General Explanations of the Administration's Fiscal Year 2015 Revenue Proposals

Department of the Treasury
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REPEAL DOMESTIC MANUFACTURING DEDUCTION FOR THE PRODUCTION OF COAL AND OTHER HARD MINERAL FOSSIL FUELS

Current Law

A deduction is allowed with respect to income attributable to domestic production activities (the manufacturing deduction). For taxable years beginning after 2009, the manufacturing deduction is generally equal to nine percent of the lesser of qualified production activities income for the taxable year or taxable income for the taxable year, limited to 50 percent of the W-2 wages of the taxpayer for the taxable year.

Qualified production activities income is generally calculated as a taxpayer's domestic production gross receipts (i.e., the gross receipts derived from any lease, rental, license, sale, exchange, or other disposition of qualifying production property manufactured, produced, grown, or extracted by the taxpayer in whole or significant part within the United States; any qualified film produced by the taxpayer; or electricity, natural gas, or potable water produced by the taxpayer in the United States) minus the cost of goods sold and other expenses, losses, or deductions attributable to such receipts.

The manufacturing deduction generally is available to all taxpayers that generate qualified production activities income, which under current law includes income from the sale, exchange or disposition of coal, other hard-mineral fossil fuels, or primary products thereof produced in the United States.

Reasons for Change

The President agreed at the G-20 Summit in Pittsburgh to phase out subsidies for fossil fuels so that the United States can transition to a 21st-century energy economy. The manufacturing deduction for coal and other hard mineral fossil fuels effectively provides a lower rate of tax with respect to a favored source of income. The lower rate of tax, like other fossil-fuel preferences the Administration proposes to repeal, distorts markets by encouraging more investment in fossil-fuel production than would occur under a neutral system. This market distortion is inconsistent with the Administration's policy of supporting a clean energy economy and cutting carbon pollution. Moreover, the tax subsidy for coal and other hard-mineral fossil fuels must ultimately be financed with taxes that cause other economic distortions, e.g., underinvestment in other, potentially more productive, areas of the economy.

Proposal

The proposal would retain the overall manufacturing deduction, but exclude from the definition of domestic production gross receipts all gross receipts derived from the sale, exchange or other disposition of coal, other hard-mineral fossil fuels, or a primary product thereof. The hard mineral fossil fuels to which the exclusion would apply include lignite and oil shale to which a 15-percent depletion rate applies. There is a parallel proposal to repeal the domestic manufacturing deduction for oil and natural gas companies. The proposal would be effective for taxable years beginning after December 31, 2014.