



# ATR ENERGY TAX HIKE SERIES

## OBAMA 2011 BUDGET ANALYSIS

### *Repeal of Percentage Depletion*

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#### Current Law

The IRS defines depletion as “the using up of natural resources by mining, quarrying, drilling, or felling. The depletion deduction allows an owner or operator to account for the reduction of a product’s reserves.” For over a century there have been two ways to calculate deductions: cost depletion and percentage depletion.

The preferred method of deduction, percentage depletion allows the producer to deduct the gross income derived from extracting fossil fuels or other minerals. Originally implemented to encourage domestic development of natural resources, percentage depletion allows for producers to collect a percentage, depending on the resource being mined, of their income tax-free.

Traditionally, oil producers have been able to deduct approximately 15% of their income while coal producers have deducted 10%. Comparatively, sulphur and uranium producers deduct 22%.

#### Obama 2011 Budget

- Impact on oil and natural gas: Repealing percentage depletion will raise taxes by **\$522 million in 2011 and 10.026 billion by 2020**
- Impact on hard mineral fossil fuels (coal): – Repealing percentage depletion will raise taxes by **\$57 million in 2011 and \$1.062 billion by 2020.**
- Total impact: **\$579 million tax increases in 2011 and 11.088 billion in tax increases by 2020**

#### ATR Analysis

Mining natural resources continues to be one of the riskiest investments and requires enormous amounts of capital. Furthermore, it may take years to recuperate investments because resource extraction does not begin immediately. Percentage depletion has gone a long way to alleviate the concerns of investors and small companies, its repeal will only add uncertainty to already weary producers.

While producers of other minerals (gravel, clay, gold, etc) will be allowed to continue percentage depletion discounts, oil, natural gas and coal producers will face enormous tax increases.