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The Honorable Dave Camp
Chairman
U.S. House Committee on Ways and Means
1102 Longworth House Office Building
Washington, D.C. 20515

The Honorable Sander Levin
Ranking Member
U.S. House Committee on Ways and Means
1106 Longworth House Office Building
Washington, D.C. 20515

The Honorable Kevin Brady
Energy Tax Reform Working Group
U.S. House Committee on Ways and Means
301 Cannon House Office Building
Washington, D.C. 20515

The Honorable Mike Thompson
Energy Tax Reform Working Group
U.S. House Committee on Ways and Means
231 Cannon House Office Building
Washington, D.C. 20515

The Honorable Jim Gerlach
Manufacturing Tax Reform Working Group
U.S. House Committee on Ways and Means
2442 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Linda Sánchez
Manufacturing Tax Reform Working Group
U.S. House Committee on Ways and Means
2423 Rayburn House Office Building
Washington, D.C. 20515

RE: AFPM's Comments to the Energy and Manufacturing Tax Reform Working Groups with the Committee on Ways and Means

Dear Chairman Camp, Ranking Member Levin and Honorable Members of the Tax Reform Working Groups:

The American Fuel & Petrochemical Manufacturers (AFPM) supports reforms to the tax code that will make all U.S. businesses more competitive, promote investment in America and create jobs. As the Ways and Means Committee and the Tax Reform Working Groups explore reforms to the tax code, AFPM would like to submit the following comments. In general, fuels refining and petrochemical manufacturing are capital intensive industries. Tax changes that enhance our ability to recover capitol costs will result in more investment in the U.S., more growth and more jobs. On the other hand, tax changes that increase our cost of capital or cost of holding inventories will result in less investment in the U.S., less growth and fewer jobs. As a trade-exposed industry, domestic tax policies that increase the costs of production will make imported fuel and petrochemicals more attractive and could simply result in exporting these high-paying manufacturing jobs to other nations. Furthermore, increases in our overall taxes means increased pressure on the costs for the fuels and products that we produce.

AFPM is a trade association representing high-tech American manufacturers of virtually the entire U.S. supply of gasoline, diesel, jet fuel, other fuels and home heating oil, as well as the petrochemicals used as building blocks for thousands of products vital to everyday life. AFPM's members operate in a highly competitive international market, where fractions of a penny on a per gallon basis can mean the difference between a refinery continuing operations or shuttering its doors.

With the U.S. economy still continuing its recovery, AFPM supports a reduction in the statutory tax rate, which will make us more competitive in the global marketplace and create additional jobs. U.S. refiners provide more than 95% of the fuel consumed in the domestic market. A lower statutory tax rate will help keep domestically produced fuel and petrochemical products competitive with imports. Reducing the regulatory and effective tax burdens on U.S. refiners and petrochemical manufacturers, and all other domestic manufacturers, should be the goal, as these changes will have a positive effect on American companies' competitiveness and provide high-quality, high-paying jobs in the U.S.

In addition to lower statutory rates, AFPM also supports tax reform that produces a fairer, simpler tax code that does not pick winners or losers. However, AFPM cautions against indiscriminate use of "base-broadeners" to achieve a lower tax rate if the result is a higher effective tax rate on American manufacturers. AFPM members already operate in a highly competitive marketplace and raising the tax burden on refiners would exacerbate the many challenges that the industry faces. As the Committee and the Energy and Manufacturing Tax Reform Working Groups examine potential reforms to the tax code, AFPM would like to point out certain policies embedded in the current tax law that if changed would have a disproportionate impact on domestic manufacturers. The domestic manufacturing sector should share the burden of "base broadening" with all other sectors and should not be singled out in order to buy down the tax rate for other sectors. Yet, that is exactly what would happen to capital intensive industries such as ours if the cost of maintaining inventories or raising capital were increased. AFPM encourages policymakers to consider the impacts on domestic manufacturing jobs when judging the trade-offs between base-broadeners and rate reduction in comprehensive tax reform. In particular, AFPM would like to reiterate the importance of the following tax code provisions in preserving the competiveness of U.S. refining and petrochemical manufacturers:

"Last-In, First-Out" (LIFO)

LIFO is a well-accepted accounting method used by an estimated 36 to 40 percent of all American businesses, including but not limited to manufacturers, wholesalers, retailers, and automobile and equipment dealers since the 1930s. LIFO is commonly used to determine both financial and taxable income when companies anticipate inflation or rising prices of their inventory over the course of their operations. For refiners and petrochemical facilities, it is the most effective way to account for replacement costs, particularly as the cost of crude oil increases. A retroactive repeal of LIFO accounting for all taxpayers would amount to a multi-billion dollar tax penalty that would redefine the value of inventory on hand resulting in taxable income. Refineries keep large inventories in order to avoid product supply shortages that could lead to price spikes for consumers and keep an even predictive flow of crude costs. Repealing LIFO is likely to cause companies to redirect cash or sell assets in order to cover the tax payment, potentially devastating businesses and American jobs. This could also result in reduced capital investment in new productive assets and projects (meaning fewer jobs) or higher consumer costs at the pump, and could make the U.S. more reliant on foreign imports of refined product. There is no justification to enact a retroactive tax on American businesses and because LIFO is an accepted accounting method, AFPM believes that it should not be considered during comprehensive tax reform discussions.

Accelerated Depreciation

The U.S. tax code allows for the use of several cost recovery methods for businesses known as depreciation. American manufacturers use accelerated depreciation through the Modified Accelerated Cost Recovery System (MACRS), which helps manufacturers mitigate the cost of investing in machinery and equipment needed to expand and grow their operations. Accelerated depreciation is especially important to fuel and petrochemical manufacturers who must invest billions of dollars in equipment for general operations and costly equipment needed to comply with changing environmental regulations. In an increasingly uncertain world in which market demand and production costs can shift quickly, the rapid cash payback from MACRS depreciation substantially reduces the risk premium and internal return on investments needed to make new investments attractive. Studies have shown that U.S. depreciation rates are similar to those used by our trading partners. Recent tax reform discussions have focused on the potential repeal of MACRS, and replacing it with a longer depreciation rate as a way to finance a reduction in the corporate tax rate. Studies have shown that such a change will increase the cost of capital and the cost of new equipment, which will reduce the amount of new investment in the U.S. and result in lost jobs.

Master Limited Partnerships (MLPs)

Publicly traded partnerships (PTPs) are limited partnerships in which “units” are traded on public exchanges. The PTPs which engage in active businesses are commonly known as master limited partnerships (MLPs). MLPs are important to the refining and petrochemical industries as they are the primary builders of midstream energy infrastructure, such as pipelines. MLPs have invested $113 billion in the U.S. economy since 2007 and are expected to invest $25 billion more in 2013 to build and maintain the U.S. energy infrastructure. MLPs do not pay entity-level corporate taxes, instead MLP income flows through and is taxed to unitholders, who are often domestic individuals, such as seniors and individuals close to retirement. During the upcoming consideration of tax reform initiatives, there will be an effort by some to tax these pass-through entities more like corporations, which would have the impact of double-taxing and thus disincentivizing these investments. MLPs are extremely successful at encouraging investment in domestic energy infrastructure at levels that otherwise may not occur, as the MLP vehicle allows for easier access to capital. The capital intensive nature of building and maintaining energy infrastructure projects is somewhat ameliorated by the lower cost of equity capital associated with PTPs and should not be discounted. We ask that the Committee retain the current treatment of PTPs within the tax Code.

Section 199

The American Jobs Creation Act of 2004 enacted the "Section 199 Domestic Production Activities Deduction," often referred to as the "domestic manufacturing deduction." The Section 199 deduction applies broadly to income from property "manufactured, produced, grown, or extracted by the taxpayer" in the U.S., and further applies to qualified films, electricity, natural gas, or potable water produced in the U.S. and construction of real property in the U.S., including associated engineering or architectural services (see I.R.C. Section 199(c)). It provides needed tax relief for domestic production activities of all kinds, which support middle class jobs, including support to help stimulate manufacturing activity in U.S. Petroleum refining and the production of domestic oil and natural gas resources are one of many sectors eligible for this deduction, which supports the expansion of U.S. refining capacity, energy supplies, and infrastructure. The deduction is needed to keep American fuel and petrochemical manufacturers competitive in an increasingly tough global marketplace. Petroleum industry opponents continue to point to $4 billion in tax subsidies going to the oil industry. In fact, these so-called petroleum industry subsidies flow from the Sec. 199 deduction, which is applicable to all domestic manufacturers, such as automobile manufacturers, computer manufacturers, and steel producers. As a matter of fact, even biofuel producers rely upon this deduction. Congress already has discriminated against the oil industry by lowering the amount of the deduction to six percent, while affording other manufacturers a nine percent deduction. Refiner and petrochemical manufacturers should have a level playing field and Congress should eliminate this discriminatory treatment.

AFPM appreciates your consideration of our views. In addition to our comments, AFPM has attached four fact sheets to provide additional information on each of the issues outlined in these comments. Please contact Geoff Moody, AFPM's director of government relations, with any questions. He can be reached at gmoody@afpm.org or 202-552-8489.

Sincerely,

Charles T. Drevna
President