

[COMMITTEE PRINT]

TAX REFORM BILL OF 1974

Descriptions of Tentative Decisions
Corresponding to Sections of Draft Bill

TITLE IV—OIL AND GAS ENERGY PROVISIONS

PREPARED FOR THE USE OF
THE COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

BY

THE STAFF

OF THE

JOINT COMMITTEE ON INTERNAL
REVENUE TAXATION



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TITLE IV—OIL AND GAS ENERGY PROVISIONS

In the first three pamphlets issued, the material appearing in the press releases has been rearranged in the order in which the material appears in the tentative draft bill. However, the press releases with respect to the oil and gas energy provisions appear in the press release only to the extent there were modifications in the Oil and Gas Energy Tax Act of 1974 as reported by the Committee on Ways and Means. This meant the press release material in this case does not by itself represent a description of these provisions. As a result, the general description which follows has been taken from the summary of the committee report on the Oil and Gas Energy Tax Act but modified to take into account changes in these provisions as previously announced in the press releases.

PART I—TAX TREATMENT OF DOMESTIC OIL AND GAS PRODUCTION

Sec. 411. Windfall Profits Tax; Plowback Credit.

“Windfall profits” tax.—An excise tax of 5 years duration is imposed on the “windfall profit” element of the price of domestically produced crude oil. The windfall profit, for this purpose, begins at fifty cents per barrel above the ceiling price established by the Cost-of-Living Council as of December 1, 1973 (on the average about \$4 per barrel). The level at which the tax is to apply rises so that the tax is gradually phased out over the 5-year period. Graduated rates ranging from 10 percent to 85 percent are imposed on these windfall profits. The windfall profits tax before taking account of reductions for reinvestment is estimated at \$5.0 billion in 1975, \$6.5 billion in 1976, and \$5.2 billion in 1977 and a total of \$18.1 billion over the period 1975 through 1979.

Credit for reinvested earnings.—A credit for certain types of investments is allowed to reduce the windfall profits tax otherwise payable. This is known as a “plowback credit”. After 1975 this plowback credit may offset the entire windfall profits tax liability. In 1975 the credit may not exceed 50 percent of the tax plus the proportion of the remaining 50 percent represented by the production of 3,000 barrels a day or less. Investment which qualifies for reduction of this tax includes expenditures for: (1) intangible drilling and development costs and geological and geophysical costs; (2) depreciable assets used in exploration and development of oil or gas (including oil shale); (3) the conversion of oil shale, coal, or liquid hydrocarbons into oil or gas; (4) the refining of oil or gas; (5) oil or gas pipelines and related facilities; (6) secondary or tertiary recovery of oil or gas; and (7) to a limited extent, the acquisition of oil and gas leases (other than offshore leases). It is estimated that this provision in combination

with other provisions will reduce the net revenue gain from the windfall profits tax to \$1.1 billion in 1975, \$0.5 billion in 1976, and \$0.4 billion in 1977 and for the period from 1975 through 1979 to about \$2.1 billion.

Sec. 412. Phaseout of Percentage Depletion for Domestic Oil and Gas Production.

Percentage depletion for domestic oil and gas is generally phased out by reducing the 22 percent depletion rate to 15 percent in 1974, 8 percent in 1975, and zero thereafter. However, under certain conditions, a taxpayer may elect one of three provisions, any one of which holds the depletion rate on oil to 15 percent until 1979, at which time it is to be reduced to zero. The first of these three provisions relates to production of up to 3,000 barrels a day, the second to production from "stripper" wells (those producing 10 barrels or less per day), and the third to production from wells located north of the Arctic Circle.

In the case of federally regulated natural gas, the rate of percentage depletion is to remain at 22 percent until the price of this gas, on a BTU equivalency basis, equals or exceeds the price of free oil. In the case of other natural gas, the rate of percentage depletion generally is to go down as specified above in the case of oil—to 15 percent in 1974, 8 percent in 1975 and zero in 1976. However, the rate is to remain at 22 percent as long as fixed price contracts in force on April 10, 1974, continue in effect.

The estimated revenue gain from the phaseout of percentage depletion on domestic oil and gas production is approximately \$600 million in 1974, \$900 million in 1975, \$1.6 billion in 1976, \$1.9 billion in 1977, \$2.3 billion in 1978 and \$3.3 billion in 1979, for a total of \$10.5 billion for the period from 1974 through 1979.

Other changes include a provision for expensing, rather than capitalizing, geological and geophysical costs after 1976, the repeal of the limitation of percentage depletion to 50 percent of net income, and assurance that geothermal deposits, if eligible for percentage depletion under present law, are not to be affected by the bill.

Sec. 413. Treatment for Purposes of the Investment Credit of Certain Property Used in International or Territorial Waters.

The bill also eliminates the investment credit for seagoing drilling rigs in the case of future orders, except those used in the waters of the northern portion of the western hemisphere.

PART II—TAX TREATMENT OF FOREIGN OIL AND GAS PRODUCTION

Sec. 421. Repeal of Percentage Depletion in Case of Foreign Oil and Gas Wells.

Percentage depletion on income from foreign oil and gas production is repealed for 1974 and subsequent years. The estimated revenue gain from this provision is \$40 million a year beginning in 1974 or a total of \$240 million in the period 1974 through 1979.

Sec. 422. Limitation on Foreign Taxes Attributable to Foreign Oil and Gas Extraction Income; Separate Computation of Foreign Tax Credit for Oil and Gas Related Income.

Foreign tax credits from foreign oil and gas extraction income are limited to a level of 10 percent above the U.S. rate (52.8 percent). The excess credits which are allowable may only be used to offset United States tax on foreign oil-related income. These rules generally are applicable for 1974 and subsequent years. The estimated revenue gain from this provision is \$300 million a year beginning in 1974, or a total of \$1.8 billion for the period 1974 through 1979.

Repeal of per country limitation.—The limitation on the foreign tax credit, which permits foreign losses to be offset against domestic income while foreign tax credits are claimed on foreign income in other countries, is repealed effective for 1975 and subsequent years. The estimated gain from this provision is \$120 million a year beginning in 1975, or \$600 million in the period 1975 through 1979.

Recapture of losses offset against domestic income.—To the extent foreign oil-related losses may still offset domestic source income with the repeal of the per country limitation (referred to above), the losses in effect are to be recaptured in subsequent years when foreign oil-related income is earned or foreign oil-related assets are disposed of. This applies to losses incurred in 1975 and subsequent years. The estimated revenue gain from this provision is \$10 million in 1977 and \$20 million a year thereafter, resulting in \$50 million of estimated revenue gain in the years 1977 through 1979.

Sec. 423. Denial of DISC Benefits With Respect to Energy Resources.

DISC (Domestic International Sales Corporation) tax-deferral benefits are denied to income from export sales of oil, gas, coal, uranium and their primary products after March 28, 1974. The estimated revenue gain from this provision is \$20 million a year beginning in 1974, or \$120 million for the period 1974 through 1979.

Sec. 424. Imposition of Quantitative Limitations, Duties, Taxes, or Fees on the Importation of Petroleum and Products Derived From Petroleum.

The right of the President to impose any quota, duty, tax or fee on the importation of petroleum is to be restricted to cases where the price of the imported petroleum is equal to or less than the price of petroleum produced in the United States and the goal of national self-sufficiency would be adversely affected without the action. Similarly, any duty, tax or fee imposed on gasoline or other products derived from petroleum may not exceed the charge currently applicable to petroleum unless the President determines the action is necessary to offset the cost advantage of refineries located outside of the United States. The quota, duty, tax, or fee provided in either of the two situations referred to above may not be on a discriminatory basis except: (1) to encourage new refinery capacity in the United States; (2) to preserve the competitive position of small refineries, independ-

ent marketers or the petrochemical industry; (3) because of considerations of national security; or (4) to favor imports from possessions of the United States. Provision is also made that Congress may override any Presidential action in these areas. The estimated revenue loss from this provision is \$30 million in 1974, \$80 million in 1975, \$130 million in 1976 and \$1.3 billion in the period from 1974 through 1979.

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