

Texas Alliance of Energy  
Producers  
Fiscal Policy of the Obama  
Administration & Impact  
on the Oil & Gas Industry

Jeff Wright - April 22, 2009



# Agenda

- Introduction
- American Recovery and Reinvestment Act
- Overview of President Obama's Budget
- Next Steps

# Monetary vs. Fiscal Policies

## Monetary Policy

Monetary policy is under the control of the Federal Reserve System (our central bank) and is completely discretionary. It is the **changes in interest rates and money supply** to expand or contract aggregate demand.

In a recession, the Fed will lower interest rates and increase the money supply.

In an overheated expansion, the Fed will raise interest rates and decrease the money supply.

## Fiscal Policy

Fiscal policy is **changes in the taxing and spending of the federal government** for purposes of expanding or contracting the level of aggregate demand.

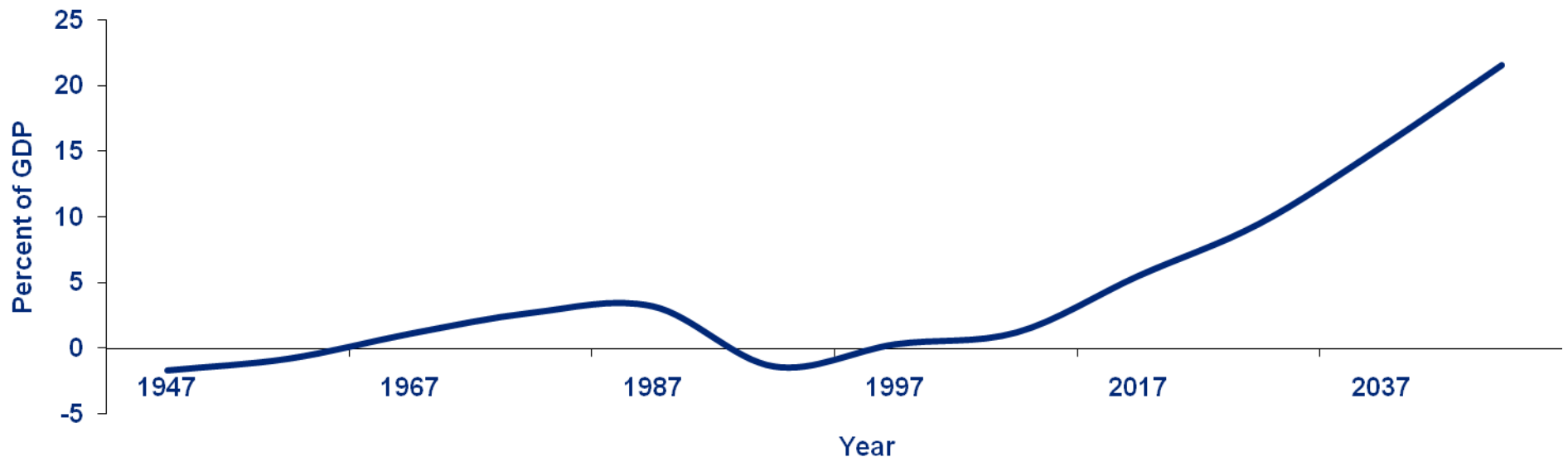
In recession, an expansionary fiscal policy involves lowering taxes and increasing government spending.

In an overheated expansion, a contractionary fiscal policy requires higher taxes and reduced spending.

# Deficit as % of GDP 1947-2047

As of September 2008

- By 2027, without tax increases and entitlement reforms, the only way to balance the budget would be to eliminate all “discretionary” spending (including military spending)
- By 2047, tax receipts would no longer be sufficient to service even the interest on national debt



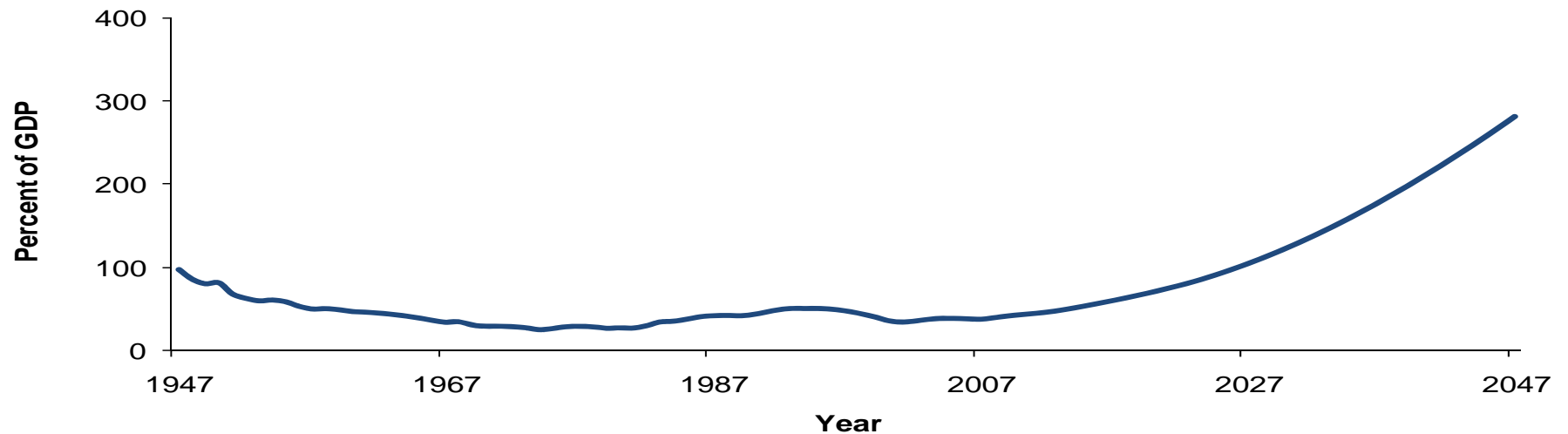
Sources: OMB Historical tables and GAO September 2008 Alternative Analysis

negative % = budget surplus

# Public Debt as % of GDP 1947-2047

As of September 2008

- Pre-stimulus, the government's debt on track to exceed 100 percent of GDP by 2027
- Pre-stimulus, Social Security expenditures on track to exceed payroll tax receipts by 2017



Sources: OMB Historical tables and GAO September 2008 Alternative Analysis

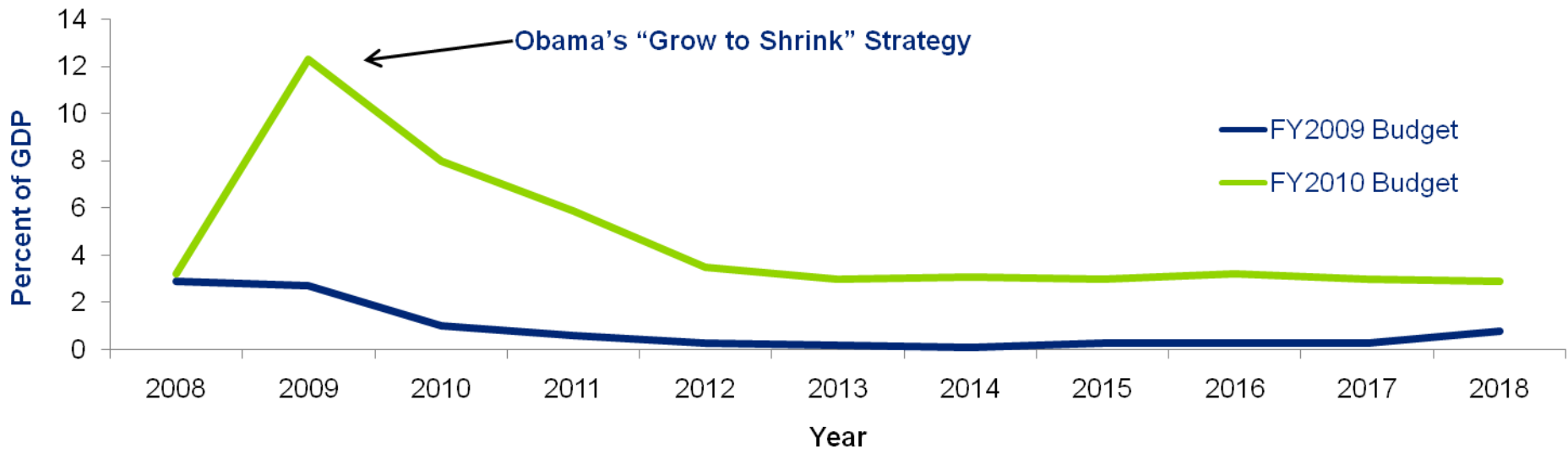
# Priorities as Articulated by President Obama and Advisors



# Change in Deficit and Debt Since FY2009 Budget

	Deficit	Public Debt
<b>FY2009 Projection</b> (as stated in the FY2010 Obama Budget published on February 26, 2009)	\$1.7 trillion, or equal to 12.3 percent of GDP	\$8.4 trillion, or equal to 58.7 percent of GDP
<b>FY2009 Projection</b> (as stated in the FY2009 Bush Budget published on February 4, 2008)	\$407 billion, or equal to 2.7 percent of GDP	\$5.9 trillion, or equal to 39 percent of GDP

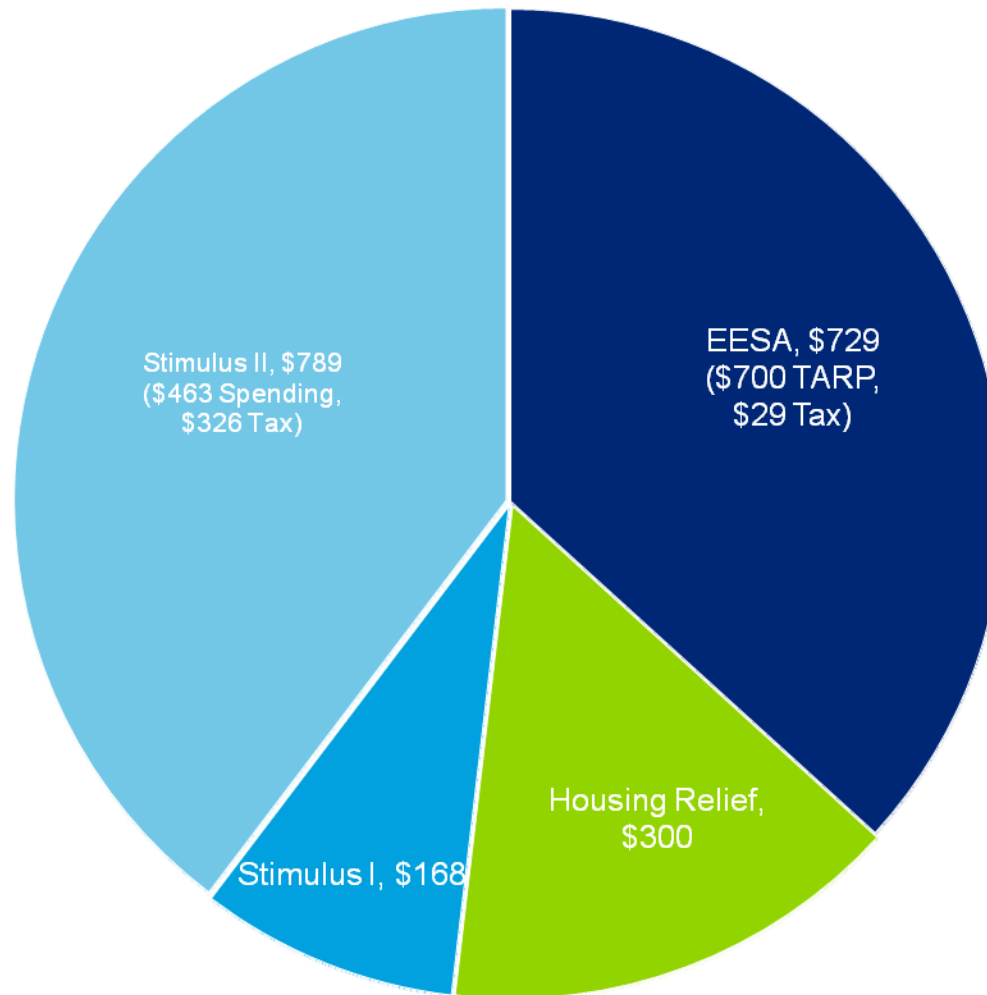
**Comparison of Deficit Projections**



Sources: FY2010 and FY2009 Budget Tables; CBO March 2008 Analysis of President's FY2009 Budget Proposals

# Recent government fiscal initiatives outside normal processes

Total Fiscal Initiatives: \$1.986 Trillion



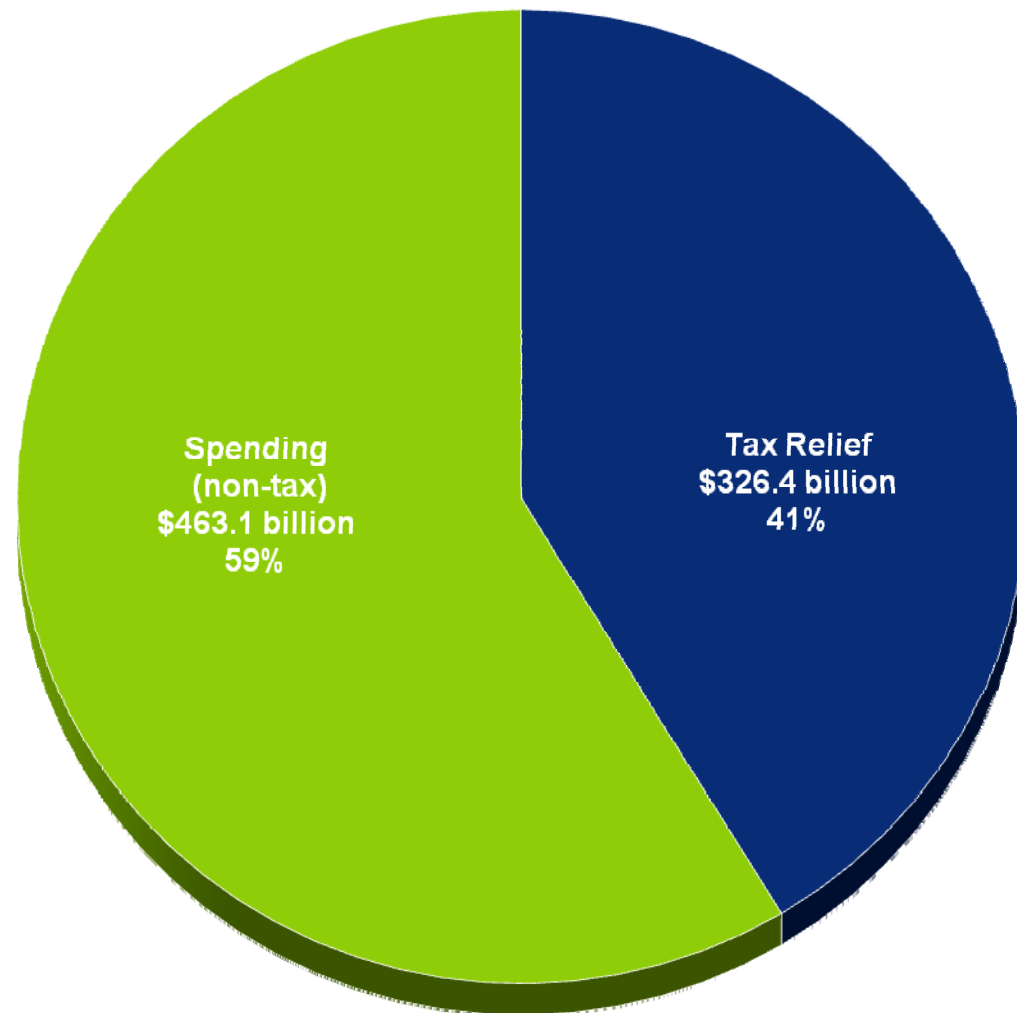
Numbers in billions of dollars

# ARRA – American Recovery and Reinvestment Act

# Stimulus II: american recovery and reinvestment act (P.L. 111-5)

- Enacted February 17, 2009
- Total Cost: \$789.5 billion

**Composition of Total Cost**

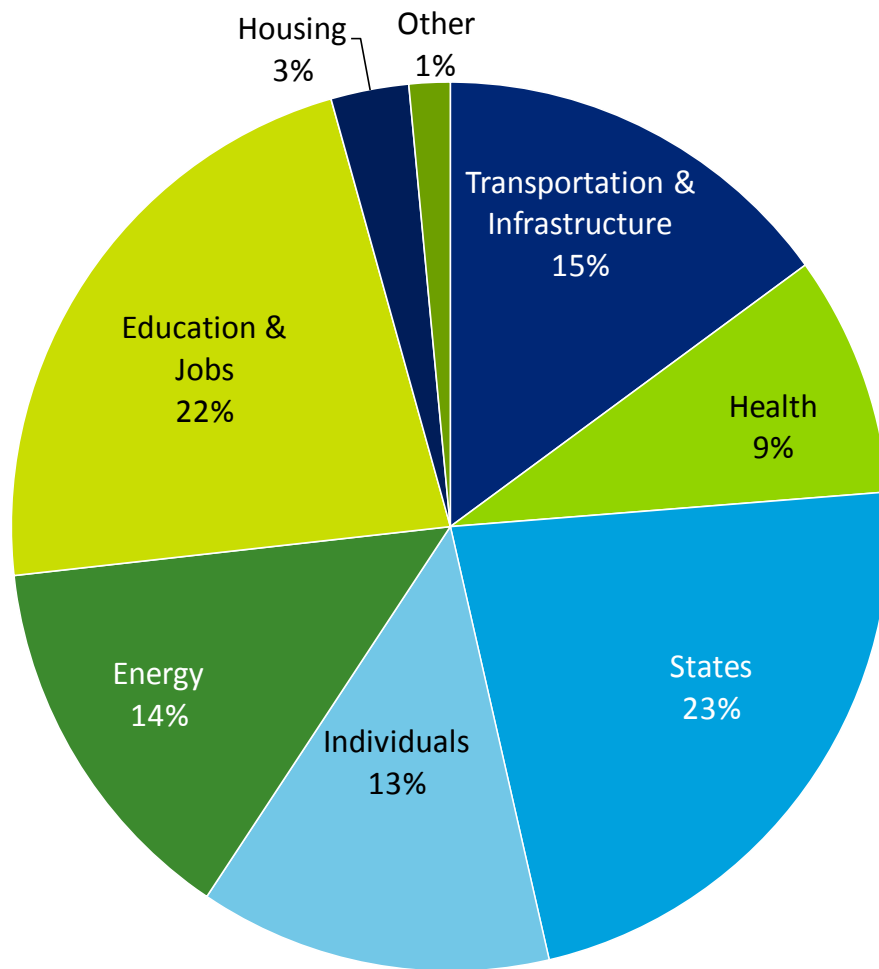


# Tax provisions in the ARRA

Provision	10-year Revenue Estimate
<b>Key Business Provisions</b>	
Extends 50 percent bonus depreciation through 2009	<b>\$5.1 billion</b>
Extends election to accelerate AMT and R&D benefits in lieu of bonus depreciation	<b>\$805 million (Total: \$5.9 billion)</b>
<b>Key Energy Provisions</b>	
Extends Section 45 production tax credit through 2012	<b>\$13.1 billion</b>
Creates new advanced energy investment credit under Sec. 48	<b>\$1.6 billion</b>
Allows temporary investment tax credit in lieu of the production tax credit	<b>\$285 million</b>
Provides grants for energy property in lieu of production tax credit/investment tax credit	<b>\$5 million</b>
Modifies storage requirement for carbon dioxide sequestration credit	<b>Negligible Revenue Effect</b>
Increases the credit for non-hydrogen alternative fuel vehicle refueling property	<b>\$54 million (Total: \$15.1 billion)</b>
<b>Key Individual Provisions</b>	
Provides one-year AMT patch	<b>\$69.8 billion</b>
Creates two year "Make Work Pay Credit" <b>(largest tax incentive in bill)</b>	<b>\$116.2 billion</b>
Extends first-time homebuyer credit, increases amount to \$8,000, and removes repayment requirement	<b>\$6.6 billion</b>
Allows deduction for state sales tax, and excise tax on purchase of qualified motor vehicle	<b>\$1.7 billion (Total: \$194.3 billion)</b>

# Spending in the American Recovery and Reinvestment Act of 2009

- The \$463.1 billion of spending in the bill can be broken down into the following broad categories:



Category	Amount
Transportation and Infrastructure	\$69.4 billion
Health	\$40.6 billion
States	\$104.8 billion
Individuals ("transfer payments")	\$60.1 billion
Energy	\$64.3 billion
Education and Jobs	\$103.6 billion
Housing	\$13.3 billion
Other	\$7 billion

# ARRA Spending on Energy

## Energy Spending Highlights

### Energy Efficiency

Federal building construction and repair including installation of photovoltaic cells (solar panels) on rooftops	<b>\$4.5 billion</b>
Weatherization Assistance Program	<b>\$5 billion</b>
Energy Department R&D, including \$800 million for biomass energy technology development and \$400 million for geothermal projects	<b>\$2.5 billion</b>
Transportation electrification	<b>\$400 million</b>

### Energy Production

Loan guarantees to private entities to fund alternative energy research, including biofuel projects	<b>\$6 billion</b>
R&D and demonstration of carbon sequestration	<b>\$3.4 billion</b>

### Energy Transmission

Implementation of Smart grid technologies	<b>\$4.5 billion</b>
Authority for hydroelectric transmission projects	<b>\$3.25 billion</b>

# Additional energy tax provisions

Code	Provision	Description
§ 25C § 25D	Non-business energy property & residential energy-efficient property	<ul style="list-style-type: none"> <li>Increases credit from 10% to 30%; aggregate limitation \$1,500 for 2009 and 2010</li> <li>Removes the maximum individual credit amount for residential energy-efficient property (30%)</li> </ul>
§ 30D § 30	Qualified plug-in electric motor vehicles, Certain plug-in electric vehicles	<ul style="list-style-type: none"> <li>Increases credit from 30 percent to 50 percent</li> <li>Modifies and increases tax credit (10%; \$2,500 limit)</li> </ul>
§ 30B	Alternative motor vehicle credit	<ul style="list-style-type: none"> <li>New credit for conversion to plug-in vehicle</li> <li>Creditable against AMT</li> </ul>
§ 30C	Alternative fuel vehicle refueling property credit	<ul style="list-style-type: none"> <li>Expands the maximum available credit from \$30,000 to \$200,000 for hydrogen refueling property and from \$30,000 to \$50,000 for nonhydrogen property</li> </ul>
§ 48C	Energy Credit	<ul style="list-style-type: none"> <li>30% ITC for eligible property placed in service during the taxable year which is part of a “qualifying advanced energy project.”</li> </ul>
§ 54C	Clean renewable energy bonds	<ul style="list-style-type: none"> <li>Additional \$1.6 billion of new clean renewable energy bonds to finance facilities that generate electricity from certain renewable resources</li> </ul>
§ 54D	Qualified energy conservation bonds	<ul style="list-style-type: none"> <li>\$2.4 billion in new qualified energy conservation bonds, available for a variety of capital expenditures or conservation expenditures related to reduction of energy consumption, etc.</li> </ul>
§ 45Q	Carbon dioxide sequestration	<ul style="list-style-type: none"> <li>Limitation of credit to only that carbon dioxide which is sequestered in <i>secure</i> geologic storage</li> </ul>

# Bonus depreciation

## ARRA & Bonus Depreciation

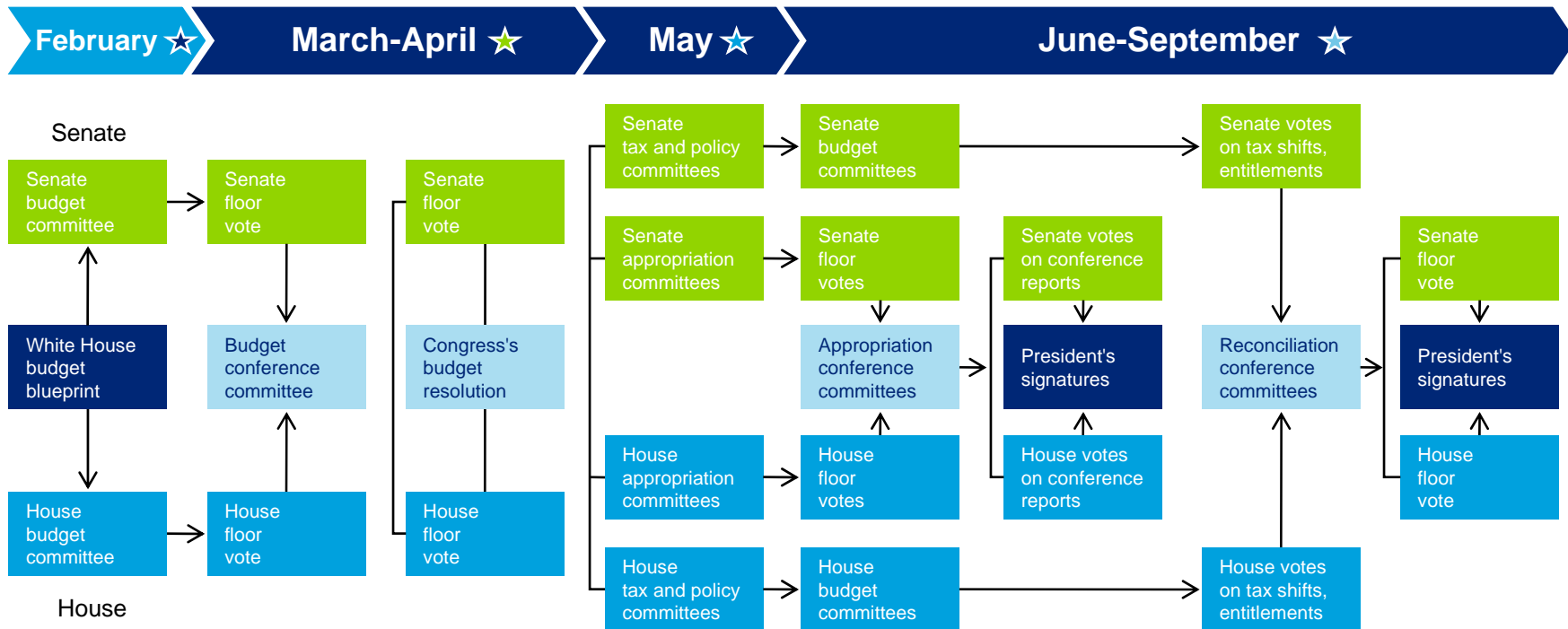
- One year extension of 50% bonus depreciation under IRC § 168(k)(1)
- Now applies to qualified property placed in service during 2008 or 2009 (or in 2010 for certain long-lived property)
- Original-use and binding contract rules apply
- See IRC § 68(k)(2) and Treas. Reg. § 1.168(k)-1
- Bonus depreciation automatically applies for regular tax and AMT purposes, unless taxpayer “elects out” for an entire class of property

## ARRA & Credit in Lieu of Bonus Depreciation

- One year extension of IRC § 168(k)(4)
  - Election now available for qualified property placed in service between April 1, 2008 – December 31, 2009 (or in 2010 for certain long-lived assets)
- Credit equals 20% of forgone additional depreciation
  - Not to exceed the lesser of (a) 6% of carryforward AMT credits and R&D, or (b) \$30 million
- Straight-line depreciation required if election made
- Separate election and credit computation for property placed in service in 2008 or under H.R. 1
- Note: Controlled-group rule (using > 50% ownership test) and complex time and manner rules governing elections
  - See Rev. Proc. 2009-16

# Overview of President Obama's Budget Proposal

# Stages of the Congressional Budget Process\*\*



- ★ February – The president submits his budget request to congress. It contains detailed information on how the White House wants to spend public funds over the next several years. The House and Senate budget committees open hearings with administration officials to develop their own fiscal priorities.
- ★ March – April – The budget committees formulate separate “budget” resolutions. Which must be passed on the House and Senate floors before a conference committee is formed to work out the difference between the two versions  
Both chambers must approve the compromise version known as the concurrent budget resolution. The resolution sets targets but is not formally a law.
- ★ May – The budget resolution instructs the appropriations committees on how to allocate discretionary funds – those that must be enacted each year. In addition, tax policy committees may plan legislation to comply with requested changes in budget changes for taxes and “entitlements” such as food stamps and veterans benefits. The legislation is referred to as the budget “reconciliation”.
- ★ June-September – Each appropriations bill must be approved by the House and Senate Floors before heading to a conference committee to work out the differences. Separately, for tax changes and entitlement spending, the tax and policy committees forward their recommendation to the budget committees, which must approve the reconciliation bill before they can move to the next stage.

When a compromise appropriations bill passes in the House and Senate, it goes before the president, who may sign it or veto it. Often, several appropriation bills will be grouped together into a single Omnibus bill for passage.

The parallel reconciliation legislation for taxes and entitlement spending must be approved on the House and Senate floors before heading to conference committees.

When the compromise reconciliation legislation on taxes and entitlement spending passes in the House and Senate, it goes before the president who may sign it or veto it, sending it back to the conference committee for more work.

Source: Wall Street Journal article “White House to Hunt for New Tax Revenues”

# Overview of FY2010 budget blueprint

## Budget Proposal Release

- Released February 26, 2009
- Detailed Budget not expected until late March or early April

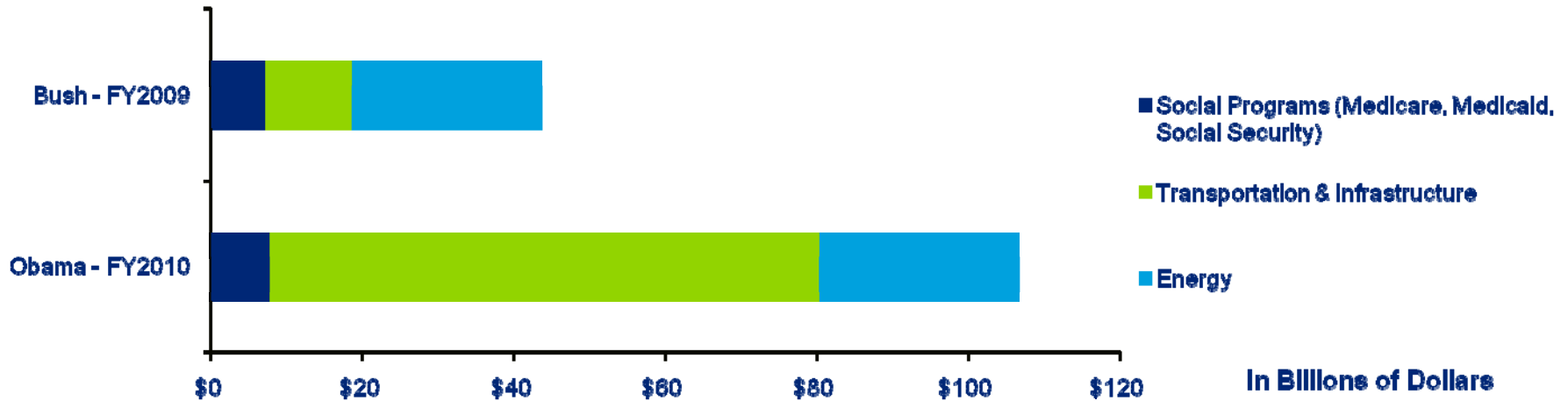


## Overall Impact

- Significantly **increases corporate taxes** with no recognition of the need for lower statutory rates
- Fundamentally **shifts individual tax burden to high-income taxpayers**
  - \$800 billion tax cut for low- and middle-income taxpayers
  - \$1 trillion tax increase for high-income taxpayers
- Creates a **significant new revenue source** in the form of a 100 percent **auction-based cap and trade carbon program**

# Spending in FY 2010 budget blueprint

Comparison of Requested Funds



## Alternative and “Clean” Energy Spending in Obama’s Budget

- Renewable energy projects, transmission projects, and carbon sequestration projects
- Development and deployment of clean energy technologies such as solar, biomass, geothermal, wind, and low-carbon emission coal power
- Carbon capture and storage technology
- Development and demonstration of smart grid technologies
- Clean energy technologies, including biofuels, renewable energy, and energy efficiency projects

# Key individual tax proposals in FY2010 budget blueprint

Provision	Revenue Estimate
<b>Individual Tax Increase</b>	
Increase top two ordinary income tax rates to 35 and 39.6 percent	<b>\$338.8 billion</b>
Increase capital gains and dividends rate to 20 percent for high income taxpayers	<b>\$118.1 billion</b>
Limit benefit of itemized deductions to 28 percent for high-income taxpayers	<b>\$317.8 million</b>
Reinstate phase outs of itemized deductions and personal exemptions for high-income taxpayers	<b>\$179.8 billion (Total 954.5 billion)</b>
<b>Individual Tax Relief</b>	
Extend the Making Work Pay Credit Permanently ( <b>offset by revenue from cap and trade program</b> )	<b>\$536.7 billion</b>
Provide American Opportunity Tax Credit	<b>\$74.9 billion (Total: \$611.6 billion)</b>

# Key business tax proposals in FY2010 budget blueprint

Provision	Revenue Estimate	Industry Impact
<b>Business Tax Increase</b>		
International Tax enforcement, and “reform” of deferral	<b>\$210 billion</b>	US multinationals with foreign subsidiaries across a broad spectrum of industries
Reinstate Superfund taxes	<b>\$17.2 billion</b>	Oil and Gas, Chemical, and Manufacturing
Repeal LIFO	<b>\$61.1 billion</b>	Oil and Gas, Pharma, Auto, Chemical, Distilled Spirits, Manufacturing
Tax carried interests as ordinary income	<b>\$23.9 billion</b>	Private Equity, Hedge Funds, Venture Capital, Energy and Real Estate Partnerships
Require information reporting for rental payments	<b>\$4 billion (Total: \$316.2 billion)</b>	Real Estate
<b>Business Tax Relief</b>		
Expand general NOL relief to all businesses for 2008 and 2009 losses	<b>\$9.3 billion</b>	Broad support particularly from homebuilders and multinationals
Extend 2009 expiring tax provisions	<b>\$20.7 billion</b>	Multinationals
Permanently extend R&D credit	<b>\$74.5 billion (Total: \$104.5 billion)</b>	Venture Capital, Tech and Biotech, “Green” Energy

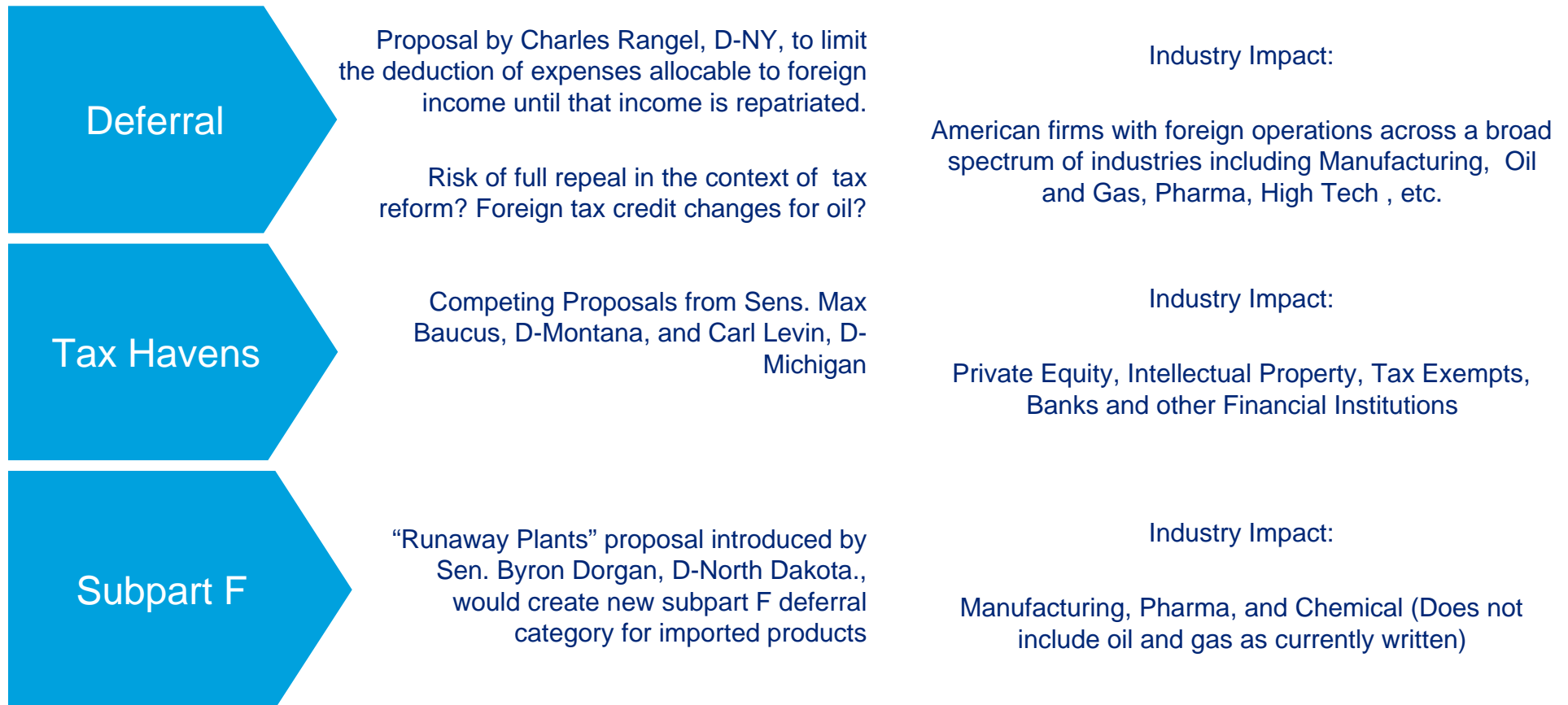
# Key energy tax proposals in FY2010 budget blueprint

Provision	Revenue Estimate
<b>Eliminate Traditional Oil and Gas Tax Preferences</b>	
Create new excise tax on Gulf of Mexico oil and gas	<b>\$5.3 billion</b>
Repeal expensing of intangible drilling costs	<b>\$3.3 billion</b>
Repeal deduction for tertiary injectants	<b>\$62 million</b>
Repeal section 199 manufacturing deduction	<b>\$13.3 billion</b>
Repeal ultra-deepwater oil and gas research and development program	<b>\$250 million</b>
Increase geological and geophysical amortization period from 5 years to 7 years	<b>\$1.5 billion</b>
Increase fee on nonproducing leases (“use or lose”)	<b>\$1.2 billion</b> <b>(Total: \$24.9 billion)</b>

# International tax provisions in FY2010 budget blueprint

\$210 billion in unspecified international enforcement including “reform” of deferral

- Details may come in full budget this spring



## Cap & trade program with 100% carbon auction

- Expected to begin in FY 2012 and to generate more than \$645 billion in revenues over 10 years
- Rising annual costs to Hess over period from 2012 to 2030 estimated as:
  - ~\$7mm to \$9mm in 2012, rising to
  - ~\$55mm to \$70mm by 2030
- Strong support among key Democratic leaders of jurisdictional House and Senate Committees: Henry Waxman (D-California), Jeff Bingaman (D-New Mexico), Barbara Boxer (D-California)
- Cap & Trade vs. Carbon Tax
- Key industry sectors already markedly divided on this issue
- Key Industry Impact: Auto, Electricity/Utilities, Energy, Manufacturing, Transportation

# Next Steps

# 2010 and beyond

- High-income rate increases
- Middle-class relief
- Permanent resolutions on AMT and estate tax
- Corporate tax rates and reform
- Entitlement reform
- Unthinkable new taxes

# Common energy PAYGO options

- Capitalization of IDCs
- Amortization of G&G
- 15-year recovery for distribution lines
- 7-year recovery for gathering lines
- Excise tax on OCS leases
- Limit or repeal of section 199 deduction



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