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CHAIRMAN ADAM PUTNAM WASHINGTON D.C. 226-2302

January 18, 2007

Floor Prep

H.R. 6 – The CLEAN Energy Act of 2007

Floor Situation:
The CLEAN Energy Act of 2007 (H.R. 6) will be considered under a closed rule.

The rule provides for 3 hours of debate with 60 minutes equally divided and controlled by the Chairman and Ranking Member of the Committee on Ways and Means, 60 minutes equally divided and controlled by the Chairman and Ranking Member of the Committee on Natural Resources, 30 minutes equally divided and controlled by the Committee on Agriculture, and 30 minutes equally divided and controlled by the Chairman and Ranking Member of the Committee on Science and Technology.

The bill waives all points of order except for clause 9 (earmark disclosure requirements included in rules package for 110th Congress) and 10 ("PAYGO" point of order included in rules package for 110th Congress) of Rule XXI.

The rule provides for one motion to recommit the bill.

The rule provides that, notwithstanding the operation of the previous question, the Chair may postpone further consideration of the bill to a time designated by the Speaker.

Summary:
H.R. 6 will increase taxes on domestic oil and gas producers and place the additional federal revenues and increases in federal receipts in a fund that will pay for future legislation to subsidize energy conservation and alternative energy programs.

Exclusion of oil and gas industry from domestic manufacturing tax benefits
The CLEAN Energy Act of 2007 (H.R. 6) removes tax incentives for oil and natural gas companies to produce and manufacture their products in the United States. Oil and natural gas companies will be excluded from a tax break enacted in 2005 that allows companies to write off a percentage of their costs from domestic manufacturing, production, construction, and extraction. All other companies that qualify as "domestic

manufacturers" will continue to receive this tax incentive. The tax deduction was initiated in 2005 at a rate of 3% of income from domestic production, and is being phased in for domestic producers to ultimately reach a 9% tax deduction by 2010. (Title I, section 102)

CBO estimates that repealing these tax incentives will result in $7.6 billion in increased taxes to oil and natural gas companies over the next 10 years.

**Note: The domestic manufacturing tax deduction was enacted in the American Jobs Creation Act of 2004 (PL 108-357)*

Correcting the Clinton Administration's mistakes in 1998-1999 OCS leases
The Department of the Interior under President Clinton mistakenly omitted a clause in deepwater oil and natural gas leases in 1998 and 1999 that defined the price thresholds that would trigger royalty payments. This legislation directs the Department of the Interior to renegotiate the 1998-1999 leases with any leaseholders who will voluntarily agree to amend their leases to include the standard price triggers for royalty payments retroactively back to October 1, 2006. (Title II, section 202) (See "Background" section below for further explanation)

- Penalty fees for not renegotiating leases
  Companies that do not elect to renegotiate their leases will be required to pay an annual "conservation of resources fee" amounting to $9 per barrel of oil and $1.25 per million Btu of natural gas retroactively due back through October 1, 2006. The conservation of resources fees amount to a penalty as they are somewhat higher payments than would be required by the standard royalties. (Title II, section 204(b))

  **Note: The language is considered by some to be ambiguous and may potentially authorize the Secretary of the Interior to levy conservation of resource fees on ALL oil and natural gas lease holders in the Gulf of Mexico, not just the 1998-1999 leaseholders.*

  **Note: A similar provision that repaired the Clinton-era leases from 1998-1999 was adopted in Section 6 of the Deep Ocean Energy Resources Act of 2006 (H.R. 4761), which passed the House on June 29, 2006.*

- Refusal to either renegotiate or to pay penalty fees will result in restrictions on a leaseholder's ability to buy and sell leases in the future
  If leaseholders do not renegotiate their leases or agree to pay the conservation fees they will be barred from:

  - Purchasing any leases from the U.S. Government in the future
  - Receiving any "economic benefit" (undefined) from the 1998-1999 leases they currently hold
  - Selling any of their 1998-1999 leases

(Title II, section 204)

Note: Both the denial of "economic benefits" and the ineligibility to sign future leases with the U.S. Government are thought by some to constitute a "taking" in direct* ***violation to the 5th Amendment to the Constitution* *which stipulates: "[N]or shall private property be taken for public use without compensation."*

*Note: An amendment to the FY2007 Interior Appropriations bill (H.R. 5386) stated that non compliant leaseholders would be barred from purchasing any U.S. Government leases in the future. H.R. 6 goes much farther than any past language by including the new provision to bar noncompliant leaseholders from receiving undefined "economic benefits" from the leases they currently hold.

CBO estimates that the royalties and conservation of resources fees will cost oil and gas companies (and consequently increase federal government offsetting receipts by) $4.35 billion over the next 10 years.

Additional fees
New and existing leases in the Gulf of Mexico that are not producing oil or natural gas will be charged the "conservation of resources fee" at a rate of $3.75 per acre, which CBO estimates will cost lease holders (and increase federal government offsetting receipts by) $1.75 billion over the next 10 years. (Title II, section 204(b)(3))

Revoking tax incentives for the Big 6
Major oil companies (6 in total), currently required to amortize (depreciate an expense evenly over a duration of time) their geological and geophysical costs over a period of 5 years will have their amortization period extended to 7 years. CBO estimates that extending the depreciation period of these costs from 5 to 7 years will increase the taxes on the 6 largest oil companies a combined total of $104 million over the next 10 years. (Title I, section 103)

Tax money and offsetting receipts to fund Alternative Energy & Conservation
All federal revenues and royalties collected from the taxes, fees, and offsetting receipts imposed by this bill will be deposited in a reserve account that will fund (unspecified) future legislation that:

- Accelerates the use of clean, domestic, renewable and alternative energy fuels
- Promotes the utilization of conservation and energy-efficient products and practices
- Increases research and development of renewable energy technology

(Title III, section 301)

**Note: Republicans designated oil and gas lease royalty revenues to be divided amongst coastal states and the federal government in a similar provision of the Deep Ocean Energy Resources Act of 2006 (H.R. 4761), which passed the House on June 29, 2006.*

Authorization for Budget Committee Chairman to make adjustments to budgetary levels
This legislation requires the Chairman of the Budget Committee to adjust: the discretionary spending limits, if applicable; the Budget authority (allocation) of any committee that has jurisdiction over future alternative energy or energy conservation legislation that will be funded by the oil and gas tax increases and additional offsetting receipts (adjustment to allocations will reflect amounts in excess of those provided for that purpose in FY2007), and the overall budget levels in the budget resolution. (Title III, Section 301)

**Note: Sec. 306 of the Congressional Budget Act, which applies to Title III, precludes consideration of any bill that contains matter within the jurisdiction of the House Budget Committee unless that committee has reported the underlying bill, or been discharged from consideration of the bill. The rule for H.R. 6 waives all points of order against the bill and its consideration.*

Repeal of additional royalty relief
This legislation will repeal royalty relief provisions that were enacted to provide incentives for oil and gas companies to explore for resources in extreme oceanic and geological environments that require drilling through extraordinarily deep water and earth. (Title II, section 205)

**Note: The royalty relief that provided incentives to explore in extreme environments was enacted in Sections 344 and 345 of the Energy Policy Act of 2005 (PL 109-58).*

Additionally, this legislation will repeal royalty relief provisions for oil and gas production in Alaska's OCS and authorizes the Secretary of the Interior to modify the terms of oil and gas leases in the National Petroleum Reserve in Alaska.

CBO estimates that the collective repeal of royalty relief for exploration in both the extreme environments and Alaska's OCS, combined with the changes to Alaskan oil and gas leases, will increase taxes on oil and gas companies by $210 million over the next 10 years.

Background:
Royalties with respect to oil and natural gas leases are generally defined as the landowner's share of the value of minerals produced and sold from a lease.

Offsetting Receipts are voluntary payments to the government in return for goods or services. For example: royalties collected by the government on the lease of government lands by private businesses are offsetting receipts.

Clinton Administration lease errors

In an effort to encourage exploration of domestic resources in the OCS at a time of low oil and natural gas prices (1998–1999) the Department of the Interior offered oil and gas companies deepwater leases where they were not obligated to make royalty payments until prices rose above a set price threshold. The Department of the Interior under President Clinton mistakenly omitted the clause in the 1998-1999 leases that defined the price thresholds that would trigger royalty payments. The faulty leases were drafted by the Department of the Interior and signed by over 50 oil and gas companies that collectively purchased 1,032 deepwater leases between 1998 and 1999.

CRS reported that currently 19 of the Clinton Administration 1998-1999 leases in the Gulf of Mexico are productive. Under these 19 leases, the lease holders benefit from royalty relief irregardless of the rise and fall of oil and natural gas prices.

> The Minerals Management Service (MMS) and the Government Accountability Office (GAO), estimate that this leasing error could cost the federal government at least $10 billion. The MMS estimated that about $956 million in royalty revenue was forgone through FY2006. (CRS RS22567)

MMS announced in December 2006 that 5 companies that own leases issued in 1998-1999 (collectively they own approximately 25% of the leases) signed voluntarily agreements to amend those leases to retroactively establish standard price thresholds to trigger royalty payments starting from October 1, 2006.

G&G costs

Geological and Geophysical (G&G) costs are the costs incurred by oil and gas companies in prospecting for commercially viable deposits of natural resources. They include the costs of drilling holes, seismic surveys, and employing geologists to evaluate submerged lands. Companies incur these costs long before they can begin extraction and production.

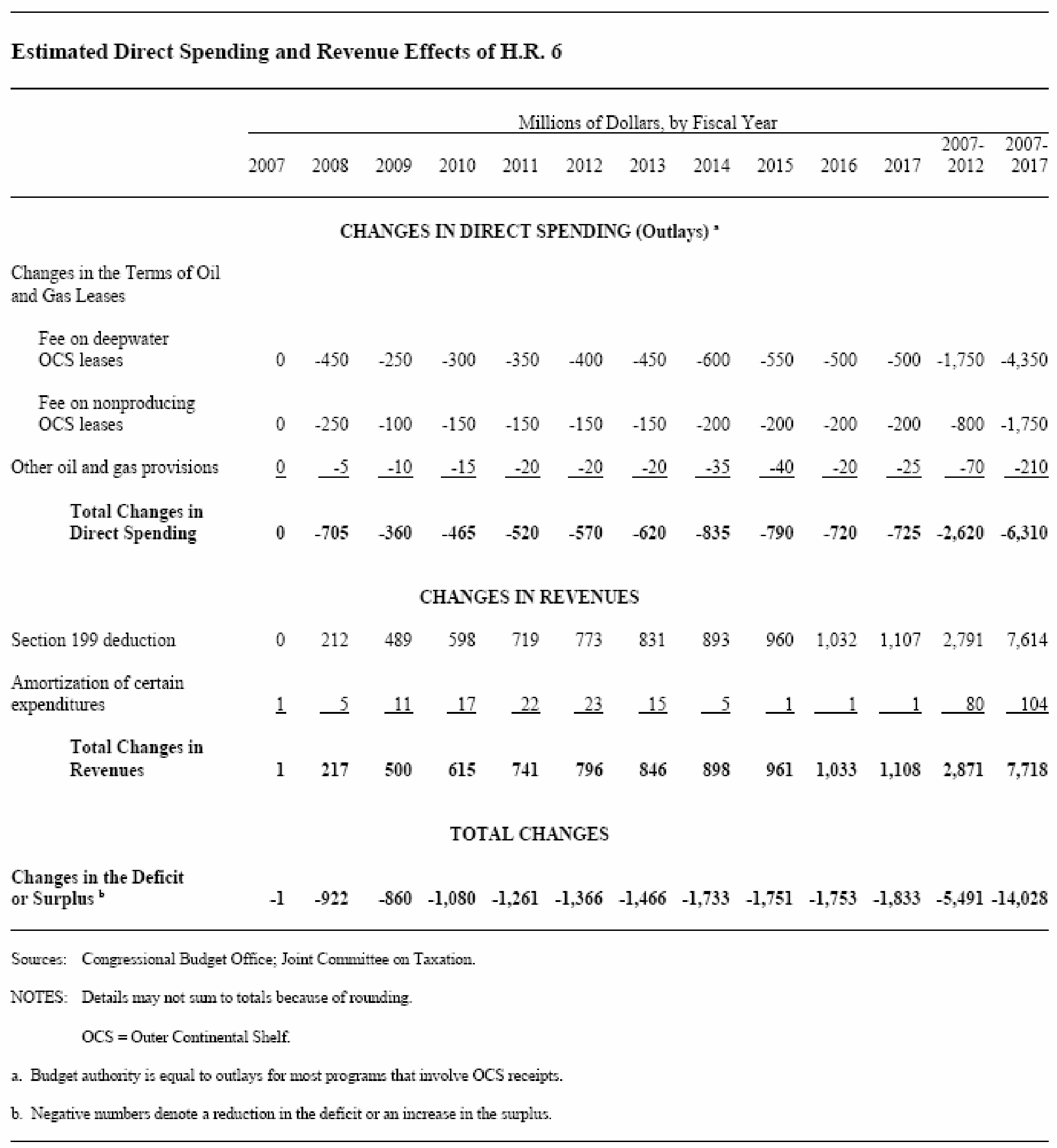
Before 2005, G&G costs incurred by oil and natural gas companies were capitalized, meaning they were only expensed in the income from a product that the G&G cost went into. For instance: the G&G cost of drilling an oil well could only be expensed in the income statement from the eventual sale of oil or of the oil well itself.

The Energy Policy Act of 2005 (PL 109-58) allowed oil and gas companies to amortize their G&G costs over a period of 2 years. For example: oil and natural gas companies could expense 50% of the cost of drilling an oil well in the year it was drilled and 50% the following year.

The Tax Increase Prevention and Reconciliation Act of 2006 (PL 109-222) singled out “major integrated oil companies” (the 6 largest oil companies meet this definition) and extended the amortization period of their G&G costs from 2 years to 5 years. Smaller oil and natural gas companies continued to amortize their cost over 2 years.

Costs:

CBO Table detailing the changes in direct spending and federal revenue increases from enacting H.R. 6.



Estimated Direct Spending and Revenue Effects of H.R. 6

	Millions of Dollars, by Fiscal Year												
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2007-2012	2007-2017
CHANGES IN DIRECT SPENDING (Outlays) [a]													
Changes in the Terms of Oil and Gas Leases													
Fee on deepwater OCS leases	0	-450	-250	-300	-350	-400	-450	-600	-550	-500	-500	-1,750	-4,350
Fee on nonproducing OCS leases	0	-250	-100	-150	-150	-150	-150	-200	-200	-200	-200	-800	-1,750
Other oil and gas provisions	0	-5	-10	-15	-20	-20	-20	-35	-40	-20	-25	-70	-210
Total Changes in Direct Spending	**0**	**-705**	**-360**	**-465**	**-520**	**-570**	**-620**	**-835**	**-790**	**-720**	**-725**	**-2,620**	**-6,310**
CHANGES IN REVENUES													
Section 199 deduction	0	212	489	598	719	773	831	893	960	1,032	1,107	2,791	7,614
Amortization of certain expenditures	1	5	11	17	22	23	15	5	1	1	1	80	104
Total Changes in Revenues	**1**	**217**	**500**	**615**	**741**	**796**	**846**	**898**	**961**	**1,033**	**1,108**	**2,871**	**7,718**
TOTAL CHANGES													
Changes in the Deficit or Surplus [b]	**-1**	**-922**	**-860**	**-1,080**	**-1,261**	**-1,366**	**-1,466**	**-1,733**	**-1,751**	**-1,753**	**-1,833**	**-5,491**	**-14,028**

Sources: Congressional Budget Office; Joint Committee on Taxation.

NOTES: Details may not sum to totals because of rounding.

OCS = Outer Continental Shelf.

a. Budget authority is equal to outlays for most programs that involve OCS receipts.

b. Negative numbers denote a reduction in the deficit or an increase in the surplus.

Source: CBO Preliminary Review of the CLEAN Energy Act of 2007 (H.R. 6) January 12, 2007.

Additional Information:

CBO Preliminary Review of the CLEAN Energy Act of 2007 (H.R. 6) January 12, 2007.

CRS Report: Royalty Relief for U.S. Deepwater Oil and Gas Leases RS22567

CRS Report: Oil and Gas Tax Subsidies: Current Status and Analysis RL33763

CRS Report: Energy Tax Policy: History and Current Issues RL33578

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