Senate Finance Committee – Tax Reform: Impact on U.S. Energy Policy
The Honorable Don Nickles, U.S. Senate 1981-2004
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Chairman Baucus, Ranking Member Hatch, and members of the committee, thank you very much for inviting me to testify today. As a former member of this committee, it is a particular honor and privilege to be here. I love the Senate, and I loved the ten years I spent on this committee.

When I left the Senate seven years ago, Mr. Chairman, I started a company called The Nickles Group. While the opinions I give today are solely my own, I believe it is important to disclose that I and my company proudly represent some of the best energy companies in the world, including ExxonMobil, Anadarko Petroleum, National Oilwell Varco, ITC Holdings, and a coalition of electric industry companies called COMPETE. I am also a member of the corporate boards of Chesapeake Energy, Valero Energy, and the Washington Mutual Investors Mutual Fund.

Mr. Chairman, our nation faces an enormous economic and fiscal crisis that requires the strongest leadership from the President, the Congress, and most specifically this committee. I am very pleased that you are working on tax reform, as it is an essential component to both getting our economy moving again and addressing our massive deficit and debt. I would encourage you to work even harder, and more quickly. I am also pleased with all the work on tax reform occurring in the House under the leadership of Ways and Means Chairman Dave Camp. Congressional committees are all too often ignored these days by congressional leaders and regular order is abandoned. That strategy is proven to fail, and tax reform will almost certainly fail if these two important committees are not allowed to play their appropriate leadership role.

Mr. Chairman, I am also very encouraged with the degree of general agreement that appears to be growing on a bipartisan basis in Congress on the issue of corporate tax reform. Nearly everyone acknowledges that our high corporate

rate and antiquated international tax system make our companies uncompetitive. The debate now is not whether to reduce the corporate rate – but by how much, and that is a great start!

Today I will briefly discuss the convergence of my two favorite policy subjects – energy policy and tax policy. As mentioned previously, I was a member of this committee for ten years, I was a member of the Senate Energy and Natural Resources Committee for twenty-four years, and I have worked in and around the energy industry my entire life. I originally ran for the Senate in large part because I wanted to reverse President Carter's energy policies that were hostile to domestic energy production, picked winners and losers, and stifled competition. I was mostly successful in my efforts, but unfortunately today I see our current President seeking to repeat many of the energy and tax policy mistakes of the Carter era.

This is an exciting time for U.S. energy industry with amazing technology-driven revolutions in shale gas, shale oil, and offshore exploration. I am particularly proud that many Oklahoma energy companies including Chesapeake, Devon, Sandridge, and of course Continental Resources are leading the way. These companies are investing billions of dollars and creating thousands of new jobs.

Mr. Chairman, if you do tax reform correctly, there will never be a need to hold an "energy" tax hearing ever again, because tax reform should seek to treat energy companies and the products they produce just like everybody else. No subsidies, and no penalties. If the tax system you devise encourages investment (as it should), energy companies will benefit just like other companies. If a lower corporate rate and simplified territorial system make U.S. companies more competitive (which it will), energy companies will benefit just like other companies.

Just as the tax code should not subsidize energy, neither should it impose punitive penalties on energy companies as the President's tax proposals seek to do.

The President loves to talk about tax "subsidies" received by oil and gas companies. By doing so, I suppose he hopes to create the impression with voters that our energy companies are receiving checks from the government. In fact, the President has it exactly backwards. U.S. oil and gas companies pay more than $86 million dollars EVERY DAY to the federal government in income taxes, rents, royalties, and lease payments. Last year, the income tax expenses for those companies averaged 40.6 percent, compared to 25.1 percent for other S&P industrial companies. Who is subsidizing whom?

The hostility toward domestic oil and gas companies from this administration has no foundation in tax or economic policy. In Treasury's FY2010 Green Book justifying the President's tax proposals, they had this to say about intangible drilling costs, or IDC's: *"The expensing of IDCs, like other oil and gas preferences the Administration proposes to repeal, distorts markets by encouraging more investment in the oil and gas industry than would occur under a neutral system. <u>To the extent expensing encourages overproduction of oil and gas, it is detrimental to long-term energy security</u> and is also inconsistent with the Administration's policy of reducing carbon emissions and encouraging the use of renewable energy sources through a cap-and-trade program."*

Mr. Chairman, I am not quite sure why this President believes we are in danger of overproducing oil and gas, and I am completely confused about how that would be detrimental to long-term energy security.

Most of the President's energy tax proposals are purely punitive. Oil and gas companies already receive a smaller benefit from the Section 199 manufacturing deduction than other manufacturers, but the President believes even that should be taken away. While I personally believe all corporations should pay the same rate regardless of whether they are a manufacturer, retailer, or service provider – but it makes no sense to take that benefit away from one industry in the absence of comprehensive tax reform.

Other proposals from the President would be specifically harmful to independent oil and gas producers, such as his proposal to lengthen the recovery period intangible drilling costs.   IDCs are primarily wages, and they are the research and development costs of energy producers. Other companies can not only deduct, but often get a tax credit for their R&D spending, but the President thinks energy companies should be required to capitalize these costs. That makes no sense whatsoever, Mr. Chairman, and I can tell you that the best way to kill the current shale gas revolution that is creating millions of jobs all over the country would be to enact the President's IDC proposal.

Finally, Mr. Chairman, the President has one particularly onerous proposal that would penalize only U.S.-based oil and gas companies and disadvantage them relative to their foreign competitors. Known as the "dual capacity" provision, this proposal would deny U.S. oil and gas companies a credit for taxes paid to foreign governments, causing them to be taxed twice. This higher tax burden means U.S. companies would be disadvantaged as they compete to win access to oil and gas production projects all over the world. Now why, Mr. Chairman, would we want ExxonMobil, ConocoPhillips, or Chevron to be disadvantaged in their worldwide competition with PetroChina, Lukoil, Total, BP, and Shell?

In summary Mr. Chairman, I encourage you and this committee to continue working as hard as you can on tax reform, because it is so very necessary. And as you work to lower rates, broaden the base, and update our international tax scheme, please endeavor to treat U.S. energy companies and their products the same as everyone else.

Let's eliminate the need for "energy" tax hearings.