

for the reasons set out briefly in Appendix "E", that the present language of the Regulations is an inadvertence and that a penalty for shale oil is not intended. However, the Oil Import Administration is a part of the Department of the Interior, and there appears to be no reason why, as a part of its policy, the Department should not promptly remove the cloud of nuclear regulatory language. It is relevant for TOSCO to add that in all of its economics on commercial production, it has been forced by prudence to assume against itself the resolution of this unnecessary question, and shale oil production planning has therefore been needlessly impaired.

Depletion Deduction

No discussion of this new petroleum source would be complete without at least a mention of the discriminatory treatment which shale crude oil produced by above-ground retorting is presently subject to for purposes of the depletion deduction under Federal income tax laws. The problem is stated separately, for your convenience, in Appendix "D". It can be summarized briefly as follows.

Today it is the stated position of the Internal Revenue Service that the Internal Revenue Code confines the depletion rate applicable to shale oil to 15%; and, perhaps more important, that it confines the application of the rate to the value of mined and crushed shale rock rather than to the value of the first oil produced at the retort. The costs of mining and crushing are approximately one-half the cost of production of the first oil product. Under the law then, the value of the mined and crushed rock would be approximately one-half the value of the oil. The result is anomalous. The significant value of oil shale lies in its contained kerogen which is extracted as petroleum. No practical way is known today to extract the kerogen other than retorting to produce petroleum. The anomaly is heightened when the depletion treatment of oil shale as a petroleum source is compared to the treatment of conventional petroleum; and it is still worse when shale oil that is mined and retorted is compared to shale oil produced by in situ retorting techniques. In the case of in situ, the principal product is the petroleum recovered at the surface of the ground so that value of the petroleum would have to be the point of application of the depletion rate.

We are not here concerned with the divisive question whether percentage depletion in mineral production is or is not a desirable policy. What we are concerned with is that this material must compete as petroleum in the marketplace. If we are to have a depletion policy, it must surely not discriminate among competing products. Precisely that point was made in the deliberations of the Senate on the Gore Amendment which became Section 613(c) of the Internal Revenue Code in 1960, and which governs this question.

It is worth noting that the imposition of such an economic penalty on shale oil producers will ultimately affect the small producer more severely than the large, which is merely an illustration of the fact that this question is one of competitive inequity and not one of fundamental depletion policy.

APPENDIX A

TABLE 1.—U.S. petroleum demand,¹ 1954-66

Year:	[Thousands of barrels per day]	
1954	-----	7,760
1955	-----	8,460
1956	-----	8,779
1957	-----	8,818
1958	-----	9,083
1959	-----	9,451
1960	-----	9,661
1961	-----	9,806
1962	-----	10,234
1963	-----	10,551
1964	-----	10,816
1965	-----	11,304
1966	-----	² 12,080

¹ Demand is satisfied by domestic crude oil production, natural gas liquids production, and net imports of crude oil and refined products.

² Preliminary.

Source: U.S. Bureau of Mines.