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STATEMENT OF

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BEFORE THE
SUBCOMMITTEE ON COMMERCE, CONSUMER AND
MONETARY AFFAIRS
OF THE
COMMITTEE ON GOVERNMENT OPERATIONS
UNITED STATES HOUSE OF REPRESENTATIVES
ON
ENERGY TAX POLICY ANALYSIS

Mr. Chairman and Members of the Subcommittee:

We appreciate your invitation to appear before the Subcommittee to discuss with you the findings of our review of the Administration's analysis of energy tax policy. Our report entitled, "A Review of the Department of Energy's Energy Tax Policy Analysis," concentrates on the Department of Energy's role in this regard; however, in the process of our review, we also considered the impact of the Department of the Treasury on energy tax policy, and the crucial interaction between the two agencies. Our report is brief. With your approval, Mr. Chairman, I would like to submit a copy of it for inclusion in the record.

I would first like to briefly discuss our concern about the inadequacy of energy tax policy analysis and then summarize the conclusions of our review.

We are concerned that many tax measures affecting energy have been implemented without sufficient consideration being given to their impact on national energy policy. Since tax legislation can have a significant influence on energy supply and demand, and on energy programs, we believe that more careful analysis should be performed to evaluate the energy effects of any proposed measures which directly or indirectly affect energy industries. Examples of recently enacted tax changes which were not analyzed by the Energy Department but which affect the energy sector include: (1) elimination of the percentage depletion allowance for oil and gas, (2) limitations on the foreign tax credit, and (3) liberalization of the tax treatment for intangible drilling costs.

We reviewed the Department of Energy's analysis relating to the energy effects of taxes in recent years and found that the Department, in fact, performed supportive analysis of the energy effects of the National Energy Plan's tax provisions and provided this to the Congress. This analysis is illustrative of the type of work that we believe the Department of Energy should be providing in this area on a continuing basis.

However, excluding their analysis of the National Energy Plan, we found that:

--The Energy Department simply has not performed this type of analysis.

--The little work that the Energy Department has done relative to energy tax issues has been primarily of an internal nature. The only contacts outside the agency--for example, coordination with other Federal agencies--have been of an informal nature, and, for the most part, have not been effective.

--The Department of Energy has failed to provide the Congress with analysis or recommendations regarding these energy-related tax measures nor has it taken a formal position on them.

--The Energy Department has not analyzed the energy effects of major tax changes after they have been adopted, in order to determine whether future changes are required or advisable.

IMPROVED EXECUTIVE BRANCH COORDINATION IS NEEDED IN ENERGY TAX POLICY ANALYSIS

We believe that energy tax policy analysis is a basic responsibility of the Department in carrying out its duties to develop and implement national energy policy. Its analysis should include proposed legislation as well as existing legislation to determine when further adjustments to the tax structure are needed.

To insure that energy concerns are given proper consideration in in the formulation of Administration tax policies, the Department of Energy must also participate with other executive branch agencies such as the Office of Management and Budget, and particularly, the Department of the Treasury. Such participation has been ineffective or non-existent. The responsibility for this lack of coordination falls not only on the Energy Department but on the other relevant agencies as well.

In the course of our review, we found that the Department of Energy is aware of the inadequacy of consultation on energy tax issues between the Energy and the Treasury Departments, but DOE and GAO believes that the Treasury Department will not be supportive of such consultations unless required to do so by Congress.

Because the Treasury Department has the primary responsibility for formulating and implementing tax policy, it has a definite role in the area of energy tax policy. Treasury should seek out the views of the Department of Energy at an early stage when tax changes with potentially major effects on the energy sector or on energy policy are being considered. This includes not only energy-specific tax changes such as percentage depletion, intangible drilling costs, etc., but also general tax changes that have a broader application than just energy but which could have a major impact on the energy sector. Examples of such general tax changes are the phase-out of the Western Hemisphere Trade Corporation deduction (a special deduction for firms operating primarily within the Western Hemisphere), the elimination of the "per country" method of computing the foreign tax credit, and the proposed termination of domestic tax deferral of foreign source income.

The Treasury Department does not agree with us on this point, however. It contends that the Department of Energy should have very limited involvement in "general tax measures." Treasury includes in their definition of "general tax measures," the Western Hemisphere Trade Corporation deduction, the elimination of the "per country" method of computing the foreign tax credit limitation, and the termination of domestic tax deferral of foreign source income. On the other hand, the Treasury Department, in commenting on our report, stated that, "industry-specific" taxes, those tax measures affecting only the energy sector, require close cooperation between Treasury and the Department of

Energy, beginning in the initial stages of energy tax policy development. The problem we found, however is that the Treasury Department has apparently failed to formally obtain even such industry-specific analysis from the Energy Department.

The Treasury Department also distinguishes between the formulation of tax policy through legislation and the administrative implementation of that policy through regulations and rulings. According to the Treasury Department, after the statute has been enacted and regulations published, other agencies have no role to play in further administration of the tax law by the Internal Revenue Service, and that it would be improper for other agencies to intervene with comments about substantive policy implications.

Notwithstanding Treasury's position, GAO continues to believe that the responsibility of the Department of Energy to analyze the energy impact of tax changes extends beyond taxes which affect only the energy sector. The Energy Department's tax analysis must include general taxes if it is expected that these taxes would have a significant impact on the energy sector. Over three-fourths of the foreign tax credit, for example, is claimed by oil and gas firms. Over 85 percent of the Western Hemisphere Trade Corporation deduction was claimed by oil and gas firms in 1975. The impact of these general tax provisions on U.S. energy policy is most pronounced. The Treasury Department's belief that the Energy Department should have little involvement in general tax measures, and its failure to solicit DOE's analysis and views on energy-specific taxes has greatly restricted the Department of Energy's ability to have an input into the development of energy tax policy.

In addition, while we recognize that tax policy and tax administration are the responsibility of the Treasury Department, and the Internal Revenue Service, it is the responsibility of the Department of Energy to alert the Treasury Department, the Office of Management and Budget, the Congress, and others of any potentially significant energy impacts of tax rulings and procedures which materially affect U.S. energy objectives. The Department of Energy has been largely deficient in this area.

In addition, we believe that the Treasury Department, on a formal basis, needs the early views of other executive branch agencies on tax changes affecting those agencies' areas of responsibility such as energy policy.

RECOMMENDATIONS

In concluding my remarks, Mr. Chairman, I would like to summarize our recommendations regarding imporvements in the analysis of energy tax policy.

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--(1) ~~First~~, the Secretary of Energy should perform adequate analysis of tax measures which have substantive energy effects. The Department's analysis should include not only proposed legislation but also legislation currently in force. This analysis should be of a continuing nature to determine if and when further adjustments to the tax structure are in order.

--(2) Second, the Secretary of Energy also should participate with other executive branch agencies, particularly the Treasury and OMB, on a formal basis to insure that energy concerns are given proper consideration in the formulation of administration tax policies. A formal mechanism for this inter-agency communication should be established.

and (3)

--~~Third~~, the Secretary of Treasury should seek out the views of the Department of Energy at an early stage when tax changes are being considered which have potentially significant impacts on the energy sector or on energy policy. This includes general tax measures which have a broader application than just on the energy sector; ~~and (4)~~

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--~~Finally~~, congressional committees, when considering energy-related tax measures, should require the Department of Energy to provide its analysis of the energy implications.

This concludes my prepared remarks. I will now be happy to answer any questions concerning our study.