $0.3 billion in state income taxes.\(^{29}\) Much of the rest came out of our pockets, every time sales tax was added to our gas bills.

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\(^{25}\) *Id.*

\(^{26}\) *Id.*


**MYTH:** The oil industry is being picked on – many of the subsidies that oil and gas gets are economy-wide and benefit other sectors as well.

- **FACT:** Of the nine subsidies\(^\text{30}\) that go specifically to the oil and gas industry, only one also goes to other industries – the domestic manufacturing tax credit. The other eight subsidies apply exclusively to oil and gas. These include the percentage depletion allowance for oil and gas wells and the deduction allowance for intangible drilling costs. Setting aside the domestic manufacturing tax credit, oil and gas companies still receive over $2 billion in subsidies each year.

But even in the case of the domestic manufacturing credit, as it applies to oil and gas companies it allows for the deduction of 6% of the income derived from oil and gas extraction in the U.S. – hardly a “manufacturing” activity. While such a subsidy may make sense to encourage manufacturers to stay in or move to the U.S., as manufacturing operations can move fluidly from one nation to the other, oil and gas production cannot move fluidly from one nation to another, as the oil and gas resources themselves can’t shift. Therefore, applying this credit to oil and gas does not serve the same purpose.

In addition to the nine subsidies that specifically target the oil and gas industry, there are two that are economy-wide by definition, but due to their design are mostly exploited by the oil and gas industry. These subsidies are allowances for last-in, first-out (“LIFO”) accounting and foreign tax credits for dual capacity taxpayers. Of the combined $6.3 billion expenditure per year under these two subsidies, the majority goes to oil and gas companies.\(^\text{31}\)

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\(^{30}\) Those subsidies are enhanced oil recovery, production from marginal wells, intangible drilling costs, tertiary injectants, passive loss limitations, percentage depletion for oil and gas wells, domestic manufacturing, geological and geophysical amortization, and refinery expensing.