EXECUTIVE SESSION

- - -

WEDNESDAY, OCTOBER 3, 1979

- - -

United States Senate,
Committee on Finance,
Washington, D. C.

The Committee met, pursuant to recess, at 10:45 a.m. in room 2221, Dirksen Senate Office Building, Hon. Russell B. Long, Chairman of the Subcommittee, presiding.

Present: Senators Long, Byrd, Nelson, Gravel, Bentsen, Baucus, Boren, Bradley, Dole, Packwood, Danforth, Chafee and Wallop.

The Chairman: I have been hoping that we could dispose of the Alaskan issue and Senator Gravel is here.

Are you ready to go on that, Senator?

Senator Gravel: I would like to take it up tomorrow morning and just press for a couple of members that I know that I would like to see subjected to the edification of some charts that I have.

Otherwise, I would be talking, and the votes would be crucial to this. I need that.

Why do we not start, Mr. Chairman. If you would permit me, I would be ready first thing in the morning.

The Chairman: Well, then, I would like to report this bill this week, gentlemen, if we can. I would like to get this package together to see what it looks like and start seeing if we have to make adjustments and, if so, where.

How about upper tier? I suggest that we act on that. Tell us what the situation is on the upper tier now, Mr. Shapiro.

Mr. Shapiro: That is a subject you have not gotten to yet. The definition of upper tier is essentially all oil that has been produced after 1972, '73 and afterwards, the so-called upper tier, Tier II, oil.

Senator Nelson: Before?

Mr. Shapiro: You have lower tier.

Senator Nelson: No. Upper tier goes from '72 to what date?

Mr. Shapiro: To '78.

Senator Nelson: Everything after '78 is new?

Mr. Shapiro: Newly-discovered oil, so essentially you have the three major categories: oil that was in existence in 1972 is lower tier, old oil; oil after '73 to 1978 is Tier II, upper tier oil; and all oil discovered after 1978 is newly-discovered oil.

There are some cases where you have incentives, for example, where you have these decline curves on lower-tier oil. Where oil is produced above that decline curve it is treated as second tier, Tier II, oil.

Also, marginal oil has been placed in Tier II in the House bill and is proposed by the administration, as well, to do that. That is the definition of Tier II oil.

In the House bill, you have a rate of 60 percent for the windfall profits tax and you also get a deduction for the state severance taxes. As you may recall, the administration proposed a bill with the 50 percent rate and no deduction for state severance taxes.

The House increased the rate to 60 percent and, at the same time, added a deduction for state severance taxes. The base price for the windfall profits tax for the upper tier is $13. As you recall for Tier I, it is $6.

So you have $13, and that is adjusted for inflation.

The way the tax works, once again you have the windfall profits tax equal the rate, which is 60 percent, times the selling price, whatever that selling price is, minus the base price. The base price in upper tier is $13 and that is adjusted for inflation.

The House bill, as the administration proposes phasing out the tax between 1986 to the end of 1990, so the tax is phased out over that period of time. The effect of that is that base price phases out from $13 to $16. When I say phases out, all that I mean is that the oil that would be subject to tax in the second tier is phased up to the third tier.

There is still a tax on that oil, but instead of being a tax at the second tier, which has a base price of $13, after 1990, that same oil would be subject to tax in the third tier, essentially with a base price of $16. Of course, that is adjusted for inflation.

There are a series of proposals that are before the committee. They are the options that the staff has presented that we are aware of. On your memorandum dated September 24th, you will find the outline that I just summarized as well as a series of revenue effects of the various proposals.

For example, if you take the House-passed bill, increase the rate from 60 percent to 75 percent, you would increase revenues by $9.5 billion over the eleven-year period from 1980 to 1990.

Senator Chafee: I wonder if we could get clear, we are now working from this sheet here with the long charts.

Mr. Shapiro: The long chart, the heading that says, "Revenue Effects of Windfall Profits Tax Proposals - Tier II."

The Chairman: You are looking at the spread sheet now?

Mr. Shapiro: The spread sheet, the heading would be Tier II on the heading.

Senator Nelson: Do you have any extra copies of that? I do not see it.

Mr. Shapiro: Yes, we will have copies. So there are extra copies, if any member does not have a copy of it. The heading of the long chart that has Tier II on it, the first proposal has a House bill with a 75 percent rate. That raises, over the eleven-year period, 1980 to 1990, $9.5 billion.

On the other hand, if we reduce the House-passed rate from 60 percent to 50 percent, you see that is a reduction of $6 billion. On the other hand, there are a series of phaseout proposals that have been suggested between 1985 and 1989, or 1986 to 1990. This would be phasing out that oil income tax.

What the House bill does is it phases out Tier II by saying that the Tier II oil would be phased in to Tier III, so that oil would still have a tax after 1990, but it would be taxed in Tier III.

These phaseouts suggest that the oli would no longer be subject to tax at the end of that phaseout period, so it would end the tax on that particular oil.

You see the phaseouts there that are just on the existing House bill, and then you see a phaseout with a 75 percent rate and a 50 percent rate. We understand this morning that there are possibly some other suggestions that have differentials between majors and independents rates. We are trying to get those revenue effects as well.

So I would think that the major issues that the committee has to decide is, first, not necessarily first -- it has to be taken into account the rate, the House's 60 percent rate. You can go higher, 70 to 75 percent, or you can go lower to 50 percent.

Second, do you want a phase out of that oil completely so after a period of time the oil in this particular tier would not be subject to any tax, and then do you want any type of a decline? What type of a decline curve which, is in a sense, your phase out.

Senator Dole: You mentioned Tier III. Maybe I missed something.

Mr. Shapiro: You say Tier III?

Senator Dole: Right.

Mr. Shapiro: Tier III is essentially stripper oil. It used to be that Tier III was everything that was not in Tier I and Tier II and then the House modified those other categories and you had a special rule for newly-discovered, a special rule for incremental tertiary, a special for Alaska, so that the regular Tier II, as proposed by the administration in effect only applied to striper.

Now that you have exempted newly-discovered and incremental tertiary you just have stripper oil as the regular Tier III and that is the modification you made yesterday, and then you have Alaska, which has its own special rule.

Senator Chafee: Mr. Chairman?

The Chairman: Yes, sir.

Senator Chafee: Mr. Chairman, I have submitted legislation and have supported a position which is a 75 percent tax with a phaseout as set forth in the line next to the bottom.

Now, I think there are two things that are important -- three things, I guess, that we should say. First, this is a greater tax than the President has proposed, than the House bill has proposed, which, as you know, is 60 percent. Mind you, all of these figures that we are looking at are variations from the House bill.

Secondly, it has a phaseout. That is a very, very, I believe, important factor. This is a complete phaseout, not just a phaseout the way Bob was mentioning earier. This gets rid of the tax completely.

And finally, I think that we have to take into account what took place yesterday, namely the passage of the Dole substitute or amendment that followed on what Senator Boren proposed which is, as I understand it, costs about -- was that $7 billion?

Senator Dole: $7.7 billion.

Senator Chafee: $7.7 billion.

So, Mr. Chairman, I would ask if we could do this. If people -- this exercise will not take long, but just set down what we have done now, variations from the House bill. The stripper is $7.7 billion. The heavy oil -- these are all minus figures -- is $5 billion. The newly-discovered is $14.

The Chairman: What is heavy?

Senator Chafee: The heavy is $5 billion, the newly-discovered is $14 billion. The incremental tertiary is $9.9 billion.

Bob, if you have any differentiations from these --

Mr. Shapiro: There is some interaction. When you look at each one separately, the figures you have are correct, but when you take into account having exempted newly-discovered and incremental tertiary, there is some overlap in that and some other things you have done, so that tertiary you can put down to about $7.5 billion. That is just the interaction. That is the heavy oil.

The heavy oil, incremental tertiary.

The Chairman: Does it all come within tertiary?

Mr. Shapiro: A lot of the heavy oil is incremental tertiary.

Senator Chafee: All right. Let's go with my figures and put that correction at the bottom of the column. We are up to incremental tertiary at $9.9 billion. Political subdivisions, $6.5 billion.

The Chairman: Hold on a minute. Political subdivisions was never in there. That was never in there at all.

Mr. Shapiro: That is a part of the House bill of $104 billion in the House bill, included an exemption for the states.

Senator Danforth: $104 billion in the House bill. We sweetened that, did we not?

Mr. Shapiro: Not yet. You have added a little bit of both. You added some, you have taken away some. We are down.

Senator Danforth: I see. I thought the House bill only exempted where the proceeds were used for educational purposes.

Mr. Shapiro: You are correct in the sense that the House proisin technically said that it had to be dedicated for educational purposes. For estimating purposes, we assumed that if it passed in that form that every state would do that, so we assumed the full revenue loss, even though it was dedicated to educational purposes.

We just felt that every state would find a way of changing their books, just saying that the oil royalties would be dedicated to education and they would shift it around so they would get the full benefit of that provision.

Senator Bentsen: As you say, there is interaction there. We also did the heavy oil exemption and we did the tertiary recovery. I was very interested to see when we talked about the public lands that what was attributed to Texas was relatively small compared to some other states like California and Alaska.

Particularly it would seem that in California with your heavy oils and your tertiary that a very substantial amount of that would be coming through that exemption and therefore would modify very substantially the amount we are talking about.

Mr. Shapiro: Senator Bentsen is actually correct in that regard. What he is saying, when we are giving each of these figures separately, it is if you ignore any other change and you look at that one provision, and that is the revenue effect. When we talked about the state lands yesterday, we talked about $6.5 billion. That is actually the amount that is attributed to the House bill.

When you deal with incremental tertiary or heavy oil, much of the oil owned by the states is that type of oil, so having exempted that, you would not pick up any revenue, even if you were to tax the states.

So the $6.5 billion, which is the correct figure, just looking at that alone is too high, taking into account the other exemptions that the Committee has already agreed to.

We do not have the lower figure, but it would be somewhat less than the $6.5 billion.

Senator Chafee: I wonder if we could kind of continue down this and then make the corrections. I took out the political subdivisions so I get that add up, not with the adjustment that you made, Bob. We will do that in a minute.

I get that $36.6 billion, is that correct? Leaving out the political subdivisions?

Mr. Shapiro: Would you mind running through that?

Senator Chafee: $7.7 billion. Heavy oil, $5 billion. Newly-discovered, $13 billion. Incremental tertiary, $9.9 billion.

Mr. Shapiro: $36.6 billion.

Senator Chafee: All right. Make your adjustment for what you figure is the duplication between the newly-discovered or the incremental tertiary and the heavy.

Mr. Shapiro: Almost $2.5 billion for the interaction. You also picked up $1 billion with your higher rate on the first tier oil, so I think you add that approximately $3.5 billion.

Senator Chafee: All right. Where are you now?

Senator Dole: $33.1 billion.

Senator Chafee: Now you are down to $33.1 billion, right?

Mr. Shapiro: Approximately $33 billion. The interaction is $33.2 billion.

Senator Chafee: We have not yet dealt with the Indians, which was not in the House bill, or was it?

Mr. Shapiro: No.

Senator Chafee: That is relatively minor and Alaska. So that it appears, Mr. Chairman, that no matter where we are, we are going to be down from the House bill $33 billion as of now, and then, of course, on the other side -- obviously, we are setting aside how much the credits are and all of that, as you know. We have indicated here a considerable interest in low income. I will just list some of the ones --

The Chairman: Let me just stop you just a minute on lower income. That is a very important thing in our calculations.

The administration's recommendation for low income, if I recall it, is not on the taxing side. It is on the spending side and it comes in at about $1.6 billion. There are two items involved in it, but both for budget purposes fall on the spending side of the budget.

Mr. Stern: That is correct.

The Chairman: My thought is that is not to be funding on the net figures here. That is funded by general revenues, and on general revenues.

Now, the Senate budget figure on the spending side has $500 million for that, and on the House side, I think they have got something near the administration figure. Could somebody tell me what the figures are on the House side.

Mr. Stern: I do not know the answer to that.

The Chairman: I think it is something like the administration figure. The administration has $1.6 billion. Somewhere between $1.2 billion to $1.6 billion, somewhere in there.

The way that I look at that part of it, if you are going to do anything worthy of the name, you are not going to be able to stay with the Senate budget figure. You are going to have to go more like the House figure, or even above that, but assuming that you are going to have a meaningful program, that part of it ought to be financed out of general revenues in which the deregulation itself, aside from the tax, increases government revenues by $2.5 billion.

We have not been counting that in this tax. We have not been counting it at all.

So that I do not think that, for our purposes, we are talking about the tax part of the bill. I do not think that we have to cushion that $1.4 billion. If we give the administration what they are asking for at low income, it seems to me as though -- because otherwise that would use up about 75 percent of the $2 billion that we are thinking about working with to begin with.

It seems to me if you think in terms of that we have one-third of what we could have in here in terms of new production, of additional production and incentives in the traditional sense of producing oil, if you think of perhaps one-third of it in terms of the kind of thing that you sponsored, Senator, where you encouraged conservation and encouraged insulation, and then planned at about one-third of it being for these other committees to spend for syn fuels and the various things that fall outside our jurisdiction, it seems to me as though we are pretty close to target on this side of the taxing side.

That is about the way I have been thinking. The others may be thinking in entirely different terms.

It seems to me, assuming that we can hold our conservation package down, our conservation and alternative sources, to about the same general ballpark that we are talking about producing more oil, then we are in pretty good shape.

That is the way I have been thinking. When we go to conference with the House -- well, of course, they do not have anything on the alternative sources, even the administration recommendations. Mr. Shapiro?

Mr. Shapiro: The House had one session. They made no decisions. They do not have any sessions set in the Ways and Means Committee to consider credits. As of now, they have no position.

The Chairman: Because, if you are trying to finance any meaningful program for the poor, in addition to some of the things we are talking about, there is no way you could find the revenues for that, but the administration, I do not think, has been thinking in those terms. They start out thinking $2 billion, $2 billion for syn fuels, for urban transit, and matters of that sort, as I recall.

It was not this program for the poor.

Mr. Shapiro: As we understand what the administration was originally contemplating, maybe they should speak more specifically to it. They had a program that included the tax, the additional revenue for the corporate tax, all of that to be segmented, separated into what account, a trust fund or separate account, and everything for the poor and all of that to come out of that, and they contemplated using the increased revenue from the additional income tax to be used at all.

The Chairman: They were working with the gross figures?

Mr. Shapiro: Gross figures, windfall, plus the additional corporate income tax.

The Chairman: If you look at the way the administration was thinking about all of this, they were thinking from the $3.5 billion rather than $3.0 billion..

Mr. Shapiro: It is even higher than that. The $3.0 billion is the net. They were talking about the gross revenues from windfall plus the increase in the individual corporate income taxes.

The Chairman: Were they including in their figures the increase on Federal royalties?

Mr. Shapiro: No.

The Chairman: They might as well. That is an additional source of income that they receive.

The point is, Senator, I want you to understand that I do not think we ought to be trying to look -- that we should be saying that the $2.3 billion net figure should be cushioned as aid for the poor. When you think about aid for the poor, you are entitled to look at the gross figure.

Senator Chafee: I am not sure that I completely understand that, but I do know, as I understand it, in the administration they had nothing for fiscal '80 for the poor out of this. It came from general revenue.

Then I thought of the ten-year period. They were $24 billion. Is that correct, or wrong.

Mr. Stern: It is correct, that they assumesd $24 billion. That $24 billion, they concede as coming out of a gross windfall profits tax.

Mr. Shapiro: Senator, we have two sources of revenue from energy. First, when you have deregulation, first is that you have additional income taxes on the higher prices and second, we are talking about the gross windfall profit taxes. It was contemplated that those monies together would be put into a trust fund or a segregated account in the Treasury and that anything that you do with energy would come from that.

For example, it would include the money for the poor, the mass transit, the Energy Security Corporation. All of that would come from the segregated account or from the trust fund.

When the bill was sent to the Ways and Means Committee, they only sent the tax. They did not send up any of their spending programs either for the poor or from the credits or from the Security Corporation.

The Ways and Means Committee made a decision to put the money into the trust fund, not to deal with any of the spending. Also, the decision was made by the Ways and Means Committee that the Chairman was contemplating not to use the money for the poor out of the trust fund.

At that time, it was thought that the administration might send to the Congress a tax relief proposal rather than a grant type proposal.

What the Ways and Means Committee was contemplating, let the increased income taxes from the higher prices go into general revenues and any money that was to go to the poor would come from general revenues and to put only the windfall profit taxes into the trust fund, and then to use that trust fund only for energy purposes, not the poor.

They even contemplated having the credits come from general revenues. So the money for the poor and the credits to come from general revenues.

Senator Chafee: What has the Budget Committee done with all of that.

Mr. Shapiro: Subsequent to the time that the Ways and Means Committee acted, the administration came forth with their credit proposal. The Ways and Means Committee has not acted on that, and just recently in the last several weeks, the administration came forward with their program for the poor which was an expenditure program rather than a tax credit type of proposal.

The Budget Committee, as I understand it -- Mike can speak more specifically to this -- has taken that as far as an expenditure, and there are differences in the way the House and Senate is treated.

Mr. Stern: On the Senate side, they have included $500 million. Specifically, I should say, earmarked in their Committee Report that they contemplated $500 million for low-income assistance.

Senator Chafee: For '80.

Mr. Stern: For fiscal year 1980 for which $400 million was for this crisis program that is already in the law under the Human Resources Committee jurisdiction.

Senator Chafee: How about for '81. Have they given some thought to that?

Mr. Stern: I do not know that there is a specific amount of money.

Senator Bradley: How about for the full ten-year period, the numbers?

Mr. Stern: The Budget Committee, of course, really is only fairly specific about fiscal year 1980. The administration proposal is $2.4 billion a year.

Senator Bradley: Over a ten-year period for the poor?

Mr. Stern: That is correct. $1.6 billion is for part of the year. The full-year cost of that program is for $2.4

billion.

Senator Bradley: The administration suggested what, for public transit?

Mr. Shapiro: The administration, over the eleven-year period, they have a total of $142 billion. The transportation efficiency part of it is $16.5 billion.

Of course, as you recall, they had $88 billion set aside for the Energy Security Corporation.

Senator Chafee: If I could interrupt one minute, where I get mixed up, did the administration have that money -- say the $24 billion or the $14 billion -- for transportation, was that to come from the mixed fund of the income tax and the windfall or was it to come from solely the windfall.

Mr. Sunley: Senator Chafee, the administration proposed putting the gross amount of the windfall profits tax into the Energy Security Trust Fund. Also, the administration proposed for a three-year period only, only the first three years transferring the additional income taxes paid by producers and royalty holders. But out of that trust fund was to be funded the alternative fuels programs, mass transit and income for the poor.

The Chairman: Senator, please understand by the time we get confused about that matter, I suffered exactly that same confusion, but I just thought -- I think I ran into the problem about three days sooner than you did. How, in the world, can you get all of this out of that?

You look at $2 billion and you are looking at about $4 billion cold on the money? How in the world can you do it.

Well, the answer is that they were working from gross figures where they were using this additional money that comes from the deregulation in terms of personal income taxes and corporate income taxes, quite apart from this windfall tax.

And so when you go back and look at the revenues they were counting on using, and think of those terms, it is very easy to figure out how you can handle it.

I must admit that I spent about three days around here saying this, there is no way on earth that you can get there from here. But if you look at it in terms of how they had in mind to get there to begin with, it is possible.

Senator Bradley : Mr. Chairman?

Senator Danforth: Mr. Chairman?

The Chairman: Yes.

Senator Danofrth: How much do they expect to get frm the windfall tax, net. Net proceeds, how much did the administration expect from the windfalls tax, $105 was it not?

Mr. Sunley: Under the original administration proposal, costed out under the assumptions that the Joint Committee staff used, it was $110 billion, just a little bit above the House-passed bill, and then the modifications to the House-passed bill that Secretary Blumenthal endorsed before your Committee came out at $118 billion, somewhat above the original administration proposal.

Senator Danforth: $118 billion net.

Mr. Sunley: That is the net number.

Senator Danforth: What adjustments, if any, have been made by the admnistration for expectations from the net windfall tax since that time? Is it still at $118 billion?

Mr. Sunley: The administration has not altered its position.

Senator Danforth: So, then, the administration wants $118 billion and the House provided for about $105 billion.

Mr. Sunley: $104 billion.

Senator Danforth: The administration is at $118 billion, the House is at $104 billion and, as Senator Chafee says, presently the Senate is where?

Senator Chafee: $71 billion.

Senator Danforth: $71 billion.

Senator Chafee: Without Alaska.

Senator Danforth: Any way you cut it it is fair to say that there is a very significant difference between these three figures.

Senator Bradley: That is correct. If we accept your assumptions that the administration made about how the money would be spent, if you look at the biggest chunk, it is $88 billion for the syn fuels program and what we are talking about in the Energy Committee and in the House and in the Banking Committee is a program scaled down to about $20 billion, and so if you take a look at the figures that the administration proposed in the other areas, $24 billion for low-income, $16 billion for mass transit, or public transit, then you have $20 billion for syn fuels and then you have the alternate fuel and conservation scaled down to, say, $20 billion or $25 billion, you are at a figure of $85 billion, which is well within the reach of this committee on the net revenue side, and it seems to me that if you are going to make the argument that something should be pushed off into the gross revenue side, that what you would push off is syn fuels and not push off the idea of low income or the idea that public transit has to be on the gross revenues side, because the fact is that there is probably not going to be an approval of $88 billion in syn fuels.

So what we are arguing about here is a figure that has disappeared.

Mr. Sunley: As I understand it, the initial proposal the administration had for the syn fuels, the $88 billion, involved four installments of $22 billion each, and the idea was that the Congress would approve authority for those four installments, all at one time.

The President has agreed at this time to seek authority only for the first installment. However, the President is still interested in having room so that if that first installment proves to be desirable that, at a subsequent date, Congress could approve a second or third or fourth installment.

So, in a sense, I think it is sort of important that we leave some room. It is true that this one budget only has to approve that first installment, but if you have spent everything for the next ten years, you really have foreclosed a larger syn fuels program other than the first $20 billion to $22 billion installment.

Senator Bradley: The question is, when the technologies that are going to be in the first phase would have proven themselves to be competitive and not competitive, and there is a wide range of dispute here as to whether they would prove that in five, six, seven or eight years so that if we are formulating a program for ten years it is quite possible that if you are putting in an $88 billion cushion that you will not need that $88 billion cushion at all.

The Banking Committee already acted not on one phase but on the syn fuels program.

Senator Bentsen: If the Senator would yield for a question, also you have the situation of how you do the funding. Is it in subsidies, is it in guaranteed prices, guaranteed government loans, and that certainly does not necessarily mean that you have to match each of those with a dollar.

Senator Bradley: Under the Syn Fuels Corporation bill that is now proceeding through the Energy Committee, a loan guarantee or a price guarantee would match part of that $20 billion.

Senator Bentsen: You do not have to match the full $88 billion.

Senator Bradley: That is correct.

Senator Gravel: Mr. Chairman?

The Chairman: Mr. Gravel?

Senatoar Gravel: Going through the premise itself, taking the premise of the discussion, taking the chart the staff has put forward, we see that we can get $174 billion worth of revenue straight out just from the deregulation, not even talking about the windfall profits which can go from $100 million to $110 million.

That is only figuring a 1 percent increase in the price of oil, which I do not thilnk there is anybody at this table thinks that is going to happen in the next ten years.

Assuming a 4 percent increase, this chart prepared by staff -- and I think it is probably not unreasonable, based upon what we have seen in the last decade, that the income is going to be $274 million to the Treasury. You can handle as many syn fuel projects as you think you want to get into. I had asked -- billion dollars ---not one sou from windfall profits.

If we take the testimony we have received, in order to keep the oil production at its present level, not expanded, we need to double the amount going into the depot area from $20 billion to $40 billion. That amounts to, in five years, $100 billion. When we are talking about this windfall profit tax itself, we are talking about exactly the sum of money that it takes in five years to keep oil at the present rate of production and if we would then have some faith in the charts that our own staff has prepared for us, that we are going to have more money than we can save grace over to do whatever we want just in the first year, 1980, at 1 percent, $3.4 billion. 1980, out of a 4 percent rise, we have already had a 4 percent this year.

I stand to be corrected. This is the first of the year.

The Chairman: 60 percent.

Senator Gravel: We could figure we have done a couple or three years already.

That means the projections for 1980 of $3.6 million are very, very conservative. How much money do you need to do whatever you want to do.

I was under the impression that the feeling abroad in this country was that we want less government. I am really astounded to see from this side of the aisle the push for greater government and the funding of this. I just do not understand this.

I would think that we should examine the fundamentals of the premise. These are not my figures. These are charts that were put forth by the Committee. I would be happy to hear a comment.

Senator Danforth: I would be happy to comment on it, just to relieve the astounding moment. I do not think we should have any more government than is absolutely necessary and I think that there is a fair chance that Senator Roth and I will offer some proposal for some kind of a tax cut along with this for that very reason.

I do not think that we want to produce government revenues which are far in excess of any need for an energy program, but what we have been getting an answer for now for a month or more is how much do we want to spend for an energy program and how much do we want to raise in windfall taxes. If we can agree that the total amount of the energy program is X, whatever it is, say for example, $85 billion over ten years, we are going to raise that amount from a windfall tax; if you want to raise it from a windfall tax, then you can try to figure out what is going to be the overage, what are we going to produce over and above that and provide for reductions of Social Security taxes, provide for incentives, for rebuilding our industrial plant and equipment out of those proceeds. We are trying to see the whole picture and I think we have failed to see the whole picture. Right now, we are right back to the very basic question: how much do we want to spend, in total, in the energy program and how much of that do we want to raise from the windfall tax?

Senator Gravel: I just wanted to say to my colleague he shed some interesting light on the problem, because if he is talking about raising money for energy then I have not heard of a program and I think Senator Bradley pointed out very clearly -- I have not heard of a program, regardless of what we have passed here, that is not on the order of $174 billion to $274 billion. That is the money we are going to raise, just with deregulation alone.

Now, when you advance the argument that we now, in addition to that $174 billion to $274 billion that is going to flow into the Treasury of the United States for the next ten years, that you want to offer now a tax cut. I have supported tax cuts in the past, but I want to tell you that you are going to begin to lose me on that effort because I do not understand a tax cut which is going to go out and give the people something. That sounds real good.

But since you cannot cut expenditures, you are going to now try to raise it elsewhere and you are going to raise it by turning around and robbing from an industry, but interestingly enough, the most important industry in the United States because energy is the heart of our industrial system.

So if you are going to take money from that heart so it will not function well and think that you can turn around and give a rapid write-off to industry which is now going to be more inefficient regardless of how fast you write it off, because you are going to have to pay more for energy, or you are not going to have the energy compared to other nations, then you have not advanced the productive enterprise of this country one iota.

So I would submit that maybe if you look closely at the figures of $174 billion, and actually more properly, $274 billion, you might find the ability to have a tax cut in the figure rather than to perform a raid on an industry that needs this capital in order to just keep the amount of oil that the industries you are concerned about in your part of the country are using.

The Chairman: Gentlemen, let me just make this suggestion now. If we do full justice to all sides of these arguments ---and I guess I am the worst offender in that regard -- we are not going to get this bill out this week. We might not get it out next week.

What we are going to have to do is give everybody a reasonable opportunity to state his case and then just vote, because in the end, it is just a matter of votes. As good as some of these speeches are, they are not going to change many votes.

Go ahead and state your proposition, Senator Chafee.

Senator Chafee: My proposition, Mr. Chairman, is that we need additional revenue under this windfall profits tax. I have supported the second line from the bottom which will give us in the Tier II at the 75 percent rate at the phase-out, will give us 3.2. That phase-out would start January 1st, 1990.

However, because of the additional loss rates, I would like somebody to pass out these sheets, if they would. The only way we will make it up is to extend the phase-out. We are talking solely now about the period 1980 to 1990.

If you see on these sheets that I give you the first line as the phaseout, as of starting January 1, 1986 at 2 percent per month and you are through January 1st, 1990, and that gives you, at the 75 rate, $2.2 billion over the House bill.

If you delay it two years, you would then pick up $5.5 billion over the House bill and if you delay it until January 1, 1991 -- and again, on the Floor, let me say this, Mr. Chairman, I do not think you can have a phaseout more precipitous than four years. If you make it too precipitous, then people will hold back, and if you delay it, at that final period, you get the nine.

Why is nine important? Because yesterday we lost under the stripper, from where we had been, we lost $7.7 billion and that was quite a loss from the anticipated revenues.

So I would be interested if we might, Mr. Chairman, a brief discussion in the phaseout period, and then I would like to make a motion. Do you want me to make it now, or could we just hear kind of the sentiment on which of the three phaseout periods seems to be -- maybe no one wants this tax to go, but I am for the phaseout. I think it was important.

Senator Nelson: Let me say, Mr. Chairman, I agree with Senator Chafee. With the exemptions that we have put in, stripper yesterday, I think we have to recoup some money and I was intending to support the proposition probably at the 75 percent rate with the phaseout starting in '85 or '86. But I think item number one at the top is what you are going to have to do, start to phase out in 1991 in order to get the $9,495,000,000 so I endorse number one.

Senator Chafee: Do you mean the one at the bottom of the page?

Senator Nelson: No. The proposed phase out starting in 1991. Does that not produce $9 billion something? I am not looking at the same sheet. The one on the bottom of the page you just passed out. I was looking at the big chart.

Senator Gravel: Mr. Chairan, could I ask Senator Chafee a question relative to this proposal?

The Chairman: Sure.

Senator Gravel: Senator Chafee, you stated you needed additional revenues. What is the purpose of the additional revenues that you feel you have to raise with this amendment?

Senator Chafee: I just pointed out, if you sat in here, as you have part of the time, and you have seen that we have had -- well, in the alternate fuels, Senator Danforth's proposal was $14 billion. It was accepted. The syn fuel -- I do not know how much the people want to spend on that -- the credits on which I had a hand.

I pitched right in and helped that out. That got up to, my figures show, $90 billion, and I just figured we have got to shoot for a figure in the neighborhood of $85 billion or, say, $80 billion, to have the revenue to match these things which are already way above the total of $85 billion, and already we are down to $71 billion that we are going to get.

You went through the statistics earlier this morning. That is not taking whatever results from the Alaskan oil situation. So we are some ways from the '80, '85.

The Chairman: Let me ask you this.

Senator Gravel: Mr. Chairman, if I may respond to that one point.

The Chairman: Yes.

Senator Gravel: The figures that we have from the Committee staff is that we are going to raise, with a 4 percent increase per year over the same period, $274 million.

Senator Chafee: Could I just say, the ground rules as set forth by the Chairman was only to consider the windfall profits tax, and that is the basis on which we proceeded in this committee.

The Chairman: Well --

Senator Gravel: I did not understand those ground rules.

The Chairman: Let me just get that straight, because I have no power to bind anybody to anything. I suggested that in discussing these figures we were in here with at least two sets of figures or more and I proposed that we discussed what we are doing here in terms of one set of figures, because otherwise, every time you try to talk about something there is no way you could relate one thing to the other, unless you decided -- it is almost like saying, well, if we are going to talk on an issue, we are going to talk in French. What language are we going to talk?

It seemed to me that we should talk in terms of the net figures for purposes of talking about the tax, because the tax we are talking about levying is a net tax.

Now, that being the case, it might have led to some confusion in people's thinking and including my own, but when we are talking about what do we propose to do, we had a whole lot of items that the administration was thinking about that they had in mind, not funding just from a net tax, but the revenue that you are going to get from that decontrol itself, as well as the tax, that has been explained here today.

I hope that those who are our guests in the room have some understanding of what we are talking about here. We adopted that for purposes of knowing -- of eliminating the confusion about what we are talking about. We are talking about what the tax is going to bring. From this tax, we are talking about what you get when you deregulate.

I would think, and I would hope in terms of what we propose to raise and what we hope to spend in terms of tax expenditures or in terms of tax cuts and tax credits would fit inside those net figures, and I think now some of us on the producing end for purposes of getting it all out there so that we can talk about it went all the way with our friends from the conservation end and from the alternate sources and saying, yes, let us agree to all of this, and so, in that area alone, as I recall, the things we agreed to exceeded the entire net figure.

So we agreed, all right, that is going to be -- we knew all the time in doing that that that has to be reconciled, that that will be reconciled, all right?

Now, here on the other side of it, we are talking about what we think we would get more production in terms of not putting so much tax on, such as exempting a new production.

But some Senators, including the Senator from Rhode Island, take the view since we have already run over on the side, anything that is done in the way of producing oil is concerned, you are just that much more over.

I do not quite think that is necessarily the way it is going to have to be. It seems to me that we think in terms by the time you get through reconciling these alternative uses and the conservation end of it, hopefully you will show up with a figure that will use up one-third of the revenue, and if you will think in terms of the other side of doing this thing and the other committees in the syn fuel area, take one-third of the revenue we can raise here on a net basis, I would think that we would have a very well-balanced bill.

That does not think you are going to get that much by the time you go to conference with the House. That does not have anything in the alternative areas. We are going to have to compromise with them.

Just like I would think on the tax cuts we are talking about, we have to compromise. Oftentimes, if we cannot agree, you just get completely at loggerheads and you just split the difference.

Whatever we do here, that is not the bill the President is going to send, that is just what the Senate Committee comes out recommending, and I think we ought to keep that in mind. There is a long distance between this committee and the President's desk.

Senator Chafee: I appreciate that. I might point out, Mr. Chairman, you indicated that I have the view that anything we come down in one area we have got to go up in another. We started out with a House bill that was $104 billion and none of us, certainly speaking on my part, have made any effort to get anywhere near that $104 billion.

I have talked here in terms of $80 billion to $85 billion.

The Chariman: But, Senator, let's try to keep our thinking together if we can. Keep in mind that even if we look at the administration figure, they were not planning to use that to balance the budget. They were planning to use that to help meet the problem, to use that to bring about more production, to bring about more conservation, produce alternative sources of energy, including the synthetics.

Senator Chafee: I appreciate that, and they have set forth figures as to what they think they require. If you add all of that up, you get to this $80 billion to $85 billion that I am talking about, whether it is credits or alternate fuels or syn fuels.

The Chairman: Senator, for the purpose they had in mind -- I want Mr. Shapiro to hear this -- for the purposes of what the administration had in mind, they had in mind not only the $104 billion that we started out with that they assumed the tax is going to raise, but they also had in mind the revenue that you were going to get by deregulation which is what -- give us that figure?

Mr. Shapiro: As I understand it, two changes, Senator, one that contemplated the first three years of the additional taxes as a result of deregulation to be used; second, the gross revenues, not the net revenues, the gross revenues to be used; and we have so far been talking about the net revenues.

Let me just give you a little background as to where the confusion is to help some of the problem on the House side. There was no decision of spending.

At that time, they were talking about not much money. OPEC did not raise prices. We started talking at the House side in early June. At that time, we were talking about using gross revenues in the trust fund. Also, there was no budget concern at that time. We did not know where we were going to have to come out in the Budget Resolution.

It is after the House had passed the bill, when all the discussion in the House side was on gross revenues in the trust fund and no discussion on the spending programs. Then when the bill came to the Senate side, you started talking about the gross and the net because you started focusing more on the budget consequences, and then the budget was focusing more on the net figures and the spending programs had been submitted to Congress, at least the energy credits as well as the gross amount that the Treasury wanted to spend, even though the administration had not sent up their low-income program, they did say how much they wanted to spend. They just did not submit to Congress how they wanted to do it, and that is what brought in all of this discussion of how to spend those amounts.

The Chairman: Senator Chafee, I want one more thing to be understood in this room, especially these able people who represent the media.

It was my thought in the beginning ---and Chairman Ullman knew this. I assume he communicated with his members, I hope he did, because we discussed it. The House was going to get this bill to us and the were going to go to work, then, on the rest of the administration recommendations so that by the time that we were through considering this one, they would have their other bills to us, and that we would do what the Senate always tends to do. People bring in amendments that involve the alternative uses of energy and all the rest.

By the time we got back to them, we would go back with one bill where they sent us three, but we would be working on the tax and we would be looking at these alternative uses all at the same time.

The way it is looking right now, they may never get here with these other two bills and we may have to take these other parts of the program, the part for the poor and the part for the alternative users and the part for the conservation, the parts of all within our jurisdiction and go over there and talk to them in conference about what we had in mind talking about, except that ti would be our bill rather than talking about their ill plus ours.

So that they started out sending us a bill, having told the House, "Look fellows, and girls, let's worry about passing. Let's get the tax passed and we will talk about what we are going to do with the money later on," so that is this bill.

When it got over here, our people looked at it, and they said, as they always do, "Look, we want to talk about both the tax, and we want to talk about what you plan to do with the money."

So we have been talking about that and we have been voting on a lot of it, in so far as it is within our jurisdiction. What we are moving to do has been to take what they were planning to send us at about three bills and put it in one and go back to them. It may be that they are just going to have to go back out there with a conference report that takes care of the other parts of the program. After the conduct committee hearings without passing a bill.

In any event, we are here talking about the whole program that falls within our jursidiction.

If we can pass that bill -- and I believe we can ---by the time we get through, we will have done the whole job in what will have been three bills sent to us by the House.

Senator Bentsen: Mr. Chairman, if I might just a moment, on another phase of the problem, I understand the concern of the problem of trying to make up some of the funds that have been lost by the exemptions, but I think when we say we are going to increase the tax from the 50 --

Senator Chafee: 60.

Senator Bentsen: If you would let me finish, please -- from the 50 as proposed by the administration and then the 60 as proposed by the House and you go on to 75 percent the assumption apparently has to be that there will not be an adverse supply response and I think that one is dead wrong. I think you will have an adverse supply response.

If you follow it through, what you have done on the one side, you have given the market incentive. On the other side, you have taken away, and what you finally end up, you are only leaving about 7 cents out of the incremental dollar that will finally be invested by the producer. I think you really have a real deterence that takes effect when you get it that high.

You get to the point that you have taken away the incentive that was brought about in the marketplace by the deregulation.

Senator Chafee: I would just like to say this. As you know, Mr. Chairman, we debated this rather extensively before and producing oil at $13, there is an inflation facotr in here. There is some -- you keep something. It is not a 100 percent tax which, as you know, one of the majors certainly introduced and supported a 100 percent tax.

Furthermore, there is a phaseout which I think is a very significant factor, and I am sure there is going to be some supply response. There is anything, absent a free market. I do not think the supply response will be that significant.

The Chairman: Senator, that 100 percent tax you are talking about, I assume you are talking about the kind of thing the Governor of Texas was talking about, a 100 percent tax on anything that people do not put back into that they are trying to get more energy. Do not tax the part they do. I think that is the kind of thing you are talking about, which is quite different from what you are talking about here.

We really ought to, in considering this, look at those two assumptions that we talked about in the committee hearing. One of them is assuming that the person does not put any of this back into trying to produce more energy.

Mr. Lubick has checked that out. Mr. Cowan gave you a chart on that. Do you have those figures somewhere where we can come right up with them, because one of them assumed he does not put any of it back. The other assumes that he puts it all back and you can see in one case how much he has left and in the other case you can see how much he has to put back.

Senator Chafee: While they are looking for that, Mr. Chairman, my reference was not to the Governor or Texas, it was one of the majors who said, keep the price controls, keep the regulation on lower and upper tier oil. When you keep price controls in effect, that is a 100 percent tax.

The Chairman: They also said give us no tax on the new oil. That particular proposal.

If anybody recommends a 100 percent tax, there is something else in his kit. You can bet on that. Maybe you had better put it on the board. Maybe you can put it on the board so we can look at it. Mr. Stern has a nice, neat handwriting. I tell you, he could be my schoolteacher any day in the week.

Mike, how about putting on the blackboard what the figures show?

May I say that these figures here, Senator -- and I believe you perhaps know -- they have got to be good figures because Mr. Lubick agrees with these figures and the man who had his job before him who came here representing producers, they agreed on these figures, so we get a lot of bad information up here, but I wanted you to know that this is good information. By the time you get Mr. Lubick and Mr. Cowan to agree on it, being two great lawyers and two great philosophers with something of a difference of opinion in some areas that they have got to be good figures.

Now, these figures here are not in dispute. These were agreed to by the Treasury and by Mr. Cowan, who used to have the same job that Mr. Lubick has now at the Treasury, and these figures are not in dispute. This is how the tax actually works out.

If you assume no windfall tax, a producer -- and it varies some by states, but it does not vary enough to change the principle around much. It varies some, but not to a great difference, or a major difference.

If you assume no tax and you assume if a producer is putting back into the ground 100 percent of what he had available in cash to put back in and the independents testified that they are doing better than that, and the majors as well, they say they put a lot back, but they do not claim any 100 percent.

Now, assuming no investment under existing law, the government would take about $58.70. Look at that number one item. He would have $41.30 he could put back in. Now, if you assume that he reinvested all his money, look at the next figure. By virtue of the fact that he gets his intangible drilling costs as a tax deferral -- not an ultimate exemption, but it defers a tax from this year to the following year and by doing that, he could put $63.79 back in.

Now, if you put the 60 percent tax on him, then out of each additional dollar made because of the decontrol, assuming no reinvestment, the way the House bill would stand, he could put $10.31 back in. If you assume that he reinvested everything that he had available to him, that would be $15.92 that he could reinvest, part of which, of course, he could reinvest because of the intangible drilling expense that he would gain by doing so.

Make the same assumptions against the 50 percent tax rate, and you work out to $11.05 compared to $17.07, but when you look in terms of how much a person has to reinvest or how much he has left, that is what you assume.

You are starting out assuming $100 income. When you are looking at what you have left to tax, there is not much left there to tax away anyway. When you say well, at the 60 percent rate, assuming that he reinvested all, all you can tax is $15.92 and if you assume that he is a fellow who is not reinvesting it ---say a royalty owner who is just going to use it on his farm operation, he only has $10.31.

So the tax, combined with the other taxes add up to a situation where you don't really have much left to tax.

Can someone give us a calculation as to what that figure would be if you moved that tax up from 60 percent up to 75 percent?

Mr. Shapiro: It has been calculated, the breakdown.

The Chairman: If you could give us that figure --

We have a vote now, and we will come back at 3:00. Can you give us that figure before I leave here, please?

(Whereupon, at 12:00 noon the committee recessed, to reconvene at 3:00 this same day.)

\- - -

AFTERNOON SESSION

(3:15 p.m.)

The Chairman. The Senate Committee on Finance will come to order, please.

Did the Treasury finally compute the figure I asked them to compute, to show me how much revenue a person would have left? I would like to put it on the board, if you would.

Mr. Sunley. If you had a 70-percent tax --

The Chairman. You said it was 75 percent.

Mr. Sunley. Excuse me, a 75-percent tax, the 1031 number, that is to say, the producer, no re-investment, that number would be 585. The re-investment case would be $9.02.

I should explain what appears to be a paradox from the numbers. If you take the no re-investment case at the 50-percent tax, Eddie Cohen gave you the number at $11.05; in the 60-percent tax $10.31 - which looks like 75 cents less - and then you go up to a 75-percent rate, it falls all the way to $5.85. The reason for that paradox is then, in the 50-percent case that Mr. Cohen gave you, he assumed the Administration's original proposal which did not have an adjustment for State severance taxes, so that the windfall profits tax applied to the full $100 of revenue; whereas in the 60-percent case, Mr. Cohen assumed the House-passed bill, which is a higher nominal rate - 60 percent - that you get a deduction for the State severance taxes attributed to the windfall. So, the base of the tax, after a 12.5 percent State severance tax would be $87.50, rather than $100.

The 75-percent case we calculated similar to the 60-percent case, in that it assumes a 12.5 percent State severance tax which is deductible in determining the windfall profits tax base.

The Chairman. Well, what that really means, then, if you look at the cumulative tax with the 50-percent rate, if you take the other factors into account, it works out - federal plus State - to a 94 percent tax; right? Just in round figures. They are able to keep $5.85, so it is a 94-percent tax. Now, if he plows back everything he makes it does not take quite as much, but he is still paying 91 percent in taxes, and that leaves him only $9 to put back into the ground; that is, of the additional money.

Now, I assume that your revenue estimates are based on that they are going to produce the same amount of oil. Is that a fair assumption?

Mr. Sunley. No. With respect to newly discovered oil --

The Chairman. No, I am talking about the old oil to which the tax would apply.

Mr. Sunley. With respect to old oil, yes.

The Chairman. So, you are assuming that you are going to get the same amount of oil; right?

Now, I am here to tell you, that is not a safe assumption and I can show you reasons why. Let us assume that to get the best production out of your well, you have to keep working the well over, which you have to do periodically. Well, anybody who is thinking in terms of fact, surely, that 95-percent tax cannot go on forever. At some time between now and eternity you would think it would come to an end. Whatever is left down there, I will then be able to sell at the free market price, at some point in history.

Now, you would also be thinking, "I can take that same drilling rig and can put that to work developing a field with new oil, and I will be getting $22 a barrel or more. So, why should I put it over here where I am only getting $6, when I can work that rig getting $22 oil?"

It would seem to me that against those kinds of disincentives you would just have to lose some production. Now, how much is hard to say, but it seems to me you have to lose some. Do you think that is fair, or not?

Mr. Sunley. I do not disagree that there may be a production response here. I think the issue is always how large a response. I am saying either the Energy Department model, as you said before, or the revenue-estimating model that, as I understand it, the Joint Committee is using, has any built-in elasticity assumption that gets at that number.

So, I think compared to taxing new oil where we were able to build in an elasticity assumption, that the production response here has to be much smaller, and that is why it has not been taken into account.

The Chairman. Does the Joint Committee staff have a supply response built in, in that feature?

Mr. Shapiro. No, Senator. We essentially have the supply response built in for newly discovered oil. It does not take into account any of the elasticities that may apply with respect to the older oil, or the new oil.

Your point is well taken, however, that it may very well be the case that some of the producers will look at a higher rate and decide that they may want to wait until the first tier or the second tier is phased out, and they want to put their efforts to other areas. But, it is very difficult to make any determinations with respect to those elasticities, whether the judgment is correct.

Senator Chafee. Mr. Chairman, might I say something in connection with this?

I suppose that the best reply response of all would be if there was no tax of any kind. But we are working with the theory, the assumption, that the country should develop alternate sources to oil, and the way to get those is to spend ~~some~~ federal money which is going to come from this so-called windfall profits tax.

Now, I think it is important to note that first of all we are not working on a base of $6, but we are now in the upper tier and working with the $13 base at which oil is presently being produced, presumably at a profit.

Furthermore, there is the inflation factor that is not in these figures, I presume. This is the first year, where we are

4

at this moment, 1979. Is that correct, Mr. Sunley?

Mr. Sunley. The $100 potentially subject to the windfall profits tax is before a severance tax adjustment.

Senator Chafee. Yes, but you allowed something for inflation under this proposal.

Mr. Sunley. Yes. Over time the $13 base price is adjusted for inflation.

Senator Chafee. Again, Mr. Chairman, I have to get back to the point that we have given a whole host of incentives here - not just for conservation, but I mean exemptions, I should call them, for new oil, tertiary, incremental tertiary, for heavy and so forth. The question is, where do you draw the line?

My feeling is - particularly with the phase-out, and no one has discussed the phase-out. As you know, that is not in the House bill, it is not in the President's bill, and I think it is very important to get this thing over with, get out of the whole business.

Senator Dole. It is going to phase out anyway, in the House bill.

Senator Chafee. I do not know how you figure that.

Mr. Shapiro. The distinction is that in the House bill the upper tier phases into tier three, which means that the oil that is subject to tax in tier two between 1986 and 1990 is phased into the tier three tax, which means the base. Senator Chafee's amendment would phase it out completely in 1990, there would be no tax on that oil. It phases the tax out completely.

Senator Chafee. Under my bill, since we have already exempted the new oil, under my bill there would be no so-called "windfall profits" at all, on any oil; it is gone.

Mr.Lubick. Senator Chafee, we still have some tier three oil, I suppose. Presumably, it would not be logical if you are going to have a phase-out for tier two, not to have a phase-out in tier three. So, that probably should be taken into account in your revenue estimates.

Senator Chafee. Well, I do not know what tier three is. What is tier three?

Mr. Shapiro. Tier three is what the Administration proposed to be what covers everything other than old oil and new oil; it would be newly discovered oil, incremental tertiary.

Senator Chafee. We have taken care of newly discovered oil.

Mr. Shapiro. But now the tier three only applies to stripper oil. Now, there is a separate category for Alaskan oil.

Senator Chafee. We are going to deal with Alaskan separately tomorrow. Let us set that aside. But, on the stripper, I think all of it should go.

Mr. Shapiro. That is the point where we are going to suggest that if the committee were to agree to phase out the tax completely on tier two, and having the tax terminated or exempt by the committee on incremental tertiary annually discovered, it would appear that if the committee were to agree to phase out the tax entirely on this tier, that it may want to review Alaskan oil, whatever you decide tomorrow, if you do not exempt it all at a certain point except stripper oil. It does not appear that you would want to have one category subject to tax and all other categories being exempt at a certain time.

Senator Chafee. No. Each of us has our own ideas on Alaskan oil. There is considerable sentiment that Alaskan oil would go into this upper tier, and that would disappear, too.

Mr. Shapiro. As far as the revenue is concerned, whatever you do, if you phase out, when you finished this tier, you may want to review the stripper oil because that would be the only category of oil - putting aside Alaskan oil - that would still have a tax on it after the date that your phase-in - if it was agreed by the committee - would come into effect.

Senator Dole. We spent a lot of time on it yesterday, and it is really Senator Packwood's question, but I will ask it. What effect does raising the tax have on production? What is going to be your production response, or disincentive, if you continue to raise the tax? Do you have any figures on that, what the cost is of that?

Mr. Shapiro. Let me make an initial response and let DOE respond more specifically because they worked more on these energy supply models than we did.

It is clear that when you raise the tax you are going to have some effect. We cannot quantify as to what that would be. As far as our model is concerned for revenue effects, we have only a supply response with respect to newly-discovered oil. However, when you talk about a 50 or 60-percent rate, there is not that much difference in those rates that it would affect the model, that would affect the supply response to a great extent.

I must say, however, that when you get to a 75-percent rate I do think that the supply response there would have a much greater effect. It is not programmed into the computer to take that elasticity into effect.

Senator Dole. Right. We have been told that a 75-percent rate - at least we have been told by one company, and again, maybe they cannot be trusted because they are in the business - would reduce production in 1985 by 200,000 barrels per day, and recoverable reserves by 700 million barrels.

Mr. Shapiro. Maybe DOE should respond more specifically.

Senator Dole. Again, if we are talking about producing energy, then we ought to have not just "how high can we make the tax" but "what impact would it have on the response".

Mr. McGregor. Senator Dole, your question is addressed to Senator Chafee's amendment, which would increase the tier two rate from 60 to 75 percent.

Senator Dole. Any increase in tax.

Mr. McGregor. I believe the number that the individual company gave you does sound high. Given the fact, again, that the committee has provided for very good treatment, very beneficial

8

treatment for newly discovered oil and incremental tertiary oil, those two categories especially, the environment for a supply response has already been established. It is the market price that will be available in those two categories that will be the most attractive means for a resulting supply response.

Now, the tier two category, which Senator Chafee's amendment goes to, is existing production. It is either lower tier oil that is being released up to the upper tier bracket, or it is upper tier oil, or it is what we are calling "marginal oil" - and I understand there are some more amendments to extend the marginal definition.

Now, it is possible that, as those categories of oil, as the reserves which underlie those categories, mature, that the costs for producing oil from those reserves will increase. But they are already receiving a substantially high price.

Now, to the extent that the Chafee amendment cuts into revenues that might otherwise be available for sustaining production, especially in a secondary recovery area such as water flood, you might have some impact in terms of preventing abandonment. This gets to the point that Senator Heinz was making yesterday about stripper wells which go out at a low volume, something less than three barrels per day.

Senator Dole. Do you have any estimate?

Mr. McGregor. I would say the high range of our estimate that we are comfortable with is 50,000 barrels a day, in that range.

The low end would run negligible to 50,000 barrels a day.

Senator Dole. And yet, if we made the tax a hundred percent, it would not make any difference?

Mr. McGregor. Another way of saying it is that the tier two tax is primarily cutting into what is defined as windfall. If you moved it up to a hundred percent, certainly, the 50,000 barrel per day number would move up somewhat because at the margin there is always going to be an effect. But it gets back to the two arguments which cut against each other, which have been presented to the committee in all different versions. That is, is it market price that is your primary factor in determining supply response, or is it cash flow?

Senator Dole. If we are going to lose production, I guess we raise enough money to buy from the OPEC countries, if we make the tax high enough. We lose domestic production, but I guess as long as we are going to get enough tax money we can buy it from other countries, if that is what we are trying to do.

What is it going to cost us a barrel, to lose 50,000?

Mr. McGregor. Well, assuming the 50,000 is accurate - and I put it in the high range - the make-up is going to depend on what the world oil price is at a given time. I understand the Joint Committee staff has been using a real-world oil price of $22 with a one-percent price increase, real price increase. So, you just extrapolate out from there, if indeed that 50,000 barrels holds up.

Senator Wallop. I wonder if you read the paper this morning.

Mr. McGregor. Unfortunately, I have not had the opportunity to read a paper today.

Senator Wallop. Well, just for the information of the Department of Energy, in case somebody over there overlooked it, the Iranians have talked about raising the price of non-contract oil to $36; and either the Lybians or Algerians talk about reducing their contract oil and raising the price to $32 or $33.

The problem I think you have not addressed, Mr. McGregor, in the supply response figures, is the necessity for raising capital, having money enough to sustain the exploration. Now, with a 91-percent tax, which is what this demonstrates --

The Chairman. 91 percent, providing you put it all back in the ground.

Senator Wallop. That is what I mean.

The Chairman. If you are not going to put it all back in the ground, it is 94 percent.

Senator Wallop. That is what I mean. I wonder how the Department of Energy squares that with no supply response. I mean, if all you have left is $9.02, if you put everything back in the ground, there has to be a supply response in terms of new oil, I do not care how disengaged it is from the rest of the tax. There simply has to be a supply response. The world, and this country in particular, is dramatically capital short right now.

The kinds of things we are going into in other parts of the energy field, the environmental requirements and other things, are a tremendous strain on capital. Where do you suppose these people are going to get the capital?

Mr. McGregor. Senator Wallop, the tier two oil that we are talking about, the large majority of that oil, is what is also known as upper tier oil. That is oil that has been brought into production on or after the end of 1972.

Mr. Wallop. I know that.

Mr. McGregor. The prices which have been allowed by statute and by administrative action implementing that statute, are currently in the range of about $13 a barrel. That has been quite sufficient to sustain upper tier production.

Senator Wallop. Yes, but you are missing the point, I think. The point is that you can sustain production for as long as you get anything at all out of it. That does not do anything about replacing production. That is the point that people are trying to make here, that you have to have something to spend to get the rest of it. You cannot just pull that financial reserve out of the sky to drill new wells.

You are taking it from that. You have to have a supply response that is greater than the Department of Energy is willing to admit, simply because of the lack of capital.

Senator Danforth. Mr. Chairman?

The Chairman. Senator Danforth.

Senator Danforth. Could I ask Mike Stern, or whoever did this, on this chart, what is that second line? I do not understand the second line of that chart.

Mr. Stern. The line which says "State"?

Senator Danforth? Yes. What is that?

Mr. Shapiro. Those are the State taxes. It may be the severance tax, or the income tax; whatever the State portion of the tax that is,imposed on that $100, is included in that line.

Senator Danforth. So that what the meaning of this chart in part is, that as a result of decontrol for every extra $100 the producer gets, the State gets over $13 of that?

Mr. Shapiro. We are talking about $100 of so-called windfall profit.

Sentor Danforth. Yes.

Mr. Shapiro. Of that $100 the State would get $13, and that would cover either or both, a severance tax or an income tax. Some States have both.

Senator Danforth. Is that just tax income of the States, or does that include royalty as well?

Mr. Shapiro. We are talking about the taxes that the State imposes on that $100.

Senator Danforth. The tax that the State imposes. Now, what States impose those taxes? Are those taxes imposed by Missouri?

Mr. Shapiro. All States that produce oil,..have oil in their

States, have severance taxes in the range up to 12.5 percent. That is imposed on all oil taken out of the ground. There is a 12.5 severance tax at the wellhead.

Senator Danforth. So, States which are fortunate enough to have oil will have their State income increased by roughly $13, a little more than $13 for every $100 increase in price; is that right?

Mr. Shapiro. That is correct. Now, it is either made up of severance taxes or income taxes.

Senator Danforth. Severance or income.

Mr. Shapiro. Most of the States will have both. Severance is a larger share, in most cases.

Senator Danforth. Now, what are those funds used for? Are they used for general purposes of the State?

Mr. Shapiro. In some cases the severance tax may be dedicated for certain purposes, but I think in most cases, however, it is just used for general purposes, as all revenues would be.

Senator Danforth. Now, yesterday, when we were talking about whether or not the windfall tax should be applied to State governments, that did not have anything to do with line two; is that not correct?

Mr. Shapiro. That is correct. What we were talking about yesterday, where the State owns the land and is getting royalty income. That was a different issue than this.

Senator Danforth. So, as a result of decontrol, States that have oil are going to have two sources of increased revenues for their States. One is the State tax on oil that is owned by somebody else; and the other is when the State or local government, political subdivisions of the State, own oil themselves, they themselves will be making money. Right?

Mr. Shapiro. That is correct.

Senator Danforth. Do you know the total amount of increased revenue to the States by virtue of decontrol, both from increased tax proceeds and from increased income from oil?

Mr. Shapiro. We have an estimate we may be able to give you; Jim is trying to find that now.

Senator Danforth. While you are looking for that, let me just ask this: Is there any supply response particularly from this money, whatever it is?

Mr. Shapiro. Let me give you the figure. I think DOE would have to give you the supply response. I am using a figure that the Treasury has. They say that before the windfall profits tax, in the years 1979 through 1990 - which is an eleven-year period - you would have royalty income of $13.9 billion, and the income and severance tax income is $50.4 billion for a total of $64.3 billion. That is before any windfall profits tax. So, that are the additional revenues that the Treasury has computed with regard to the State and local receipts as a result of decontrol.

If you impose a windfall profits tax, if that is imposed, these figures are reduced from $64.3 down to $59.7 billion.

Senator Danforth. So, what you have here is basically a transfer of wealth - not just to oil companies, or not just to the Federal Government as Senator Gravel was talking about today - you have a transfer of wealth over a ten-year period of time from the American people to a few States, a few lucky States, in the amount of $64.3 billion, or $59.7 - call it a $60 billion transfer of wealth.

I do not want to horn in because you have the floor, but I just noticed that second line up there. If I recall the proposal that I made yesterday, it had to do with whether or not we could increase the revenues for the Federal Government by a mere $6.5 billion, which would be a little more than ten percent of the amount by which these particular States are going to realize this increase in revenue.

I might say that this increase in revenue dwarfs federal revenue sharing, it dwarfs it.

The Chairman. Might I just comment on that? I see a lot of up-side-down thinking, and that is about the ultimate of up-side-down thinking in my judgment.

Now, let us just analyze that for a moment. Here the State government has a severance tax on its natural resources. That is an irreplaceable resource that you have. It would be just like State land, when it is gone, it is gone. So, you have a resource there. You say, "Well, now, when you come and severe our resources and haul them away from here, I do not care whether you are from inside the State or outside the State, you owe us a tax of 12.5 percent." That is looked upon as part of the State's resources. When you haul it away, you have to pay us something to come take our resource and use it for whatever purpose you want it.

The Federal Government comes in with price controls, and by using price controls it holds the price down, and that holds down the State's revenue just like it holds down the producer price and everything else. With price control you say, "All right, let us reduce the revenue the State would otherwise have." The State is not raising its tax, it has been there all the time.

So, now all of a sudden they want to say it is unjust enrichment when finally our price controls will not work any more. The damned fool things just do not work. We are not getting production. You have taken all the incentive out. You have put a 94-percent tax on any additional income someone gets, and you are not getting production.

So, if you want to get anywhere, you are going to have to face the fact that the price will have to go up, and we will have to pay more for a product. You are going to let the free market system begin to operate again. When you do that, what happens?

Well, the Federal Government picks up $76.56 with an additional tax up there. Now, we have not put the "add-on" there for the 75-percent rate, which would take it up to about $80. The State by its tax, which has been there all the time on the severing of its resource, makes the price that it gets in a free market. So, by virtue of the fact that you deny the State the opportunity to sell its resources for what everybody else on God's green earth gets, you now say the States are robbing you because they are now getting what they would have had all the time.

Now, I must say that is just getting pretty ridiculous to complain at all about a transfer of wealth because the State collects a tax that has been there all the time.

Now, maybe you can repeal the State's taxing power, and I welcome you to try it.

Senator Danforth. Well, Mr. Chairman, there is no doubt, though, that as a result of decontrol we are hoping to improve the situation of the American people by increasing their sources of energy. In doing so, we are going to impose real hardships on people. People are going to be paying more for energy as a result of that. There is no doubt that when you do something like that, there are going to be some winners and some losers.

All I am doing is to point out that some of the biggest winners are some of the States. I do not happen to represent one of those States. Somehow, I am going to have to go back to my people in Missouri and say, "Folks, I did away with your Amtrak", I mean, they know that.

(Laughter.)

Senator Danforth. "Let me tell you what else I have done for you: I have just bought new limousines for the Governor of

Louisiana and for the Governor of Texas." I do not know how to explain that.

The Chairman. Why not go back and explain to them that you have tried to tax Louisiana, you have tried to tax the State government itself. You have tried to remove the State's taxing power. You tried all that, and it did not work. Now, if you got the votes, it did work. Of course, we will see you in court if it does.

(Laughter.)

The Chairman. In any event, you had your chance.

Senator Bentsèn. Mr. Chairman, I see I have been well represented in my absence. Thank you very much.

(Laughter.)

Senator Gravel. Mr. Chairman, the unfortunate part is, that approach is "beggar thy neighbor".

Senator Danforth. Is what?

Senator Gravel. "Beggar thy neighbor". That is, everybody else can go to hell, and you are going to take care of your people, that is really what it means.

Senator Danforth. I have heard that around here for a long time.

Senator Gravel. Oh, yes, there is no question. If it can be done, it will be done, and we are going to dismember this country on a regional basis. That is going to be very tragic. I think the legitimate person in an arid State could then say, "Well, if the price of wheat is going up and the companies that refine that wheat, or the companies that own the large lands, the agribusiness that is doing that,they are making a lot of money as the price goes up." I might tell you, since 1946, when we had control over it, the American Oil Cartel had control over it, it was below the price of food.

But, be that as it may. Manufactured products in other States when their price goes up and the State collects income taxes because those companies are doing well on the rest of the nation, then of course if the rest of the nation has the numbers, they can gang up on you and put onerous taxes on you to impair your ability to act efficiently in your industrial capacity.

Now, we have not done this by and large in this country. We have had wage and price controls across the board for everybody. When we took them off in 1973, we left them on for energy. That is the part of this country that is in bad shape.

Now, you can tell the people - and I want to see that because I am going to suggest one thing. I hope that you bring forth right now, or in the reasonable future, for this bill the tax cut that you want to see happen because I think we want to focus on that situation where we are going to have a tax cut and give money to all those people out there, the consumers; and we are going to have that tax cut at the expense of the most vital industry in this country. I think we want to vote on that, we want to get a good balance on that because there have been two windfalls. There has been a windfall for the Federal Government, and over the ten-year period that is in the order of $274 billion. I would like to know how we are going to spend that. I am prepared to spend it all, if you want to spend it all.

But when some of us are here saying, "Well, let us at least spend that before you go and get a windfall right from the industry which is going to supply your farmers and your people in your State with energy." If the American energy industry cannot do it, then your people will have to buy it from the Middle East. They are not going to be happy with the price.

Senator Danforth. I am not talking about the industry, I am talking about State governments who, for nothing in return, are going to get $60 billion out of the pockets of people all over this country.

Senator Gravel. No, not nothing in return.

As Senator Long has pointed out, these are assets that we own as a State. Now, you have some assets in your State, and you covet them just as much as we covet ours. There is nothing wrong in that.

The Chairman. Might I see if I can get back to the point. Right now we are not voting on the Danforth amendment, we are trying to talk about the Chafee amendment. The Chafee amendment does not have anything to do with what the State gets; the Chafee amendment has to do with what the producer gets. As far as I am concerned, I am ready to vote on it.

Senator Chafee. I am ready to vote, Mr. Chairman. I propose that we provide a 75-percent tax on upper tier oil with, starting in January, 1991, a two-percent per month decline, so that all upper tier oil taxes are phased out completely by January 1, 1995. That will produce us $9.45 billion above the House bill.

Mr. Chairman, I will say that if that Dole amendment had not passed yesterday, I would have had this with a phase-in starting on January 1, 1986, and phasing out on January 1, 1990. But to make the seven-point-odd fit in, I am having the phase-out starting on January 1, 1991.

I would remind everybody that this committee so far has exempted new oil; exempted heavy oil; exempted incremental tertiary; has given special treatment to small producers of stripper oil. The only thing we have done on the cost side is put a $1 billion additional revenue as a result of the 75-percent tax on lower tier. I move the amendment.

Senator Dole. Mr. Chairman?

The Chairman. Senator Dole.

Senator Dole. Does the Treasury support the phase-out?

Mr. Lubick. We are opposed to the phase-out, Senator Dole.

Senator Dole. I think we ought to vote separately on them, then. I would not want the Administration to have confusion. So, I would suggest that we divide the amendment and vote first on the phase-out.

Senator Bentsen. I would like to know also how they stand on the 75 percent. I know the Administration's position originally was 50 percent. Where are they on this one?

Mr. Lubick. Our preference, Senator Bentsen, was for the tax as we proposed it, which was at a lower rate. We regret that the committee has made a number of decisions which will make it more difficult to finance those things that we think have to be financed. We would like to see the committee come out with a bill that produces more revenue, however, consistent with maintaining supply.

So, while we are not enthusiastic, we think the objective of getting more revenue is a desirable objective.

Senator Bentsen. But you also said, consistent with getting more supply. That is pretty tough to accomplish.

The Chairman. When does this phase-out start?

Senator Chafee. In 1991.

The Chairman. A man could discover a well and be completely depleted between now and 1991. It seems to me as though to start a phase-out in 1991, you might as well forget about it.

Mr. Lubick. This is upper-tier production, Mr. Chairman.

Senator Chafee. Discovered now, with no tax.

The Chairman. But a phase-out in 1991, it seems to me you might just leave people with the hope, rather than to say you start phasing out in 1991. I personally do not see any point in voting on a phase-out that far along.

Senator Boren. The change in the Senate raises $9.4 billion;

is that correct?

Senator Chafee. That is correct. The bottom line on that sheet we handed out.

Senator Boren. And what does the phase-out cost. Of course if we begin in 1991, it has no impact through 1990. What would it be normally? What if you began in 1986?

Senator Chafee. I did not understand the question.

Senator Boren. What would be the revenue impact of the phase-out if it began in 1986?

Senator Chafee. Bob?

Mr. Shapiro. Clearly, the revenues we are using are between 1980 and 1990. So, during that period, of course, since the phase-out does not begin until after that --

Senator Boren. Suppose the phase-out was from '86 to '90?

Mr. Shapiro. From 1986 to '90, the phase-out would have in effect plus $3.3 billion; which means that you pick up money because of the 75-percent rate between 1980 and 1985. But, when you start the phase-out, you start losing money.

Senator. Boren. No, I am sorry. If the rate were kept at 60 percent and you had a phase-out from 1986 to '90; what would the effect be? If the rate were kept at 60 percent, as it is in the House-passed bill, what would the effect be?

Mr. Shapiro. I think I can roughly say that the phase-out would cost approximately $6 billion.

Senator Boren. The phase-out would cost $6 billion?

Mr. Shapiro. Six billion dollars. That is looking at 1986 to 1991. Once you vary the years you come to different quantities of oil, and it would have a different effect.

But for your purpose, if you were to start it in 1986, it would have an effect of $6 billion.

Mr. Boren. Six billion dollars would be the cost of the phase-out by itself. If you granted it from '86 to '90, you would make no change in rate.

Mr. Shapiro. I should point out that then the committee would probably want to look at the effects on stripper oil and whatever you may do with Alaskan. -

Senator Borden. That would reduce the costs; would it not?

Mr. Shapiro. It would not reduce it, it just means that you have another category of oil. Stripper, for example, would be the only oil subject to tax, depending what you do with Alaska. You would have that, would have a permanent tax where everything else would be exempted or in the process of being phased out.

Senator Boren. Mr. Chairman, I wonder if it would be in order to offer - not with the thought of trying to cut off a vote on all those alternatives, but to offer another alternative as an amendment, perhaps, to the Chafee proposal, to phase out between January, 1986 and 1990, keeping the rate at 60 percent, as it is in the House-passed bill.

Senator Chafee. Well, can you not hold that? You will get your chance, depending on how this comes along.

Senator Dole. Mr. Chairman?

The Chairman. Yes, Senator Dole?

Senator Dole. Say, the Chafee amendment should pass, you can still offer another amendment, as I understand the parliamentary procedure. Is that right?

Senator Boren. I could offer an amendment to the Chafee amendment, then?

Mr. Stern. It has the precedent in this committee that you can offer an amendment even if it is inconsistent. Any Senator can offer an amendment.

(Laughter.)

Senator Dole. I do not want to break precedent.

Senator Boren. I will be glad to withhold mine.

The Chairman. The way we have done business here - and I think it is the best way of doing business - we try to abide by what the committee wants to do. We try to keep anybody from being cut off by parliamentary maneuver. Anything we agree to can be reconsidered. So, if Mr. Chafee's motion carries and is agreed to, someone can come along and offer an amendment to make it more or make it less; or reconsider. By doing that, we make better headway because people feel contend and vote because if they think they made a mistake, they can always change it later on.

Senator Dole. Along that line - maybe Senator Boren has another amendment - it seems to me to accomodate both the desire that Senator Chafee has, in the event his amendment succeeds, I will offer an amendment to make the tax rate 70 percent for major companies and 50 percent for independents, which would still increase the revenue by $4 billion. I think that addresses the question in a little different way and still produces additional revenue.

Senator Wallop. Good.

Senator Bentsen. Mr. Chairman, if I can just comment for a minute here. I think the response of Secretary Lubick on that was one that was the response of a lot of members here. He talked of wanting to raise the additional revenue, and he was very careful to say, "We still want the supply". That troubles us because there obviously is a supply response problem.

Now, these reservoirs do not just continue to service themselves without additional revenues being put into them. That means that if you cut this down, you put the market incentive on one side, and you turn around, taking it away from them on the other side, that means, that cuts substantially back on the cash flow for the reinvestment, for development, and keeping the reservoir going.

So, I understand Secretary Lubick's response to that. He is obviously troubled by the question of diminishing returns if you go too high on your tax. I think that is where you are.

The Chairman. Well, let us call the roll on the Chafee amendment.

Senator Dole. Is this on the whole amendment?

Mr. Stern. This is both a 75 percent rate and a phase-out between 1991 and 1995.

The Chairman. I think we ought to divide the amendment. I would like to ask for division. I would suggest we vote on the 75 percent. Or, if you want to vote on the phase-out, we can vote on that first, either way.

Senator Chafee. Mr. Chairman, I would prefer if we could go with it as proposed. Then, if people subsequently want to tamper with it, why, obviously that is everybody's privilege. It seems to me there is a phase-out here, and that is an important part. I would be put in a quandary here myself. Suppose we voted on the phase-out first. I would not personally vote for the phase-out if we did not have the tax. If I could, I would rather have it as proposed.

Senator Dole. I think the only point there, the Administration is opposed to a phase-out; the House is opposed to a phase-out. There is probably not going to be a phase-out. What we are going to end up doing is increasing taxes because the House would certainly recede and let us increase the tax to 75 percent. We would be stuck with a higher tax and no phase-out.

The Chairman. I really think that anybody has the right to insist on a division, that is how the Senate Rules read. But, I will not insist on it at this point if you want to vote on the whole thi..g, it does not make that much difference to me. So, why not call the roll, then?

Mr. Stern. Mr. Talmadge?

Senator Talmadge. No.

Mr. Stern. Mr. Ribicoff?

Senator Bradley. Aye by proxy.

Mr. Stern. Mr. Byrd?

Senator Byrd. No.

Mr. Stern. Mr. Nelson?

Senator Nelson. Aye.

Mr. Stern. Mr. Gravel?

Senator Gravel. No.

Mr. Stern. Mr. Bentsen?

Senator Bentsen. No.

Mr. Stern. Mr. Matsunaga?

The Chairman. No, there is a proxy here.

Mr. Stern. Mr. Moynihan?

Senator Bradley. Aye by proxy.

Mr. Stern. Mr. Baucus, Mr. Boren, Mr. Bradley?

Senator Bradley. Aye.

Mr. Stern. Mr. Dole?

Senator Dole. No.

Mr. Stern. Mr. Packwood?

Senator Packwood. Aye.

Mr. Stern. Mr. Roth?

Senator Roth. Aye.

Mr. Stern. Mr. Danforth?

Senator Danforth. Ahe.

Mr. Stern. Mr. Chafee?

Senator Chafee. Aye.

Mr. Stern. Mr. Heinz, Mr. Wallop?

Senator Wallop. No.

Mr. Stern. Mr. Duerenberger?

Senator Duerenberger. Aye.

Mr. Stern. Mr. Chairman?

The Chairman. No.

Well, the ayes are nine, and the nays are nine. Mr. Baucus is not here, and Mr. Heinz is absent. So, it failed. As of now it has failed on a tie vote.

Senator Gravel. Mr. Chairman, could I pursue a question with Mr. Lubick?

Mr. Lubick, you have stated that the government is trying to produce additional revenue. What are the plans for this revenue that comes from the increase in taxes from the deregulation.

That money, that $275 billion, or $174 billion, what is going to happen to that?

Mr. Lubick. Well, Senator Gravel, we have pointed out that those are gross figures, there are corresponding offsets in the economy, reduced income tax revenues from sources other than the producers. So, there are very substantial offsets to those figures. So, we do not have that money to spend.

Senator Gravel. I do not particularly understand the offset. What do you mean?

Mr. Lubick. Well, just as increased prices of petroleum and petroleum products represent increased income to suppliers, that results in increased costs to the rest of the economy.

Senator Gravel. Well, we are taxing them profits, are we not?

Mr. Lubick. That is correct.

Senator Gravel. Supposing a tractor company in Minneapolis has to pay more for its fuel for the tractor, they are still going to try and make the profit they were making as a company before. So, you should not get much of a shortfall there, should you?

Mr. Lubick. No. There is a shortfall in that there is, first of all, less money available for the users, the consumers of these products to spend on other things. That has its effects on the economy in reducing income.

The cost itself is a deductible item, reducing proceeds. I think we have gone into this in rather great detail, and a lot of it turns on various assumptions as to what monetary policy is and what the effect of inflation is. But it is perfectly clear that there are very substantial offsets and that we do not have those revenues available.

Senator Gravel. If we have a four percent increase in price per year, and you have an income of $274 billion, and you are talking about offsets, what is going to be the net in the Federal

Treasury of money to spend?

Mr. Lubick. Well, it turns on various assumptions, and I am going to let Mr. Sunley run through the chart, which I believe you have in front of you. It was prepared by the Joint Committee, it is their Table 3. There are three different assumptions set forth. They are matters of economics.

Senator Gravel. Is that the one of September 5?

Mr. Lubick. Yes, it is.

Senator Gravel. I do not see the offsets.

Mr. Sunley. Senator Gravel, there are three banks in that table. The $274 billion is the first number in the upper right-hand column. That was the amount of increased income taxes on the oil industry that you would get from decontrol.

But you will notice, when you get to the second bank, they assume under the Joint Committee analysis that Federal spending will go up $104 billion. So, it is a net impact on the deficit from decontrol of only $171 billion.

At the bottom section of the table they assume that the impact of spending more money for oil is that we have less money spent on other products, less income of other sectors of the economy, and these other sectors of the economy will pay $166 billion less in income taxes. So, the net increase in income taxes under those assumptions is $108 billion.

Senator Gravel. That we will have.

Mr. Sunley. That is under the four percent real growth assumption. I think the conclusion we reached the day we went over this table was, how much additional revenue you get from decontrol depends crucially on the assumptions that you want to make. It takes a fairly extreme set of assumptions, however, to reach the conclusion that you get the whole $274 billion. In other words, the increased taxes paid by the oil industry are not offset by either lower taxes paid by other sectors of the economy, or increased government spending somewhere in the economy.

Senator Gravel. So, what we are saying is, we may receive just in straight-out revenues, without doing a thing, somewhere between $100 and $200 billion.

Mr. Sunley. Yes. The Administration, in structuring its initial program, if you recall, puts the whole gross tax into the trust fund, and we essentially spend the whole gross tax. When we look at the windfall profits tax itself, the net increase in revenue to the windfall profits tax is obviously less than the gross. In effect, we spend not only the net windfall profits tax in the Administration's proposal, but something more. That something more is in fact financed, or covered by the net increase in revenue from decontrol, net increase in income tax receipts from decontrol.

So, we think there is a significant amount of revenue that comes from decontrol. I think the Joint Committee would agree with me. I guess the question is how much additional revenue there is.

Senator Gravel. Is it safe to say that it is somewhere between $100 and $200 billion?

Mr. Sunley. As I said, you get a minimum of $108 billion if you assume that the real growth in oil prices in the future is going to be four percent a year, compounded.

Senator Gravel. Has the performance been that in the last five years?

Mr. Sunley. No. I think if you take 1973 to 1979, there was a decline in the real price of oil. Obviously, this year there has been a 60 percent increase.

Senator Gravel. Then again the straight-out question, can we expect less than $100 billion? $100 billion? $150 billion? As I read the scenarios, we would be getting somewhere between $100 and $150 billion.

Mr. Sunley. I think I would want to be fairly prudent here and assume a lower real growth rate. As far as being committing Federal spending on various programs, either direct or tax credits for a ten-year period, I would want to make certain in my assumptions of how much revenue we are going to have on the conservative side to be prudent.

Senator Gravel. Well, when we sit here and you cannot even give us a proper supply response for what happens with oil, something we are very familiar with; and we throw figures out as to what solar is going to bring, and what is shale is going to bring -- for some reason you get awfully precise when it serves your argument. But then, when we are talking about what the revenue is going to be you are very imprecise and are not sure.

Mr. Sunley. Senator Gravel, I think from the very beginning we have said on revenues that how much revenue you receive is very sensitive to what the basic price of oil is, and what you expect the future increases in that price to be.

I think there is no way that any of us can be certain of what that answer is. I mean, the Administration in every news release, or Presidential statement, has always included using at least two assumptions, and sometimes three assumptions in terms of what the future price will be, to show that there is uncertainty. In fact, that you are dealing with a fairly wide range of possible outcomes.

I do not think there is any way I can reduce that uncertainty. I will not come before the committee, nor will the Administration, and say that the answer is that there will be no real price increases; or that there will be only one percent real; or that there will be four percent real.

Senator Gravel. Thank you, Mr. Chairman.

Senator Wallop. Mr. Chairman, if the committee wishes, I would like to bring up tribal exemptions at this time again. We had a fair discussion on it yesterday.

The Chairman. What is that?

Senator Wallop. The Indian tribe exemptions.

The Chairman. Go ahead.

Senator Wallop. I would like to point out, there is a telegram which I could read, from the Western Governors' Association, on the point. But basically, for those that are worried that this is the kind of exemption as the charitable exemption in 501(b)(3), I just point out that it is not.

These are tribal properties. I think Mr. Lubick will agree later on when I ask him that the case I cited to him yesterday probably makes such an amendment unnecessary; but the Indian people and their lawyers are unwilling to have to prove that they do not have to pay a tax when there has been a Supreme Court decision that it is unnecessary for them.

The total cost in terms of the bill is $328 million over the ten-year period. I point out again that the average tribal income is something like $1,900 a year. The tribe uses this revenue to develop other kinds of things which relieve the pressure on the budget in terms of appropriations for the Bureau of Indian Affairs, and a number of extraordinary programs that the country indulges in.

I would be happy to answer questions of any members, but I would ask Mr. Lubick if he agrees with that court test I referred to yesterday, that it would probably mean that they would be exempt from the tax anyway; but they would have to prove it in the absence of a clear exception.

Mr. Lubick. The case cited by Senator Wallop was decided by the Supreme Court, and it dealt with whether the sale on behalf of a protected Indian subject to this trusteed land would be subject to the capital gains tax imposed by the general income tax statute.

The Supreme Court held that in spite of the provision of the Income Tax taxing all gains generally, the allotment act dealing with Indian lands which said that these particular trusteed lands would be free from all charge or incumbrance whatsoever, which was enacted before the income tax, and was not superseded by the income tax.

So, it would appear under this decision that we would urge the committee to do the opposite of what Senator Wallop suggests, namely, to specifically impose tax in this case because otherwise it appears to us under the House bill, having read this opinion, that it is very likely that as the bill has come over to you from the House, that this exemption he is seeking is already there and that unless you positively enact taxation in this case, we are not going to get it.

Senator Packwood. Don, your conclusion is, though, that was a statutory interpretation out of the Constitution or a treaty?

Mr. Lubick. Yes, this is a question of statutory interpretation by the Supreme Court.

Senator Wallop. My point is, this $328 million is not worth us getting into the business of challenging negotiated tribal rights. These are, after all, treaty rights, these Indian properties. It is different than the 501(1)(c) charitable organizations, which is troubling people. I would just point out, the Western Governors say, "The proposed rulings would tax tribes at a higher rate than oil producers because tribes are not able to take advantage of various deductions allowable to oil companies under the act. Generated revenues affected by the exemption of Indian tribes would be less than one-tenth of one percent of the anticipated revenue."

Finally, the tribes depend exclusively on their Indian resource royalties in order to pay for essential social services for their people.

I think it is in the interest of the committee and the country not to get involved in that fight for this minuscule amount of money that is involved.

Senator Bentsen. Mr. Chairman, on a procedural point. I would like, when we get these things distributed to us and we get so many of them - and I have been guilty of this, too - that a name be put on the top, so I know whose bias I am dealing with.

Senator Wallop. I apologize.

Senator Bentsen. But whether it is Treasury, or any one of us individuals, I think it would be helpful if we had a name at the top. I have been guilty of that many times.

Sentor Wallop. I apologize, that is my fault. The memo was prepared by a Law Firm called Wilkinson, Cragun & Barker at our request.

Senator Bentsen. I just want to know if this is something you put your name to.

Senator Wallop. Yes, sir; I would.

The Chairman. You called for a vote. All in favor say aye.

(Chorus of ayes.)

Senator Gravel. Now that I voted, are my Alaskan Indians included? Aye.

The Chairman. Do you want a roll-call?

Senator Wallop. Yes.

Mr. Stern. Mr. Talmadge?

Senator Talmadge. Aye.

Mr. Stern. Mr. Ribicoff,Mr. Byrd, Mr. Nelson?

Senator Nelson. Aye.

Mr. Stern. Mr. Gravel?

Senator Gravel. Aye.

Mr. Stern. Mr. Bentsen?

Senator Bentsen. Aye.

Mr. Stern. Mr. Matsunage, Mr. Moinyhan, Mr. Baucus?

Senator Wallop. Aye by proxy.

Mr. Stern. Mr. Boren?

Senator Boren. Aye.

Mr. Stern. Mr. Bradley?

Senator Boren. Aye by proxy.

Mr. Stern. Mr. Dole?

Senator Dole. Aye.

Mr. Stern. Mr. Packwood?

Senator Packwood. No.

Mr. Stern. Mr. Roth?

Senator Roth. No.

Mr. Stern. Mr. Danforth, Mr. Chafee?

Senator Chafee. No.

Mr. Stern. Mr. Heinz, Mr. Wallop?

Senator Wallop. Aye.

Mr. Stern. Mr. Duerenberger?

Senator Duerenberger. Aye.

Mr. Stern. Mr. Chairman?

The Chairman. Aye.

The ayes are eleven, and the noes are three. The amendment is agreed to.

Senator Boren. Mr. Chairman?

The Chairman. Yes, sir.

Senator Boren. I have a very small amendment that may perhaps be in order at this time. I will say at the outset, by way of introduction, that the revenue figures attached to this amendment are roughly one-half of one percent of the amendment that I proposed yesterday, just to put people at ease.

(Laughter.)

Senator Boren. This amendment, this proposal would state that the definition of marginal properties, marginal wells which now receive a tier two treatment under the House-passed bill, would be expanded. The definition of "marginal well" to be expanded to include what we would call high-water cut wells. That is wells which produce at least a ratio of nine barrels of water for every barrel of oil.

Now, this is not an exemption, it is not asking for an outright exemption for this kind of property, it simply would include it in the definition of marginal production. The Administration has already recognized that high-cost production, special high-cost production should receive special treatment.

Now, the cost figures on this are roughly, over the ten-year period from 1980 to 1990, somewhere between $200 million and probably $275 million total - roughly $20 million a year. That is the estimate. Now, there are some low and high ranges. I think it is based on an estimate of there being between 250,000 barrels to 350,000 barrels per day of production, which is old oil. In other words, tier one, which would be moved to tier two, which is the treatment that marginal receives.

Just to give you an example of how this works - and by the way, the estimate of the increased production over the House bill, the only figure I have is a figure from Professor Erickson at North Carolina State, and it is based upon figures provided to him by the industry in terms of their own production experience, is 11,000 barrels a day additional production. So, you are in about a $14 range, to change it.

Now, let me give you one example how this works. I have pulled the actual facts on one field that I know of in Oklahoma, the North Antioch Oil Creek Unit. This is a unit where there are nine producing wells. Those nine wells, every day, produce

350 barrels of oil and 9,133 barrels of salt water. That water has to be recycled back into the ground. They are using pressure, they are putting water down into the ground to force oil up - very old fields. That has to be recycled, which greatly increases the costs.

The company which operates that particular field, which is the Coastal States Corporation of Houston, says that if they continue to get the tier one price on that particular property - and it is a good example - that they estimate they will be able to produce 550,000 more barrels of oil from that particular field. However, at a tier two price, which is the price marginal wells get, they estimate from that particular field they would produce 1,200,000 more barrels.

Their profit margin is so small that they simply cannot afford to produce those other barrels at the lower price because of the great water production. This is a very small percentage of total production in the country, but I think it is important in terms of encouraging water flood, and it fits the marginal definition. As you know, the idea behind a marginal well is, you might have a well that is producing much more than ten barrels a day but still because of its depth of high operating costs it is only marginally profitable.

So, the same principle in some ways applies, as applies to strippers, an economic definition, you might say.

So, I would be happy to yield to any questions on it.

Senator Bentsen. If I might, Senator, I would like to cosponsor it. This is what happens in the secondary stage of recovery projects. Once your wells get nine to one water to oil ratio, they get uneconomic awfully fast.

What it means is, you squeeze a little more oil out of some of the old reservoirs and preserve them long enough to carry them through, hopefully, to tertiary recovery. That is what it does.

Senator Gravel. Mr. Chairman, I would like to add my name, also because although most of ours is new oil, recent reports and briefings I have had are that Prudeau Bay is some day going to be at that point, maybe, depending on what we do here, five years from now, ten years from now, or twenty years from now.

The Chairman. Is there further discussion? Mr. Lubick?

Mr. Lubick. Mr. Chairman, I looked into this, and our problem is - as a matter of fact, I understand the DOE considered this problem when it was trying to establish its definition of "marginal" that administratively it is just going to be something that we just cannot handle. Unless we are standing there all the time with our cups, measuring the nine to one, it is just going to be almost impossible for us to administer this type of provision.

So, we would urge you not to support the amendment.

Senator Bentsen. I would say this is also something, Mr. Chairman, it would be very difficult to play games with. If you started changing your ratios of water and oil substantially, you would have serious problems in your reservoir.

Senator Boren. That is correct, and I am a little surprised at Mr. Lubick's comment because I understand the DOE objection is not that strong to it. I would like to ask them for a comment. They do monitor by property right now. They are going to have the same problem with marginal wells, which they have already recognized themselves and put in the definition. I am not changing any of that, just like this property. This is a property like the North Antioch Creek field. It is a fact that they get 350 barrels of oil and 9,133 barrels of water. It is pretty easy monitoring that, to determine that there is no hanky-panky, by looking at it by property unit.

Senator Dole. You want to move it to tier two.

Senator Boren. It is not an exemption. I am talking about expanding it as a minute expansion in terms of numbers of the definition of "marginal wells". It seems to me it is economically justifiable.

The Chairman. What is the DOE's view about that?

Mr. McGregor. If I perhaps could provide some background on previous DOE positions on a water-cut type of marginal amendment. Proposals we have seen in the past have been in the range of an 80-percent cut, 85-percent cut, which is substantially less than a 90-percent cut. 80 percent is more like four to one, rather than nine to one. I think the marginal economics, once again, as Senator Bentsen has pointed out, of keeping those fields and wells in production until incremental tertiary can be installed, has some merit in providing the economic incentive for doing that.

However, as Mr. Lubick has so accurately pointed out, there is a very substantial administrative burden involved with measuring water cut from a given well. I am told that individual wells are not metered, that the water cut metering actually occurs on a field basis.

In addition, in the past there has been no water-cut type of incentive, and certainly the record-keeping in the past has just not existed in terms of a producer or purchaser being able to say, "Well, this particular barrel of oil came out with so many barrels of water."

And, Mr. Chairman, I have to go back to your point yesterday about how severe or how high is that administrative cost, if you want to put some very detailed and difficult to comply with regulations on individuals who are producing with water cut.

Senator Boren. Mr. McGregor, let me ask you this question: I hear you saying that it would appear that there might be some good economic justifications, but difficult administrative problems. Is it not true that there are administrative problems with the whole approach on the marginal which the Administration has advocated; the other thing being that very often, are you not dealing with properties here that are generally water flood properties that are handled as properties, much like this field I am talking about here, where it would be clear with 96.3 percent of everything being produced in that field being water, it would really be impossible for any cheating to go on in this field. It would be a pretty easily verifiable situation in terms of water products on many of these fields because they are operated as water-flood units.

Mr. McGregor. I would say you have found "a" field that is measurable in terms of a very high water cut. Probably it is allocable to the wells that they would also come in, not only because it is a field that has a 96-percent water cut level, but also because of the amount of production and presumably the number of wells involved in that production would be low.

Senator Wallop. Mr. Chairman, I want to say, I find it amazing to find somebody from any part of the bureaucracy saying that they are not looking forward to the opportunity of writing very detailed and complicated regulations.

(Laughter.)

Mr. McGregor. I speak from my heart, Senator Wallop.

Senator Wallop. Would it not just this once be possible to do this without very detailed, complicated regulations, and just look at the interest of the country in retaining reservoirs that the country would be better off producing, than abandoning?

Mr. McGregor. I think I have stated what the administrative and regulatory problems are.

The Chairman. Well, let us vote on it.

Mr. Shapiro. I need to ask Senator Boren one question for purposes of understanding his amendment. The marginal property is defined as having been a marginal property last year, 1978. You cannot get to be marginal after that, you cannot lose it. Is your water cut at any time, or do you want the same definition of "marginal"? Would you contemplate whenever you have the nine to one ratio, you can go?

Senator Boren. If you wanted to put an absolute text in and say that it has been that way for a year before you can start drawing, or something like that. Whenever you reach that ratio.

Mr. Shapiro. You want to get the same treatment as marginal.

Senator Boren. The same treatment as marginal. Just say when you have a nine to one water to oil production ratio, that the property thereby is defined as "marginal", would receive marginal treatment, phrase it that way, "would receive marginal treatment".

Mr. Shapiro. Did you say it has to be that way for a period of time?

Senator Boren. I do not think so. I think when you reached that point you reached the high-cost point. Given the nature of these things, it is not the kind of thing you would deliberately get yourself into, you would drown out your production. No one would increase their water ratio deliberately because you would drown out what production you are getting.

The Chairman. Well, how much revenue is involved in this?

Mr. Shapiro. Senator Boren has an estimate that is based on when the tax is at a 60-percent level. In view of the Chafee amendment it went up to 75 percent. It has now gone up to close to the range of about $350 million. That is because of a higher rate.

The Chairman. I do not think we passed the Chafee amendment yet.

Mr. Shapiro. On tier one.

The Chairman. Is that over the entire period?

Mr. Shapiro. The entire period.

The Chairman. So, that is about $35 million a year.

Senator Boren. The only thing you are affecting is bringing what is tier one high water up to tier two. Of course, tier one is all going to phase out by 1984 anyway. So, the tax effect would be over with by 1984.

The Chairman. Well, those in favor of the amendment say aye.

(Chorus of ayes.)

The Chairman. Opposed, no.

Senator Packwood. No.

The Chairman. The ayes appear to have it. The ayes have it.

Let me bring up this matter of severance tax limitation. I think we ought to dispose of it, if we can. Would you mind explaining what that is, and how that works?

Mr. Shapiro. The Administration proposed the tax that did not have an adjustment for severance taxes. When the House bill went to a 60-percent rate, it was believed appropriate to have a deduction for the severance tax because the rate is getting to a higher point.

However, when the House made an adjustment for the severance tax, what it says is that it is limited to the severance tax rate that was in effect in March of 1979.

Now, what we mean by the severance tax deduction is that you take your rate - your 50, 60, or 70 percent rate --

The Chairman. Well, the highest severance tax rate you have is 12.5.

Mr. Shapiro. Right. I am talking about the rate of the tax. In other words, here is the way the tax works: You have a rate of tax, 60 percent, the windfall rate, times your selling price, minus your base price, and minus your severance tax.

The Chairman. Hold on, I want to write it down.

Mr. Shapiro. All right. What you have is your rate, your windfall profits tax rate.

The Chairman. That says 60 percent?

Mr. Shapiro. That is 60 percent.

The Chairman. All right.

Mr. Shapiro. Times your selling price of the oil; minus the base price; minus the severance tax.

Now, when the Administration made its proposal it had a 50 percent rate and no severance tax deduction. When the House went to a 60-percent rate, or the Ways and Means Committee actually went to a 70-percent rate, when they were considering either a 60 or

70-percent rate, it was believed that they should make a severance tax deduction. So, they added the severance tax deduction. However, they limited the severance tax to that which was in effect in March of 1979: that is the amount of the deduction. There have been some suggestions of allowing that rate to go up, or to eliminate the limitation that the House had that said you only had the severance tax rate that was in effect by a State in March, 1979.

The reason the House did that, they were concerned that some States would increase the severance tax rate and therefore the money that would otherwise go to the Federal Government, would go to the State. There was some concern that that may only apply to the windfall profits element.

Some of the Senators have expressed interest in eliminating that House-passed limit which says you can only use the severance rate as of March, 1979. If the committee would like to deal with that issue, we could just eliminate that March, 1979 date altogether; or it could provide a limitation, for example, that said if you increased your severance tax rate you have to do it across the board; meaning you cannot do it just on the windfall profits portion, but you have to do it on all the oil, the entire price of the oil.

The Chairman. Frankly, I have found reason to resent the idea of trying to tell the States they could not tax, but I would have no objection to saying that if the State wants to raise its tax, wants to increase its tax, it has to be across the board. It seems to me that might be a fair way to settle the issue. Basically, what you are trying to say is, in view of the fact that you have a tax up here that works out to better than 90 percent, that if the State comes in and grabs some of it, 90 percent of what they grabbed would have been money the Federal Government would have collected. You say that you cannot deduct the severance tax unless it is a tax across the board.

Senator Packwood. Across the board on what?

The Chairman. All your taxes.

Senator Wallop. The total receipts.

The Chairman. In other words, if somebody levied a severance tax, and he levied it just on the part that is subject to the windfall tax, that would be kind of a cute trick because if he did that the government would take 90 percent of it anyway. So, it is only costing you six cents on the dollar to pay it to the State.

But if you say right now, "You cannot deduct the severance tax if it is levied just on the windfall part of the income. But, if it is levied across the board, you can. That is how they all work, is it not?

I would like to ask Senator Gravel. I know that the Louisiana tax is an across-the-board tax, it does not make any distinction between the part the Federal Government is collecting and the part the State is getting. I guess in Alaska it is probably the same thing.

Senator Gravel. And I think Wyoming has the same thing.

Senator Wallop. I do not know that we have ever contemplated that. Ours is wellhead severance.

The Chairman. Frankly, if anybody is worried about that, that is all right with me.

Senator Wallop. I agree entirely. I would only ask, again, that the same contemplated treatment would be extended to the tribal rights; that they would in effect be treated the same way as the States.

Senator Gravel. My State would be included in what you are proposing? My State and Wyoming would be included?

The Chairman. It would apply to everybody. It would apply to all States. In other words, if a State wants to raise its severance tax it has the power to do so, but it has to raise it across the board. You cannot just raise it on the portion of the price that is taxed by the windfall tax.

Senator Bentsen. I understand that. Mr. Chairman, I will probably be at another point in these meetings offering a limitation on the severance tax that can be brought about by the State on Federal lands. But, as I understand it, that is not affected in this issue. What you are trying to now to get uniformity in the levying of the tax, so that they do not play games with the windfall profits tax.

Senator Wallop. I think it is important that the tribal severance be included.

The Chairman. Without objection, then, we will agree to that suggestion, Mr. Shapiro. If they levy it, it cannot be deducted. So, actually it would be a brutal thing to do to the producer if you did it that way because by the time you levied such a tax on top of the windfall tax, he would be paying more than a hundred percent of his income in taxes.

Mr. Shapiro. All right, now, I want to clarify two things, one that Senator Gravel has mentioned, and one that Senator Wallop mentioned.

In the case of Alaska the House bill does not allow a deduction of severance tax because that is a 50-percent rate. The House bill only allows a severance tax deduction where the rate is above 50 percent. So, when you deal with Alaska tomorrow you might want to address yourself to severance tax because that is a sub-issue. The deduction is not allowed in the House bill.

The Chairman. What was that?

Mr. Shapiro. The Alaskan oil is not eligible for a severance tax deduction under the House bill because the way the House approached it was that any oil on which there was a 50-percent rate, they did not allow a severance tax deduction. Under the House bill the Alaskan oil had a 50-percent rate. Other oil had a 60-percent rate. Where, in the cases of Alaskan oil and in the House bill newly discovered oil and incremental tertiary, where there was a 50-percent rate, the House voted not to allow a severance tax deduction.

So, when Senator Gravel made the statement that it covers Alaska, I just want to clarify that under the House bill, which you are addressing now, that is not the case; unless the committee decides that specifically now, or deals with it when you deal with Alaska.

The Chairman. Well, how much revenue would you pick up by doing that to Alaska?

Mr. Wetzler. Senator, allowing the severance tax deduction for Alaska would reduce revenues by about $1.5 billion over the eleven-year period, I should say that the Administration proposed putting Alaska into the second tier, which means they would go from a 50 percent to a 60-percent rate and would get the severance tax deduction.

The Chairman. If you followed the Administration's recommendation for Alaska, that would be no problem.

Senator Gravel. Well, except that we are not very keen on the "leprosy" they are selling this year.

Mr. Wetzler. It would be $1.5 billion out of the $6.9 billion that the Administration has proposed. So, it probably would be easiest if the committee were to look at that issue when it deals with the Alaskan oil question.

Senator Gravel. Maybe that might be the best way to do it because the Administration does not particularly look to get any more oil out of Alaska and is trying to close it out as fast as they can. That may be the judgment of the committee, and that may be the judgment of the Congress.

(Laughter.)

Senator Gravel. So, we are not particularly "up tight" about that. So, I would rather you give us a shot and not tie us to anything that Administration offers in this regard - really, anything.

Mr. Shapiro. The second point with regard to Senator Wallop's comment in the case of the Indian tribes, the House bill does not allow a severance tax reduction, anything other than a State severance tax - it does not allow it for local, municipalities, anything else.

So, if the committee wants to deal with the severance tax imposed by tribes, I think you should specifically provide for it.

Senator Wallop. Let me just say, a tribal government is much more akin to a State government than it is to a municipal government. It is in effect, really, in its dealings with the United States, more on the footing of a State.

Mr. Shapiro. I understand. The only point is, I do not think on the House side there was ever any focus on Indian tribes specifically. So, it is not that the House decided not to do it, it was never specifically raised.

Senator Wallop. The reason I bring it up, I thought I had specifically brought it up by offering the amendment, which I did, which was my bill. I am told by my staff that you all do not think that it was raised.

Mr. Shapiro. We were not sure whether that was part of that amendment, or whether it would be brought up on the severance tax specifically.

All I am saying, the committee should just mention it specifically.

Senator Wallop. I would suggest to the committee to treat tribal governments the same as State governments. They are not like a municipality in any way.

Senator Gravel. I would suggest also that we take you at your word, Mr. Chairman. Your proposal was that every State be treated equally. That our severance tax would be deductible. We can adjust what we do with Alaskan oil over here, but I would like one thing clear now. That is, if you can deduct your severance taxes and not play games, that we do not want to play any more games, either; we want to deduct our severance taxes.

Now, we may want to do things for Alaska that we are not doing elsewhere, but at least let us have that understanding that what is good for one State, is good for all the States.

I know what the staff is smiling about, but I will deal with that problem tomorrow. Right now I want it clearly understood that Alaska deduct its severance tax just like anybody else can.

The Chairman. As far as I am concerned, we will do it; I will be glad to. But it seems to me, we might just as well wait and see what the situation is.

Mr. Shapiro. What Senator Wallop is proposing is that we did not deal with his issue on the severance tax because it was a specific item. He is suggesting treating the Indian tribes the same way as the States. In other words, it is not like a municipality. It was just not focused on at all in the House.

The Chairman. Well, do Indian tribes have a severance tax?

Senator Wallop. In some cases they do, Mr. Chairman.

The Chairman. Can you tell me what kind of severance tax they have?

Senator Wallop. On resources within their reservation.

The Chairman. How high is that severance?

Senator Wallop. Well, I cannot talk about all over the country. I think on the Wind River Indian Reservation it is substantially lower than in the State of Wyoming.

Mr. Shapiro. I should point out to the committee that we understand now that they did treat Indian tribes as States in the Gas Bill for purposes of severance tax.

The Chairman. It is consistent, they were treated as States for purposes of severance tax in the Gas bill?

Mr. Shapiro. That is right. This would be consistent with that decision.

The Chairman. All in favor say aye.

(Chorus of ayes.)

The Chairman. Opposed, no.

(No response.)

The Chairman. The ayes have it.

Now, what remains here in this category, Mr. Gravel wants to make his case on Alaska tomorrow. As of now, have we gone through all the things? What is this net income limitation, did we cover that item?

Mr. Shapiro. Which one, Senator?

The Chairman. You have something down here about net income limitation. Have we covered that item?

Mr. Shapiro. No, we have not. Now, have you made a decision on upper tier oil? You voted down the Chafee amendment on the upper tier oil, second tier; but you have not agreed to anything positively on second tier. Senator Dole said he had a suggestion. Is this the appropriate time to deal with upper tier?

Senator Chafee. We have not quite voted it down, the votes are not all in.

Mr. Shapiro. I am sorry, it was nine to nine. A tie vote would lose. So, both of the absentees would have to agree to it; that is correct. So, the committee would like to wait until both absentees are polled, and then Senator Dole would offer his proposal?

The Chairman. Are those two absentees somewhere in the environ? If they are around, we could get them.

Senator Chafee. Baucus is here, he could be recorded.

The Chairman. Why not contact Senator Baucus and tell him about this, and ask if he would record himself.

Senator Wallop. Do you have any instructions, Mr. Chairman?

Senator Dole. We have a direct line up here.

(Laughter.)

The Chairman. I will put it this way, I will not talk to him if it is agreed that Mr. Chafee will not talk to him.

(Laughter.)

Senator Wallop. Depending on how that comes out, Mr. Chairman., I have an amendment on the percentage depletion which we have to deal with at some time.

4:55 p.m.
lderson
ls.

Alderson
edm

S
Finance
F
/3

fols
Hansen

The Chairman. While we are waiting to resolve this issue, we could at least talk about some of the other things. For example, I would like to know what is interesting about this energy trust fund. Are we still considering that? What did you advise me on where we stand on that issue?

That is number six but while we are waiting to get the late returns on the Chafee amendment, maybe we can get to the energy trust fund.

Mr. Shapiro. The Administration was originally contemplating having a separate account to keep the energy revenues separated and have any amounts reserved from that in a separate account. When it was proposed in the Ways and Means Committee, they had to settle for the trust fund and the Administration responded to the request of many members of the Ways and Means Committee. The House bill contains a trust fund which puts the monies into it but does not spend anything out of it.

Subsequent to the Ways and Means Committee creating a trust fund, there was a lot of concern as to whether or not that is the right decision, meaning that some of the members did not favor a trust fund but had the assurance of the chair and other members that when they came to the spending programs, credits and so forth, that they would revisit the issue of the trust fund and it was left as an open issue.

It was in the bill that the receipts go into a trust fund. However, when they later considered the spending, they would subsequently decide that. As it is now then, the bill has come over to you with a trust fund in it. The windfall profits tax goes into that fund and no spending from it.

That is somewhat of a question among some members as to whether or not they want to have a separate trust fund for the windfall profit revenues or whether or not they want to just let the revenues go in the general revenues and deal with it in that manner.

Senator Gravel. All right, we will proceed.

Senator Dole. I missed the last part of that trust fund discussion. How do we get rid of it? Is it in the House bill?

Mr. Shapiro. It is in the House bill.

Senator Dole. If we do not do anything, it won't be in our bill?

Mr. Shapiro. Well, we do not know whether the committee is voting to delete it in the House bill, and I do not know whether you have to make an affirmative action or whether you just say nothing and you won't have a trust fund.

Senator Dole. I think we are building our own monument here if we do not put that log in.

Senator Gravel. Do you really want a trust fund?

Senator Dole. Some may; I don't know. Is anybody for the trust fund?

Senator Gravel. Is there anybody in the audience for the trust fund?

Senator Dole. Is there anybody with a vote for the trust fund?

Mr. Lubick. The purpose of the trust fund was to maintain control over the expenditures. The President stated that the purposes to be served by the program of decontrol and windfall profits tax were to create an energy security trust fund to carry out his three purposes.

We think it is important that we have this reckoning and this accounting and this firm hold on it. It is for that purpose that the trust fund was proposed, so we know exactly what we are getting.

The President said the expenditures and tax credits and direct expenditures and the Energy Security Corporation and the aid to the poor and the mass transit were all to be financed out of the proceeds of the tax. The trust fund is a part of that mechanism to assure the link between the two.

Senator Durenberger. On the theory that expenditures of this committee are already under control, I move that the proceeds of the windfall profitx tax go to the place where all other uncontrolled expenditures are, in general revenue.

Senator Gravel. Are you ready to vote?

Senator Dole. What is the vote?

Senator Gravel. That we leave it alone. All in favor of

4

leaving the trust fund concept alone say, "aye;" opposed, "no."

Hearing no opposition, there goes the trust fund. We are ready to take up anything you want to take up. Could I ask Mr. Shapiro, were there any comparisons made by the Joint Committee in respect to Japan and Germany? Both of those countries enjoy very, very high energy cost and they have less unemployment than us and less inflation than we have.

Has there been anything done to make comparisons since they are doing a better job of their economy than we are doing, and have any comparisons been made on that basis?

Mr. Shapiro. You are talking with respect to the overall dealings on this?

The Chairman. Has the trust fund been disposed of? I will take it on faith. I am sure the committee has done the right thing.

Now, Senator Chafee is on the telephone and talking to Senator Baucus and after that we will hear from the Senator. Now, what else do we talk about here? Is there anything that we can clean up?

Senator Gravel. It is after 5:00 o'clock, Mr. Chairman.

Mr. Shapiro. We have some questions and we need to work with the Treasury and we need to talk about it because each time we bring it up there has been a little confusion. We would like to sit down and discuss it so we all have the same understanding. I would like to ask one thing for the record.

Senator Dole. I think there may be some difference of opinion on the refineries.

Mr. Shapiro. We have a whole series of technical provisions that we will bring back.

Senator Wallop. Do you want to wait on the waiting requirements?

Mr. Shapiro. Yes. It is not clear to us, and we are trying to put together a decision as to whether the committee would act with regard to the severance tax on Alaska, and deal with it tomorrow or deal with it today. We discussed it in both respects.

Senator Gravel. I think what we have dealt with today is a severance tax. Everyone who has a severance tax can deduct that.

The Chairman. So far as I am concerned, I am ready to vote now. I think we ought to treat Alaska the same as we treat anybody else and I do not think we should do anything different. I do not see why anybody should object to that.

It seems to me that so far we have voted to treat everybody the same. All we have voted to do about severance tax is if someone wants to play games with us by getting cute and to zero in on something where the federal government will take 90 percent and he is zeroing in on that point, that is not deductible. It is to remove the temptation of people to play games with us and with Unkle Sam.

It is the same with Alaska. You say you cannot deduct the severance tax there but you can do it here. There is no point in it. Are there some technical things that we can clean up?

Senator Gravel. This is on the use of tax exempt bonds for hydro. You have a lot of hydro that can take place in the areas of government, that is local government, or with the use of authorities. We have one example in Alaska where we are prepared to sell bonds and to go ahead state-wide through an authority and build a large dam and produce eight percent of the power being used in the state of Alaska.

The feasibility apparently hinges on whether or not we can sell tax exempt bonds. If we could solve that problem, I am sure that it must affect a whole host of other states in that regard. So, I would be desirous of offering an amendment, particularly for a small hydro that Senator Nelson is interested in and the East Coast is interested in, and let us say any hydro facility that is sponsored by public authorities would be able to sell tax exempt bonds for the construction of that facility. I would like some comment on it.

The Chairman. What does Treasury have to say about that?

Mr. Shapiro. We did not hear that, Mr. Chairman.

Senator Gravel. If it is a public authority and not a private corporation.

The Chairman. It is a public authority then, limited to that.

Mr. Shapiro. The committee has agreed to a version of the hydro regarding Senator Nelson's amendment which is 25 kilowatts. The committee has instructed the staff to deal with all of these issues and bring back the various alternatives that can be dealt with in regard to credits, and we can put that on the list.

Senator Gravel. Put it on the list, and what I am suggesting is that right across the board in this the United States, any governmental authority or arm of government that builds a hydro facility, whether it is small or big, that it enjoy the ability to sell tax exempt bonds.

The Chairman. Well, the states can do that now, can't they, if the state wants to do it?

Mr. Lubick. There are some limits as to the extent to which industrial revenue bonds can be used to finance these facilities. We went into that last year in the Revenue Act and we had the two-county rule and the question of whether they are used for a private use versus a public use.

That is a very serious matter which you are opening up, if you try to open this whole thing up to a significant amount of industrial development bond financing.

Senator Gravel. We like to do serious things in this committee, and I want to say that I did not say that this was an industrial bond. I did not say this was for an industrial park to build factories. What I said was that this is to build hydro facilities by public entity. You want to call them industrial bonds and I choose to call them a tax exempt bond.

I am familiar with the two-county rule, but what we are talking about is, we want to produce some energy in this country. Maybe the Administration does not want to do it with oil and gas, but I would think that we would see the wisdom of doing it with a little hydro. We have studies that show that today we produce 60,000 megawatts in this country and with a little incentive we could produce five times that. We could probably double the amount of hydro that is produced in this country. Right now it is 13 percent.

So, I think one of the ways to do it, and we can talk in terms of credits or what have you, but these public facilities could use tax exempt bonds like they do for their water systems and sewer systems, and I think we might be able to see something worthwhile happen.

I am not advocating that they go out and build industrial sites.

Mr. Lubick. I assume, or what is the problem today?

Senator Gravel. The problem, as I know it in Alaska, is that we cannot build a dam that may cost $5 billion and we cannot build that dam unless we can sell tax exempt bonds because it goes for the whole state and crosses two counties or boroughs and we cannot build it. I do not think that the law was envisioned for that.

I think the law was envisioned that if a public authority, be it a state or what have you, sells bonds that they can be tax exempt. Because of some capriciousness of the law, we cannot do it. I am sure that that affects other parts of this country that cannot do it because they sell their power across two counties.

The Chairman. I thought we had agreed then that you were going to work on this matter and you hope to bring something back hopefully that would accommodate the Senator. If it does not accommodate him, he will offer it the way he thinks it would.

Now, we have been here, taking of a few hours that we had, until 5:00 o'clock and unless someone has something that he would like to vote on right now, I think we ought to quite until tomorrow.

I am told Senator Baucus informed the staff that he wanted to be recorded "no" on the Chafee amendment so that even if the other fellows voted, the amendment would not carry. It might lose by one vote or two votes but it would not carry. We can consider whatever we want to do about that subject.

Now, we are going to have a vote sometime soon on the

10 edm end of trans

Ribicoff amendment as modified by the Johnston amendment and Muskie amendment, to 1308 at 5:10.

Senator Dole. We can come back to the unfinished business tomorrow morning.

The Chairman. We haven't agreed on what the rate of tax will be on the oil.

Senator Dole. If we don't have anything, the tax is zero.

Senator Chafee. I thought we were always working from the House bill. Are we?

The Chairman. As a practical matter, gentlemen, what the tax is going to be or whatever the tax is going to be, it will have a majority vote in this committee, and we haven't arrived at it right now. We know what the Administration recommended and we know what the House did, and we know what a lot of fearful minds in this committee can recommend, so we will just vote on the alternatives until we find whatever meets the approval of the majority of the committee.

I hope by the time we are through we can agree on something that has rather broad support. So, we will stand in recess then until 10:00 o'clock tomorrow.

(Whereupon, the committee was recessed until 10:00 a.m., Thursday, October 4, 1979.)