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SEN. MAX BAUCUS HOLDS A HEARING ON TAX INCENTIVES AND RISING ENERGY PRICES

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SENATE COMMITTEE ON FINANCE HOLDS A HEARING ON OIL AND GAS TAX INCENTIVES

MAY 12, 2011

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WITNESSES: JOHN WATSON, CEO AND CHAIRMAN, CHEVRON

JAMES MULVA, CEO AND CHAIRMAN, CONOCOPHILLIPS

MARVIN ODUM, PRESIDENT, SHELL OIL

H. LAMAR MCKAY, PRESIDENT AND CHAIRMAN, BP AMERICA INC.

REX TILLERSON, CEO AND CHAIRMAN, EXXONMOBIL

[*] BAUCUS: In 2005, President George H. -- George W. Bush said, quote, "With \$55 (ph) oil, we don't need incentives to oil and gas companies to explore. There are plenty of incentives." That was President Bush, 2005.

Today, oil costs more than \$100 a barrel. So today we'll again evaluate those oil and gas incentives. We will consider how they have affected profits in the industry and prices at the pump.

We will ask the same question our 43rd president answered more than five years ago: Is it wise to continue these tax breaks given to the largest oil and gas companies every year?

Gas prices are nearly \$4 a gallon today, and experts anticipate they will remain close to \$4 for the remainder of the season. That means gas prices are up more than \$1 a gallon compared to last summer.

In fact, families will pay an average of about \$825 more for gas this year than they did last year. In the rural areas like Montana, where people drive farther, the increase is more like \$1,200 per household.

At the same time, the five largest oil companies, who are here today, collectively earned more than \$35 billion in profits the first quarter of 2011 alone. At this pace, 2011 will be their most profitable year.

Now businesses should, of course, make a profit. That's the American way. It's what drives our economy. But do these very profitable companies actually need these taxpayer subsidies?

Energy incentives should help us build the energy future we want to see, not pad oil company profits. Americans want us to work toward an energy future made in America. They want us to develop energy sources that won't be depleted, like wind and sun.

We can't reduce using fossil fuels overnight. They're here for a long time. We must work with them, make them as clean as possible as we convert over to renewables. But investment in clean energy will move us away from the oil and gas bills that are squeezing consumers today.

To reach a clean American-made energy future, we have to scrutinize every dollar of energy subsidies we spend. The \$2.1 billion we spend every year on subsidies for the largest oil and gas companies are not moving us closer to our energy goals.

Everyone today find their budgets are tight -- families, government, households. Congress is also debating the best way to address our deficits and debt.

Some are proposing cutting Medicare for seniors; others, slashing programs for students. I think all Americans agree, as we tighten our belts, we all must sacrifice together, equally, shared.

So we have to take a hard look at every subsidy and every spending program to be sure if we are (ph) using our dollars wisely.

In 2004, Congress created the domestic manufacturing deduction, often referred to as Section 199. This deduction is designed to stimulate manufacturing here in America.

In fact, I might -- I remember back when it was enacted to replace the FSC/ETI. FSC/ETI was basically not used by the majors so the 199 is -- it was essentially a gift given to the majors because they were not, according to my recollection -- I could be corrected here -- were not using the so-called FSC/ETI. So 199 was essentially a gift.

Each company here today has claimed this deduction. And what have taxpayers received in return? Have these tax breaks proven to be more valuable than Medicare or Pell Grants? These tax breaks have not lowered prices.

When these tax breaks were created, retail gasoline prices averaged about \$1.80 per gallon. In fact, prices have increased.

By 2008, prices have risen to an average of \$3.26 per gallon, and last week they approached \$4.

These tax breaks have not moved us toward energy independence. According to a Treasury Department study in 2009, if all the subsidies for the oil and gas industry all were eliminated, domestic production would fall by less than one-half of 1 percent. And that's for the entire industry.

Today we're only talking about the five largest -- reduce (inaudible) only about one-third of domestic oil.

They have the most resources and are the least dependent -- excuse me -- the big five have the most resources and are the least dependent on government subsidies.

So the effect on domestic production from repealing these subsidies for these companies could be even less.

Despite these facts, some still argue that eliminating tax breaks for the largest oil and gas companies will raise prices at the pump or force layoffs. The oil and gas industry has launched ad campaigns arguing that repealing these tax breaks will hurt consumers.

But a 2007 Joint Economic Committee analysis found the repealing the oil and gas tax breaks would not raise energy prices for consumers -- would not.

Why? Very simple. Oil prices are set on a world market, and the U.S. share of production is only about 10 percent. That makes it difficult, if not impossible, to pass on the cost of losing these subsidies to consumers.

Given profits of \$35 billion in just the first quarter alone, it's hard to find evidence that repealing these subsidies would cut domestic production or cause layoffs. After all, based on first quarter profits, these tax breaks represent less than 2 percent of what these companies are on pace to make this year.

And even without these tax breaks, these companies will be clearly highly profitable.

The chart here behind me, to my right, this chart looks at financial documents the companies here today have filed with the Securities and Exchange Commission. These are the footnotes and in the 10Ks, and basically documents filed with the SEC.

BAUCUS: According to those documents, the average cost to produce a barrel of oil was about \$11 in 2010. And the average price these companies received for a barrel of oil was about \$72. I don't say (ph) it's exact. But it's -- it's roughly what the documents -- the SEC documents show.

Today oil prices are higher -- a lot higher -- 40 percent higher, which would increase these large profit margins much further than shown on this chart. So it's hard to imagine that companies faced with these opportunities would cut production.

Now some might argue that these subsidies, or these record profits, create much needed jobs. But those same documents, public documents, filed at the Securities Exchange Commission show that nearly 60 percent of these companies' 2010 profits went to stock buybacks and to dividends -- not to job creation.

You can put this money to better use, I believe. And we should.

We should use this money to reduce our deficit instead of putting the burden on seniors and our children's future. This is choices, everybody. It's shared choice.

It's America working together and look at the facts and seeing the degree to which limiting these subsidies would in fact be a fairer way for us to start to reduce our deficit because reducing these subsidies, evidence shows, will have virtually no effect on jobs -- or loss of jobs in the -- in this country for the reasons I've indicated.

So I -- I just urge us to do what's right, what's wise for our country. And this is one place to -- we should examine, look at it, see what the facts are.

And there will be lots of other areas that we're going to be looking at, not just the big five oil companies, with looking -- today, we can only (ph) -- we -- we can only do -- have -- only address one subject at a time.

And the subject today is the one at hand.

Senator Hatch?

HATCH: Well, thank you, Mr. Chairman.

Everybody's angry about high gas prices. And I can tell you that I'm angry about it. The press keeps telling us that we need America to come together and put aside partisanship. Well nothing makes for a kumbaya moment like high gas prices.

Republicans don't like paying high gas prices any more than Democrats do. And with one voice, Americans are telling us to do something about them.

Unfortunately for some people, the political philosophy of Rahm Emanuel is too hard to resist. And that is, never let a crisis go to waste.

And so faced with an issue of legitimate concern for the American people, politicians and their immediate allies decide to exploit high gas prices for political gain. Now this was a double game for those politicians.

On the one hand, they are able to score some cheap political points against the politically unpopular oil companies. On the other hand, all of their sound and fury signifies nothing. It is designed to distract their constituents from the simple fact that the Democrats have no energy policy whatsoever.

Let me take that back. Actually they do have an energy policy.

Are you ready for this?

Their energy policy is to increase the cost of energy. You heard that right.

This is the president's energy secretary, Steven Chu, quote, "Somehow we have to figure out how to boost the price of gasoline to the levels in Europe," unquote.

So while the American people ask Congress to do something about high gas prices, the response of Democrats is to rail against oil executives to mask the fact that their policy is actually to make the price at the pump more painful.

And for whatever it's worth for all of their talk about the shrinking middle class and the income inequality, high gas prices don't hit Warren Buffett and Warren Beatty the hardest. They hit moms and dads who have to live far from where they work and drive minivans and SUVs because they have children.

When Al Gore has to pay a little more to gas up the private jet to fly to Cannes in France, he doesn't feel any pain. But when my constituents in Utah see gas go above \$4 a gallon, they have to make real choices about whether they have to work longer hours to make ends meet, and whether they can send their children to -- to camp this summer.

David Letterman captured this current situation brilliantly. Here's how Mr. Letterman put it. "Gas prices, aren't they crazy? It's so expensive, the rats are carpooling in from New Jersey." Now I'd expect my friend from New Jersey to change the joke and stipulate that the rats arrived from the opposite direction. Of course my friend from New York might take exception to that.

Now we don't have as many rats in my home state of Utah, but like folks in New Jersey and New York, Utahans are plenty angry about high gas prices. They are bearing the brunt of gas prices near \$4 per gallon.

This is very discouraging because we are still recovering from one of the worst recessions our country has ever faced. And all that these increased gas prices do is put the brakes on an already fragile economy.

Now I hear from small businesses that they are trying to make a profit and possibly hire more workers. But now have to make room for added energy expenses.

I hear from families who are trying to work out how these gas prices will fit in their budgets. And I hear from those who are still looking for employment.

What the people of Utah and this country need is a forward thinking energy policy that will address rising gas prices that are a lead weight around the neck of the economy.

I'm not here to defend any particular industry. After all, I'm one of the leading proponents of promoting alternative fuels.

But let's not make any mistake about what we are talking about here. And I might add, I've passed legislation that does do exactly that.

Let's not gloss over the plan that is being offered here. The plan that is being offered here is to raise taxes.

Americans are rightly upset about the cost of gasoline. And the solution being offered here, let's raise some taxes.

Lawyers would call this a non sequitur. Every day Americans would call it, beside the point.

Raising taxes to address high energy prices is about as relevant as a person walking into a doctor's office, complaining of chest pain and having the doctor respond by offering to reupholster the patient's couch.

Families and businesses are being hit by high gas prices. This demands an energy policy.

But all this hearing is about is providing a justification for tax increases.

Now I wish I could say I was surprised. No matter what the question is, it seems that for the president and some of my colleagues, the answer is always raise taxes. Government spends too much, raise some taxes. Health care too expensive, raise some taxes. Gas prices too expensive, I've got it. Let's raise some taxes.

I would be doing a grave disservice to my constituents if I was to ignore the consequences of these tax increases. Some of us are trying to create American jobs, increase energy supply, and reduce dependence on foreign oil at a time when we are still recovering from an historic economic collapse.

The proposals that will be discussed today are completely divorced from those pressing needs. The reasoning put forth for repealing these tax provisions, rising gas prices and reporting high first quarter profits would set a bad precedent for future tax increases.

Are we to increase taxes any time a company sees an increase in quarterly profits due to high demand of a commodity? What if Walmart's profits increased due to a spike in global demand for cotton?

What if an increase in demand for coffee results in Starbucks reporting record profits? What if the Hollywood studios hit a few homeruns with some new films and record profits result?

Well I'm not going to hold my breath waiting for Democrats to haul George Clooney up here to justify -- to justify his income. I do not believe we really want to go down the dangerous road of deterring American businesses from becoming too profitable.

This hearing should not be used to score cheap political points. But I'm afraid with all due respect, Mr. Chairman, that that's what we're going to see here today.

I have a chart depicting what I expect this hearing to turn into. And there you go.

(LAUGHTER)

That's a really nice picture. I think that's pretty good myself.

(UNKNOWN): Who's the horse and who's the dog?

HATCH: I think we both know.

(LAUGHTER)

I know who the horse's ass is. I'll put it that way.

It is perfectly (ph) -- I shouldn't have said that.

(UNKNOWN): Obviously (ph).

HATCH: Elaine's (ph) going to give me heck when I get home. I'll tell you. You'll notice I used the appropriate term there. Now it's perfectly appropriate to examine the purpose, design, intent, and effectiveness of certain tax incentives that promote the domestic production of oil and gas.

Let's have that debate. I'm ready for it. Let's have it.

In 2004, Congress passed the American Jobs Creation Act. The centerpiece of that legislation was the Domestic Manufacturing Deduction.

Now this particular provision was designed to strengthen the domestic manufacturing sector. It is a deduction for manufacturing everything from coffee to appliances, to the domestic production of oil and gas.

The amount of the deduction is specifically tied to wages paid to American workers. The intent was not to incentivize manufacturing and production, but to manufacture and produce within the United States rather than overseas.

Congress passed this provision with the expectation that it would promote economic growth and job creation here in the United States.

Now it is important to note that this provision is not just tied to oil and gas, and to the oil and gas industry. But applies to income derived from all manufacturing within the United States.

Maybe we should have a meaningful conversation about whether this provision is good tax policy. Given that it impacts industries far outside the scope of the oil and gas industry, it is a conversation more properly suited to a debate over tax reform.

But I'm not going to hold my breath waiting for this adult discussion of tax policy. I know the chairman, the distinguished chairman, has been trying to do a series of hearings on tax policy. And I'm personally very appreciative of that. And I applaud his leadership.

Instead though, I expect some good political theater here today. The liberal mouthpieces over at MSNBC certainly had the talking points yesterday afternoon and they're already -- ready to make some political hay at the expense of our witnesses today.

Many will point to a comment made by a former CEO, that oil and gas companies do not need these tax provisions. That CEO might -- might be right.

Oil and gas companies would probably drill with or without these tax incentives. But let's be clear. They would be less likely to do so in the United States.

HATCH: We have to ask whether we want to help increase the market share for U.S. corporations in the global oil and gas marketplace, or do we want to decrease that market share and put ourselves at the mercy of foreign importers?

Now I'm not going to wait for the MSNBC lineup to put on their hardhats and stand on an oil rig and do a promotional ad asking this tough question about the potential loss of blue collar American jobs.

We have a great number of resources that could be used to promote energy security within the United States. I applauded President Obama's recent pledge to reduce foreign oil imports by a third by 2020.

However, I was taken aback when he told Brazil that we want to be their best customers, if they increased their oil production. So it's OK for other countries to produce the energy that will drive our economy, but it is wrong to produce it here at home.

To be honest, I do not know what the president and his administration's agenda is for energy security. And I don't expect to get any clarity on that point today. And I think that is the point.

The American people are upset that high gas prices and are demanding energy solutions. The president has no solution. In fact, his policies would do precisely the opposite of what our constituents are asking for. They would increase the cost of domestic production and harm our economy.

So faced with the uncomfortable fact that the buck stops at the Oval Office and the president's only solution to high energy prices is to double down on them, liberals hope to distract the American people from their failure to develop a coherent energy strategy.

Now, I do know that we currently depend on oil for our energy needs, because it is abundant, and it's dependable. Demand is and will remain high for the next decade and certainly beyond that.

There's a reason why Florida's demand for petroleum-based transportation fuels is among the highest in the United States. There's a reason why states like New Jersey and Maryland consume more gas per capita than most states. And we certainly have the resources to meet that demand.

Just recently, geologists have discovered...

BAUCUS: Senator Hatch, are you almost through? I mean, you've been talking for a long time. We don't have our testimony yet.

HATCH: No, I'm not through yet, and I'm not going to be through until I get through.

We certainly have the resources in this country to meet that demand.

But I'm almost through.

Just recently, geologists have discovered in the western part of North Dakota and parts of Montana a 25,000 square mile sea of oil that could hold the largest accumulation of oil identified in North America since 1968. They have dubbed it the Kuwait on the prairie. About 100 new oil wells are developed each month.

We also have a great deal of oil in the Rockies, on public lands and off our coast. But our president has done everything in his power to shut down federal leases in these areas. Maybe it's just the people working for him. I don't know.

Look, we all know politics is thick in the air here today. Our dog and Connie (ph) would feel very much at home. I gotta tell you that. Many Democratic senators have admitted that it's good politics to take on oil companies when gas prices are high. We all know everyone is angry about high pump prices. We don't need to hold a hearing on that.

But if we want to do something about it, three questions come to mind, and I'll pursue these questions with the witnesses. First question, will the policies proposed by the president and the Democratic leadership caused pump prices to drop?

Second question, if pump prices do not drop, then what will the policies proposed by the president and the Democratic leadership do? One possibility might be that these policies will cause the U.S. to become more dependent on imported oil.

The third question, with respect to tax incentives available for all U.S. manufacturers, is it wise -- and this is an important question -- is it wise to single out one industry and treated differently from others?

I'll put a finer point on the question. Is it wise to conduct business tax reform on a selective and punitive basis? It's a legitimate question, and we ought to answer it.

Let's send the pony back to the stable. That's what we ought to do. Let's send the dog back to the kennel. Let's get back to reforming the tax code to support economic growth.

So far this Congress, we've been making progress in making the tax code more efficient, simpler and fairer. And I know that the chairman is dedicated to that, as am I, and I hope the chairman will continue in these efforts.

Thanks so much, Mr. Chairman. BAUCUS: Thank you very much, Senator.

I would now like to introduce the panel before us. Our first witness is Dr. John Watson, chairman and CEO of Chevron; second, Mr. Marvin Odum, the U.S. president of Shell Oil Company; third, Mr. Lamar McKay, chairman and president of BP America; fourth, Mr. James Mulva, who is the chairman and CEO of Conoco Phillips; and finally, Rex Tillerson, chairman and CEO of Exxon Mobil.

So, Mr. Watson, why don't you begin?

You probably know our customary procedure here is to have your statements included in the record. They will automatically be included. You could then summarize for about five minutes.

WATSON: OK.

BAUCUS: Thank you very much.

Mr. Watson?

WATSON: Mr. Chairman, Raking Member Hatch and members of the committee, I am John Watson, chairman and chief executive officer of Chevron Corporation.

Affordable, reliable energy is the backbone of America's economy and competitiveness. Fortunately, our nation is endowed with abundant supplies of energy, including oil and natural gas.

Each time we come to Capitol Hill, we advocate for measures that would better help America develop our energy supplies. More domestic supply, along with aggressive measures to use energy more wisely, is one of the most effective ways to counter rising energy prices, enhance our energy security, and stimulate economic growth.

Tax increases on the oil and gas industry, which will result if you change long-standing provisions in the U.S. tax code, will hinder development of energy supplies needed to moderate rising energy prices. It will also mean fewer dollars to state and federal treasuries and fewer jobs, all at a time when our economic recovery remains fragile, and America needs all three.

Because my time is limited, I'll make three points today. First, the oil and gas business pays its fair share of taxes. Despite the current debate on energy taxes, few businesses pay more in taxes than oil and gas companies. The worldwide effective tax rate for our industry in 2010 was 40 percent. That's higher than the U.S. statutory rate of 35 percent and the rate for manufacturers of 26.5 percent.

Between 2005 and 2009, our industry paid or accrued to the U.S. government almost \$158 billion in taxes, royalties and fees, including \$98 billion in federal income taxes. That totals nearly \$86 million a day.

Changing important tax provision outside the context of broader corporate tax reform would achieve one unmistakable outcome. It would restrain domestic development and reduced tax revenues at a time when they are needed most.

Likewise, calls to raise royalty fees will increase the cost of doing businesses in place like that deep water Gulf of Mexico and impede development of these resources just when we're getting back to work.

Second, long-standing oil and gas provisions in the tax code parallel tax treatment of other industries or are designed to prevent double taxation of income. For all U.S. businesses, a basic tax principle is that they are taxed on income after costs. All companies in all sectors may detect these costs in various ways.

The oil and gas industry can deduct intangible drilling costs, such as site preparation, labor, engineering and design. These expenses are similar to the research expenses deducted by pharmaceutical and technology firms. These deductions allow companies to recover the costs of risky investments necessary for the viability of their business.

That tax provision some seek to change our long-standing provisions in the tax code. Many apply to other segments of the U.S. economy, including the manufacturers' deduction and LIFO accounting.

We are deeply concerned about proposals to curtail foreign tax credits for dual capacity taxpayers. Credits for foreign income taxes are critical, because without these credits, which are available to all taxpayers, we would pay taxed twice on income generated overseas. This would make us less competitive internationally and cost U.S. jobs that support our overseas operations.

My third point is that there should be equitable treatment for all forms of energy and for all energy producers, large and small. I am an advocate for developing all forms of energy and using energy more wisely, but it's wrong to increase taxes on oil and gas companies to subsidize other forms of energy. This is also likely to have serious unintended consequences for productions, jobs and revenues.

Singling out five companies because of their size is even more troubling. Such measures are anti-competitive and discriminatory. After all, our five companies are providing the technical, operating and managerial expertise that is allowing the global energy industry to operate at the forefront of energy development.

Let me close by suggesting that the most sensible path is simple. Don't punish our industry for doing its job well. Create energy and tax policies that make our country a more attractive place to do business.

Allow us to develop our nation's vast energy resources. And strengthen -- don't weaken -- our ability to compete against large national oil companies, who are major players in the U.S. and global energy markets.

Responsible development of our resources, which will be enabled by sound tax and energy policy, will add more high-paying jobs, provide billions in new tax revenues, and reduce our dependence on foreign energy supplies.

If our nation's concern is keeping investments here at home and ensuring reliable, affordable energy for all Americans, then what we ask for here is what we look for anywhere we invest -- conditions that are not punitive and discriminatory, but stable, transparent and equitable.

Mr. Chairman, I'm proud to lead a 132-year-old American company. I'm proud of the vital role we play in our economy. And I'm proud of the profits allowing us to make significant investments in our communities and the long-term health of our country. Thank you.

BAUCUS: Thank you very much, Mr. Watson.

Mr. Odum? You're next.

ODUM: Thank you, Chairman Baucus, Ranking Member Hatch and members of the committee.

I'm Marvin Odum, president of Shell Oil Company, a shelter global energy company with more than 90,000 employees in 90 countries. Approximately 19,000 of those are here in the U.S., working to discover, produce, market and deliver to consumers today's energy and tomorrow's energy technology. Thank you for the opportunity to speak to you today.

I'd like to address right up front the issue that's on many American's minds -- the rising cost of energy, particularly the cost of gasoline. Because fuels are refined from crude oil, the biggest impact on the price of fuel is the price of crude oil. Everything from weather to politics and the global economy determines the price of oil and the fuels made from it.

Weak economic conditions in 2008 and 2009 lower demand, which helped push prices down. Now with worldwide economic recovery under way, demand is on the rise, sending prices upwards. In addition, because oil is sold in U.S. dollars throughout much of the world, as the dollar becomes weaker, it takes more dollars to buy the same amount of oil.

Simply stated, oil is a global commodity, so while we can't predict or control the price at the pump, we do know that we can increase the stability of our energy future through a combination of efficiency gains and increased supply.

ODUM: And the surest way to address a challenge of this magnitude is to focus on what we can control, using what we know to safeguard against what we don't. Without question, our government is facing significant challenges right now, particularly in terms of economic and energy security. But when you face a deficit, be it energy or financial, choices are usually straightforward - get more or use less. And often it is a combination of both that achieves the best results. And there are choices on how to get more.

I think it can be tempting to assume that there is something to be gained by attempting by taking more from a few. However, one must also balance the implications of increased industry costs on both supply and the cost of fuel. The opportunity in front of us is to put policies in place that allow the energy industry to become an economic growth engine for America.

Developing our own resources, we would tens of thousands of new, well-paying jobs, and many, many billions of dollars in revenue for local, state, and federal governments. Some perspective, last year Shell

reported global earnings of \$18.6 billion. We also invested some \$29 billion, mostly in new projects to bring energy supply to the consumer.

In addition, we spent more than \$40 billion to run our existing businesses worldwide. Last year, in the Gulf of Mexico government policies caused Shell to defer some \$700 million in capital expenditures. We expect to lose an additional or an estimated \$500 - sorry - 50,000 barrel equivalents per day in 2011 alone as a result of that.

Now, thinking about that impact to date, it represents lost gasoline production, just to Shell, that could have powered on average 633,000 cars and light trucks every day since January 1st. And here in the U.S., at the invitation of the federal government, we have invested more \$3.5 billion since 2005 to develop energy resources in Alaska.

Six years later, we have been prevented from drilling a single exploration well due to the government's inability to deliver timely permits to allow this potential new resource to be developed. And during that time we have drilled more than 400 exploration wells worldwide.

My point is this. Investments in our industry carry huge amounts of capital and risk. Policymakers must consider this when thinking about the U.S. relative to other regions. The president recently acknowledged that reducing dependence on certain imports was a national policy imperative. We agree. The U.S. is resource-rich in many ways, especially in oil and gas. Yet is a country we import more than 60 percent of our petroleum at a cost of more than \$350 billion a year.

The bottom line is this. If we don't develop our own energy sources, we will have to accept the costs, both financial and geopolitical, of bringing it into this country from places that can be less secure and less stable.

In closing, Shell is grateful for the widespread recognition in Congress of the daunting energy challenge facing this nation. Although some of our opinions differ, we stand ready to work with you on developing a more secure, affordable, and efficient energy supply for this nation.

Thank you.

BAUCUS: Thank you, Mr. Odum, very much.

Mr. McKay?

MCKAY: Thank you, Mr. Chairman, Ranking Member Hatch, members of the committee. Good morning.

My name is Lamar McKay and I'm chairman and president of BP America. I appreciate the opportunity to address the issue of energy tax incentives today. Before doing so, I want to recognize that last month marked the one year since the Deepwater Horizon accident, and BP continues to work very hard to meet our commitments in the Gulf.

Now, I'd like to provide just a little bit of context on BP's operations and investments in the U.S., both in traditional and renewable energy. BP has a very long history in the United States, over 100 years, with 23,000 U.S. employees and operations spread across the country.

We are committed to providing the U.S. with the energy it needs to grow in the coming decades, and doing so in a responsible and sustainable manner. We're one of the largest oil and natural gas producers in the U.S., and one of the nation's largest energy investors. Now, over the five years ending in 2009, we have invested more \$37 billion in development of U.S. energy supplies. We continue to invest in natural gas production from the Rocky Mountain West and our existing shale gas regions. We have significant oil production in Alaska and the Gulf of Mexico.

Further, we have made and are continuing to make significant investments in our refineries in the U.S., including major capital projects that will increase gasoline production capacity at our key Midwestern refineries. We also invest actively in renewable energy. During 2009, we invested nearly a billion dollars, or 10 percent of our \$9.9 billion of U.S. capital budget, in alternative energy.

These investments include the operation of wind farms in 10 states, development of the first commercial-scale cellulosic biofuel facility in Florida, and work on an advanced biofuels molecule, biobutanol, with Dupont. And we have our solar business, which we've been in operation for over 35 years.

BP supports a comprehensive energy policy that includes all forms of energy, including oil, natural gas, coal, nuclear, biofuels, wind and solar, and encourages efficiency and conservation. The reality is that even with major improvements in energy efficiency and the rapid growth of biofuels, wind and solar, that 20 years from now in 2030 the United States will still depend on oil, natural gas, and coal to meet more than three-quarters of its energy needs.

On the supply side we support properly scaled transitional incentives for alternative energy. But raising taxes on form of energy to encourage production of another will reduce industry's ability to keep up with growing U.S. energy demand. The result could be less investment, less production, tighter energy markets, and over time, potentially higher prices for consumers. Instead, our nation should be encouraging production of all forms of energy, including oil and natural gas.

On the demand side, energy policy should encourage conservation and help drive energy efficiency. The energy challenges facing the U.S. are enormous. The impacts of high energy prices on the overall economy and the American people are very real. We cannot change the international crude oil market which drives those prices, and on which the country relies for more than 60 percent of the oil it consumes. But we can work with the Congress, with the administration, and consumers across the nation to move towards greater energy security and a lower carbon energy future.

Congress establishes the rules regarding energy and tax policy. Companies take those rules into account in making their investment decisions. Because of the long term nature of the significant capital investments that are required to develop and produce energy, a stable and competitive tax framework is critical to the United States remaining attractive in the global demand for capital investment.

The currently contemplated changes to the tax rules would limit the resources companies like BP have to invest, not only in conventional energy production, but also in new and emerging technologies like wind, biofuels, and solar. BP is very serious about bringing new sources of oil and natural gas to market. We're also serious about building a sustainable, profitable, alternative energy business capable of delivering clean, affordable power. And my company stands ready to work with you and others to address the energy and environmental needs of this nation.

Thank you.

BAUCUS: Thank you very much, Mr. McKay.

Mr. Mulva, you're next.

MULVA: Good morning, Chairman Baucus and Ranking Member Hatch and committee members. My hope today is to bring clarity to this vital debate on tax policy regarding the major oil companies. To begin, there's a great deal of misinformation about our tax liabilities. And unfortunately, it's being used to justify further increases. So my objective is to convey, first, the realities of our current tax burden, and second, the negative impacts of new proposals, for there would be impacts to our company, our industry, American consumers, U.S. job creation, and national energy security.

So let's take a look at what we already pay. I have a chart that we've - pointing to. It shows the effective worldwide tax rates of the 20 largest U.S. non-financial companies. And there are a lot of familiar names on this chart. On average, the group paid 27 percent for the years 2006 to 2010. But look at those in three and red.

BAUCUS: Yes, Mr. Mulva, if you could identify a few. I can't read some of those over on the left. If you could just outline two or three during your testimony, that would...

MULVA: OK. It comes after the three red in oil companies, Wal*Mart, Berkshire-Hathaway, Apple, Intel, Microsoft, Procter & Gamble...

BAUCUS: Who's down at the bottom?

MULVA: The bottom? G.E., Pfizer, Merck, Verizon, Coca-Cola, Cisco.

BAUCUS: OK, thank you.

MULVA: So you see at the top, ConocoPhillips 46 percent, followed by the two international American companies. The three major U.S. oil companies already pay the highest effective tax rates in the top 20. And keep in mind that this is after taking the allowable tax deductions and credits.

What does this mean in hard dollars? Well, for our company, we earned \$11.4 billion last year, and we paid \$8.3 billion in income taxes, as well as \$3.1 billion in other taxes. So our total worldwide taxes paid actually equaled our income. So any fair-minded person would likely agree that we pay our full share.

Remember, too, that companies like ours carry the plague of U.S. competitiveness into the battle for global business, and every day we fight for access to energy resources and opportunities around the world. Our rivals are typically nationally owned companies from other countries and they literally dwarf us in size. Some are dozens of times bigger than we are, and they enjoy explicit support from their governments.

Despite these compelling numbers, and despite the need to maintain a competitive U.S. oil industry, some would have us pay even more. In fact, one proposal would only impact the three major oil

companies that already carry the heaviest burdens, would further restrict the oil and tax credits that are available to us. So it would seriously undermine our ability to conduct our business internationally.

That's because when we decide to bid for foreign energy opportunities, we have to include taxes among the total project costs when we can make these investment decisions.

So all else being equal, overseas companies with lower tax obligations can bid -- outbid us and win the opportunities. And unfortunately, this does impact U.S. jobs. For our company, we operate worldwide with 29,000 employees, of which 20,000 are right here at home and some of them, 3,000 U.S. based employees work to support what we do internationally around the world.

So reducing our foreign tax credits, will have a cascading effect on our business. We would lose projects and opportunities to foreign competitors. Cash flows that would otherwise generate tax revenue here, would instead go elsewhere.

Our U.S. job creation and investments would suffer. Further, as profitability declined, it would reduce our ability to invest in domestic energy. And ultimately we could even see more energy and development here conducted by foreign competitors. Which, by the way, would inevitably send dollars back to their home countries.

We currently hear a lot about the so-called tax subsidies. This calls for another reality check. The major companies do not get special subsidies. In fact some deductions and credits available to the industry are not allowed to the three major companies.

And the ones we are allowed, either match or closely mirror those available to all U.S. companies. Even in these cases, the law limits how much we can benefit. That hardly sounds like special industry subsidies. Congress and administrations often speak of enhancing U.S. competitiveness, but enacting the foreign tax credit restrictions and other proposals, would be very counterproductive.

They would penalize U.S. workers and the American public that invest in our shares and they would harm the well being of companies like ourselves that must carry our country into the energy future. And that certainly cannot be your intent. So I urge you to objectively and dispassionately consider the facts and reject these unfair and unwarranted tax proposals.

Thank you.

BAUCUS: Thank you, Mr. Mulva.

Mr. Tillerson? You're next.

TILLERSON: Chairman Baucus, Ranking Member Hatch, members of the committee. I appreciate the opportunity to address the topic of today's hearings; oil and gas tax incentives and rising energy prices.

All of us here today recognize the strain that high gasoline prices impose on many Americans, particularly during difficult economic times. And we owe it to our customers and to your constituents to address the topic of energy prices and taxes in an open, honest and factual way.

Unfortunately, the tax changes under consideration that target the five U.S. companies represented here today, fail to honor those goals. It is not simply that they are misinformed and discriminatory, they are counterproductive. By undermining U.S. competitiveness, they would discourage future investments in energy projects in the United States and; therefore, undercut job creation and economic growth.

And because they would hinder investment in new energy supplies, they do nothing to help reduce prices. There is a more effective way to take steps to reduce prices and raise revenues. But, unfortunately, it is a way Congress and the administration has so far rejected.

If the U.S. oil and gas industry was permitted to develop our nation's enormous untapped energy supplies, it would put downward pressure on energy prices and increase revenues for government budgets. Working together, industry and government can achieve our shared goals. In that spirit, I would like to offer several important facts on the specific tax proposals that are currently being advocated by some in Washington. First, it is important to make clear that tax provisions, such as the Section-199, "Domestic Production Activity Deduction", are not special incentives preferences more subsidies for oil and gas, but rather they are standard deductions applied across all businesses in the United States.

Section-199 applies today to all U.S. domestic producers and manufacturers, from newspaper publishers to corn farmers, to movie producers and even coffee roasters all can claim this deduction, which is intended to support job creation and retention in the United States.

By any reasonable definition, it is not an oil and gas industry incentive. In fact, our industry is currently limited to only a six percent deduction, while all other U.S. manufacturers are allowed a nine percent deduction.

Frankly, to then deny a select few companies within the oil and gas industry this standard deduction, is tantamount to job discrimination. Why should an American refinery worker employed by a major U.S. oil and gas company in Billings, Montana, be treated as inferior to an American movie producer in Hollywood, an American newspaper worker in New York, or an employee of a foreign owned refinery in Lemont, Illinois?

Another tax measure that is misleadingly labeled a subsidy is the "Foreign Tax Credit Provision", which upholds a basic tenant of tax fairness by preventing our overseas earnings from being double-taxed. This provision applies to all U.S. companies with overseas income and has been in place since 1918.

It is mean to protect U.S. competitiveness abroad. Again, U.S. oil and gas companies are already treated differently from other businesses under this provision, which includes unique and prescriptive rules on our industry requiring us to actually prove our foreign tax payments are indeed income taxes and not royalties.

If these rules were changed that the foreign income for select U.S. oil and gas companies like Exxon-Mobile, were to be double-taxed, our foreign-based competitors and the full range of foreign government owned oil companies would gain a significant competitive advantage.

Clearly these tax provisions and others under consideration are not special industry incentives or subsidies. They are economy-wide, generally available deductions and credits under the tax code.

Removing them for a select few U.S. oil and gas companies is; therefore, nothing less than discriminatory and a punitive tax hike, which jeopardizes the jobs of American workers.

Doing so would also do nothing to reduce the prices Americans pay at the pump. Gasoline prices are primarily a function of crude oil prices, which are set in the marketplace by global supply and demand, not by companies such as ours. Furthermore, arbitrarily punishing five U.S. oil and gas companies by raising their taxes, will generate far less government revenue than if we were allowed to compete and produce our nation's own resources.

In August 2010, a Wood McKenzie study estimates that approximately \$10 to \$17 billion in direct upstream investment in this country is at risk per year if the Section-199 and other tax provisions are repealed for our industry. Another recent Wood McKenzie study found that opening up federal lands that Congress has kept off limits for decades, could generate 400,000 new jobs by the year 2025.

And another analysis shows that such actions could generate as much as \$1.7 trillion in government revenue over the life of those resources. The fact is that raising taxes on five U.S. oil and gas companies is simply not the way to reduce prices or raise revenues.

Increasing these company's taxes would only discriminate against certain U.S. workers, make our companies less competitive against others who are in the same business that we are in and discourage future energy investment in this country.

A much better solution lies in permitting our industry to increase energy supplies, including supplies found here in North America such as oil and natural gas found off our shores and in our shale formations. Access, not taxes will enable us to meet the goals of increasing affordable energy supplies for Americans, strengthening U.S. energy security and powering our nation's economy forward.

Exxon-Mobile shares these goals and we look forward to working with you, to achieve them. Thank you.

BAUCUS: Thank you Mr. Tillerson. Gentleman, I appreciate your taking the time to come here. Let me tell you my perspective, which is, as Chairman of the Finance Committee and I speak for all members of Congress, we've got to find ways to reduce our annual deficits and our debt.

It's not an easy task. And to do so we have to find an approach that's balanced across the board. There are lots of interests, lots of competing areas where we can cut. We all know that. So we've got to find a fair solution.

One that's shared by American's and received by American's to be pretty fair, pretty balanced, you know, within the bounds of reason. What you said Mr. Tillerson and what you all have said in many respects is true. You do pay high taxes, that is true.

But it is also true your foreign taxes are higher than your domestic taxes. That chart showed worldwide rate, your domestic tax rate is, you know, quite a bit lower than your worldwide rate. It is also true that the price of gasoline is determined primarily by the world price of crude.

That's the primary determinate. World price goes way up, gasoline prices go up. But it is also true that when the world price goes up, the after tax profits of your companies go up very significantly. Because

your costs don't go up as much, at least in the last year or so, as the world price has gone up -- of crude. When world crude prices go up at such a high rate, your profit margins go way up. That's true. And it also seems to me, based on the evidence, that according to our financial recording statements, if your average cost is roughly \$10.00-\$11.00 a barrel if you add in tangible drilling, maybe it goes up to closer to \$20.00 a barrel.

But in 1910 (sic) your profits, your after tax profits is about \$72.00. Your after tax - no, your revenue, your gross revenue was about \$72.00 a barrel and this year it's much higher. So it just looks, according to the evidence, this is not a matter of singling anybody out, just it's your companies and how much gross profits you make.

BAUCUS: And it's not based on your subsidies; it's based on the world price of crude, that's that it's really based on. It may be a fair way of getting at reducing our deficit and our debt is to reduce, scale back, if not eliminate the tax breaks, which do not have much effect on your decisions to produce.

It doesn't have much effect because your, your profits are so high. The current -- according to these reports, Exxon-Mobile, for every dollar increase in crude, Exxon-Mobile's after tax profits go up to, I think it's \$300-\$350 -- \$375 million a year. If you add all five of you together it's about for every \$1.00 increase in crude, your after tax, your after tax profits go up a billion dollars, you know all together, totaled all up.

And the subsidies were talking about here, there's \$21 billion over '10, roughly \$2 billion one year. Take that down to a quarter, a quarter of two, that's \$500 million.

So if you -- and this is rough, I grant you, this is rough. But if the price of oil which would go down \$2 a barrel, that would be more than the elimination of these subsidies.

So these subsidies really do not have much effect on your decisions where to produce.

Is there profits you have and your -- and your rate of return you're going to get in different locations that really, I'm guessing, have a much greater effect on your ability to produce.

So tell me what's wrong with my analysis. Just seems, frankly, that you're making a lot of money. That's fine. It's the American way.

But it also seems that maybe the subsidies are not really that necessary any more, because many of them were given many years ago.

Mr. Tillerson, 199 is really the aftermath, as we all know, to substitute for FSC-ETI. FSC-ETI was intended to give American companies a break, an export break.

WTO ruled it illegal, so Congress passed 199 for everybody. And it's my recollection that the FSC-ETI really wasn't used very much by you guys. And so it was kind of a gift, 199.

And other companies do use it for export. (Inaudible), in fact, who has -- you don't as much. So I just ask the question. I don't know who wants to answer it.

Just seems to me as we try to get our deficits and debt under control that -- and if oil price is so high and because the subsidies are so low compared to increase in crude oil prices, that they don't -- you don't need it near as much as one might initially think.

I'll let anybody go ahead.

(UNKNOWN): Well, I'll make this a couple of points here. I think...

BAUCUS: My time has expired. I'm sorry.

(CROSSTALK)

BAUCUS: ... very brief, please.

ODUM: So just a couple of quick points.

I think, first of all, if you look at ways to impact the deficit and you think about this in terms of a used word a lot these days, which is sustainability, the way to impact the deficit and get more money into the federal government is through more production, where we pay more bonuses for the access.

We pay more royalties on the production. Those numbers are potentially much, much larger than anything we're talking about here. And that's the -- that's the way, I think, to impact the deficit piece.

I did want to comment on your production costs chart, just because I think it misses a pretty important point, which is the investments that have to be made to produce oil and gas that has those kind of ongoing production costs.

So it doesn't include not only the huge investments, the billions of dollars that go in, but also the time lag from when those investments starts to when that production actually starts to happen.

And the other piece, I think, it probably misses is that looks at all of the existing production that exists across the country today, I would assume, by the -- by what you said.

The cost of future production is not the same as the cost of historic production that's currently online. It is more expensive now.

BAUCUS: Thank you. Anybody else?

Tillerson?

TILLERSON: Well, I think it's helpful if we kind of think about are we going to talk about the past or we going to talk about the future, because a lot of the numbers you're displaying -- and they're not -- they're not entirely accurate in terms of total costs, as Marvin said, are really talking about things in the past and what we've already done.

We are in the depletion business. So we invest in resources that deplete. So we constantly must replace those if we want to have a sustainable business. And we've been around for almost 130 years.

You heard John Watson say 130 years.

So that's what we've been doing for more than a century, is taking the revenues from the past decisions and finding ways to invest that to replace the barrels that are depleting.

As we have to go out and find and locate those replacement barrels, they are -- they are more and more difficult to find. And the real question is not, OK, well, can we afford more taxes.

Well, if we're never going to invest any more, and we're just going to liquidate the company, there's going to be a lot of revenue around. But that's not what we're doing.

We're sustaining the viability of the enterprise for many years to come. So we have to make very large investments.

And the real question is what do these tax changes mean to that next incremental investment decision we're going to make? And that is made on an asset-by-asset, investment-by-investment basis.

So in the United States, if I want to look at a shale oil lease in North Dakota, I got to run the cost of acquiring those leases and drilling and developing and producing and paying all of that.

And I got to put the tax burden on there. You give me a different tax burden than my competitor has, I don't get to develop that lease.

I'm going to take my capital (inaudible) U.S. is not attractive, I've got to go somewhere else.

Offshore, you want to raise the incremental cost of royalty or development cost or taxes on the next investment decision, it's that marginal barrel that you're going to take out of our system.

BAUCUS: (Inaudible) wish I had more time, Mr. Tillerson. My time is more than expired. This is not the greatest forum in the world to get in deeper depth.

Senator Hatch?

HATCH: Well, thank you, Mr. Chairman.

Now this question is for the entire panel. I'd like it answered yes or no if you can, or you can certainly add to it if you want.

As you know, President Obama and numerous congressional Democrats have proposed raising taxes on United States oil and gas production.

However, an Associated Press article from Tuesday about Senator Menendez's bill to increase taxes on oil and gas stated, quote, "Menendez acknowledged that the legislation slated for a vote next week won't do anything about gas prices exceeding \$4 a gallon in many places," unquote.

Now with rising taxes on United States oil and gas production, will raising taxes on oil and gas production lower the price of gas at the pump?

And are you aware of any good or service that has become expensive as a result of being taxed more heavily?

Let me just start with you.

(UNKNOWN): Sure. Senator, directionally, raising taxes on producers raises the cost of crude oil. And the cost of crude oil is the prime ingredient in the price of gasoline.

So raising our taxes will not reduce the price of gasoline.

HATCH: OK.

Do you all agree with that?

(UNKNOWN): I certainly do agree with that, and I think the bigger point behind it is if the production here in the U.S., either you don't have access to it or it's disadvantaged relative to other opportunities in the world. That moves somewhere else.

Therefore, the jobs move somewhere else, the trade benefits move somewhere else. All the attendant benefits go away as well.

HATCH: OK.

(UNKNOWN): No, I don't -- I don't believe, obviously, that raising taxes will lower prices.

I do think the important thing is to have a competitive fiscal environment to attract investments. More investments can raise supply and have an effect on prices.

HATCH: OK.

(UNKNOWN): Raising taxes will lead to less investment, less production, and most likely higher cost per gallon, and less employment.

HATCH: OK. Mr. Tillerman -- Tillerson?

TILLERSON: It's going to have little immediate effect. But the effect will come in the months and years to come, and in terms of raising the cost of development here.

And if a loss of -- like 199 deductions puts more pressure on refining margins, refineries already lose money most quarters.

So if we lose more refinery capacity in the U.S., it means more imported product rather than refining product here.

HATCH: Well, let me ask this question.

My colleague from the state of New Jersey, Senator Menendez, recently introduced a bill that would increase taxes on the top five integrated (ph) oil companies, meaning your companies.

He said in a statement that these so-called subsidies, quote, "only benefit big oil and CEOs," unquote.

Now I'd like to point out to my friend that, actually, corporate management, as I understand it, only makes up about 1.5 percent of the shareholders.

Now, in fact, 41 percent of the shareholders are individual retirement accounts, if I'm right on this, or pension funds.

There is a chart showing the -- this shows the top 10 holdings of the New Jersey Public Employee pension fund.

Now just point to this. As you can see, ExxonMobil and ConocoPhillips are listed among the top 10 holdings.

Now my question to you, Mr. Mulva, Mr. Tillerson, is would increasing taxes on your company affect your earnings?

MULVA: Increasing taxes, obviously, would have an impact on our earnings, and ultimately on the value of our companies and the valuation and the share performance to our shareholders.

So it would have an impact with respect to these shareholders.

HATCH: And all these pension funds.

MULVA: To the pension funds.

HATCH: Those aren't the only -- New Jersey is not the only state that has pension funds.

MULVA: That's true.

And if you take all Americans and retirees and employees, if they are involved in one way or another, directly or indirectly, with a pension fund, they probably are a shareholder and an oil and gas company.

HATCH: Do you agree with that, Mr. Tillerson?

TILLERSON: Yes, raising the taxes, obviously, would affect our cash flow that's available to pay dividends, which go back to the pension companies and institutions that own our shares.

It can affect the overall cash flow and financial management of the company.

HATCH: OK. One last question I -- in my time that I have. I'm sure that you're aware the United States already has the highest statutory corporate tax rate among OECD countries.

Now according to Compustat, a database that collects information from companies' financial statements, the oil and gas industry has an effective tax rate of 41.1 percent, while other industrial companies have an effective tax rate -- tax rate of 26.5 percent.

Yours is a very high tax rate. All of the tax increases we're talking about today would eliminate incentives to produce oil and gas within the United States, it seems to me.

Now do these tax increases encourage you to produce oil and gas, move jobs and investment outside the United States rather than doing it here?

Anybody can -- anyone (inaudible) answer that.

(UNKNOWN): Certainly, tax is a big cost of doing business for us. And it's considered in all the decisions that we make. And it -- to the extent that taxes are higher in the United States, we'll look elsewhere.

To the extent that foreign tax credits are limited, we'll -- it'll be even more difficult for us to compete overseas as well.

So with all the provisions that have been considered, it will make it more difficult for us to do business, raise the cost of doing business, ultimately produce less in revenue for the U.S. government, fewer jobs and move against the president's agenda of reducing imported oil.

HATCH: OK, my time is up, Mr. Chairman.

BAUCUS: Thank you, Senator.

WYDEN: Thank you, Mr. Chairman.

Gentlemen, as you know, this is not the first time that Congress has dealt with this issue.

Five years ago, those who were serving as CEOs then of your companies were asked -- I specifically got into it -- whether they agreed with President Bush's statement.

And I quote here, "With \$55 oil, we don't need incentives for oil and gas companies to explore."

In conditions today, you're pretty much like they were in 2005, record profits, price hikes, certainly above inflation. And Mr. Mulva, you'll recall, you were at the hearing.

And what I'd like to do, briefly for the committee, Mr. Chairman, is actually replay the portion of that hearing where the oil company CEO said they did not need incentives from the federal government when oil was at \$55 a barrel. If we could just show that video briefly.

UNKNOWN: Could you please (inaudible)? Thanks.

(BEGIN VIDEOTAPE)

(UNKNOWN): (inaudible) \$55 oil. We don't need incentives (inaudible). There are plenty of incentives. Today the price of oil is above \$55 per barrel. Is the president wrong when he says we don't need incentives for oil and gas exploration? If I could just have a yes or no answer (inaudible).

(UNKNOWN): No. I don't think our (ph) companies asked for any incentives for exploration.

(UNKNOWN): Sir?

(UNKNOWN): (inaudible) oil companies (inaudible) do not need (inaudible).

(UNKNOWN): Yes, he is.

(UNKNOWN): All right. (END VIDEOTAPE)

WYDEN: John, the reason I wanted to get into this is today's conditions are much like they were in 2005. That's why I mentioned the profits. Certainly the prices are far in excess of inflation. Mr. Mulva, you were there. You specifically said in 2005, "Senator, with respect to oil and gas production, we do not need incentives."

So oil is now right around \$100 a barrel. And my question, I want to start with you, Mr. Mulva, because of your history. If your company didn't need incentives to drill for oil at \$55 a barrel, how in the world can you possibly need incentives when oil is at \$100 a barrel?

MULVA: Well, two -- two aspects of that question first. At \$55 going to \$100, we look at the past. And the easy to find oil has already been found. Our costs go up. Taxes have gone up. Oil is more difficult to find, more challenging. Our costs are changed.

I would also say that in response to the question several years in the past, we don't view the items that we're talking about, foreign tax credits, Section 199, and intangibles to development cost, we don't view those as subsidies. We -- a sense we view those as similar types of provisions that are made available to other companies, all industries in a similar way. So we don't need incentives to drill, as I said several years ago.

WYDEN: Mr. Mulva, then, as now, I'm talking about industry-specific incentives. Percentage depletion, intangible drilling costs, geologic and geophysical costs. These are industry-specific incentives. You all said you didn't need them in 2005. Markets, by the way, were global in 2005, just as they are -- are now.

And I just can't understand how even if you account for all the possibilities in the world how you can make the case that you need these industry-specific incentives when oil's at \$100 a barrel when you told me you didn't need them at \$55.

MULVA: We essentially -- intangible development expenses. We view these essentially similar to research and development technology. Similar types of provisions that are made available to other industries.

WYDEN: No. These are industry-specific incentives, sir. They were in 2005. They continue to be today.

MULVA: Yes, but they're very similar to what's offered to other industries as well.

WYDEN: And -- and I would note you also get the R&D credit as well. But let me just go right down the row. Mr. Watson, your predecessor at Chevron said that he didn't need incentives as well at \$55 a barrel.

WATSON: Senator, I'd like to offer several comments, first in response to a couple of things you said. You talked about percentage depletion. These companies aren't eligible for percentage depletion. So perhaps there's some confusion about what we're eligible for.

WYDEN: When -- when - we're talking about industry-specific provisions. And that's what the president was talking about in 2005. That's what I'm talking about today. He just said incentives. And you all said you didn't need them in 2005. And it sure seems to be a different story today.

WATSON: First, we're not eligible for percentage depletion, which you cited. Second...

WYDEN: You're eligible for a lot of incentives.

WATSON: There are -- you cited the conditions were exactly the same as 2005. They're not, respectfully. We have seen costs rise dramatically in our business. Any of a number of published indices would tell you that the costs of doing business have more than doubled in our industry since that time. We're not asking for special treatment. We're asking for the same treatment and comparable treatment to other industries, Senator.

WYDEN: If -- if you look at what the Congressional Research Service has even said, and they've said that - that recently, you all continue to go way beyond inflation in terms of your costs. In fact, if you took inflation-adjusted prices, today the price of oil is higher than it was in 2005. That is adjusting for inflation. Thank you, Mr. Chairman.

BAUCUS: Senator Snowe.

SNOWE: Thank you, Mr. Chairman. And I welcome all of you here today. And I felt like I was in a time warp when Senator Wyden was mentioning that hearing because I was there as well back in 2005.

I think the greatest travesty for this country frankly is that we don't even have an energy policy. I don't know how many energy crises that have to occur in more than a generation to prompt and compel a president and a Congress to develop a comprehensive energy policy. It's transcended many administrations and many Congresses and it's alluded us. And hence, you know, what we're dealing with here today.

So we're going to have multiple hearings. But if the hearings don't result in action in creating that policy, we have let down the American people. And we should be examining all aspects and all facets of what we do.

And that's the necessity of why we have this hearing today. But we should examine all the subsidies and all the tax incentives that we provide in the tax code, frankly. We've put many of them on cruise control for so long.

The challenge that we're facing today -- and I hope Mr. Chairman will have more hearings on all these other subsidies and tax incentives, because, you know, we haven't looked at them in terms of their effectiveness. I think we need to have an energy policy. I think the president and the Congress ought to do it. That's what people are asking. "Why can't we get an energy policy?" We just put, you know -- so I think that that is an abject failure without question. The real issue for us here today is to address the effectiveness of the tax incentives that you're -- given your industry, given that you obviously provide a very basic commodity to the American people.

And in my state, they pay on average \$3,500 for oil and electricity, and another \$1,650 for gasoline. American consumers right now are paying the third highest consumer bills in one month, which was last month. So obviously we have to look at everything in terms of what we can do to mitigate those prices.

Now, back in 2005 oil per barrel was \$65. Today it's, as you know, \$100, \$104, \$110, it may be estimated. Oil's gone up, a 87 percent increase. Gasoline in 2005 was \$3. Now it's more than \$4. A question I have for all of you, there are two things.

One is, you know, what can you tell us that we can tell the American people and our constituents how effective these benefits have been to your country in helping to mitigate those prices. First of all.

Secondly, there was a report that was done by Wood MacKenzie for the American Petroleum Institute last August. And they talked about in speculating about removing these tax incentives how it would alter the break-even point for oil, that is the cost or profitability from an average of \$47 per barrel to \$52 per barrel. And that if oil is placed at points higher than \$80, the (inaudible) of these incentives would not result in any lost oil production.

So I'd like to have your comments on whether or not you agree with that. Is there a point at which, you know, we've removed these incentives at a price point, you know, beyond \$80 or beyond \$100? I'd like to have your response to that as well.

But first, what about the effectiveness of these? What can we tell the American people. How have they benefited? That's what we have to examine. And that's what we should examine, by the way, on all tax incentives and breaks that are in the current tax code. Mr. Watson?

WATSON: Senator, thank you. I understand some of the concerns. In California we have very high gasoline prices, a high unemployment rate, and a lot of people are hurting these days. And they ask the same -- the same questions.

I would tell you that the -- the policies that we've had over the last decade have provided some benefit in terms of U.S. oil production. Last year we did increase oil production because over the last decade we had opened up acreage to development and we had had stable and predictable tax policies in place.

What we've seen recently is that we haven't conducted lead (ph) sales. We've had a moratorium on drilling in this country, and we're contemplating tax increases that will only move production in the other way -- the other way.

The Woodmac (ph) study that -- some of the Woodmac (ph) studies that I've seen indicate that the impact of a \$5 billion increase on our industry would have a dramatic impact on production going forward.

They've talked about reductions in production, domestic production of some 400,000 barrels a day with substantially more at risk. So that's -- that's -- that's the dilemma that I think we have when we think about increasing taxes on the producers in this business.

SNOWE: Even in the context of record profits, I mean, it would still have an enormous impact on your industry?

WATSON: We make about -- we make about 6 cents on sales. And we make about 6 cents a gallon in our gasoline business. If there's a big concern about gasoline prices, federal and state governments make 50 cents a gallon. There's an opportunity to reduce prices significantly.

SNOWE: Mr. Odum?

ODUM: Well first of all, I couldn't agree with you more about needing a long-term energy policy. Because I think ultimately we have to get to the fundamental issue here, which is something that has to be addressed over a period of decades in my opinion. But you need a real strategy to execute to do that.

I think if I -- to go to the question of has -- has the current tax structure helped investment, I think we're in a position today where the U.S. is competitive and it attracts investment. So to give you an example, we're growing our business in the U.S. We've made on average over the last five years about \$3 billion a year in income from just the U.S. We've invested about \$6 billion a year in capital projects for new energy projects. So I think that shows you that -- that this is competitive.

ODUM: The -- the issue then, to address the more fundamental issue and to (ph) have the larger financial impact on the U.S. is to provide more access, bring more production on line, and bring more revenues into the federal government.

And I -- I can give you a very clear example. And then I'll -- I'll yield to somebody else. But if you look at offshore Alaska, the University of Alaska has done some studies there to where it's -- of course it's an enormous resource potential. But the -- the estimated number of jobs associated with developing that resource is over 50,000 for a multi-decade period of time. The amount of revenue that would come from developing those resources is something on the order of \$200 billion to -- to government, to the U.S. state, local and federal governments. So there is a real opportunity here, but we have to take a longer term view.

BAUCUS: Thank you very much, Senator.

(UNKNOWN): Thank you.

BAUCUS: Senator Schumer?

SCHUMER: Thank you Mr. Chairman. Thank you all for coming. First, one of my colleagues suggested that this hearing is nothing more than a dog and pony show. We'll, you'd have an easier time convincing

the American people that a unicorn just flew into this hearing room, than that these big oil companies need taxpayer subsidies. That's the real fairy tale.

And I would just say to everybody, the average American family getting gouged at the gas pump across America and being asked to sacrifice because of a budget deficit, certainly doesn't think this is a dog and pony show.

Now, I'd like to just ask my colleagues here about the question of priorities because we frankly sit in different seats than you do. And your job is to maximize that's good for your stockholders and good for your employees and I think we all understand that.

But we have to choose priorities and right now we have a huge budget deficit. And many, particularly my colleagues who will put forward budgets on the other side of aisle have said, that budget deficit even though we don't like it, says we should cut aid to students who need to go to college.

We should cut cancer research. We should cut homeland security and veterans funds. And it boils down to priorities because we have to get the deficit to a certain level and we have choices. So I want to ask you sitting in our shoes, just about your priorities.

So, my first question is to Mr. Mulva and I'm asking you for a reason, do you think that your subsidy is more important than the financial aid we give to students to go to college? Could you answer that yes or no?

MULVA: Well that's a very difficult question for me. They are two different, totally different questions.

SCHUMER: But we have to weigh those two things, Mr. Mulva. We have to weigh it. Because we have to get the deficit down to a certain level. Which would be -- if you had a choice of one or the other as an American citizen, which would you choose?

MULVA: Well, Senator, that's a choice that legislatively you're going to have to be making.

SCHUMER: We are.

MULVA: For our company, what we are tasked with is to provide energy in an affordable way for, for the American public.

SCHUMER: So you would choose the oil subsidy over aid to students? That's what you're telling me. Which, I think, most Americans, even those who worked in oil industry would probably agree with. And I want to ask you one other question, that's why I asked you first.

Your company put out a press release yesterday. Here's what the headline was; "Conoco-Phillips Highlights Solid Results and Raises Concerns Over Un-American Tax Proposals at Annual Meeting of Shareholders." Do you think people who advocate cutting student aid, are they un-American too?

MULVA: Well Senator, that media release is ...

SCHUMER: You know, what do you mean ...

MULVA: Nothing was intended personally or anything like that. Quite contrary, our release specifically refers to tax proposals and the subject matter that we're talking here today.

SCHUMER: I want to ask you a specific question, do you think anyone who advocates cutting these subsidies is un-American? Yes or no?

MULVA: Well ...

SCHUMER: Yes or no, Sir. That one we deserve a yes or no answer on. It was your release that said un-American? Yes or no?

MULVA: Senator, maybe you could hear me out on this because it's a very important question so I just - if I could, make a comment or two to respond to your ... SCHUMER: Do you apologize for it?

MULVA: Make no mistake, were these proposals enacted that we're talking about today, which you say subsidies, incentives -- if they were proposals that the Senate is considering and the committee is considering, if they were enacted into law, they would place the U.S. based oil companies, natural gas companies like our company, and probably others ...

SCHUMER: We have limited time. I know your view on the issue. Do you consider it un-American to have a different view? Yes or no?

MULVA: Senator, I believe that the proposals under consideration are going to have a very adverse impact with respect to energy policy ...

SCHUMER: I know, but ...

(CROSSTALK)

SCHUMER: But, Sir, there are many people who disagree with that. You obviously have your point of view. That's why you're here, I'm glad the chairman let you do it. But do any of you others consider it un-American to be against the subsidy that you're for. If you do, raise your hand.

All right, thank you. I appreciate the other four of your not labeling those who are different from you, un-American. Thank you, Mr. Chairman.

BAUCUS: Thank you, Senator.

Senator Roberts?

ROBERTS: Very difficult to follow the unicorn from New York.

(LAUGHTER)

ROBERTS: ... who has a very sharp horn. Are you all right over there?

(LAUGHTER)

ROBERTS: Sometimes the unicorn can sort of morph into a rhinoceros and you don't want to mess with the rhinoceros.

(LAUGHTER)

ROBERTS: At any rate, I'm not making assertions there Chuck, yet. Mr. Tillerson, I met with a young man yesterday who was the manager of a small Exxon refinery, partly owned by CITGO, OK -- Hugo Chavez -- in the Mountain West region of the U.S. who was seriously concerned about his job security and the job security of his 250 other employees working at his refinery because of the legislation seeking to repeal Section-199. And I note that because his refinery is partially owned by CITGO, that repeal of this tax expenditure would, would not affect Hugo Chavez's interests. But what is? Now I'd call that sort of un-American. Sorry, Chuck, but why on earth would we be taxing a U.S. company and this young man very worried about his future and then letting big Hugo do his thing in Latin America, Central America?

There might be some confusion, I think when some of my friends claim that removing these tax expenditures won't have any impact on the domestic oil industry. So why would this young man, Mr. Tillerson, think differently? Hasn't the refining sector seen as much profitability as the oil exploration and production sector? Are the jobs really at risk if these taxes are revoked?

TILLERSON: Well, if you look at our own refining operations, refining has lost money five of the last eight quarters. We made some money in the first quarter. We lost money in the fourth quarter. And it gets back to what is the price of gasoline? What's in that?

And it's fundamentally the cost of the crude oil that the refinery has to acquire. We are one of the largest refineries in the world. We produce about 2.5 million barrels a day of crude oil. We refine five million barrels a day of crude oil.

So we are in the market of having to purchase 2.5 to three million barrels of crude oil every day to feed our refineries. So when the cost of the oil is high, as the refiner's margin gets squeezed, they're unable to pass that through to the finished products fully.

So the refiners do struggle with very thin margins. So, when you increase the tax burden on the refiner, you erode his margin. And when you lose money five out of eight quarters, obviously it's pretty skinny already.

ROBERTS: I appreciate your answer and I'm sorry for staff getting me straightened out. Mr. Chairman it was my marching orders, now I understand, to present the statement by Senator Cornyn and I've got a minute 37 that I'm going to yield back and I would like permission to express Mr. Cornyn's statement at this point if that be permissible. I don't want to tread on anybody's time over there, or whatever.

BAUCUS: Go ahead, you've got some time. Let's use it.

ROBERTS: All right. Well, I'm going to skip the thank yous to you and to Ranking Member Hatch, although I certainly want to thank you and so does Senator Cornyn.

BAUCUS: Great.

ROBERTS: And obviously I'm not Senator Cornyn. I don't even look like him. But at any rate, he goes into how important this issue is. A multitude of variables impact on the cost of gasoline, that we don't overlook the main factor. In fact the prices at the pump, that's what Senator Hatch said -- I'm skipping here -- with roughly 70 percent of the price of gasoline and diesel contingent on the price of crude, it's easy to understand any fluctuations in global supply and demand of crude is the most important factor at what the consumer pays for at the pump.

And he goes into the fact that we're already relying on foreign countries and understanding again that this commodity is traded on a global scale. And increased production can't serve as an immediate magic bullet for solving rising gas prices, but it's a strong start.

And he supports the domestic exploration and drilling and to fight against our almost national -- or nine percent national unemployment rate, why then would we pursue any policy that's counter to this type of job creation? And he indicates that the proposals -- we'll now call them the unicorn proposals, by some of my colleagues in Congress and by all present would be counterproductive.

And then he has a video. I'm not a chart man. I'm not a video man, but I'm now Senator Cornyn and so we have a video and I would like to have somebody play it ...

BAUCUS: Senator you've gone over 20-30 seconds already. How long is this video?

ROBERTS: Well, its two minutes and I, see I ...

(CROSSTALK)

ROBERTS: I'm Senator Cornyn, so now I have 10 minutes and I've still got time.

BAUCUS: You are one Senator. There's no one -- you're the incomparable Senator Roberts. There's no other Senator.

ROBERTS: I appreciate that. We weren't jointed at the hip. We were separated, but if we could play this thing then I'm going to be in a lot better shape with my colleagues. It's only 30 seconds, I'm sorry. We just cut it down from two minutes ...

(CROSSTALK)

ROBERTS: OK, 30 seconds. Here we go. Sir, you're right in front of the television.

(BEGIN VIDEO CLIP)

PRESIDENT BARACK OBAMA: Oil you recently discovered off the shores of Brazil could amount to twice the reserves we have in the United States. And when you're ready to start drilling, we want to be one of your best customers.

(END VIDEO CLIP)

ROBERTS: See, that was 30 seconds that a little over a week ago the president called for reducing foreign imports by a third. There's a serious disconnect and that is the comment by Senator Cornyn and I truly appreciate your lenience and your, your treatment of this poor minority member.

Thank you, sir.

BAUCUS: Thank you, Senator.

Senator Cantwell?

CANTWELL: Thank you, Mr. Chairman and thank you gentleman for being here today. I know the subject of this hearing is about tax subsidies and the effects on the deficit, but I would also like to get your opinion about this issue, obviously on the price of oil today.

Because many Americans are definitely feeling the impact at the pumps.

And Mr. Odum's testimony talked about how oil is a global commodity and that oil companies are price takers, not price makers. I'm assuming generally people agree with that statement that Mr. Odum had in his testimony.

Thank you.

What role do you think the excessive speculation in the futures market is having on elevated oil prices? And I know that, you know, some of your colleagues -- I think, Mr. Tillerson, the past you talked about speculation and a weakening dollar having more of an effect than supply and demand.

So could you comment about speculation, excessive speculation in the market and what effect you think it's having on today's prices?

TILLERSON: Well, it is -- it is very difficult to precisely say what impact it has, and it's also very difficult to separate in the marketplace speculation and risk management, because the two are actually quite intertwined in terms of how people manage the risk of the price of the fuel, whether they're a consumer or a producer.

I would give you just one benchmark. Immediately after the Libyan outbreak, the fighting that we have, within the next day the price of oil went up \$12. Now, nothing had changed in the global supply the next day, so what was the market reacting to?

It was reacting to some level of insecurity about what the future supply was going to be. So that is people pricing into the global market what they believed their cost is going to be sometime in the future, building in their concerns and their worries about other possible supply disruptions and the ability of the market to respond to that.

As time goes by and people see how the market responds, then it'd just back, so it goes up and down.

CANTWELL: What do you think -- what do you think the price would be today, if it was based on fundamentals of just supply and demand?

TILLERSON: Well, again, it's -- if you were to use a pure economic approach, the economist would say it would be set at the price to develop the next marginal barrel, OK?

CANTWELL: What do you think that would -- what do you think that would be today?

TILLERSON: Well, it's -- it's pretty hard to -- to judge, but it would be -- you know, when we look at it, it's going to be somewhere in the \$60 to \$70 range if you said if I had access. That's the assumption. If I had access to the next marginal barrel, what would it cost, everything in, to put the next barrel of supply in?

Now, as soon as I develop that one and it depletes, then the next barrel marginal cost goes up, OK? Now, over the years the industry has historically done a very, I think, successful job of mitigating that technology advancements, efficiencies, things we learn how to do better to get -- keep the cost of the marginal barrel down.

But in a purely economic, you know, if all things were according to economics and people didn't risk manage and they didn't do everything else they do, it would be set at the marginal cost of the next increment of supply.

CANTWELL: \$60 to \$70 a barrel sounds pretty good today. I can tell you that.

TILLERSON: And then when we produce that barrel, it'll be what's the next barrel cost.

CANTWELL: You know, I am and, oil dropped to 5.5 percent yesterday. Last week it was 8.6. I don't think that has to do with the dollar, Mr. Odum, or weather. I think that has to do with a lot happening in the volatility of the market. And I'm curious as to what you think that -- what we should be doing about that volatility.

Mr. Odum, do you have any comments?

ODUM: Yes, I can -- some of the factors that I mentioned are clearly factors. Now, neither one may be dominant in the current day or the current week that we're talking about, but all of those are very real factors on the price.

I think on the -- on the topic of trading, though, it's -- you know, I'm -- I'm anything but a trading expert, but I do know it's been studied many, many times by the CFTC and others to try to understand some of the questions you're asking. What is -- what is the -- the increase in price that could be associated with that?

I do know that it serves a very important function, you know. Whether it's an airline trying to have predictability around its -- its fuel costs for the future and so forth, it does serve a very important function.

CANTWELL: Well, I -- I would just say this, that with 70 percent of that futures market now being made up of speculators, that are not the end use of not oil product, is a problem.

To go from having the market made up of 30 percent today of people who legitimately have to hedge dominated by 70 percent of people who are just getting, obviously, in on this oil game is a problem.

Do you -- do you agree? Or do you think that that's -- that's OK to have the market driver your price and you come here to talk about these subsidies as an end result?

Mr. Tillerson, I see you smiling. Do you have any comment about that?

TILLERSON: Well, we don't -- we're not traitors ourselves, so we are not in that part of the market, so we're observers. And that's why I say we're price takers. We're physical buyers and sellers of barrels.

The market decide, again, as I said, based on their view of -- and it's really a view of the future, because it is a depleting resource. What's going to be the availability of the oil sometime in the future?

And the market tries to decide that based on a whole range of things it worries about, and then it translates that back to a price today. And that's the price we take.

And -- and it'll be -- it'll just be wherever it will be. And it's been at \$9 a barrel. It's been at \$8 a barrel during my career, and it's been at \$147 a barrel. And that's the nature of a commodity. And it's the nature in this case of a very volatile commodity.

CANTWELL: I -- I disagree. I don't think that's the nature of how the commodity markets were established. The commodity markets were established to basically prevent or to basically lessen the risk that individual users have to take.

And now with 70 percent of the market being driven by speculators that are not be and takers of any product, I think you're seeing this price driven up way in excess of what the fundamentals of \$60 to \$70 a barrel that you say would be supply and demand.

So thank you, Mr. Chairman.

BAUCUS: Thank you, Senator.

Senator Menendez?

MENENDEZ: Well, thank you, Mr. Chairman.

You know, first of all, let me say I really appreciate Senator Hatch spending so much time on the research he has done on New Jersey, although I take offense to -- in his opening statement -- to aspersions cast on New Jersey, even though they're subscribed to some comedian.

And the fact of the matter is what we have is a lot of hard- working New Jerseyans who are being hit really hard at the pump and at the same time are subsidizing these big five oil companies. So I'm sure my colleague from Utah will be happy to tell his taxpayers why he supports that.

And I agree about the dog and pony show. I would not hold my breath, waiting for Republicans to say to our friends in the oil industry, "You have to be part of shared sacrifice in reducing the deficit of this country" when the average American is making median income of \$50,000 and these companies on average are making about \$25 billion projected this year and somehow only in Washington would be eliminating those corporate subsidies a tax increase.

So I'm glad I didn't hold my breath for that.

I want to first ask Mr. Mulva. Yesterday in a press release your company called proposals to eliminate wasteful oil subsidies un-American. And I want to hear from you do you make those accusations lightly, or did you really mean to question my patriotism and the patriotism of the 28th of the United States senators who are co-sponsors?

Do you believe that President Obama is un-American, because he has proposed cutting oil subsidies? Do you believe that former President Bush, Speaker Boehner, Congressman Ryan are un-American, because they have expressed cutting oil subsidies?

MULVA: Senator, there was the media title of our media release. Nothing was intended to be personally directed to you, any of the centers, colleagues or anyone.

It was merely utilized in a way that we felt that tax proposals that are being under consideration were inconsistent with the treatment of all taxpayers in a similar way and to highlight or in a discriminatory way different companies for different tax treatment.

MENENDEZ: But if you -- but if you believe at the end of the day that those proposals, which I can understand you might disagree with, but you classify them as un-American, that means those who promote them are un-American.

And I -- I just -- I think that's beyond the pale. That is beyond the pale. And I was hoping you were going to come here and apologize for that, because it's simply beyond the pale. So are -- are you willing to apologize for what your company...

MULVA: Senator, what I -- what I just said, there was nothing intended personally. What was is...

MENENDEZ: So you're not willing to apologize.

MULVA: ... we felt that the tax proposals under consideration were a question of fairness. And the other was that tax proposals under consideration were inconsistent without -- without having an energy policy, but it would have an adverse impact...

MENENDEZ: OK. So the bottom line is you're unwilling to apologize for a company's statement. OK, so I'll continue to take offense to it.

Last year, could fill up spent nearly \$4 billion buying back its own stock, which, of course, helps raise stock prices and enrich investors in the companies like yourself. It seems to me if subsidies were cut, couldn't you simply buy back less stock and make consumers whole?

MULVA: Senator, our share repurchase that we've announced is in the neighborhood of about \$10 billion, and it essentially equates to the sale of our 20 percent interest in a Russian oil company called Lukoil. And we felt the opportunities for investment in Russia were not as great as opportunities of essentially in owning shares in a Russian oil company were better treated by owning our own shares.

That had nothing to do with respect to our capability in investment for energy opportunities, as well as paying dividends to our shareholders.

MENENDEZ: But you took those profits. You had a lot of decisions as to how you would take those profits, and you put it in -- in the whole purchase of stock repurchase.

Let me ask Mr. Tillerson. I've heard a vigorous defense of preserving tax rules that allow oil companies to disguise foreign royalty payments as foreign tax payments and therefore get a U.S. foreign tax credit.

Now, why should taxpayers in the United States these subsidizing your drilling in Indonesia, where royalty payments are hidden as a 44 percent tax on oil companies? Why should U.S. taxpayers be in essence subsidizing the foreign production of oil?

TILLERSON: They're not.

MENENDEZ: How are they not, when in fact that those are royalty payments.

TILLERSON: They're legitimate income taxes paid to the government of Indonesia. As I said in my statement, one of the ways our industry is treated differently on the foreign tax code than others is that we must prove that these are income tax payments and not royalty payments.

So the Internal Revenue Service, which we house 35 auditors 365 days a year in our offices, look at those very thoroughly. And we must prove to them that in fact they represent income taxes and not royalties.

MENENDEZ: Well, clearly, if you pay as a structure taxes to a foreign country, the IRS doesn't have a lot of opportunity to dispute that. But if, in fact, you devise your agreements in such a way that having the payment of royalties be a tax, you get a deduction here in the United States. And that simply means U.S. taxpayers are subsidizing.

I -- I find it hard, gentlemen -- I see my time is up.

But I find it hard to understand how you can come here before this committee and the American people and say, when you are projected to make \$125 billion in profits this year, that you simply cannot -- which the marketplace is driving you to exploration and production; you really don't need this to pursue production and exploration -- that somehow the loss of \$2 billion a year, which means you would only make \$123 billion dollars in profits, is somehow so punishing, somehow not part of shared sacrifice, somehow you need to go back at them at the pump to make up for it. It's hard to understand. It is hard to understand.

I really thought you'd come here with a different view, like when the auto industry came here in a different context. They came in a different view. You are really surprising to me.

And, Mr. Mulva, I am shocked that you're not willing to acknowledge that your company's statement, that this is un-American, is ultimately casting an aspersion upon all of us who have a different point of view with you.

(CROSSTALK)

(UNKNOWN): Thank you, Mr. Chairman.

BAUCUS: Senator Cardin?

CARDIN: Thank you, Mr. Chairman, and I thank all five of our witnesses for being here today.

I want to make an observation first in regards to some of the points Senator Hatch made.

I think the best thing we can do to strengthen pension plans in this country is that a growing, strong economy with stable energy prices, I don't think the profits of the five big oil companies have much to do with the stability of the pension systems. And I'd just make one other observation, and that -- the point that Senator Menendez made, the math here just -- I listened to your responses.

And the math is so overwhelming with five companies that are making in excess of \$100 billion a year, I don't want to say that \$4 billion, which is, I think, the number of these tax issues, is insignificant.

But it's certainly a very small amount of money, whereas \$4 billion is a huge amount of money in regards to the decisions that we have to make here on priorities, whether it's our children or our seniors or America's growth.

I just think we have to put this in proper context. We have to make some tough decisions. And it seems to me this is one area that we should be able to reach some common understanding.

And I would just urge you to understand the difficulties of our economy on balancing our budget and the long-term impact of this deficit. And we're all going to have to make sacrifices in that regard.

And it seems to me that five companies that make over \$100 billion, there's a reason why we're looking at this.

I want to go, though, to a bipartisan issue, one which Senator Lugar and I have championed, and that deals with the issue, Mr. Odum, that you mentioned, on stability of the supply of oil globally, and that is to deal with good governance and transparency.

In so many countries that have mineral wealth, the countries are incredibly poor as far as the living conditions of the people in that country.

And the reason is that the mineral wealth never gets to the people.

It's used, in many cases, to finance the corrupt system, leading to the instability, as we've seen in recent months, when you have autocratic systems that are not transparent, the people ultimately will stand up to that.

But in the meantime, we have an unstable supply causing investors to be very nervous about putting money into those countries.

So Senator Lugar and I have been working for some time to support, first, the Extractive Industries Transparency Initiative, which works in some countries, but many of the oil-rich countries of the world do not participate in the extractive industries.

And therefore we were successful in getting as part of the Dodd- Frank legislation a disclosure to be made with the SEC as it relates to payments paid by oil and gas companies to other countries -- oil and gas companies to countries so that we can have more transparency and better good governance in these countries. The industry, at times, has been helpful to us on transparency. For reasons I quite don't understand, there seems to be a reluctance (sic) as it relates to this most recent change.

This applies not to U.S. companies, it applies to all companies that have to move on the SEC.

And the news, quite frankly, is that we have friends in Europe, in Canada, in other countries that want to see this made worldwide on all the exchanges, so that all companies will, as a matter of good governance, is going to have to disclose these payments.

There was a time when bribes paid to other countries for business was a way of life.

But we stood up to that and said no to that type of practice, because we knew that this was not in the U.S.'s long-term interest.

I would just urge you -- and I would like to get your response -- urge you to work with us so that we can get more stable countries around the world, which is in our interest as well as the people who live in those countries. And we need your help.

And I just am curious as to why we seem to be at odds on this issue.

And I would hope that you would not only comply with the spirit of the bill that was passed in Congress, but help us make sure this is implemented in a fair way to accomplish its results.

Mr. Odum, you're the one who mentioned stability, so that's the reason I directed the question, at least, first to you.

ODUM: Well, no, I appreciate your comments, Senator.

I think it's pretty clear that I think with our interchange, you know, between our company and yourself and others, that we support the intent of transparency.

We actually work quite hard for transparency around the world through various initiatives.

I think some of the constructive and pretty comprehensive input that we try to give is that we need to do that in a way that doesn't force these companies into an uncompetitive situation, that recognizes some of the challenges that we have with the foreign governments in terms of enforcing something that may actually be illegal in some of these countries, and sorting out that balance.

So I'd -- there are complications associated with this. Support the intent and trying to work with you on how to get to the right answer...

(CROSSTALK)

CARDIN: (Inaudible), the standard contracts that they're deal (ph) with have exclusions for SEC-required followings.

So it seems to me that the points that you've raised, that you would be in conflict with the host country is not what's in the standard contracts that you deal with. But...

(UNKNOWN): Senator, if I could just perhaps offer a couple of comments on this item, we, too, have been very active in EITI.

We have a comprehensive human rights policy and, frankly, agree with the objectives of what you're describing.

Forcing U.S. registrants to disclose the voluminous information that is required under the law not only is onerous, but puts us at a competitive advantage to those that don't have to comply with the law.

It's very one-sided law at this point.

CARDIN: Work with us so that everyone has to comply with it. That's what we want to do.

We have friends in Europe, friends in Canada, friends around the world who want to work with us to make sure this is a uniform policy.

(UNKNOWN): If you can -- if you can find a way to have Russian, Chinese, Indian and other companies comply with the law, so that everyone is forced to comply, that might be a different story.

CARDIN: With you on my side, I can get there.

BAUCUS: (OFF-MIKE): Thank you, Senator.

Thank you, Senator.

Senator Rockefeller?

ROCKEFELLER: Thank you, Mr. Chairman.

It's been interesting to -- just to observe the hearing. I mean, the polemic that started it out, and then the five of you. And, you know, Mr. Tillerson, you're doing very good things with the Boy Scouts.

It affects my state of West Virginia. But I can't -- I can thank you for that, but I can't thank you for a lot of other things.

I get the feeling that it's almost like you're -- the five of you are like -- are like Saudi Arabia, that you're caught up in your profits. You're highly defensive. You yield on nothing.

The concept of sharing means almost what you've said, it almost means that you'd have to move to another country, which I don't accept, because you're all already in all kinds of other countries.

You're all over the world, all of you. I guess, most (inaudible) all of you are. But I'll -- sort of being out of touch, not only with what we're going through in terms of Chuck Schumer's questions, but with American people. I don't think I can blame you for that.

I think I can just observe that, that the nature of your life, the nature of your international travel, the nature of the size of your profits, I don't think you have any idea of what the size of your profits does to the American people's willingness to accept what you have to say, which is basically anything you do to increase our costs is going to force us to go overseas, which I don't accept.

I mean, I think you're saying that. You can get away with it. I can't prove you wrong. But I don't believe. So, I mean, I just want that on the record. I think you're really out of touch.

We are making, in these budget decisions -- the Ryan budget would cut the U.S. government in half, in half, people dollars (ph). And all kinds of things would just stop happening.

Now I come from West Virginia and I care a lot about Medicaid. I care a lot about education, about Head Start, about the National Cancer Institute, about NIH.

All kinds of things are going to take enormous hits while you're not.

My guess is that you will be able to protect yourselves because traditionally all companies have been able to, through their lobbyists and through friendships and through placements of refineries in so many senators' states, et cetera, you're able to prevail.

You're accustomed to prevailing. You assume you're going to prevail, which is part of what I think creates the distance between us and you and perhaps between you and the problems that this country faces.

I don't know how serious you are about those problems. I mean, we're kind of terrified up here. I mean, what -- the thought -- we had a meeting with the president yesterday. The sizes of the cuts were awful.

I mean, there -- it means people lose their health insurance.

It means all kinds of things, Head Start, all kinds of things just stop happening, not in what he suggested, but in the scenario that possibly could come out of this budget-cutting atmosphere.

So let me just stipulate that.

I think you're out of touch, deeply, profoundly out of touch, and deeply and profoundly committed to sharing nothing, because if you share something, you get on the slippery slope.

If you give up something, you're on the slippery slope. If you -- if you give up something that, you know, would have you explain that to you stockholders and all the rest of it. Let me ask you just two questions.

Senator Wyden made very well the point about the \$55 a barrel. And now you're at \$102 a barrel.

ROCKEFELLER: And talk about having to move overseas, et cetera, how much profit on a barrel of oil do you have to make to not be needful of these subsidies that we think you don't need, but you say your life depends on?

At some point, you know, you wouldn't need the subsidies. I don't -- I think you're there already, but you don't. So at what point do you think that you don't need these subsidies?

TILLERSON: As we've described, we don't receive subsidies, Senator. What we do require is a reasonable return on our invested capital. And I would tell you that I don't think the American want shared sacrifice. I think they want shared prosperity. And what we have to offer...

ROCKEFELLER: Oh, yes.

TILLERSON: ...what we have to offer...

ROCKEFELLER: It's a lovely statement. But do you understand how out of touch that is? We don't get to shared prosperity until we get to shared sacrifice.

TILLERSON: My oil field workers are unable to work...

ROCKEFELLER: I met with - I met with...

TILLERSON: ...today because we can't receive drilling permits, or they are leases that are not being made available. They feel that.

ROCKEFELLER: What about the fact that, in the case of ExxonMobil, that your effective federal tax rate is substantially is three percent lower than what the average individual federal tax rate is? Does that mean anything to you?

TILLERSON: Well first, Senator, I want to assure you I'm not out of touch at all. And we do understand the big picture. We understand the enormous challenges confronting the American people with respect to this enormous deficit that has to be dealt with. And ultimately, it's got to be dealt with in a very large way. And so, I just want to acknowledge that we are well aware of that.

ROCKEFELLER: OK. So what do you to (inaudible)?

TILLERSON: My effective United States income tax rate on my United States income from 2005 to 2010 was 32 percent. Now, if you look at any individual year, it could be as low as a single digit. It can be as high as 38 to 39 percent, because we don't settle our taxes in - for that year in that year. We have tax filings that are open for multiple years, as we resolve issues with the IRS, they are recognized in the year we file. So in some years when our taxes appear low, it's because we have recognized closing of issues with the IRS where we overpaid.

ROCKEFELLER: And I understand. But still, do you understand the American - the average American's feeling - that over between 2008 and 2010 your effective tax rate was about 20 - about 17 percent, and theirs was about 20 percent?

TILLERSON: From 2005 to 2010 our effective tax rate is right at 32 percent.

ROCKEFELLER: Yes. Well then, that leads me to the next round of questions, if we have those.

BAUCUS: Thank you, Senator.

Next, Senator Stabenow?

STABENOW: Thank you very much, Mr. Chairman.

And we appreciate all of you coming here.

This really is about our priorities as a country, and in a time of tremendous challenges and deficits we have a responsibility to review everything. And taxpayers are expecting us to ask tough questions and determine priorities and look at what's needed, not needed, works, doesn't work. That's our job.

And when we look at the fact that it was 1916 when one of these tax subsidies that we're talking about repealing was put into place, deductions for intangible drilling and development costs and it was roughly \$15 to \$17 dollars a barrel for oil at that time. I'm sure you would agree things have changed since then.

And it's very appropriate to look at whether or not when we were developing then and creating an industrial revolution, which we're very proud to have led in Michigan, whether now when you fast-forward, it's not \$17 it's \$100 or more, and you're in a very different position in terms of success and corporate profits, does it make sense for taxpayers to subsidize what you are doing? Not that we don't want you to be successful, does it make sense for taxpayers to subsidize what you're doing.

And essentially, folks in Michigan feel like they're getting hit twice. They're paying the high price at the pump. There's not enough competition and consumer choice so they can choose not to pay your prices. And at the same time, they're turning around and paying out of pocket as well. And so, people are extremely concerned when we have to make choices about whether or not these subsidies are working right now.

And so, the question that I would have when we look at the facts that - if you just look at the last three months and the corporate profits together that all of you have made. The highest corporate profits, I think, ever. And the fact that the taxpayer subsidies are one to two percent of that profit, and that's the reality, it's one to two percent of all of your profits. And you're now saying that in light of massive deficits and you have massive profits, that taxpayers should keep providing one to two percent of your profits or you're going to raise gas prices again.

So my question is the opposite. And I would like each of you to answer. What would it take in level of taxpayer subsidies for you to bring our gas prices down?

Mr. Tillerson?

TILLERSON: Well, first, it's not a subsidy, it's a legitimate tax deduction. And I think, again, the important question is what is necessary to develop additional supply in this country.

STABENOW: But what would it take? It's one to two percent right now.

TILLERSON: And those...

STABENOW: So what does it take - what do we have to pay you to bring prices down?

TILLERSON: In the intangible drilling cost structure, it's structured to incentivize and help people go out and invest in the next incremental barrel of supply. And in this country today, that is largely coming from the shale resources in the Bakken.

STABENOW: I appreciate that. But in the interests of time I'm going to ask you...

TILLERSON: Well, but I'm trying to answer your question, which is so if you don't want the incremental supply, you make the tax structure higher and an incremental barrel doesn't get developed. It's as simple as that.

STABENOW: So one to two percent that we're talking about, which is a big deal for taxpayers, by the way. When we're looking at a colleague on the other side of the aisle wanting to eliminate Medicare as we know it, and we have to make choices here, which by the way, certainly I'm not going to support that, the question is where - what's effective? What works?

It's really not credible to say that you're going to raise gas prices simply because we are asking you to forgo one to two percent of your profits. It's so the - but if you are saying that, and you're going to raise our prices...

TILLERSON: No, we're not.

STABENOW: ...and right now there's not enough competition - we're held hostage - not enough competition for us to be able to deal with that. So we take one to two percent of your profits and you're saying that that will cause you to raise up prices again. My question is, what will get you to lower in terms of the subsidy? If taking away one to two percent will cause you to raise prices, if we give you four percent, five percent? How much more do we have to give you?

TILLERSON: We did not - I did not say we would be raising gas prices at the pump.

STABENOW: OK.

TILLERSON: But we're not. And I didn't really hear anyone else say that either.

STABENOW: I certainly - there was a real threat here...

TILLERSON: And it really is about - it really is about - it really is about, if we want to solve the problem by getting some more supply developed, which also in this country will generate additional revenues for

the federal government and will relieve the price pressure in the years to come, that's the role that the tax structure plays. And if you want...

STABENOW: Mr. Tillerson, I understand that.

TILLERSON: ...to eliminate it, then the (inaudible) barrel...

STABENOW: And before my time runs out --

TILLERSON: ...doesn't get developed.

STABENOW: I appreciate that, and I'm not being disrespectful. But let me just say we have to decide where is the most effective place to invest taxpayer dollars that are very hard to come by right now. People in my state want us to stretch every single dollar and look for what's the most effective and needed support and subsidy.

And so just very quickly, Mr. Mulva, what, you know, how much do we have to give you in additional tax subsidies in order to bring prices down?

MULVA: Senator, we're not asking for tax subsidies or incentives. What we're asking for is access to put our people back to work with the opportunity to start drilling, onshore and offshore. By drilling, more drilling, we will create jobs and we will create more supply. That's the best thing we can do to moderate prices.

STABENOW: I appreciate that. And we are hoping more than the sixty million acres that you've gotten leased, you'll be able to do that as well.

Mr. McKay?

I'm sorry, Mr. Chairman, I know I'm out of time. I don't know if I just might ask them to...

BAUCUS: If the answer could be very brief.

STABENOW: Thank you very much.

MCKAY: We're not asking for subsidies. Any increase in taxes will not be consistent with increasing investment for additional supply.

STABENOW: OK.

BAUCUS: Thank you, Senator.

(UNKNOWN): You say the current tax structure...

BAUCUS: I'm sorry?

(UNKNOWN): Fifteen seconds?

BAUCUS: Fifteen, OK.

(UNKNOWN): Current tax structure is globally competitive, which is why investment gets driven to the U.S. That's a good thing. Changing that will drive investment away. That's a fact.

If I could leave one point with the entire committee today, it's simply to look at the enormous opportunity the U.S. has to develop these resources, to create the jobs, and to create the additional revenue into the federal government, which will help with the long term deficit issue. That's the real opportunity.

BAUCUS: Senator Nelson?

NELSON: Good morning, gentlemen.

The American consumer naturally is quite concerned when they go to the pump and they pump gas. And what they're concerned about they see the price of the barrel of oil going up, and they see the price of the gallon of gas that they're pumping go up, And then, when that price of the barrel of oil starts coming down, they don't see the commensurate lowering quickly of that price that they're paying per gallon at the pump.

And so, they notice that back in 2008 that the price shot up to \$147 a barrel, and while they're pumping gas, it raises to \$4 a gallon. And now, they see the price at around \$100 a barrel, and they're still paying \$4 at the pump. So I want to ask that question on behalf of the American people that are pumping gas in their cars?

MCKAY: Well, it's a question of the supply chain. It takes the average time for crude oil produced overseas to reach American refineries somewhere between 40 days and 45 days. You have oil that's in inventory at the refinery, which has already been bought and paid for at some price. You have gasoline and products that are in inventory that have already been bought and paid for in some price, which then often are delivered to your local service station, where the consumer pulls up to the pump and buys it.

So when the price changes on that raw material of crude oil, that price has to make it's way through that whole supply chain. Now, when the price is going up the retailer who owns the station and operates on a very, very thin cash flow. And the vast majority of service stations are not owned by us, they're owned by individual business owners or distributors.

They have to think about what's going to happen to my cash flow as this price moves through? So they do begin to price up in advance of the actual higher cost barrels getting to them, in order to ensure they've got sufficient cash flow to buy the next tanker wagon that has to deliver.

So that's why going up, as most business people would do that worry about their cash flow, they're going to chase it a little faster on the way up.

And coming down, they have to recover the cost of what they've already spent on the barrels in inventory. So until those actual barrels make their way through the system, to the pump, the consumer is not going to see it. And typically that may take somewhere between two to three weeks, depending on how big the movement is.

NELSON: OK. I anticipated that, that would be the answer and I appreciate that. But the person that's pumping the gas is saying, wait a minute, today I'm paying four-bucks for a gallon of gas and oil is selling at \$100.00 a barrel, but three years ago I was paying \$4.00 for a gallon of gas and oil was selling at \$147.00 a barrel. Why?

MCKAY: Well the \$147.00 price didn't last very long and you remember what happened shortly after, it plummeted to the thirties. That is the nature, and we talked about this earlier, that is the nature of this commodity, which has an extreme amount of volatility in it. Why it moves that -- in that wide a range? We could have an entire hearing on that subject.

NELSON: And I would say that there's a part to the speculation that adds to that. People that don't use the oil. But Mr. McKay, let me register a difference of opinion with BP. You all in your financial report in the fourth quarter of last year, announced that the Gulf oil spill response costs were going to be approximately \$41 billion.

And that you reported a tax credit of almost \$12 billion. Now, for activities that caused such harm, does it not seem wrong that you would take as a tax credit, lessening your taxes dollar-for-dollar, on the payments that you're paying out to make people's lives right?

MCKAY: Let me first just comment that the -- we've pledged all along to meet every commitment under the law with the accident and the economic impacts of the accident. The \$41 billion is a financial charge. We did not take a \$12 billion credit. We will be following the law, following the tax code in terms of writing off standard business expenses as they occur.

(CROSSTALK)

NELSON: So you consider these as standard business expenses that you think that morally you're entitled to take as a tax credit?

MCKAY: The ones that are under the tax code as standard business expenses, yes. And we will not write off things that are not under the standard business expenses.

NELSON: You know it's interesting that the Boeing company when they had those kinds of payments, they didn't take them as a tax credit. If was also, what was the other company, Goldman Sachs, same thing. They did not because of the sensitivity, the wrong doing that occurred. Surely the Gulf oil spill was as a result of wrong doing, and yet you want to claim that as a tax credit.

Now I just want you to know that I respectfully disagree with your position and I would urge the chairman and the ranking member to consider as we -- he may be entitled to this under the law, but that doesn't make it right.

And I would ask respectfully to the chairman that we consider changing the law to follow the example set by Boeing and Goldman Sachs.

BAUCUS: Well, Senator we certainly will consider it. We'll consider any request made by any Senator, especially a Senator from Florida. Were you finished with questions? Yeah.

Next is Senator Carper?

CARPER: Thanks so much. Gentleman, thank you for joining us today. About a month ago, sitting right in the middle there was Alan Blinder, who used to be the Vice Chairman of the Federal Reserve. And he was on a panel, a three or four person panel. We were talking about deficit reduction and asking a group of really smart people what they thought we ought to be doing?

And I think it was Alan Blinder who said that the, the 800 pound gorilla in the room on deficit reduction is healthcare costs. You know, we live in a country where we spend about twice as much as they do in Japan and get worse results. They cover everybody. We don't.

But he said that's the 800 pound gorilla in the room. And I followed up his comment by saying, you know, with respect to healthcare cost containment and getting the better results for less money, what's your advice?

And he says I don't really know much about that. He said, but as a layperson I would just say this; find out what works and do more of that. That's what he said, said find out what works, do more of that. Democratic Senators were over at the White House yesterday with the president and our Republican friends are over there today and we had a conversation with the president about deficit reduction.

I shared with him Alan Blinder's comments, which I think are not only appropriate for healthcare, but really for the way we spend money all throughout the government. And my own view is, and I shared this with Alan Blinder that day, I said that we need to look in every nook and cranny of the federal government.

All of our domestic programs, our defense programs, entitlement programs, tax expenditures and really just ask this question, is there a way we can get better results for less money? Or better results for maybe the same amount of money? And we just need to change our culture in, in government. And that is to focus on what's a -- almost a culture of spendthrift or a culture of thrift.

When it comes to, to tax expenditures, we need to do the same thing. And there is assertions -- there's a strong belief in this country, you've certainly heard it here today that some of the tax expenditures that relate to your industry don't necessarily give us the best result for the amount of money that's being lost to the Treasury.

We're going to vote on legislation, I think authored by, I think Senator Menendez probably next week. My guess is there are not 60 votes to, to pass it. But later this year, we're going to be voting on an effort to try to trim the deficit by about \$4 trillion over the next 10 years and we're going to do that largely on the spending side.

Maybe \$2.00 of spending for every \$1.00 of revenue. Entitlements will be on the table, domestic spending, defense spending. Tax expenditures will be on the table. And I would just say to you that when the vote occurs next week and we don't get 60 votes for Senator Menendez's proposal, that shouldn't be the end of this conversation. And we should continue to have a conversation so we can try to figure out how to get a better result for less money, or really how do we get a better bang for the taxpayer's dollars?

And it needs to be -- your industry needs to be involved in, in that as well. If I were in your business, I don't pretend to understand it especially well, but I wouldn't consider myself an oil company and I would consider myself an energy company.

And my belief is that's what you do, most of you do that. And I would just like for you to talk to us about the efforts that you're undertaking in your companies to move us away from fossil fuels, to move us toward sources of energy that impair health less than oil does or fossil fuels do.

That enable us to come up with new technologies that we can sell and manufacture products and sell them around the world. Just let's go down the list. You want to go first? And just tell us what you're doing to help us. Do your companies have efforts to develop renewables, non-polluting and other forms of energy? And what can we do to help you there?

MCKAY (?): Well Senator, first I agree wholeheartedly with your comments on the deficit and ultimately we are an advocate for comprehensive tax reform. And all of these things we're talking about today should be on the table in comprehensive tax reform.

As to what we're doing in developing alternative fuels, and we have concentrated principally on transportation fuels because that's what we know the best. We're not an electric power generator so we're not into windmills. We're not into solar. It's just not our business. But we are in the transportation fuels business.

As we've evaluated all the various technologies available out there for alternative transportation fuels, the one that we believe has the most promise, although it is many years away, is, is to capture biofuels from algae, from various strains of algae.

And we have undertaken a joint venture initiative. We've committed \$600 million with a company called Synthetics Genomics. They have considerable expertise in mapping genomes. Because ultimately we think we're going to have to synthesize the types of algae that are necessary to be able to scale up.

First, we've got to be able to take this to scale and it's got to be delivered at a cost that the consumer can afford. So, we think there's a lot of promise in the algae space, but it is a long, long road ahead of us.

CARPER: Thank you. Please?

(UNKNOWN): Thank you. We continue to wrap up our spending on research and development for alternatives and we similarly have a program that stresses algae. I would say though that fossil fuels has and will continue to represent more than 80 percent of the energy that's required around the world.

One of the key things that's really important for our country is natural gas. It's been over the last several years through technology developments, that we're blessed with a great deal of natural gas, some thought for decades and some think even for centuries to come.

So we are really applying a lot of research and development, how we can develop natural gas even cleaner and, and more efficiently and we think that's -- just our country is well blessed with these resources for standard delivery (ph) and development of our economy.

CARPER: Thanks. Yes, Sir.

(UNKNOWN): Quickly, we think of oil and gas as the, as the main driver in our business, but on top of that and incremental to that alternative energy. Quick numbers; we've spent -- invested \$7 billion over the last several years, most of it in the U.S. around wind, biofuels, lignocelluloses biofuels, biobutanol, solar and then carbon sequestration and it's a growing business.

It's difficult, but it's growing.

CARPER: All right, thank you. Yes, Sir?

(UNKNOWN): Well we absolutely do consider ourselves an energy company and I would tell you that as a company, internally we look and say we want to be the most innovative and competitive energy company in the world. So that's the perspective we take.

We've been in all of the businesses that have been mentioned; wind, solar, hydrogen and others. The one that is emerging for us as a real opportunity is biofuels. We have just recently formed a \$12 billion joint venture around current technology for producing large- scale amounts of biofuels.

As well as then adding to that, the very intense research and development we do -- we have been doing to take that to the next level. And it's exciting stuff. I mean we're talking about, you know, using enzymes to speed up the conversion to an ethanol and another technology that potentially skips the ethanol step and goes straight from a biomass to a gasoline or diesel equivalent.

So, it's exciting business.

CARPER: All right thanks. Last one.

(UNKNOWN): Senator, just in addition to some of the comments that have been made where, we're the largest producer of renewables thanks to our geothermal business. And that's a very active business for us in Indonesia and the Philippines in particular.

We, too, are making investments in advanced biofuels. We, too, believe it will be some time before those will come to market.

One opportunity that I think is out there during this transition phase that you were talking about is energy efficiency investments. We have an energy efficiency company that goes in and makes investments in educational institutions and elsewhere to -- to reduce energy -- energy consumed. I think that's a big opportunity, and it's a near-term opportunity across this country.

BAUCUS: Thank you, Senator.

CARPER: Thank you very much.

BAUCUS: A couple of us have a couple of follow-up questions here.

Mr. Tillerson, you mentioned tax reform, that you strongly favored comprehensive tax reform. I think there isn't anyone here who doesn't disagree with that, but that's easy to say. The question is what do we mean by comprehensive tax reform.

And before I ask you what you mean, the general feeling is we lower the rate, broaden the base both on the corporate and individual. That sort of seems to be a trend similar to on the individual side what we did in 1986 on the corporate side, lower the rate. We have the highest corporate rate in the world. And then lower it, be more competitive, but broaden the base, try to find a way to do this in a revenue neutral way.

But by definition, if we're doing that, lowering the rate and broadening the base, that means we're starting to cut back on some incentives, whether it's biofuels, whether it's solar, geothermal, you name it, or you have some of the incentives that you have.

As general advice to us, I'd like to ask all five of you as we pursue tax reform, does that mean to you that maybe we should lower the rate, but also cut back on some of the credits, exclusions, deductions, so-called tax expenditures? Because by definition we have to; otherwise, we lose a lot of revenue. And that's hard to do in this -- in this big debt deficit climate.

(UNKNOWN): Well, Senator, I -- I would support all of that I think when I say comprehensive tax reform, then I think everything for everybody everywhere has to be on the table. And so if you want to talk about Section 199, repeal it for everybody across the board, gone.

And again, as you say, you're going to broaden the tax base. And if that's coupled with an overall lowering of the corporate income tax rate, I'd just use 199, because there is a whole host, as you well know, of elements to our tax code that is very complex.

I think simplifying the tax code, broadening the...

BAUCUS: Section 199's probably not a bad example, because some use it and some don't.

TILLERSON: Some -- some do; some don't.

And then when the government wants to -- because we're really just creating conditions for greater investment in the country, because we've got to grow our way out of this deficit problem. We've got to make it more attractive for people to invest, create revenues, broaden that base. And that's where a lowering of general rates would -- would be productive.

BAUCUS: OK, you go along with then, though, with scaling back a lot of the tax expenditures.

TILLERSON: Across all businesses, not just ours, across all businesses.

BAUCUS: I'm getting that, all of them.

TILLERSON: And -- and in the foreign tax code, it needs an overhaul as well. And the only principles I tend to live by is make the United States a more attractive place for investment. Do not harm American competitiveness overseas, because that brings enormous benefits and wealth back to this country.

And keep the playing field level within industries, so that everyone competes. We -- we love to compete. I mean, that's -- that is what we thrive on is the competition.

BAUCUS: Mr. Mulva?

MULVA: I completely agree. Make it simpler. Make it in a way that's consistent for everyone. And certainty that we don't anticipate changes going forward will promote investment. But I think additional revenues will help -- -- certainly help with respect to employment.

BAUCUS: But do you agree with the general principle that corporate tax reform should be revenue neutral?

MULVA: Yes. BAUCUS: You do. Thank you.

Mr. McKay?

MCKAY: I agree as well. Anything that can increase competitiveness for the U.S. in terms of investment I think would be good. And I agree with all the comments that have been made -- the simpler the better, the more predictable the better. And -- and the job number one is to get investment up.

BAUCUS: But the way to increase competitiveness in your view is...

MCKAY: It's exactly as we've been saying. If the overall tax rate goes down and is broadened and some of the complexities taken out, that should aid competitiveness.

BAUCUS: I don't want to make this too complicated, but as you well know, in the United States much business income now is no longer C-corporate -- no longer corporate income, but it's pass-throughs. You know, that's where the individual income taxes would have to be with they're not corporate, which greatly complicates this question.

MCKAY: Yes.

BAUCUS: I mean, we have more pass through business income in this country, I think, on a proportionate basis by far compared to any other country. That's a recent trend. You might want to consider being a pass-through.

But as I go down the list here, let me just ask, give you a chance, Mr. Odum.

ODUM: Well, I'm -- I'm glad the term "stability and predictability" came up, because that's very important. So I think comprehensive reform with everything on the table, yes, I agree with the comments that have been made, with the driving policy element being ensure U.S. competitiveness.

BAUCUS: Mr. Watson?

WATSON: I agree with the comments that have been made. I would only hope that over time it will raise more revenue, because it will promote growth. And I think that's -- that's really what we're -- what we're trying to achieve.

BAUCUS: Mr. Tillerson, you want to say something.

TILLERSON: Just on your comment about -- because your -- your point about pass-through and subchapter S partnerships is an important one because, as you point out, so many of small to medium sized business owners are structured under the tax -- those under the tax code.

Again, in comprehensive tax reform we deal with the corporate tax code, but also the individual tax code. We'll have to deal with that. And -- and once that is structured, then allow those entities to check the box on which -- which do they want to file as.

They -- they don't file under the corporate tax code today, because it is not advantageous for them to do so. But if that's restructured, they may find the corporate tax code to be more beneficial for their filings than having to file as under the individual tax code.

BAUCUS: One minor point here -- not so minor, perhaps, from your perspective, and that's the dual capacity question. I think you'd agree that your company -- all companies -- should get a tax credit for foreign taxes paid to -- to a foreign country. And that's -- that's the general rule. You get a tax credit.

The general rule, too, is, though, that you don't get a credit for -- for royalties. You do for income tax paid in that country, but not royalties.

I -- I think the question here is -- is characterizing that -- that payment. Is it a royalty or is it a tax payment? And I think the goal here on the dual capacity -- there's various ways to -- to structure it -- is to make sure that -- that the company, your company, any company properly gets that tax credit when it's a payment of income taxes to that as a country, but not if it's a royalty payment.

And I'm just trying to figure out what actually is royalty and what actually is -- is income taxes. And that may have something to do with the law -- I don't know -- but clearly, that royalty, that contract for the individual taxes, its general applicability just to -- to all companies that might make a profit. So we're trying to do the right thing by separating what is a royalty from what is properly a tax payment. That's the goal here.

TILLERSON: Well, and I -- I appreciate the recognition of that and -- and don't disagree with any of what you said, Senator. And it is -- it is the complexities of dealing with the foreign -- of the host country's tax system and how does it characterize payments that we're required to make to them and how that fits under the U.S. tax code.

It is -- it is a difficult task, but as I said, it's one that we must prove to the IRS that, you know, they are legitimate income taxes, not royalties. So I understand the -- the challenge.

I mean, the -- the alternative is to go to a different system, which I know, you know, because we've talked with your staff, and others have talked about going to a system of -- of foreign tax code that is more aligned with what most of the rest of the world has, which would be a territorial system.

And then, again, it's -- it's getting that system structured so that it doesn't violate that principle of mine, which is don't structure such that American companies are at a disadvantage to their competitors overseas. And I think that is achievable.

As with all things, the devil's in the details, but we have -- I think we have a way to move to a system like that. And that simplifies an awful lot of the complexities that exist in our current tax code.

BAUCUS: Before I pass on, this is going to be incredibly difficult.

TILLERSON: It is, without question.

BAUCUS: And it's going to require good faith of everybody involved. And it's -- it's analogous to our efforts to try to reduce our deficit. I mean, it's got to be shared. Everybody's going to have to give in a little bit here and there for the greater good.

Senator Hatch?

HATCH: Well, thank you, Mr. Chairman. Mr. Chairman, yesterday on the floor Senators Landrieu and Begich spoke about these hearings and related legislation, and it was quite critical, so I ask that their statements be placed in the record.

BAUCUS: Without objection.

HATCH: OK. Now, Mr. Chairman, I'd like to comment on a few items before I go into the second round of questions.

My friend from New York implied that the roughly \$60 billion in tax incentives that we're discussing today was a key factor in reducing our \$1 trillion-plus deficit. My -- my friend from Maryland made a similar point. Nobody's arguing that number is insignificant.

What we're worried about is -- is the effect removal of these domestic production incentives, what the effect of that would be. The testimony is clear. Removing these incentives is going to drive production offshore. It's just that simple. And that's what's been said here today.

But I'll tell you there were spending cuts proposed by Dr. Coburn of similar size, who is a member of our committee, that were rejected out of hand by my friends on the other side.

Those spending cuts -- another version of shared sacrifice, to use your terms -- did not involve student loans. They didn't involve low-income folks. They didn't involve infrastructure investment.

Here's an example. Dr. Coburn proposed selling federal buildings that are de facto vacant. That proposal was doggedly opposed, as reasonable as it is, by my friends on the other side. And that proposal involved \$80 billion.

So let's make no bones about it. You know, there's two sides to what's happening here.

HATCH: Let me just ask you this, Mr. Tillerson. Combining all of U.S. companies into one large company, if you took all five of you and all U.S. companies, not just the five of you, but all of them, into one large company, if we combined them all, that would give that company control over only 6 percent of the world's oil production, as I understand it.

And control over less than -- no, (inaudible) 6 percent of the global oil production, and control over less than 2 percent of global oil reserves, yes, would require them to go out into the world of titanic nationally-owned oil companies, and still provide us with a continual large supply of oil. Let me show you this chart.

The U.S. companies have a wee little sliver there. That's 1.4 percent. Look at the OPEC nations.

Beginning with -- beginning with Saudi Arabian Oil Company, National Iranian Oil Company, Iraq National Oil Company, Kuwait Petroleum, right on down the line. Here's where we are.

We're this small, little sliver here. All these others are OPEC companies, OPEC nations that own those production facilities. I guess what I'm asking is, you're the big five American companies.

Am I wrong on the small slice of petroleum exploration and production that is listed on these charts?

Mr. Tillerson?

TILLERSON: No, I think those numbers look about, to my recollection as well, that we do not represent an enormous holding of the reserves or the production.

I would say this, though, that we do represent an enormously important participant in the development of global energy supplies. And we do work in a number of the OPEC countries.

HATCH: But you don't own the -- all of these?

TILLERSON: No, no, we -- I mean, what you had would be -- would represent our share of what we...

(CROSSTALK)

HATCH: And that's that little slice in that...

TILLERSON: Right.

HATCH: ... overall pie.

TILLERSON: Yes.

HATCH: Well, Mr. Odum, did I hear you correctly, you were ready to spend \$700 million in the Gulf on enough domestic energy production to power more than 600,000 vehicles a day.

And I believe you also said that you invested \$3.5 billion in the last five years to develop large oil reserves in Alaska.

Now is your testimony that Shell has spent over \$4 billion to produce domestic oil, but that the only thing standing in your way is government refusing to allow you to go ahead?

ODUM: Well, I think the case, as you say, is emphasized by what's happening in Alaska.

So we are precisely at, you know, something around \$3.5 billion in, about five to six years now, into trying to drill in Alaska, and have yet to be able to do so because of the permitting situation and the overall coordinated -- coordination of the government agencies.

And what I tried to emphasize earlier is the impact of something like that.

So the -- again, the studies, through the University of Alaska, indicate that developing that part of the industry could be 750,000 barrels a day on a long-term, multi-decade basis.

(CROSSTALK)

ODUM: So over 50,000 (inaudible).

HATCH: (Inaudible) \$3.5 billion on the com (ph) and you can't get the doggone permits to do what you know is there.

ODUM: It doesn't reflect well on the -- on the U.S., I'm afraid, in terms of drawing investment to this country and being competitive in this business.

HATCH: One of the first acts of Secretary Salazar was to withdraw 77 onshore federal oil and gas leases in Utah after years of jumping through environment hoops. And we finally got there.

It was an agreement between the governor and the VLM, after they had already been studied, auctioned off and paid for. It was one of the strongest anti-oil signals you could have sent to the oil industry.

Could you elaborate on your experience?

Or any of the rest of you, if you care to?

(CROSSTALK) HATCH: (Inaudible) also answer this question before we finish, assuming this legislation passes, the Menendez legislation, will it bring down the prices of oil at the pump? Or is this just a big charade?

You don't have to use my terms, but answer that for me. Why are we doing this? Why are we putting you at a disadvantage when you're that little small slice of the overall pie?

And you're competing against nations that have oil companies. I mean, they're the national, nationalized oil companies.

Go ahead.

(UNKNOWN): Well, I think that, you know, the competitiveness point is exactly right. The chart is accurate, from what my information would tell me as well.

I think the thing we have to be careful not to lose in the chart is what I called earlier this enormous opportunity that exists in the U.S. We have a tremendous number of resources.

We can impact the energy balance and the domestic production of that energy balance...

HATCH: Well, why don't you do it, then?

(UNKNOWN): Well, it's a matter of access. So...

HATCH: Matter of getting the permits?

(UNKNOWN): And which goes far beyond just the limited part of the conversation today, which is around the tax code.

I think to look at a real energy policy that provides incentives through its access to those resources, we could have a significant impact on the economy, the deficit and the trade balance and the energy security of this country.

HATCH: I'd like to know if any of you believe that this bill will help decrease prices at the pump.

(UNKNOWN): (Inaudible).

(UNKNOWN): Yes.

(UNKNOWN): No.

(UNKNOWN): No.

(UNKNOWN): (Inaudible).

(UNKNOWN): No.

(UNKNOWN): (Inaudible).

(UNKNOWN): No.

(UNKNOWN): OK.

HATCH: And, by the way, I know that...

(UNKNOWN): (Inaudible).

HATCH: ... some people are a little upset that I've taken this time. I sat here while every Democrat has taken considerable extra time.

(UNKNOWN): (Inaudible).

HATCH: I'm the only one here on the Republican side, because everybody had to go to the White House. So I would hope that I could be granted a little bit more time.

(UNKNOWN): OK.

Senator Wyden.

WYDEN: Thank you, Mr. Chairman.

I just have one question. But I also want to note where we are at this point, two and a half hours into the hearing. Gentlemen, you all have done, as major oil companies, a dramatic about-face this morning.

In 2005, all of -- you were there, Mr. Mulva -- all of you said you did not need tax incentives to drill for oil. And today you've come to say you've got to have them, when oil is at \$100 a barrel.

I just think that position defies common sense. And certainly even adjusted for inflation, you're even doing better now than you were in 2005. So this debate is going to go forward.

I just want to make sure that folks who are paying attention to this pick up on that as we wrap up.

And I have one last question. I want to ask it of you, Mr. McKay, because of some of the comments that you've made, and that's the tax credit that exists for blending ethanol.

Now, as you know, you all are required by law to implement the Federal Renewable Fuel Standard and blend billions of gallons of ethanol into the gasoline that you sell.

And your testimony says, and I quote here, "BP is already one of the largest blenders of ethanol in the nation."

So my question, Mr. McKay, is why should oil companies -- not just yours, but all of the oil companies -- be getting \$6 billion a year in tax credits for complying with an existing law to blend ethanol?

MCKAY: That law was introduced to get ethanol as a biofuel into the fuel mix into the U.S., which it's been very successful as incentive to do that.

We're not opposed to that transitional incentive being phased out. We think it's important for transitional incentives for second generation biofuels.

WYDEN: I think that's constructive, and I'm glad we're noting that as we go.

Mr. Chairman, you and I have talked about this. There's no question in terms of energy policy that often you need an incentive to get something off the ground.

Clearly, what Mr. McKay is talking about is that incentive made some sense at the beginning. It doesn't make incentive now. It involves \$6 billion.

And, Mr. McKay, I think it's constructive that you said this morning that you'd be willing to phase it out.

Mr. Chairman, I'd like to talk with you and Senator Hatch and have further discussion. But I thank you.

BAUCUS: Well, thank you, Senator. I think Senator Snowe made a good point, too.

This committee should -- and we will -- look at the effectiveness of the -- all the tax expenditures, all the incentives, to see which ones are more effective than others.

And maybe we can get rid of a few of them. Your minds (inaudible), I'm sure some of you don't know this, (inaudible). It's a difficult question for all of us.

There are about 141 tax provisions that expire every year or every 18 months in the code. We call them expiring provisions. They're a nightmare.

Makes no sense for us to go back and reinvent, you know, the wheel 141 times every year or 18 months. And they've got to be paid for, and it's just -- it's just maddening.

And it diverts our time for bigger questions. And so we will be looking at a lot of these provisions and others.

I'd like to eliminate a lot of those or make them permanent so there's not a lot of uncertainty surrounding them from our side and also from the industry side.

But, anyway, I -- we're going to be looking at a lot of different tax expenditures to see which ones are effective.

Mr. -- Senator Cardin?

CARDIN: Thank you, Mr. Chairman. Let me concur in your comments in regards to tax reforming. Can assure you that there's great interest in making our tax code more competitive and more predictable. I think predictability is extremely important for investors and we got to -- we got to give you the ability to get investors, knowing what the ground rules are. So we agree on that.

I will make one comment in response to Senator Hatch. The numbers here, \$4 billion, as I understand it, all will repeal (ph), equals about 3 percent of the profits of the five companies.

Most of these profits are going back to the shareholders. So I just don't see the impact that Senator Hatch is referring to on either jobs or any of the issues that you bring up.

I just think the math is pretty...

(CROSSTALK)

HATCH: Senator, (inaudible), my point is that -- and I think they're making the point, is that if you're going to do this, you should treat them fairly along with all the other companies that receive certain tax expenditures.

Now I agree. We've got to do tax reform, and that includes looking at everything.

CARDIN: And I agree with that.

HATCH: But I don't want them mistreated just because they're an industry that people hate and because they're...

CARDIN: Well, I understand...

HATCH: ... (inaudible).

CARDIN: Let me -- let me bring it back to the point that's been used here.

I understand that business is taking -- the five companies here are taking the tax provisions that are there, taking advantage of it. That's your responsibility.

You didn't do that, you would have problems with your shareholders. But understand why we think that this is either unwarranted incentives or subsidies, particularly the Section 199.

Section 199 was a response to dealing with the fact that our corporate taxes are not border-adjusted versus Europe's and other countries' consumption taxes, which are border-adjusted.

So we did something to help our foreign sales. That was the purpose, the genesis of Section 199.

And we wanted to be able to compensate for the fact that our foreign competitors had an advantage over U.S. manufacturers on the way that taxes were handled at the border.

Now my understanding is that, in your industry, there's more importer product than exporter product.

So it doesn't make a lot of sense for you to get a tax advantage on the philosophy of what this bill was originally created for.

Now, as you know, the World Trade Organization ruled the provisions out of compliance. And then we had to go to a general manufacturing provision. And that's how this came about.

Well, on two fronts, we have questions as to whether this is a reasonable tax advantage to the oil industry. It's not traditional manufacturing. And it's not the type of export activity that was disadvantaged by the corporate structure to have a product enter the international marketplace.

So I just think we have to get to the rationale. This is the largest single source of the revenues we're talking about today that has its genesis on helping United States manufacturers get a product into the international marketplace, which is not the circumstances of the product that you are basically involved with.

You import the crude, as I understand it. The final product is mostly domestic. I'm sure some hits the international marketplace. But it's certainly not the target for why this particular tax provision was put in the tax code.

Does anyone disagree with that?

I know I'd get Mr. (inaudible) involved there.

TILLERSON (?): Well, if you want to repeal it, repeal it for everyone because I'm not sure that the coffee roasters are growing coffee here and exporting coffee. I'm not sure that the newspaper companies are exporting dominantly their newspapers.

So I don't disagree with your comment or your premise. My only point is if you want to -- if you want to get rid of it, just get rid of it across the board. Get rid of it for everybody.

CARDIN: I don't disagree with the point...

TILLERSON (?): But don't just get rid of it for one or two companies.

CARDIN: There are some manufacturing companies that this is rough justice that really helps them. I would rather to it directly on, as we did with foreign sales. We can't do that under WTO. I'd like to reform our tax code so that we have a competitive base. If we can do that, that's my first choice. If we can't do it, we should tailor this more to its purpose of helping exports who manufacture in the United States.

TILLERSON (?): My only principle that I ask you not to violate is: Do not treat companies within the same industry different. And do not treat industries on your principle of exports differently.

CARDIN: Well, we've got to -- it's tough sometimes to draw a line and I understand the point that you're raising. All I'm pointing out is that that's why some of us look at the section 199 as it relates to the oil industry as either an unjustified incentive or as a subsidy because we don't believe it is the original intent to benefit your type of activities. And I just really want to put that in the record, and I very much appreciate your response.

BAUCUS: Thank you.

Senator Rockefeller?

ROCKEFELLER: Well, thank you, Mr. Chairman.

I want to repeat, but then expand a little bit about what I said earlier. I really do believe that you're out of touch. I do believe that. Mr. Tillerson doesn't. That doesn't mean you're not good people, that you don't participate in your communities; that you don't do helpful things, along with the work that you have to do. But I think the main reason that you're out of touch, particularly with respect to Americans and the sacrifices that we're having to look at here in terms of trying to balance, or come even close to balancing a budget, is that you never lose. You've never lost. You always prevail. You always prevail in the halls of Congress.

And you do that for a whole variety of reasons, because of your lobbyists, because of friends who -- because of all the places where you do business. And I don't really know any other business that never loses; that always fails to do as well as you do.

And then I think one of the problems, and you can't help this, in a way, is the size of -- just the size of the amount of money you take is really hard for average people in West Virginia to even come close to

understanding. They don't think that that can be come by in the regular order of the way the world treats them.

They are always in the process of losing. Everything is an uphill battle. So my view of my work in West Virginia is that I'm -- which is mostly mountainous, 96 percent mountainous -- is that I'm holding onto a huge boulder, not a too-huge boulder, with both hands, and trying to push it uphill.

That's every day I feel that and I love that feeling. But I know if I take one hand off, I and the boulder disappear into the ether, or I guess the opposite of the ether, the -- gulch.

And so that then leads me to say, this is my opinion, but I really believe it. I just really believe it. I've just never seen any industry so successful, so constantly successful. So I think you all have a great sense of assurance as you are sitting there, more so than usual, and we have steel people or automobile people or other kinds of people there. You have a great sense of assurance. I don't think you feel threatened by anything that's going on here.

And I don't necessarily know that you have any reason to feel threatened because of the way votes line up in this present Congress. But I yearn for one of you to see what average people are going through and to figure out some way in your mind what can I do as a very, very large and profitable company to make sure that that bad thing doesn't happen to that person -- losing health insurance or losing unemployment insurance, or all the -- I mean, the endless number of things that people have to worry about every single day.

You don't have to worry about those. None of you took a commercial airport -- airplane to come here. I don't blame you for that. You have the money to have planes, but our people don't. And so I want to -- I just want to sort of stipulate that, and then say one more thing.

We're -- the greatest danger to this country right now, other than the deficit, but the greatest danger in terms of national security is something called cybersecurity. We're writing a bill in the Commerce Committee and the homeland security bill (sic) is participating in that, which comes up with a solution which I hope we can pass this year.

The -- there's an enormous amount of work that companies -- and expense that companies have to go through who are being attacked already. The Pentagon, I think, is hit, you know, hundreds of thousands, maybe a million times a day by people hacking in; getting secrets. Not just WikiLeaks, but anybody can do that.

So how do they defend themselves? Well, they have to go to all kinds of security measures. And you know, I met with most of them yesterday, particularly the bigger ones, and I said, "You know, you're going to have to bear that expense. The government can't do that for you. We don't have the money to do that for you, because this is going to go on for the next 50 or 100 years, we're going to be facing these problems."

They didn't object to that. In fact, they said, "We think that's the right thing, the way it should be. We should have to pay more. We should have to dig into our profits to make ourselves more secure."

And so that's why I, you know, I just -- when you talk about the R&D, your expenses are like research and development for pharmaceutical companies, somebody else, is where I think it's wrong of you to say that because it just isn't. So much of that exploration has already been done. I think that's a cost that you could absorb so easily and -- and still do very well.

But not once during this hearing have I heard any semblance of a willingness to share unless every other company also has to, which is a way of kind of building up the defense that it can't happen. Well, putting it more simply, I haven't heard anybody talk about what they're doing, what they would be willing to do to share in our budget problem and in the total concept of what keeps America together, and that is a sense of fairness; that everybody has to lose at some time. Everybody has to give something up for us to be a real country.

And do any of you have any things -- if you just don't (inaudible), so long as every other company does it to -- do any of you think about this, ways that you could -- things you could give up, things you could just stop doing, things that you could -- breaks that you now get that you wouldn't get, as a way of helping?

MULVA: Senator, I very much appreciate the comments that you're making. I can only represent how we as a company feel. I don't know how the others do, but we feel like we're constrained and restricted from our opportunities. We feel we're in a noble industry that provides the energy that has developed this country into what it is and its standard of living.

And we're constrained from what we feel that we are part of the energy solution for this country and for the world. But we're constrained, with shackles on us. We're ready to invest. We're ready to do far more. You've heard today.

So it's not a question of looking for incentives. We're looking for -- give us -- put us back to work. Open up. Give us access to the lands. Let us start drilling. Put our people back to work and we'll develop...

(CROSSTALK)

ROCKEFELLER: I'm past my time, but can I just say that -- that, you know, "we feel constrained; we can't do what we want to do." Maybe you're right and maybe you're wrong. I think you're wrong. I think the great bulk of our people across the country who are suffering in ways that you probably have no idea of, just don't understand. And I think that's sad.

BAUCUS: Thank you, Senator.

Which opens up another subject, and that is leases. I would just like an answer for my own information. I don't know the answer. I have not discussed it at any great length with anybody in the industry. But I've heard you often say and have said previously that you'd like more access around America, whether it's the Gulf or North Slope or wherever it is, more access, permits, so you can get to your work, as you said, Mr. Mulva.

But on the other hand, I hear some people say, and this is a question I have, that there are millions of acres of leases that you own that you're not utilizing. And I'm just curious what's the response to that, if there is one, because it does come up quite frequently, that question.

(UNKNOWN): If I could just start, I mean, I'm going to take you back to Alaska again and try to put this in perspective.

BAUCUS: And are there millions -- how much -- how many -- I'm just curious...

(UNKNOWN): I'll put it in terms of leases. So in the Gulf of Mexico, we're one of the top three, sometimes the second- or third- largest operator in the Gulf of Mexico. We have between 400 and 500 leases and about 35 percent of those are producing and the rest are in some stage of evaluation, or being drilled or so forth.

If you compare it to Alaska, we have over 400 leases in Alaska that are sitting idle, waiting for permission to move forward. Just to, just to put that question into balance.

BAUCUS: OK, anybody else?

WATSON (?): Senator, perhaps I, I can comment on, on lead times. A lot has been said about leases that are undeveloped. We just made a final investment decision last year on a Jack/St. Malo development. This is in 7,000 feet of water. It's a \$7.5 billion commitment. We made that decision during the moratorium on the expectation that we would get permits, which I expect we will, to drill the development wells.

Those leases were first issued in the late 90's. And we didn't know how to explore or develop in that, in that deep water. Technology has advanced. We've done exploration work. We've done exploratory drilling. We've done delineation drilling.

And now we've made a decision that will result in production in 2014. So there's a long lead time in, in the offshore area. Which is where most of the undeveloped leases are today. Now, we're having trouble getting permitting on the leases that we have, which is keeping those leases inactive.

And so I think when you hear us talking about the opportunity that's there; one is to make sure that we have timely issuance of permits on the acreage we already have so that we can continue to explore. The other is making sure that the outer continental shelf is fully explored. And the United States Geologic Survey and others have made estimates that you could create companies twice the size of Chevron with the resources that we haven't developed yet.

Now we won't know what we have until we explore those areas. But that's the opportunity that we're talking about.

(UNKNOWN): Second question is, again your reports, your public reports show I think, that -- I think it was 2010 that about 60 percent of your after tax profits were invested, stock repurchased or dividends and so forth, about 40 percent elsewhere. I suppose that's reinvestment, I don't know.

That seems to a lot of people, gee a lot of money is going back to shareholders. A lot of money that you're making is in the stock repurchase. Why isn't more of that going into, to reinvestments? So that's the first question. The second question is, how does that percentage compare with other industries with -- that may or may not be relevant, but it's just a question that came to my mind.

Mr. Tillerson?

TILLERSON: Well, last year we earned about \$30 billion. We invested \$32 billion, so we invested more than we earned. And with that cash flow, the first thing we do is we pay all of our expenses. We pay our people, their salary, wages and benefits. We pay all our bills. We pay our taxes. We fund our opportunities, \$32 billion worth. And then what's leftover we pay the dividend and if there's anything left beyond that, then we return that to shareholders through share repurchases.

It's their money. They, they invested it with us. They entrusted us with their savings to go invest it, grow it and give them some income back. So, I know it's a novel thought up here in Washington, but we actually give the money that belongs to our investors, back to them if we don't need it.

(UNKNOWN): I just -- I appreciate what you've said. I guess maybe this is inaccurate, but I've got a chart here. It's the 10K Exxon- Mobile. I have also Conoco-Phillips, Chevron and Shell here for 2010.

And it says according to this chart, stock repurchases and dividends as a percent of profit in 2010 was 70 percent. And for Conoco-Phillips it was 77 percent. That's, and that's the data -- we aren't trying to fudge anything, I just look at the ...

TILLERSON: No, I think that's roughly consistent with the numbers I just gave you.

(UNKNOWN): So, it's -- you answered \$32 billion profit.

TILLERSON: Thirty billion in profits and I -- my recollection is we returned \$19 plus billion to shareholders last year. I don't have the number immediately in front of me.

(UNKNOWN): Anyway, just -- I think when the public sees this they'll think, well gee, you know, it would be better if that money were to go back. More jobs, more investment and so forth. But, I understand that your shareholders own the company. Your board of directors ...

TILLERSON: We'd, we'd love to. Give us something to work on. we'd love to.

(UNKNOWN): All right. Here's something. How about a trade here? More leases, give up the tax breaks.

(LAUGHTER)

TILLERSON: I don't think I came to negotiate a trade with you today, Senator. I came to answer your questions.

(UNKNOWN): That just popped in my mind.

(LAUGHTER)

WATSON: Senator, I would just offer that Chevron paid \$5.6 billion in dividends last year to our shareholders. Ultimately those dividends are taxed. The government receives revenue. We don't repurchase very many shares, but when we do, our stock has gone up \$30 or \$40.00 in the last couple of years. There's a nice gain on that.

(UNKNOWN): Of course.

WATSON: That generates tax revenue for the government as well. And the money is then reinvested where the investor thinks it's appropriate. So the country still benefits from it.

BAUCUS: Do you have more questions?

OK. Senator Hatch?

HATCH: Yesterday in the Wall Street Journal, formal Democratic Congressman Harold Ford, a good friend of mine, he asked, quote, "why when gas prices are climbing, would any elected official call for new taxes on energy?" I thought that was a pretty interesting question coming from a Democrat.

I think it's a good question. In your testimony you say that, quote "changing important tax provisions outside the context of broader corporate tax reform, would achieve one unmistakable outcome. It would restrain domestic development and reduce tax revenues at a time when they are most needed", end quote.

Would you folks please elaborate on the negative economic consequences of the proposed selected or selective tax increases that the Menendez bill would impose on, only your industry? Not all the others who have similar tax expenditures or tax deductions?

WATSON (?): Certainly to the extent that taxes are increased, it increases the economic valuations we go through and we'll spend less. Natural gas prices are low today. Deep water developments are very expensive. Costs have more than doubled over the last few years.

And to the extent more onerous tax provisions are placed on us, we'll spend less money on development. That will translate to less oil and gas produced in this country.

HATCH: OK. Anybody else care to comment on that? Or do you all agree with that? OK. Well this business of dual capacity rules came up today. Generally all U.S. based companies are entitled to a foreign tax credit against U.S. tax, based on foreign taxes that they pay.

Now, you mentioned that we'd be really wise to go to a territorial system, just like everybody else in the world has. But our system is some screwed up system where we're constantly trying to find ways of resolving some of these, some of the difficulties when you earn monies overseas and are taxed by the countries overseas.

But let me go through this. So generally all U.S. based companies are entitled to a foreign tax credit against U.S. tax based on foreign taxes that they pay. In general foreign based, multinationals do not claim much U.S. foreign tax credit.

But it is essential to most American companies with global operations. Now the dual capacity rules currently in place determine to what extent a payment from a U.S. company to a foreign government is equivalent to an income tax and thus eligible for the foreign tax credit.

So -- and to what extent such payment is for specific economic benefit such as for the purchase of oil from the foreign government, or for the right to operate a gambling casino and thus only a deductible business expense and not eligible for a foreign tax credit. Now my first question is for anyone on the panel who cares to answer; is it true that repeal of the dual-capacity rules would be very harmful to American based oil companies?

But that such repeal would be of negligible affect to foreign based oil companies? And the second question is; to the best of my knowledge the dual capacity rules are only a significant benefit to two sectors in the United States. The oil and gas sector and the gambling and casino sector.

Can any of you confirm that it is the case that the recent proposal S940 would still allow the gambling casinos such as MGM Resorts, Caesar's Entertainment, Wynn Resorts, Boyd Gaming and the Vegas Sands could claim the benefit of dual capacity rules while you wouldn't be able to?

Now just to make sure I have understood correctly, I'll summarize. The proposal before us it seems to me, would harm American oil companies but would not harm foreign oil companies and would not harm gambling casinos? And I'm not for harming those. Am I wrong on that?

WATSON: I don't know much about the gambling business, but I can tell you when tax rates exceed the U.S. rate overseas, if we don't have dual capacity tax treatment, we'll be ceding business over time to our foreign rivals, whether Chinese national oil companies, Russian oil companies, even European companies.

And so it's very important. I would further add that the Internal Revenue Service is well able to distinguish between royalties and taxes. There's very little areas of the tax code that's been studied more than this subject.

So, that may have been a difficulty years ago, but there's abundant case law and abundant rules to determine the difference between a royalty and a tax. And it's important that we be allowed to take the tax credits where we've already paid taxes overseas.

HATCH: Anybody else care to comment?

TILLERSON (?): Well I would just echo John's comments that it would have a devastating impact on our ability to compete overseas.

This is one topic where you won't find the five companies aligned because two of my foreign-owned competitors are at the table. They -- they operate under a territorial system.

So we would have -- we would lose competitive -- a competitiveness relative to them and then in an already very crowded and enormously competitive world we find ourselves in the resource development space because of the growing presence of the national oil companies, which already come to the game with other advantages that we don't have, nor do we seek.

So, we have to offset that by finding other ways to out compete them. What we'd like to have is at least a level playing field from a tax standpoint and not be at a disadvantage.

HATCH: I pointed out what a small slice you are of the world's -- you're competing with national oil companies. National/international oil companies I guess I should say.

Well, let me just finish with this comment, Mr. Chairman, if I've got -- you correct me here -- what you're saying is that it would be very unfair to pass this type of legislation because it would be selective taxation against peculiarly your industry that other industries in this country have benefit from. And that that just doesn't seem right to you, as far as I can see.

I mean, that's -- if I'm summarizing this properly, you can surely correct me, but -- if I'm not -- not summarizing it in the right way -- and that that would be an unfair approach and would make you less competitive, if that happened.

And that would cost jobs. And most importantly of all, that would cost real jobs, because you employ a lot of people. If you could do your work up there in Alaska, my gosh, you'd put a lot of people to work. And Alaska would benefit greatly that's constantly coming to the Congress and asking for help, where the oil business has really helped Alaska over the years.

And you'd put these people to work. And frankly, if I understand this hearing and what you're all saying, it would be unfair and -- and probably -- well, not probably -- the bottom line is, and I don't think any of you would disagree with this, it will not bring down gas at the pump one penny. In fact, it's likely to go up because of this effective taxation approach. Am I right?

BAUCUS: Thank you, Senator. This concludes the hearing.

I'll and, though, where I began, namely, just to remind all of us here we've got a fiscal problem on our hands, a federal fiscal problem. Let's get these deficits -- deficits down.

We have to make choices, and none of them are easy. I twice a week go over to the Blair House, meet with the vice president and a couple of other members of the Senate, a couple from the House, Secretary Geithner, OMB Director Jack Lew, Gene Sperling, the president's economic adviser, going down the list, trying to figure out how we do this.

It is not easy. Agriculture -- you tell me how many farmers want their commodity supports cut. You know, it's conservation programs, it's food stamps, I mean, you name it -- this is not fun stuff.

And I just urge all of you to keep that in mind when you go back to your daily work and so on and so forth. Maybe talk to people and say, "Gee, maybe there's a way that we can contribute here, too." Because we're in this together. Everybody here clearly wants more jobs, more growth, wants America to be number one, have incentives to invest in the United States.

So if foreign corporations, foreign investors invest in the United States, we can do that more. If American investors invest more in the United States, we can find incentives to do that while we -- while we reform the corporate and individual income tax system.

And there are other measures, clearly, which encourage investment -- or encourage investment. So we - - this hearing's concluded, but to be honest with you, I'm not totally convinced that these provisions add that much to your decisions on where you invest or don't invest, or if they were taken away or

substantially reduced would make that much difference, given the huge profit margin which exists because the price of oil is so high.

I agree with Senator Hatch, you know, this is not going to change the price at the gasoline pump. That's not the issue. I don't see that as an issue at all. The issue I see is who shares and how much does each segment share as we tried to get out of debt and deficits under control and at the same time develop an energy policy.

HATCH: Mr. Chairman...

BAUCUS: I grant -- I grant you we've got to develop an energy policy in this country. It does not have an energy policy. There's a lot we have to do. But we also have to figure how we get our debt and deficits down.

HATCH: Mr. Chairman, just one last comment. I agree with you, and I know that you're sincerely devoted to doing that. And I appreciate it, and it's an honor for me to serve with you. My problem is there's not a real good reason for raising this, because I guarantee you if they raise these taxes, Congress will spend every dime of it. It won't go to pay down the deficit, because we don't have a -- we don't have a capacity right now, or even a Gramm- Rudman bill that might work better, that would cause this is to go to pay down the deficit.

I guarantee you if you raise taxes, that...

BAUCUS: Senator, I respectfully disagree, and the reason I disagree -- because we have to. We have to get these deficits and debts down so we don't bump against that...

HATCH: Anybody...

BAUCUS: ... bump up against the debt limit so we can't default, so we can't bump against that limit. We've got to get our debts and deficits down so this country's on a sound financial footing. We will do it because we have to do it.

Hearing's concluded.