The Logic of Special Tax Breaks for the Oil and Gas Industry: Is There Any?

The last substantial project that Senator Max Baucus was working on when he was tapped by the White House to become the new U.S. Ambassador to China was the overhaul of the American federal tax code. As Chair of the Senate Finance Committee, Baucus was well positioned to push through a simplification of the tax code that might get bipartisan support.

Republicans want to simplify the tax code because it is so complex and arcane that it encourages incredible waste in the form of money being spent interpreting it and dodging tax payments. In addition, the current code has incorporated so many loopholes that the pattern of taxes has arbitrary and unfair impacts on different types of economic activity.

Democrats are interested in a federal tax overhaul for those reasons and another important one: By cleaning up the tax code and simplifying it, it is possible to generate more federal tax revenues while possibly lowering the marginal tax rates that now apply to income and profits. That could allow enhanced federal revenues to support federal programs without adding to the deficit and without discouraging economic activity.

One of the areas on which the Baucus federal tax overhaul has focused has been the special tax loopholes offered to the oil and gas industry. These loopholes sometimes allow large oil companies to avoid income taxes altogether even when they are earning spectacular profits. Many of those loopholes were put in place almost a century ago to encourage more oil drilling. Others came as the result of the oil and gas
companies insisting that they get treated the same as “infant industries” struggling to get a foothold in the economy or as declining American industries that are being lured overseas and need help to stay in the U.S. Of course the American oil and gas industry is neither of these. It is a very profitable, well-established, industry that in some ways dominates the American economy. It does not need special assistance from U.S. taxpayers while those citizens have to continue to pay what appears to be permanently high prices at the gas pump.

The oil and gas industry, of course, is fighting back. Some of that effort is being focused on Montana, Baucus’ home state, that also happens to be an energy-producing state. The argument being used by oil and gas interests in Montana is that energy development in Montana, especially oil development in the Bakken fields in northeastern Montana, is central to the economic development of the state. As one op-ed piece recently published in Montana newspapers put it: “There is no doubt that tax policies singling out the energy industry would have a disproportionate impact on Montana where energy is such a large part of our export economy.”

Energy production, including oil, natural gas, coal, hydroelectric and wind-electric generation, is an important part of the Montana economy. But energy production is also very capital intensive, rather than labor intensive. As a result, except during temporary boom periods, such as is being experienced in the Bakken, the employment associated with energy production is relatively modest.

Between 2001 and 2011, job growth in Montana totaled about 69,000 jobs. That is, on average, there was a gain of about 6,900 jobs each year. All mining activities, including oil and gas, coal, metals, sand and gravel, were the direct source of about 8

percent of those new jobs, adding about 540 jobs a year. In Richland County, home of Sidney and center of the Montana Bakken boom, the oil industry added directly about 60 jobs each year. Clearly the expansion of these mineral extraction jobs does not directly explain most of the jobs gains in Montana.

Where were the bulk of the jobs being created in the Montana economy over the last decade? Over 86 percent of the jobs created were in service industries. About 9 percent were in government, and 3 percent in retail and wholesale trade. That accounts for almost all of the 69,000 jobs created over the last 10 years in Montana, 98 percent of them. If we look at the goods producing industries of agriculture, mining, and manufacturing combined, there was actually a shrinkage of 1,700 jobs over the last decade, as jobs losses in agriculture and manufacturing offset the job gains in mining.²

This description of where job creation has been taking place in the Montana economy, does not take into account the “ripple” or “multiplier” effects of the mining jobs and the high pay associated with them nor does it consider the revenues that flow into government coffers due to mineral production taxes, royalties, and rents. Both of these can be significant. Mining jobs in Montana in 2012 paid $98,000 per year and the Montana state government took in $431 million in revenues from mineral production that year. Clearly energy production in Montana is important to the workers and governments receiving that income and the communities in which they live.

However, Montana’s economy is not an “energy economy” or a “mining economy.” The “Treasure State” logo and the reference to mining on the Montana state flag is a reference to the 19th and early 20th century history of Montana. As the

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² Employment data is from the U.S. Bureau of Economic Analysis, Regional Economic Information Center, U.S. Department of Commerce.
employment data make clear, the Montana economy now is a very diversified one, not an economy driven by a single extractive industry whose political bidding we have do in order to maintain a vital and prosperous economy.