Ending Federal Subsidies to the Oil Industry

President Obama has proposed eliminating $4.4 billion annually in oil subsidies. While these are not all the subsidies that this mature and very profitable industry enjoys, they are some of the most obvious. Responsible policymakers are concerned about the impact that removing these subsidies (which the industry deceptively calls new taxes) will have on domestic production, on jobs, and on consumers at the pump. And the short answer to those three questions is little to none.

Our vulnerability to high gas prices has been a fact since the 1970s, and no amount of additional drilling or subsidies is going to change that. The only way to end our vulnerability to high gas prices is to end our dependence on all oil, not just foreign oil. According to the Treasury Department, removing these domestic subsidies will reduce U.S. oil production less than one half of one percent, and will increase exploration and production costs less than two percent. Considering the price that the domestic industry receives for crude has more than doubled over the past several years, the industry should be able to afford that – without laying anyone off or jacking up the price at the pump.

The global oil market, not the domestic industry, determines gasoline prices. The Treasury Department estimates that subsidy removal would cause a loss of less than one tenth of one percent in global oil supply, and thus would have no impact on global or U.S. prices.

"Independent" oil and gas companies: not exactly 'mom & pop shops'

For the last two years, some Senators have supported a bill that targets subsidy removal from only the "Big Five" major oil companies (BP, Chevron, ConocoPhillips, ExxonMobil and Shell). While the Big Five are significant, this targeting lets some very large American oil companies off the hook. Koch Industries would still enjoy subsidies, as would Valero, the nation's largest oil refiner and TransCanada, the company behind the Keystone XL pipeline.

Large independent producers of oil include Occidental, Amerada Hess, Marathon, Murphy Oil and a number of more diversified energy companies that also produce large quantities of the nation's oil and gas. Together with the Big 5, these companies produced 53.5 percent of U.S. oil in 2009.

The Independent Petroleum Association of America (IPAA) claims that its members would be disproportionately affected by the subsidy reforms proposed by President Obama. But who are these small producers? And do *any* oil producers really need a subsidy with prices exceeding $100 per barrel?

- Most independently-owned U.S. oil and gas production is done by companies with market capitalizations in the hundreds of millions and multi-billion dollar range.
- Some independent oil and gas companies are in fact owned by major oil companies or big multinational investment firms.
- At prevailing oil prices, U.S. oil production is hugely profitable.

- An exemption from subsidy removal for independent oil and gas producers on the basis that they are smaller and more vulnerable than 'Big Oil' would appear to disregard the large size and ownership structure of many independent producers.

The IPAA membership list is not publicly available, but our research has revealed the following about the U.S independent upstream oil and gas sector. We looked at EIA data on the top 100 oil producers by reserves and found 86 publicly listed independent oil producers.

- We found 56 independent oil producers with market capitalizations of over $1 billion. The median market capitalization of all 86 companies was over $2 billion.

- The top five independent companies by market capitalization are Apache, Anadarko, Devon, EOG and Talisman, which between them are worth over $178 billion.

- For 66 of these 86 companies, the average CEO salary in 2009 was over $4.8 million.

- Some 'independent' companies are not so independent. Aera Energy LLC is a privately held company that is among California's biggest producers. Shell and ExxonMobil jointly own it. Some companies are not owned by other oil and gas companies but instead by multinational holding companies. One such example is Fidelity Exploration and Production Company, which is owned by MDU Resources, a company with a $4.4 billion market capitalization. Others are multi-billion dollar enterprises that are registered in tax havens, which may be dodging the U.S. tax system altogether. One such company with significant U.S. oil reserves is Energy XXI, registered in Bermuda.

At today's oil prices who needs a subsidy?

In an IPAA's survey of its members, the 'Profile of Independent Producers 2009,' producers revealed the costs of operating marginal wells. These are generally wells that are close to the end of their productivity and are usually high cost and low return. However, the median operating costs for the three categories of producer (small, medium and large) ranged from $20 to $26 per barrel of oil equivalent (Boe). While operating costs may not be the only costs to consider, it is clear that at current oil prices there is plenty of room for profit on these wells.

Independent producers are in fact enjoying the most substantial boom in American oil production in decades. The production of tight oil using hydraulic fracturing (fracking) has grown from a few thousand barrels a day to some 600,000 b/d today and is expected to grow a lot further.

Tight oil producers are enjoying very comfortable margins today. Most estimate that this type of oil is economic at $50 a barrel or less. Therefore one of the key areas of production for many independents, and the most significant in terms of growth prospects in the coming decade is a steal at current oil prices. The EIA expects oil prices to remain above $100 a barrel for the next few years and currently forecasts an average oil price of $106 a barrel in 2012.

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