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:

On behalf of the undersigned, representing millions of American workers, energy producers and consumers, we are writing out of concern that future tax reform efforts could seek to limit or even eliminate the current deductibility of intangible drilling costs ("IDCs"). As you know, IDCs are those costs incurred by an operator of an oil and gas well for the labor, fuel, repairs, hauling and other non-salvageable expenses required for the drilling of oil and gas wells. They are ordinary and necessary expenses and are no different from expense deductions taken by other businesses. The tax code currently allows operators to deduct these ordinary and necessary business expenses as they are incurred.

Finding and producing domestic oil and natural gas are vitally important to the U.S. economy. This industry supports millions of U.S. jobs, accounts for almost 8 percent of the nation's GDP and invests heavily each year in domestic equipment and facilities. Moreover, the top 50 oil and gas exploration and production companies spent another $100 billion on acquiring access to various U.S. properties for future development.[1] This investment capital is enabling America to produce a greater portion of our energy needs than we have in decades.

This level of investment needs to be made on a recurring basis in order for the industry to maintain and continue to grow the production of American energy. However, due to the large capital outlays that are required, a stable and predictable stream of cash flow is critical to the economics supporting these domestic projects. Similar to research and development efforts, trial and error is the only means of determining with absolute certainty the presence of hydrocarbons in reservoir rock or sand. In addition, just like any research project, the investment analysis for exploration and drilling is sensitive to risk, capital cash needs and the ability to recover costs for future reinvestment.

We have great concern with any possible modification of the tax laws that would limit or eliminate the current deductibility of IDCs. Restrictions on expensing IDCs would discourage new American oil and natural gas exploration and undermine America's energy security. Companies would have no choice but to significantly lower their drilling budgets, resulting in lower production of American energy resources and higher energy prices for consumers and businesses. Additionally, the loss of economic activity

[1] US oil and gas E&P benchmark study, 2010. http://www.ey.com/US/en/Industries/Oil---Gas/US-oil-and-gas-E-P-benchmark-study

associated with changes to the current deductibility of IDCs could result in less revenue to the federal government. The $87 million in daily rent, royalty, lease, and tax payments this industry makes could greatly be reduced. New investment in American energy is critical to meeting future energy demand, boosting U.S. energy security, and protecting and creating jobs.

The companies that would be impacted by any modification of the current deductibility of IDCs don't stop at investing in America's infrastructure; they invest in America's workforce as well. During the economic recession, as the U.S. economy was struggling to find its footing, the oil and natural gas industry was there to provide stability in an otherwise uncertain economy. From the start of the recession (roughly 2006 through 2011), the US oil and natural gas industry directly created 119,511 jobs (a growth of 13 percent). When compared to other sectors which lost over 4.5 million jobs (a decline of 20 percent), the industry continued to do its part. It does not just provide employment; it provides high wages as well. The average annual non-service station salary for the industry in 2011 was $92,645. When compared to the average private-sector salary nationwide of almost $48,000, the oil and natural gas industry provides 93 percent higher wages. This isn't a year-by-year fluke. During this same recessionary period from 2006 to 2011, the wages in the industry grew by over 20 percent.

Tax reform should foster economic health and job creation. A limitation of the current deductibility of ordinary and necessary business expenses for companies engaged in the exploration and production of domestic natural gas and oil resources would have the opposite effect. We encourage you to oppose any movement to change the treatment of IDCs.

Thank you for your attention to this matter. We all look forward to working with you moving forward.

Sincerely,

V. Bruce Thompson
President
American Exploration & Production Council

Barry Russell
President
Independent Petroleum Association of America

Dorothy Coleman
Vice President, Tax and Domestic Economic Policy
National Association of Manufacturers

David Holt
President
Consumer Energy Alliance

Brian J. Petty
Executive Vice President – Government Affairs
International Association of Drilling Contractors

Chris Cragg
Chairman
Petroleum Equipment Suppliers Association

Randall Luthi
President
National Ocean Industries Association

Kenny Jordan
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American Petroleum Institute

R. Skip Horvath
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Natural Gas Supply Association

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Pennsylvania Independent Oil and Gas Association

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Texas Alliance of Energy Producers

Edwin Longanecker
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Executive Director
Independent Oil and Gas Association of West Virginia

Nicholas “Corky” DeMarco
Executive Director
West Virginia Oil and Natural Gas Association

Bruce Hinchey
President
Petroleum Association of Wyoming

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 Ken Salazar
The Honorable Timothy F. Geithner
All Members of the Committee on Ways and Means
All Members of the Committee on Finance