

Comparison Of Tax Provision For Majors and Independents

Tax Provision	Major Integrated Company	Independent producer
Expensing of intangible drilling costs	Not available. Majors raise their drilling capital internally. Stock holders provide funding. Most of their revenues comes from foreign operations.	Able to expense drilling costs in the year incurred. Important to smaller companies that have to drill with personal money, because the quicker costs recouped the more wells they can drill.
Percentage depletion	Has not been available to majors for more than 30 years.	Helps small producers keep marginal wells (15 barrels or less per day) producing. Percentage depletion is limited to 15% of gross oil and gas income. Also limited to first 1,000 b/d. Limited to net income from marginal properties through 2009. Amount deducted for depletion cannot exceed 65% of taxpayers income before the deduction.
Repeal of passive loss exception for working interests	Does not apply.	Working interest owners are investors who share the costs in drilling and production. Current tax law allows WI owners to be classified as an active, rather than passive, investor if they do not have limited liability.
Geological and geophysical costs	Majors must amortize costs over 7 years.	Independents currently must amortize G & G costs over 2 year period. The economic life of a property for independent is considerably less than 7 years, which is the new proposal.
Marginal well tax credit	Never been in effect because prices have never reached the trigger point since enacted.	Never been in effect because prices have never reached the trigger point since enacted.
Enhanced Oil Recovery (EOR) tax credit	Available to majors, but has been rarely used.	Available to independents, but not many have decided to apply for the credit because of bureaucratic red tape and the costs to implement.
Manufacturing tax deduction	Designed to encourage creation of jobs in U.S. rather than taking employees overseas.	This is a current benefit to independents but it is insignificant.
Excise tax on Gulf of Mexico production.	Majors are still active in the Gulf of Mexico somewhat, but most are pulling out.	Independents are drilling most of the new wells in the Gulf today. They would be hit hardest by a new tax.

Key points to remember: Independents raise capital from U.S. sources – most of it personal – while majority of majors’ income comes from foreign sources.

Independents drill 90% of the wells in the U.S. and produce 82% of the natural gas and 68% of the oil. Proposed tax changes would drive most small independents out of business, because they would not be able to raise capital for new ventures. Dry hole costs must be deductible. If not, no one will risk drilling dry holes looking for new production.