SUSPENDING PRESIDENTIAL AUTHORITY TO IMPOSE OIL IMPORT FEES; $531 BILLION DEBT LIMIT

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-FOURTH CONGRESS

FIRST SESSION

ON

H.R. 1767

AN ACT TO SUSPEND FOR A NINETY-DAY PERIOD THE AUTHORITY OF THE PRESIDENT UNDER SECTION 232 OF THE TRADE EXPANSION ACT OF 1962 OR ANY OTHER PROVISION OF LAW TO INCREASE TARIFFS, OR TO TAKE ANY OTHER IMPORT ADJUSTMENT ACTION, WITH RESPECT TO PETROLEUM OR PRODUCTS DERIVED THEREFROM; TO NEGATE ANY SUCH ACTION WHICH MAY BE TAKEN BY THE PRESIDENT AFTER JANUARY 15, 1975, AND BEFORE THE BEGINNING OF SUCH NINETY-DAY PERIOD; AND FOR OTHER PURPOSES

AND

H.R. 2634

AN ACT TO INCREASE THE TEMPORARY DEBT LIMITATION AND TO EXTEND SUCH TEMPORARY LIMITATION UNTIL JUNE 30, 1975

FEBRUARY 7 AND 10, 1975

Printed for the use of the Committee on Finance

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SUSPENDING PRESIDENTIAL AUTHORITY TO IMPOSE OIL IMPORT FEES; $531 BILLION DEBT LIMIT

FRIDAY, FEBRUARY 7, 1975

U. S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 10:08 a.m., in room 2221, Dirksen Senate Office Building, Senator Russell B. Long (Chairman of the committee) presiding.

Present: Senators Long, Byrd, Jr. of Virginia, Hartke, Mondale, Haskell, Hansen, Packwood, and Brock.

The CHAIRMAN. This hearing will come to order.

This morning the committee will receive testimony on H.R. 1767, the bill which was passed by the House of Representatives that would suspend for 90 days the President's authority to impose oil import fees.

On Monday the committee will hear administration witnesses on both this bill and on H.R. 2634, a bill to increase the temporary debt limit. Today, however, we will be hearing witnesses on the 90-day suspension bill.

[The press release announcing these hearings, the acts H.R. 1767 and H.R. 2634, S.J. Res. 12, and a staff memorandum relative to H.R. 2634, follows:]

PRESS RELEASE

FOR IMMEDIATE RELEASE
February 6, 1975

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 Dirksen Senate Office Bldg.

FINANCE COMMITTEE ANNOUNCES HEARINGS ON BILLS RAISING PUBLIC DEBT, SUSPENDING FOR 90 DAYS PRESIDENT'S AUTHORITY TO IMPOSE OIL IMPORT FEES

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee will hold hearings on Friday, February 7 and on Monday, February 10, on two measures passed by the House:

1. H.R. 2634, a bill to increase the temporary debt limit from \$495 billion to \$531 billion and extending the temporary debt limit through June 30, 1975.

2. H.R. 1767, a bill to suspend for 90 days the President's authority to increase import fees or tariffs on imports of petroleum or petroleum products.

The Chairman announced that the Committee would hear public witnesses on Friday, February 7: on Monday, February 10, the Committee will hear these Administration witnesses:

The Honorable William E. Simon, Secretary of the Treasury

The Honorable, James T. Lynn, Director, Office of Management and Budget

The Honorable Eric Zausner, Deputy Administrator of Federal Energy Administration*

The hearings will be held in Room 2221, Dirksen Senate Office Building and will begin at 10:00 a.m..

PR #3

*The Honorable Frank G. Zarb, Administrator of the Federal Energy Administration, appeared as the witness.

94TH CONGRESS
1ST SESSION

H. R. 1767

IN THE SENATE OF THE UNITED STATES

FEBRUARY 6, 1975

Read twice and referred to the Committee on Finance, under the authority of the order of the Senate of February 5, 1975

AN ACT

To suspend for a ninety-day period the authority of the President under section 232 of the Trade Expansion Act of 1962 or any other provision of law to increase tariffs, or to take any other import adjustment action, with respect to petroleum or products derived therefrom; to negate any such action which may be taken by the President after January 15, 1975, and before the beginning of such ninety-day period; and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That, during the period beginning on the date of the enactment of this Act and ending at the close of the ninetieth day thereafter, nothing in section 232 (b) of the Trade Expansion

Act of 1962 (19 U.S.C. 1862 (b)) or in any other provision of law shall be deemed to grant to the President any authority to adjust imports of petroleum or any product derived therefrom.

SEC. 2. (a) (1) Any action which is taken after January 15, 1975, and before the date of the enactment of this Act by the President under section 232 (b) of the Trade Expansion Act of 1962 or any other provision of law which results in the imposition of a rate of duty on petroleum or any product derived therefrom shall cease to have effect on the date of the enactment of this Act, and the entry or withdrawal of petroleum and any product derived therefrom on or after such date of enactment shall be duty free.

(2) Upon appropriate request therefor filed with the customs officer concerned on or before the sixtieth day after the date of the enactment of this Act, the entry or withdrawal of petroleum or any product derived therefrom to which a rate of duty imposed by the President (pursuant to any action by him after January 15, 1975, and before the date of the enactment of this Act under such section 232 (b) or any other provision of law) applies shall, notwithstanding the provisions of section 514 of the Tariff Act of 1930 or any other provision of law, be liquidated or reliquidated as if no duty applied to such entry or withdrawal.

(b) (1) Any action which is taken after January 15, 1975, and before the date of the enactment of this Act by the President under section 232 (b) of the Trade Expansion Act of 1962 or any other provision of law which results in the imposition of a tax or fee on the importation of petroleum or any product derived therefrom which is higher than the tax or fee imposed on the importation of petroleum or any such product on January 15, 1975, shall cease to have effect on the date of the enactment of this Act; and the tax or fee imposed on the importation of petroleum or any product derived therefrom after such date of enactment shall be the tax or fee in effect on January 15, 1975.

(2) Upon request therefor filed with the appropriate Federal agency on or before the sixtieth day after the date of the enactment of this Act, the amount of any tax or fee imposed by the President (pursuant to any action by him after January 15, 1975, and before the date of the enactment of this Act under such section 232 (b) or any other provision of law) and paid by any person on the importation of petroleum or any product derived therefrom which exceeds the tax or fee that was imposed with respect to the importation of petroleum or products derived therefrom on January 15, 1975, shall be rebated to such person.

SEC. 3. If during the ninety-day period referred to in the first section of this Act—

(1) the Congress declares war,

(2) United States Armed Forces are introduced into hostilities pursuant to specific statutory authorization,

(3) a national emergency is created by attack upon the United States, its territories or possessions, or its Armed Forces, or

(4) United States Armed Forces are introduced into such hostilities, situations, or places, or are enlarged in any foreign nation, under circumstances which require a report by the President to the Congress pursuant to section 4 (a) of the War Powers Resolution (50 U.S.C. 1453 (a)),

the first section of this Act shall not thereafter apply.

SEC. 4. Nothing in the first section and sections 2 and 3 of this Act shall be deemed to affect the validity of any proclamation or executive order issued before January 16, 1975, by the President under section 232 (b) of the Trade Expansion Act of 1962.

Passed the House of Representatives February 5, 1975.

Attest: W. PAT JENNINGS,

Clerk.

Calendar No. 3

94TH CONGRESS
1ST SESSION

S. J. RES. 12

IN THE SENATE OF THE UNITED STATES

JANUARY 23, 1975

Mr. KENNEDY (for himself, Mr. JACKSON, Mr. ABOUREZK, Mr. BAYH, Mr. BENTSEN, Mr. BIDEN, Mr. BROOKE, Mr. BUMPERS, Mr. BURDICK, Mr. ROBERT C. BYRD, Mr. CHILES, Mr. CHURCH, Mr. CLARK, Mr. CRANSTON, Mr. CULVER, Mr. EAGLETON, Mr. EASTLAND, Mr. FORD, Mr. GLENN, Mr. GARY W. HART, Mr. PHILIP A. HART, Mr. HARTKE, Mr. HASKELL, Mr. HATFIELD, Mr. HATHAWAY, Mr. HOLLINGS, Mr. HUDDLESTON, Mr. HUMPHREY, Mr. LEAHY, Mr. MCCLELLAN, Mr. MCGOVERN, Mr. MCINTYRE, Mr. MAGNUSON, Mr. MANSFIELD, Mr. METCALF, Mr. MONDALE, Mr. MONTOYA, Mr. MOSS, Mr. MUSKIE, Mr. NELSON, Mr. PASTORE, Mr. PELL, Mr. PROXMIRE, Mr. RANDOLPH, Mr. RIBICOFF, Mr. STAFFORD, Mr. STEVENSON, Mr. STONE, Mr. SYMINGTON, Mr. TUNNEY, Mr. WEICKER, and Mr. WILLIAMS) introduced the following joint resolution; which was read twice, and by unanimous consent, ordered to be placed on the calendar

JOINT RESOLUTION

To prohibit for a period of sixty days the imposition of tariffs, fees, and quotas on oil imports and the lifting of all price controls on domestic oil, and to thereafter require the submission to, and the right of approval of the Congress of any such action within thirty days.

Whereas the President's State of the Union message announces his intention to levy new fees on imports of crude oil and petroleum products and to lift all price controls on domestic oil under the authority of existing law;

Whereas the Congress expressed in the Trade Act of 1974 its desire that public participation be required prior to the use of the President's authority under the national security provisions of the Trade Expansion Act of 1962, as amended;

Whereas imposing import fees and lifting price controls would increase the price of crude oil and all petroleum products, including home heating oil and residual fuel oils, substantially, thereby creating major inflationary pressures throughout the economy;

Whereas consumption of home heating oil and residual fuel oil already has been reduced substantially in many areas of the country and therefore imposition of import fees and the lifting of price controls will result in higher prices to consumers with little corresponding reduction in oil consumption;

Whereas the policy of lifting price controls and using new import fees to reduce energy consumption represents a fundamental policy change as stated by the President in his State of the Union message;

Whereas the purpose of this joint resolution is to permit the Congress a reasonable period of time to review and, if desirable, to develop fair and equitable alternatives to the President's proposals to impose a $3 per barrel oil import fee and to remove all existing price controls on domestic oil by April 1, 1975: Now, therefore, be it

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That, after the date of enactment of this joint resolution—

(a) (1) No new tariff, fee or other charge, and no increase in existing tariffs, fees or other charge on imports of crude oil or petroleum products in effect on January 1, 1975, may be imposed except in accordance with subsection (b) of this section;

(2) No new quota or other limitation on imports of crude oil or petroleum product other than those in effect on January 1, 1975, may be imposed except in accordance with subsection (b) of this section; and

(3) No increase in the price permitted for oil now classified as "old" oil under regulations promulgated pursuant to section 4 of the Emergency Petroleum Allocation Act of 1973 (87 Stat. 629) and in effect on January 1, 1975, may be established except in accordance with subsection (b) of this section.

(b) No action covered by the provisions of subsections (a) (1) through (3) may be undertaken unless:

(1) such action is specifically authorized by law enacted after the date of enactment of this joint resolution; or

(2) the specific action proposed to be taken is submitted to both Houses of the Congress. Each House then shall have the opportunity to disapprove of such action within thirty days of the receipt of the proposal, pursuant to the procedures provided for in sections 906

(a), (b), and (c), 908, 909, 910, 911, 912, and 913 of title 5, United States Code, except that for the purposes of this joint resolution,

(A) the period of congressional review and opportunity shall be thirty calendar days rather than sixty calendar days;

(B) any reference in such sections to "reorganization plan" shall be deemed to be a reference to "petroleum pricing actions" which for the purposes of this joint resolution shall mean all actions referred to in subsections (a) (1) through (3) of this joint resolution; and

(C) such thirty-day review period shall begin on the sixtieth day after enactment or when such action is submitted to the Congress if it is submitted after the sixtieth day.

If such action is disapproved by either House within the thirty-day review period, no officer or agency shall have authority to take any action inconsistent with the provisions of subsection (a) of this joint resolution.

February 6, 1975

MEMORANDUM

TO : Members of the Committee on Finance

FROM : Michael Stern, Staff Director

SUBJECT: Increase in Temporary Debt Limit (H.R. 2634)

House Bill.--Under present law, the permanent debt limit is set at $400 billion, with a temporary additional limit of $95 billion, effective through March 31, 1975. H.R. 2634 would:

1. Increase the temporary debt limit from $495 billion to $531 billion; and

2. Extend the period in which the temporary debt limit applies until June 30, 1975.

Budget Outlook.--The actual fiscal year 1974 deficit on a Federal funds basis was $17.5 billion; the unified or consolidated deficit was $3.5 billion. The estimates for fiscal year 1975 in the new President's budget project a $43.0 billion deficit in Federal funds and a $34.7 billion deficit on a consolidated basis. These figures are shown in the table below:

	(dollars in billions)		
	1973 Actual	1974 Actual	1975 Estimate
Federal funds:			
Receipts	$161.4	$181.2	$186.0
Outlays	186.4	198.7	229.0
Deficit (-)	-25.0	-17.5	-43.0
Unified budget:			
Receipts	232.2	264.9	278.8
Outlays	246.5	268.4	313.4
Deficit (-)	-14.3	- 3.5	-34.7

94TH CONGRESS
1ST SESSION

H. R. 2634

IN THE SENATE OF THE UNITED STATES

FEBRUARY 6, 1975

Read twice and referred to the Committee on Finance, under the authority of the order of the Senate of February 5, 1975

AN ACT

To increase the temporary debt limitation and to extend such temporary limitation until June 30, 1975.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That during the period beginning on the date of the enactment of this Act and ending on June 30, 1975, the public debt limit set forth in the first sentence of section 21 of the Second Liberty Bond Act (31 U.S.C. 757b) shall be temporarily increased by $131,000,000,000.

SEC. 2. Effective on the date of the enactment of this Act, the first section of the Act of June 30, 1974, providing

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for a temporary increase in the public debt limit for a period ending March 31, 1975 (Public Law 93-325). is hereby repealed.

Passed the House of Representatives February 5, 1975.

Attest: W. PAT JENNINGS,

Clerk.

The CHAIRMAN. First I will call on Senator Mondale who would like to make a statement.

STATEMENT OF HON. WALTER F. MONDALE, A U.S. SENATOR FROM THE STATE OF MINNESOTA

Senator MONDALE. Mr. Chairman, I would like to commend you for the speed with which you called these hearings. I believe this issue is one of the most important pieces of legislation we will consider this year.

The effect of the entire Ford energy program, of which the $3 per barrel tariff is an integral part, will be devastating. I understand that as we meet today the Department of Labor is announcing unemployment jumped a full percentage point in a single month. It is now 8.2 percent unemployed—nearly 7½ million Americans are out of work and cannot find it.

Mr. Chairman. I asked the Library of Congress to do a study of the costs of the President's energy program upon families throughout the income scale, and I have just received these figures. And I would like to put them in the record.[1]

For a poor family earning $2,500 per year, the Library of Congress estimates that the total cost of the President's package will be $341 per year, compared with the FEA estimate of $256.

For the lower middle-income family earning $8,000 a year, the Ford package would cost $530, compared to the FEA estimate of $303.

For the middle-income family with a wage of $14,000, the Library estimates the cost would be $749 per year per family compared to the FEA estimate of $363.

And for the family earning $24,500, the Library estimates the cost would be $1,017 a year, and the FEA estimates only $399.

The Library of Congress concludes that the Ford program, when compared with incomes in each income level for 1973, has "the sharpest proportional impact on the poor category and progressively smaller effects toward higher income groups."

It seems to me we must understand the cruel, devastating impact of this new tax upon American families and working families. That is

[1] See p. 15.

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why I think it is absolutely crucial that we adopt this pending proposal and stop the adoption of this self-mutilation tax before it increases inflation, increases the recession and unemployment. And if I may make this one regional point, as I understand it, the President's authority to impose this tax must be based on a finding of national security. Well, I come from the upper Midwest. All of our crude oil comes from Canada. He is proposing to put a $3 tariff on the importation of Canadian crude. It will cost my State between $100 and $200 million next year. And how can you justify that on the basis of national security? I have checked. The Canadians are planning no attack and there are no armies massed on the border, and I do not see a single good reason for imposing this kind of burden upon the citizens of the upper Midwest. And I hope we pass this legislation as quickly as possible.

Mr. Chairman, I ask unanimous consent that the study from the Library of Congress appear in the record.

The CHAIRMAN. It will appear at this point.

Senator MONDALE. Mr. Chairman, I would also like to insert at the end of my statement a telegram sent by the Governor of Minnesota supporting the 90-day suspension bill.

[The prepared statement of Senator Walter F. Mondale, the Library of Congress study, and the telegram referred to follow. Oral testimony continues on page 16.]

[Telegram]

ST. PAUL, MINN., *February 6, 1975.*

HON. EDWARD M. KENNEDY,
U.S. Senate,
Washington, D.C.:

I support legislation now before the Senate Finance Committee to suspend for 90 days the President's proposed fee on imported oil. Minnesota's refineries, which depend almost exclusively on Canadian crude oil, would be placed at a distinct competitive disadvantage by these fees. Assuming the refineries continue operating and pass the increased costs on to consumers, it will cost Minnesotans an estimated $100 million to $200 million a year. The major burden would fall on rural Minnesota, where some 60 percent of the families heat with fuel oil. I urge you to support this legislation. I share the President's goal of reducing our dependence on imported oil, but I would hope the Congress can find a more equitable way of realizing that goal.

WENDELL R. ANDERSON,
Governor of Minnesota.

STATEMENT OF SENATOR WALTER F. MONDALE

Mr. Chairman, I would like to commend you for the speed with which you have called hearings on HR 1767. I believe it is one of the most important pieces of legislation which we will consider this year.

The effect of the entire Ford energy program—of which the $3 per barrel tariff is an integral part—will be devastating. In fact, its effect will be much more devastating than the Administration has been willing to admit.

A preliminary study prepared at my request by the Library of Congress shows that the direct and indirect costs of the President's program will hit hard at families throughout the income scale.

I am releasing this study this morning. Its principal conclusions are as follows:

For the poor family earning $2,500 per year, the Library of Congress estimates that the total costs of the President's package will be $341 per year, compared to the FEA estimate of $256.

For the lower middle income family earning $8,000, the Library estimates that the Ford package would cost $530, compared to the FEA estimate of $303.

For the upper middle income family with income of $14,000, the Library estimate comes to $749, well above the FEA estimate of $363.

And for the family with earnings of $24,500, the Library estimates additional costs of $1017, far above the FEA's $399 estimate.

Finally, the Library's conclusion is that the Ford program, when compared with incomes in each income level for 1973, has "the sharpest proportional impact in the poor category and progressively smaller effects toward higher income groups."

Mr. Chairman, I believe that this Library of Congress study places in perspective the Presidential program of which the oil import tariff is the first part. The impact on American families, and particularly the poor and middle income family, will be cruel. And in return for this cruel impact on every American family, what will we gain? I do not believe that the Administration has convincingly demonstrated the case for its program.

They have not told us why the one million barrel per day cut is needed this year—with our economy already in deep recession.

They have not told us how the $3 per barrel tariff which the President is imposing will reduce foreign oil imports.

They have not told us how a plan which takes over $50 billion per year away from consumers and returns only $19 billion per year directly to consumers will help our economy prosper.

And they have not told us why an energy program which addressed our commonly held goal of cutting energy consumption is a more gradual yet definite manner could not achieve as much both at home and abroad as the President's plan.

Yet in spite of all they have not told us, we do know that this plan will have a real impact. I'd like to briefly give some illustrations of the impact of that program on my state of Minnesota.

The President has told us that he is imposing the tariff on foreign oil on grounds of national security. Yet he included in that proclamation imports of Canadian oil, which are vital to my state. We rely on Canada for over half our entire crude oil supply. I am aware of no imminent plans of the Canadian government to invade across the Minnesota border. And I am aware that the Canadians have been a reliable source of crude oil for well over a decade. Yet they are treated in the same way as oil coming from Saudi Arabia or Kuwait.

Based on this questionable premise, the President's tariff will impose between $100 million and $200 million in added fuel costs for my state alone. Just this part of his plan—without the additional costs of the decontrol of old oil or the tax on natural gas or any of the other inflationary parts of his proposals—could add up to $200 per year to the fuel bill of the Minnesota family. And this program's impact on jobs and the economy of my state could be significant.

Mr. Chairman, I hope that the impact of this program on the nation will be thoroughly probed in these hearings. We in the Congress have a heavy responsibility to come up with meaningful alternatives to the President's plan. But our most important task must be preserving the purchasing power of American consumers while we develop those alternatives. And approval of HR 1767 is a must in fighting the most immediate inflationary and recessionary impact of an unwise policy.

THE LIBRARY OF CONGRESS,
CONGRESSIONAL RESEARCH SERVICE,
Washington, D.C.

IMPACT OF THE FORD ADMINISTRATION'S ENERGY PACKAGE BY INCOME CLASS—A PRELIMINARY ROUGH ESTIMATE

(By Henry Canaday, economic analyst and Lawrence Kumins, analyst in energy economics, Economics Division)

This report allocates the costs delineated in our paper "Administration's Energy Tax Proposals and Related Measures" dated January 23, 1975. We have allocated these increased costs to income groups as categorized in The Ford Foundation Energy Policy Project Report, "A Time To Choose—America's Energy Future," Chapter 5. Here estimates are made of each level's household energy budget. Both direct and indirect (embodied in other products) energy consumption costs are estimated. We have adjusted these 1972–73 averages upward to

1974 costs and then added in possible increases which could flow from the President's $50 billion impact package of proposals.

Indirect energy costs as calculated in the Ford Foundation report were adjusted upward to reflect our estimate that the energy proposals will raise all energy costs by about an average of 50 percent all told. Original table 28 data were first converted to dollars, using 55 cents per million Btu (the average electric utility fuel cost data collected by the FPC). This amount was then adjusted to reflect the approximate 135-percent increase in raw energy costs from the sample period to late 1974. Utility fuel costs are regarded as base line data for industrial fuel costs and are accordingly biased toward the lower end.

Household energy expenditures were adjusted upward by the appropriate Consumer Price Index components to December 1974 levels. Then the following increase factors were applied to the Ford Foundation's cost categories: Natural gas (delivered cost) 10 percent; Electricity (incl. primary fuel cost increases) 40 percent; gasoline 20 percent.

Table 1 below delineates our results as to 1974 household energy costs and how they would be affected by full implementation of the Administration's total package. Column 4 presents one measure of the package's relative impact by income class—a comparison between the dollar change in energy costs and the average income for each class. Unadjusted 1973 averages were used because no reliable means of "indexing" these figures forward to late 1974 exists which would not distort the results to some extent. If we take account of the fact that inflation has raised nominal incomes since 1973, this would reduce slightly each of the figures in column 4 but would not alter their fundamental pattern: sharpest proportional impact in the poor category and progressively smaller effects toward higher income groups.

TABLE 1.—ANNUAL ENERGY EXPENSES BY INCOME CLASS

	December 1974	Under Ford package	Difference (col. 2—col. 1)	Difference as percentage of 1973 average income for each class
Poor:				
Direct	$490	$603		
Indirect	456	684		
Total	946	1,287	$341	13.6
Lower middle:				
Direct	758	933		
Indirect	710	1,065		
Total	1,468	1,998	530	6.6
Upper middle:				
Direct	1,128	1,377		
Indirect	1,090	1,635		
Total	2,218	3,012	794	5.7
Well off:				
Direct	1,337	1,646		
Indirect	1,415	2,123		
Total	2,752	3,769	1,017	4.2

In utilizing the tabled figures, one important caveat ought to be observed. If the data in column three can be taken as, in some real sense, the "cost" of adopting President Ford's energy package, this does not mean that the cost of rejecting it is zero. Even holding individual energy commodities to present price levels would not prevent increases in the nation's energy bill—the steady displacement of natural gas by more expensive petroleum and of declining domestic oil by high-priced imports would gradually boost the average price of energy to industries and consumers. For the very immediate future, we may treat these prices as level and thus arrive at a rough gauge of the impact of the departure the President is proposing. Over the coming years, however, the difference is sure to narrow, and assessing the harsh nature of our energy options will of course require more than the simple arithmetic attempted here.

The CHAIRMAN. The next two witnesses will be Senators Kennedy and Jackson who have sponsored a resolution to suspend the President's authority. I suggest that, Senator Kennedy, you and Senator Jackson decide among yourselves how you wish to proceed.

Senator KENNEDY. Well, thank you very much.

Senator JACKSON. It appears to be unanimous.

STATEMENT OF HON. EDWARD M. KENNEDY, A U.S. SENATOR FROM THE STATE OF MASSACHUSETTS

Senator KENNEDY. Thank you very much, Mr. Chairman and members of the committee. I would like to introduce our panel here this morning, and then I would like to file my statement with the committee and make some comments.

I think there are witnesses here this morning who are all familiar to this committee. On our right is Charlie Schultz who is a distinguished economist and served with great distinction as Director of the Bureau of the Budget, and then Attorney General Jim Guy Tucker of Arkansas, and Governor Salmon of Vermont, and John Sawhill who until very recently had been the principal administration architect in developing alternatives on energy policy as FEA Administrator.

Mr. Chairman, with the permission of the committee we will be talking about H.R. 1767 that passed the House of Representatives by 309 to 114, strongly supported by Members of both sides of the aisle, and S.J. Res. 12 which is a resolution introduced by Senator Jackson and myself which now has presently some 52 cosponsors of the U.S. Senate.

First of all I want to join in expressing a warm sense of appreciation to you, Mr. Chairman, and to the members of the committee for holding this hearing this morning and permitting us the opportunity to testify in favor of H.R. 1767. You indicate at least your strong desire and willingness to permit the Senate as a whole to express itself on these matters. And this is something of which we are extremely appreciative. I think that even though we are very hopeful of gaining your support, it is a clear indication that you believe that we ought to have an opportunity to express ourselves on these matters.

Mr. Chairman, there are basically three fundamental reasons why I think H.R. 1767 ought to be considered favorably by this committee. First of all is the economic situation that we are facing in this country at the present time with the announcement of 8.2 percent unemployment in January. All we have to do to observe the trend is to look back over the period of November and December, 6.5 percent in November, 7.2 percent in December, and 8.2 percent unemployed in January. I dare say we have had a classical abdication of economic responsibility by this administration probably that we have not seen the likes of since the Hoover administration. We are facing a dire economic situation, and if we talk of an energy program taking anywhere from $55 to $60 million out of the purchasing power of the consumers of this country—these are not the figures that have been developed by individual Members of the Senate or the Congress, they have been testified to by many of the most outstanding, responsible economists who have served Democratic and Republican administrations, as well as by economists of the Library of Congress—then we are only asking to put this country into a depression.

So Mr. Chairman, this program makes no sense economically and cannot be justified economically particularly because of the recessionary pressures which exist in our society.

Second, Mr. Chairman, this program is not targeted to the principal area of need which is a reduction of gasoline. The President's program is a meat ax approach to something that ought to have a scalpel. If you look at the Federal Energy Administration report and its summary of figures, you will find out that in the three principal categories, motor gasoline, distillate, and residual fuel oils, that the total savings are going to be higher in residual, 310,000 barrels and proportionally higher in distillate 238,000, than in motor gasoline where only 278,000 barrels are expected to be reduced.

Well, the residual product is obviously a product which fuels our principal industries as well as our utilities, and they are going to be the hardest hit. Distillate, which is in the home heating area, and we have seen in our part of the country a reduction of approximately 22 or 23 percent by voluntary means, that is going to be the second area that will be hit. Yet only 278,000 barrels of motor gasoline, which all of us agree is the area where there should be the most substantial reduction are planned to be reduced. So I dare say that the program has been ill-conceived if it works even according to the optimistic estimates of the administration. If we are talking about attempting to really meet the problems of energy wastage in our society, we can fashion a much more effective program.

The third point, Mr. Chairman, is that this program works the greatest inequity on the low-income family, the workers and the elderly, and generally they are not the ones who are involved in the wasting of energy.

An additional point that I would like to make here, Mr. Chairman, is that it works a serious discrimination on different sections of the country. Senator Mondale and other Midwestern Senators have talked about how this has worked to the disadvantage of the Midwestern and Northern Midwestern States. This as well works adversely on New England. As you can see from these charts, approximately 85 percent of the energy resources of New England are developed from oil products as compared to approximately 45 percent for the other parts of the country. If you would be kind enough to move to the next chart. Second, as you can see from this chart, New England relies on foreign crude for a substantial amount of its oil so that the dollar tariff on crude still works a severe hardship on New England.

CHART 1

SOURCES OF ENERGY

[In percent]

	New England	United States
Gasoline	23	18
Distillate	24	8
Residual	32	7
Other oil	6	13
Natural gas	9	32
Coal	1	17
Hydropower/nuclear	5	5
Total	100	100

CHART 2

SOURCES OF PETROLEUM

[In percent]

	New England	United States
Foreign crude (refined in United States)	30	32
Foreign product imports	40	
Domestic	30	68
Total	100	100

CHART 3

	Direct energy Current	Per household cost increases of President's program: FEA estimate of Ford cost [1]	Low New England Regional Commission [2]	High NERCOM [3]
Total cost	$1,238	$1,418	$1,466	$1,559
Distillate	330	386	415	458
Natural gas	89	103	103	103
Electricity	255	270	278	306
Gasoline	564	659	670	692

[1] $180 more than current.
[2] $228 more than current.
[3] $321 more than current.

And the third chart, which shows, Mr. Chairman, the figures that have been developed by the FEA, which would indicate what the direct cost was going to be for New Englanders, and the far higher estimates developed by the New England Regional Commission. And we are working at this time with the administration to demonstrate quite clearly and effectively that the financial burden to the homes of New Englanders and those in the northeastern part of the country, the East Coast States, and the Northern Tier States is going to be a burden that will not be evenly shared by the other parts of the country.

We have 6 percent of the population, we consume 23 percent of the heating oil, and the President's program, even with the rebate program, is still going to produce severe inequities.

So Mr. Chairman, I would be extremely hopeful that we could develop these various points with the committee at whatever length they would so desire. Just in conclusion, let me say that, among those Members of the Senate who cosponsored S.J. Res. 12, there is strong support for the administration's program to provide additional purchasing power among the consumers of this country. So we support the President in that particular endeavor.

Second, as Senator Jackson has ably demonstrated, both in his presentation of the Energy Conservation Act last year and in the passage of the original act by the Congress, there is a strong support on both sides of the aisle in the conservation efforts of the administration.

But where we are at odds and have strong differences with the administration is in this area of input fees and price policies which has been implemented by the administration without the participation of the Congress and which we think is going to add to the problems of recession, significantly endangering our economic recovery. It has been done without the consultation of the Congress, and as the Attorney General of Arkansas and other Governors and attorneys general have pointed out, there is some question as to the legitimacy of those activities before the courts of law of this country.

The CHAIRMAN. Thank you, Senator. I think it would be best if each of you make a statement first, and then those Senators who want to ask questions can go right ahead.

[Senator Kennedy's prepared statement follows:]

STATEMENT BY SENATOR EDWARD M. KENNEDY IN SUPPORT OF A 90-DAY DELAY IN OIL IMPORT FEES

Mr. Chairman, I appreciate the opportunity to appear before the Senate Finance Committee in support of H.R. 1767 which imposes a roll-back of the $1 per barrel tariff imposed last Saturday and a 90-day delay of any additional tariff, fee or quota.

We believe that a 90-day delay will assure the Congress an opportunity to develop a cooperative approach with the executive branch in resolving our energy problems; but one which does not drive the nation's economy further into the ground.

The number one issue in America today is ending the recession and putting our labor force back to work. We cannot afford the President's budget assumption that 7 million Americans will be out of work over the next three years. We cannot afford the President's budget assumption that our gross national product will decline again. And we cannot afford the President's budget assumption that we will continue to have double-digit inflation.

Our concern is that the President's energy program was developed without any deep understanding of its devastating effect on any hopes of economic recovery.

That same concern was the foundation, I believe, for the overwhelming 309 to 114 vote of the House of Representatives on Wednesday in support of H.R. 1767. That action reflects a similar expression of opposition to the tariff and tax portions of the President's energy program in the Senate.

I introduced S.J. Res. 12 on January 23, 1975, with Senator Jackson. S.J. Res. 12 now has 52 other cosponsors from both sides of the aisle.

That resolution had two key elements: first, the delay of the effective date of any additional tariffs, fees or quotas on imported petroleum for 90 days; and, second, a similar delay of any attempt to lift the existing price ceiling of old oil. The resolution would assure a 30-day review period of any proposal following its submission to the Congress.

The House measure now before the Committee incorporates the 90-day delay of tariffs, fees or quotas contained within the Kennedy-Jackson resolution.

We fully support its provisions as the most urgent matter before the Congress.

Without the approval of this bill, the Congress would have no opportunity to interpose adjudgment whether an alternative energy program can be devised which does not jeopardize the economy.

We believe that the President's energy program, of which the import fees are a major part, is not in the national interest. We believe that it will add a minimum of $55 to $60 billion to the backs of the nation's consumers. And we believe it will subvert the positive impact of a tax cut that is essential to stimulate the economy.

The Administration talks of a $30 billion direct cost and a 2 percent increase in the cost of living index resulting from their energy program.

Those figures are challenged by economists from both parties and by the Library of Congress.

On Monday, in Boston, Dr. Otto Eckstein, former member of the Council of Economic Advisors to President Johnson, testified that his estimates showed the impact of the President's energy program would be prices between 3.5 to 4 points higher on the cost of living index.

If we want to end double-digit inflation that has produced the first decline in the take-home pay of the American worker in 20 years, then the President's energy program is unacceptable.

A $3 tariff essentially tells the OPEC producers that the price they are charging for crude oil, some $11 per barrel, is $3 too low. It makes no sense if one of our goals is to see the world price of oil decline. It makes no sense unless we want to put more money into the coffers of major oil companies.

Even more disturbing, Dr. Eckstein testified that withdrawing $55 to $60 billion in added energy and energy-related costs would doom any hopes of rescuing the economy from its deep recession. He said there would be a real threat of 9 percent unemployment nationally by the end of the year and as high as 10 percent unemployment at some point next year.

I spoke to 10,000 angry United Auto Workers on Wednesday. They want Congress to understand that every decision we make should be designed to put them and the other 7 million unemployed Americans back to work. In Massachusetts, nearly 10 percent of my state's labor force is jobless. It would be irresponsible to permit an energy program that threatened to add more men and women to the unemployment rolls to take effect.

Before the House Ways and Means Committee, a series of economists testified to the potentially devastating impact of the Ford energy program on the chance for economic recovery.

Dr. Robert Gordon, of the University of California at Berkeley stated of the energy program: "The inflationary effect is self-evident. Oil products will rise significantly in the price. At the same time, there will probably be a net depressive effect on the level of economic activity."

Dr. Joseph A. Pechman, director of economic studies, at the Brookings Institution testified: "The proposed taxes on petroleum are, unfortunately, an ill-advised approach to the energy problem. These taxes will be counter-productive in two respects: first, they will raise prices substantially—certainly more than the direct 2 percent effect to be felt initially—as the effect of the petroleum tax increases is pyramided through the economy; second, on balance, they will depress demand, because $6.5 billion of the $30 billion tax increase will be used to reduce the corporate tax rate, reduction that will have little effect on corporate spending at least in the short run. Thus, the energy program will be inflationary and deflationary at the same time."

Walter W. Heller, former chairman of the Council of Economic Advisors, now regents professor of economics at the University of Minnesota, testified: "President Ford's 30–30 energy program would deal a fourth blow to the economy—another double whammy that would boost inflation and worsen recession."

Paul A. Volcker, now a senior fellow at Princeton's Woodrow Wilson School of Public and International Affairs, testified that the President's energy program "could be another drag on business activity. . . ." He added, "Much clearer is the upward impact on the price indices, which I suspect the official 2% estimate understates significantly in seemingly accounting only for the direct price effects on oil and from the new taxes."

Philip Klutznick of the New York investment bankers, Salomon Brothers, testified: "The Administration estimates that for the average family it would mean a hike in their energy bills on the order of $250 or $300 a year. Counting indirect costs, the bill will be substantially higher. . . ."

Finally, Mr. Chairman, Arthur Okun, former chairman of the Council of Economic Advisors, testified: "Nonetheless, one aspect of energy policy looms as a dire and imminent threat to our economy. If the President levies the indicated tariff on imported oil and all oil prices are decontrolled before any offsets to these measures are enacted, the President would be draining real income away from the American consumer at the enormous annual rate of nearly $30 billion. I cannot believe that the President intends to risk a depression in order to hasten Congressional action on his energy proposals. Yet his own recent words point in that direction. The Congress must ensure against any such ruinous action—if possible, by appealing to the President's good judgment; but, if necessary, by restricting his statutory powers over tariffs and mandating the extension of price ceilings."

Mr. Chairman, these are the warnings of eminent economists of both parties who fear the consequences of the energy policy on the nation's economy.

I share their concern; and taking them at their word, I believe the most responsible course of action available is to approve H.R. 1767 and delay the $3 per barrel tariff for 90 days.

I would like to emphasize for a moment that it is not only the economists who fear the impact of this policy. The people of this country fear its impact.

I believe they are ready to sacrifice and to do their share to attempt to meet the need for reduced consumption. But they do not believe the way to do it is by raising the prices of every fuel by 20 to 30 percent and by seeing the rest of the goods and services they require jump in price as well.

The President's goal is to reduce consumption. Yet, a tariff and additional excise taxes at the wellhead are the least accurate way of achieving the goal. His program is a shotgun attack that inevitably will hit a great number of innocent victims.

The greatest reduction expected—even under the most positive estimates of the FEA—is not in gasoline, where virtually every observor believes we should focus our reduced consumption. Instead, it is in residual oil that simply makes very little sense at all. We will be directly under-cutting the ability of our industries to compete. Nor is there any consideration of conservation measures already put into effect.

Thus, even though home heating users in Massachusetts have dropped their consumption by 20 percent in the past year, they would find their heating bills—which have doubled in the past year—hit by a 30 percent increase. They have their thermostats set at the lowest possible level now and it would be unfair and unrealistic to expect any additional consumption savings.

With price hikes spread across the board, affecting home heating oil, residual as well as gasoline, I am afraid that—other than gasoline—the anticipated reductions in consumption.

My region is perhaps one of those which will be affected most severely by the President's proposal. We depend on petroleum for 85 percent of our energy. The nation as a whole depends on oil for only 46 percent of its energy use. In addition, we rely on foreign imports of crude for 30 percent of our oil and foreign imports of products for another 40 percent of our oil. The national average for foreign imports of both crude and products is only 32 percent.

It is evident that any tariff—whether it falls on crude or on products—will strike New England and the other heavy importing states heavier than most other parts of the country.

In fact, the Administration's estimate of the increased annual direct energy costs for New England is exceedingly low. They assume an annual hike of $180 per household. I should add that that in itself is a 14.5 percent hike. However, a New England Regional Commission study shows a range of between $228 and $321 added direct costs. That is a 18½ percent to 26 percent increase. Those are enormous added costs for an average family, particularly when you realize that almost one out of every ten members of the Massachusetts labor force is unemployed today.

Nor do those price hikes include any estimate at all of the ripple effect added fuel costs boost the cost to the consumer of other goods and services. The Library of Congress has estimated that incerase to be between 1.5 and 2 times the direct cost increase. The impact on our consumers and on consumers across the country will be immense.

Mr. Chairman, let me summarize the reasons why I believe it is essential that this bill be adopted by the Senate.

First, I believe the President's imposition of oil import fees will create the gravest economic damage to American consumers and American business. It will take between $55 and $60 billion out of the pockets of American consumers and it will make it far more difficult for American business to succeed against foreign competition. Its chief effect will be to raise prices and to depress an economy that already has seen industrial production plummet and unemployment skyrocket to the worst level since the depression.

Second, it is inequitable. It will place the most severe burden on those least able to bear the burden—the poor, the elderly, and the unemployed and on those regions which already have suffered the most severe increases in the cost of their energy. Massachusetts and New England now pay 30 percent more for energy than the rest of the nation. The President's program will directly increase those costs.

Third, I believe it is inappropriate for a major policy decision—such as the increase in tariff fees of such magnitude and the lifting of price controls on old oil—to be taken without full Congressional consultation and without any prior public participation in the decisionmaking process. I believe the procedure used by the President was inadequate and possibly illegal. In amending Section 232 of the Trade Act I believe we intended that only in the most dire emergencies would the opportunity for public participation be denied. Also, I believe there is a requirement for the Federal Energy Administration, prior to implementing the President's proclamation, to follow the National Environmental Policy Act procedures.

Finally, I believe that there is serious question whether the tax and tariff program announced by the President will have the desired effect of reducing consumption.

For all those reasons, Mr. Chairman, I believe it is essential that we sidetrack the unwise and deflationary energy proposal of the Administration. With a 90-day delay I am convinced that we can develop a credible energy policy that will be consistent with economic recovery which must remain our primary objective.

The CHAIRMAN. Senator Jackson?

STATEMENT OF HON. HENRY M. JACKSON, A U.S. SENATOR FROM THE STATE OF WASHINGTON

Senator JACKSON. Mr. Chairman, I shall be very brief. I want to associate myself with the able remarks of the Senator from Massachusetts. I think he has stated the case very well. I would only add one or two comments.

It is difficult to discern the rationale behind the administration's proposal. I suspect that they are saying that raising the tariff will slow down imports. I would say the real effect of it is to slow down the economy, and to accelerate the rate of inflation.

Therein lies the whole problem. We are in a serious recession. Remember that a year ago last month then President Nixon said there would not be a recession, and he guaranteed there would not be a recession. President Ford has now very forthrightly said we are in serious trouble, and he has projected ongoing high unemployment. We already have over 7 million Americans fully unemployed. And this does not take into consideration those individuals who have given up looking for jobs, nor does it take into consideration people who are working only part time. And when you add those three components together, I believe Mr. Schultze could answer better than I could, but I think it is around 10 million underemployed or unemployed.

So we have to address ourselves to the real, fundamental question of the impact which the administration program will have on the economy. It slows the economy. It accelerates the rate of inflation. This is simply the wrong remedy to deal with the problem of energy conservation.

I would like permission for my statement to be placed in the record together, may I say, with some very able remarks corroborating what I have said by Mr. Charles R. Owens, who formerly served in the administration as Deputy Assistant Administrator for the Federal Energy Administration in charge of oil price control policy. He stated yesterday at our hearings in the Interior Committee that he believes the President's program is based on several highly dubious assumptions, and he lists those. And I ask that other pertinent testimony by Paul Ignatius, head of the Air Transport Association, also be placed in the record. He gave just one example of the ripple effect if the entire administration program were carried out. He advised our committee that as many as 50,000 people could be laid off, and that airline fares could be increased by 15 percent.

I think this is simply illustrative of the ripple effect which Mr. Siedman indicated may add—in addition to the $31 billion that covers the cost of the tariff, the excise tax and the decontrol of old oil—another $25 billion in costs, as Senator Kennedy has mentioned, for a total package of about $60 billion. If you allow for only a $31 billion tax rebate or cut, you still are taking about $25 billion out of the economy at a time when it is sliding downhill.

Thank you very much.

[The prepared statement of Senator Henry M. Jackson with accompanying material follows. Oral testimony continues on page 54.]

Statement of Senator Henry M. Jackson

Mr. Chairman, Members of the Committee, I am pleased to appear before this Committee with my distinguished colleague from Massachusetts. Your Committee has before it a House passed bill, H.R. 1767, a measure which would prohibit for a period of ninety days the imposition of new tariffs, fees and quotas on oil imports.

We are at a significant crossroads in the effort to resolve our Nation's energy crisis fairly and sensibly. Decisions in the weeks and months ahead will set this country on a course which will not be easily altered. I am confident that the Congress will take decisive action based on a reasoned and thoughtful examination of the merits of alternative energy conservation programs.

The President's energy price and tax proposals would, if implemented, result in intolerable price increases for all energy consumed in the United States. With the President's proclamation increasing the fees on imported oil by $1.00 per barrel, we are already thrust down the road to "prohibitive" energy pricing. If Congressional inaction allows the President's program of import fees and domestic crude oil prices decontrol to take effect, American consumers will pay an additional $33.6 billion in higher energy costs. This amounts to nearly $150 for each man, woman and child in the United States, nearly $600 for an average family of four. These enormous cost increases would affect all petroleum products and would quickly spread to other energy sources—coal, natural gas, uranium—which compete with oil in the United States. These price increases will push up the cost of all goods and services in all regions of the country.

I believe the President's program contains the seeds of economic disaster for the United States, without substantially improving our energy situation. It will depress an economy already on the brink of depression. It will also perpetuate double digit inflation. By attempting to achieve long-term energy goals in the short run the Administration's program will create economic chaos: higher energy prices, more bankruptcies, more unemployment, more inflation, a captive foreign policy, and a weakened economic position for domestic companies which engage in international commerce.

The Joint Resolution which Senator Kennedy and I have introduced requires that the Congress be consulted on these proposals before they are implemented, that each proposal be fully justified as to rationale and impact, and that the Congress have the right of disapproval. Our resolution and the House passed bill provide time for Congressional participation and deliberation leading to the development of a fair, sensible and effective energy conservation program.

We have already learned much about the disruptive economic potential of the President's proposals. Yesterday the Interior Committee and representatives from other committees participating in the Senate's National Fuels and Energy Policy Study, heard testimony from representatives of industry, electric utilities and higher education. The testimony was as alarming as it was informative. The President's program would:

Increase fuel costs for one segment of the transportation industry alone—the airlines—by $1 billion, which could lead to a 15% increase in air fares or result in as many as 50,000 lost jobs;

Force universities and colleges to absorb higher energy costs, $1.7 million for one major university, necessitating tuition increases and a sharp curtailment in research and educational output;

Drive up utility rates to intolerable levels for business and consumers; and

Fail to limit energy consumption significantly because the demand for petroleum products is largely insensitive to price changes.

One witness, Mr. Charles R. Owens, who formerly served in the Administration as Deputy Assistant Administrator at the Federal Energy Administration in charge of oil price control policy stated that he believes "the President's program is based on several highly dubious assumptions". These include the assumption:

That a viable recession recovery program can be financed by regressive oil and natural gas taxes.

That demand elasticity for energy is significantly negative despite the contrary evidence over the entire post-World War II period. Even the past eighteen months, while admittedly exceptional, indicate almost zero elasticity.

That U.S. domestic oil production can be quickly turned around, even though under the two-tier price system U.S. output still declined by 10 percent or 900 thousand barrels per day from December 1973 to December 1974.

That exploration incentives would still be positive with the recommended excise taxes on oil, plus the excess profits tax.

That the cake is really worth the candle. A makeshift tax package—both on the input side and on the rebate side—has been constructed to show OPEC that we mean business, to put economic pressure on foreign oil producers, despite the fact that the amounts involved are only a minor fraction of producing capacity, and to prove to our European and Japanese allies that we are willing to make sacrifices. We strongly suggest that the potential strategic benefits of these "bargaining chips" ought to be balanced against a rigorous assessment of their costs.

Mr. Chairman, I would like to submit copies of this testimony for the Committee's hearing record.

Finally, Mr. Chairman, I would like to submit for the hearing record an economic analysis of the cost of the Administration's energy price, tax and tariff program which was prepared by the Interior Committee staff at my request.*

Table VIII of this analysis shows the significant effect of cost increases in the direct purchase of fuels and electricity and the even larger effect of indirect energy use on expenditures. Thus, for a poor family, approximately $125 in increased costs for direct energy purchases corresponds to nearly $340 in increased costs when purchases of nonfuel goods and services are accounted for. For middle-income families, $200 to $250 in increased costs for direct purchases of fuels and electricity become $500 to $700 in total cost increases per family when all purchases are considered.

This table also shows the disproportion between added energy costs and ability to pay. The poor must find extra cash to pay for a third as much energy as the well off, yet they must find this cash in an income which is on the average, only an 8th to a 10th as large. Thus, the basic requirements for food, shelter, heat, transportation, and essential clothing and manufactured goods place a floor on energy requirements which does not respect relative ability to pay. When basic energy prices increase, the burden falls much more heavily in proportion to ability to pay on the poor.

The table shows that added energy costs which the President's program would provide for will reduce the purchasing power of the poor by over 11 percent while for the well off, only 3 percent of income will be affected.

TABLE VIII.—INCREASED ENERGY COSTS FOR HOUSEHOLDS BY INCOME: DIRECT AND INDIRECT ENERGY PURCHASES

Category	Income [1] (1974 dollars)	Cost increases for direct energy purchases [2]	Cost increase for indirect energy purchases [3]	Total increases
Poor	$3,050	$124	$212	$336
Lower middle income	9,770	176	329	505
Upper middle income	17,000	242	506	748
Well off	29,900	287	657	944

[1] Income adjusted by the ratio of consumer price indices: December, 1971; December, 1972 = 1.221.
[2] Purchases of fuels and electricity for households; energy costs assumed to increase by 60 cents per MMBtu.
[3] Purchases of all products (food, automobiles, housing appliances, petrochemicals, services) dependent on energy; dollar-for-dollar pass-through of 60 cents per MMBtu is assumed.

Mr. Chairman, the President's energy program includes many proposals for whose adoption Congress has worked long and hard. These will receive early action and enjoy bipartisan support. His "prohibitive" energy pricing proposals have *not*, as the House vote indicates, received support.

*See Appendix B of this volume, p. 195.

I urge your Committee to act at an early date to report H.R. 1767 to the Senate floor. The sooner this ill-conceived Administration policy of huge increases in the tariff on oil imports, without any form of Congressional assent, action or review, is set aside the sooner Congress and the Administration can get at resolving the many difficult energy problems facing the nation.

STATEMENT OF PAUL R. IGNATIUS, PRESIDENT, AIR TRANSPORT ASSOCIATION

Mr. Chairman and members of the committee: My name is Paul R. Ignatius. I am President of the Air Transport Association which represents virtually all of the scheduled air lines of the United States. The airlines now account for more than 75% of all the intercity passenger miles provided by public transportation in this country, carry most of the first-class mail and thousands of tons of freight. To accomplish this, they use only about 4% of the petroleum consumed nationally.

I appreciate this opportunity to appear before the Senate Interior and Insular Affairs Committee to discuss the Administration's energy proposals, with particular emphasis on their impact on the airlines. The concern this Committee has shown for energy matters over an extended period of time and its continuing effort to insure that complex questions are resolved in a manner broadly serving the national interest are commendable.

Also commendable, I believe, are many features of the Administration's program. The airlines strongly endorse the following elements of the Administration's program:

Increased public education on energy conservation;

Activation and development of naval petroleum reserves;

Development of a strategic petroleum storage system;

Establishment of thermal efficiency standards for new buildings;

Tax credits for home insulation;

Expanded research and development of alternative energy sources; and

Continued petroleum product price controls, including incentives to allocate a greater share of costs to gasoline as a conservation measure.

We disagree, however, with the Administrations plan to impose new taxes on crude oil and to decontrol domestic oil prices. Our objection arises from the adverse impact these proposals would have on the airlines and other common carriers and because we believe they would add to the twin problems of inflation and recession that affect the U. S. economy.

On December 9, 1974, at a hearing before a panel of cabinet officers chaired by Secretary of Commerce Dent, I made the following comments on behalf of the airlines:

"As noted in the "Project Independence" Report, near-term achievement of our energy goals can be attained only on the demand side of the energy equation—conservation, and in the transportation sector, any appreciable savings are likely to come only from improved auto efficiency and shifts from the private auto to public transportation. Public transport modes, including the airlines, must be assured adequate supplies of fuel at reasonable prices. In this connection, we believe that for the present at least, existing price controls on domestic crude oil should be retained and that consideration be given to their extension to areas of domestic crude production not now under price control.

If the government believes that economic methods, such as taxes, are needed to trigger a shift from private to public transportation, it is important that the methods be in consonance with the objective. Thus, a tax on fuel used in public transportation would be inconsistent with the objective, and in addition force inflationary price increases on users of public transportation."

A month later, on January 9, 1975, at a press conference in Washington, I responded to a question on crude oil taxes that the press thought likely to be included in the Administration's program. I stated:

"The principal purpose presumably is to reduce consumption of petroleum. I don't think anybody whether he is an individual or a representative of a company or industry can do anything other than support efforts to reduce consumption. We clearly have to do it, and I think everyone who has studied the situation has concluded that.

At the same time I am hopeful that whatever programs are proposed and adopted designed to reduce consumption of fuel at the same time don't add to the inflationary pressures that are already present, or worsen the economic situation that is already present. And in that regard, I would be concerned if public transportation found it necessary to pass through in the form of substantially higher fares the amount of a new tax on petroleum. My reason is not difficult to explain. If the trucks and the trains and the busses and the airlines have to pass through this tax to the users of transportation, then the cost of everything will go up whether it is a loaf of bread or a pair of shoes or whatever."

When the President announced his energy proposals in his State of the Union message on January 15, 1975, they contained the tariff and tax on imported and domestic crude oil, and the intention to decontrol the price of "old" oil on April 1, 1975. Knowing of the concern expressed by the airlines about these proposals, FEA Administrator Frank Zarb invited me to meet with him on January 18th. Mr. Zarb told me that he and other members of the Administration understood that the energy proposals might have a severe impact on the airlines, and that the Administration's plan to lessen the impact of higher fuel prices through a reduction in the corporate income tax rate from 48% to 42% would be of only limited value to the airlines. Without in any way suggesting at that time that the Administration was prepared to make any adjustment to lessen the program's impact on the airlines, Mr. Zarb nevertheless said he was anxious to obtain additional factual information in order to have a better understanding of the extent of the problem. We have had subsequent discussions with Mr. Zarb and his staff and other Administration representatives, and I wish to commend them for the interest they have shown.

IMPACT ON THE AIRLINES

Let me now review briefly the impact on the airlines of the Administration's energy proposals. We believe that the proposals could increase our annual fuel costs by about $1 billion, as follows:

The 2/bbl. excise tax on domestic and imported crude would cost the carriers in their domestic operations about $400 million annually.

Decontrol of the price of domestic crude would cost the carriers in domestic operations about $500 million annually.

In addition to these costs, totaling some $900 million, there would be added costs of about $100 million due to the use of domestic fuel in international operations of U.S. carriers.

It is important to note that increases of this magnitude—and the amount will vary from about $1 billion to about $900 million depending upon estimates of projected fuel consumption—would be on top of the overwhelming price increases for jet fuel already sustained by the airlines. During 1974 the price of jet fuel doubled for domestic airlines and tripled for U.S. international carriers, adding approximately $1 billion to airline costs. Sizable fare increases were requested and approved but the additional costs have still not been fully recovered. With air travel markets in a weakened condition as a result of the general economic downturn, the airlines understandably are reluctant to raise fares again in order to recover additional fuel costs.

At the request of Administrator Zarb, the Air Transport Association's staff prepared estimates of the impact of the Administration's energy proposals under several different fare and capacity assumptions. These preliminary estimates are being reviewed by Administration officials. While the estimates are tentative in nature and do not necessarily represent what the aggregate of individual carrier decisions might actually be in dealing with the proposed fuel cost increases, they nevertheless reveal the general extent of the problem. The principal points emerging from the tentative analysis are these:

The airlines face a difficult year in 1975 quite apart from the problem of the proposed fuel cost increase.

The added costs of the Administration's energy proposals, amounting to approximately triple the total airline industry profits for 1974, could result in double-digit domestic fare increases as well as fewer flights, employee lay-offs, and forced grounding of valuable airline equipment—all in the face of a troubled national economy.

If the domestic trunk airlines attempted to absorb these added costs without a fare increase at a load factor of 65% (as some Administration analysts have suggested), it is estimated that capacity would have to be reduced by 25%, thereby denying air transportation to a large number of communities and individuals requiring it. In addition, between 450 and 500 aircraft would have to be grounded and between 45,000 and 50,000 airline employees would have to be furloughed. The impact of these increased costs on the operations of local service, all-cargo, and U.S. international airlines would be similar and would significantly increase the adverse effect on the nation's air transportation system.

If, on the other hand, the trunk lines attempted to deal with the problem by raising fares, the amount of the needed increase would depend upon the reduction in capacity that was tolerable from a public service standpoint. At a 15% fare increase, capacity would have to be cut by approximately 11%, aircraft grounded would total 250–275, and from 25,000–30,000 employees would have to be furloughed. Again, the effect on local service, all-cargo, and U.S. international airlines would magnify the problem.

The analysis leads to an unmistakable conclusion: the effect of the fuel cost increases on the airlines and the public service would be devastating with or without a fare increase. There is no magic solution such as raising the load factor that will make the problem go away. Airline managements more than most people understand the importance of higher load factors as a means of increasing profitability, but this approach is simply not a feasible way to deal with the problem of fuel cost increases of this magnitude.

Accordingly, we have told Administration officials that some way must be found to cushion the impact of these enormous cost increases if we are to have a viable air transportation system. This could be accomplished by exempting the airlines and other common carriers from the proposed increases. Various methods could be employed to accomplish this purpose, such as timely rebates, or exclusion of jet fuel from the pass-through of increased costs stemming from the Administration's program.

While adjustments of this type appear to us to be necessary within the framework of the Administration's proposals, the airlines continue to believe that the Administration and the Congress should adopt a different approach to the energy problem, one which, in the words of a New York Times editorial on January 31, 1975, avoids "the socially destructive consequences of dealing with the energy problem through reliance on indiscriminate price increases for essential and nonessential fuels alike." This leads me to the concluding comments of my statement.

CONCLUSION

The nation's scheduled airlines believe that the time has indeed come for serious action on energy policy and conservation strategy. That action should involve both the Executive and Legislative branches of government, as well as significant contributions from the private sector, and should proceed in an expeditious manner.

The airlines strongly support conservation efforts which will insure the most productive use of our energy supplies. Airline management and employees have already instituted conservation programs which resulted in savings of about one billion gallons of jet fuel in 1974 while, at the same time, carrying about six million more passengers. Government has a significant role to play in such efforts by providing tax and economic incentives for elimination of wasteful consumption. At the same time, government policy must recognize that a satisfactory level of economic performance requires substantial energy consumption and that an unfocused and abrupt across-the-board slash in energy consumption can cut unnecessarily and severely into our economic muscle.

Government policies which would impose substantial additional fuel costs on already hard-pressed industrial users, public utilities, and common carrier transportation would be inflationary and could add to the recession. Moreover, such measures fail to deal with the central problem of limiting consumption of gasoline. The airlines support limitations on the consumption of gasoline and believe that consideration should be given to measures designed to achieve this purpose. For example, in an editorial on February 3, 1975, arguing for a tax on gasoline rather than on all oil products, the *New York Times* pointed out that while gasoline prices had gone up about 37%, "far higher percentage increases hit other fuel prices: diesel fuel went up 49%, home heating oil 66%, aviation fuel 100%, and residual fuel oil, used in industry and electric utilities, a staggering 143%."

The airlines certainly recognize that sound government policy also requires adequate incentives for exploration and development of our domestic energy resources. They know that cheap oil is a relic of the past and that a more reasonable long-term price for petroleum is required by the changing world balance of supply and demand. However, the airlines believe that if the OPEC cartel price is embraced by the United States, it could accelerate inflation, prolong the recession, and unduly injure energy-dependent industries.

I appreciate this opportunity to state our views. We are hopeful that Congress and the Administration together will develop a program that will provide the necessary conservation of energy without adding to the nation's severe economic problems. I will be pleased now, Mr. Chairman, to respond to any questions that you and the members of the Committee may wish to raise.

Statement of Charles R. Owens

Mr. Chairman, my name is Charles R. Owens. I am President of Charles Owens and Associates, consultants on energy, economics and public policy. I am accompanied by Dr. Charles H. Jepsen, Executive Vice President of our firm and Michael D. Ware, Senior Vice President. Until July of last year I was Deputy Assistant Administrator for Policy, Planning and Regulation at the Federal Energy Administration and before that the Director of the Energy Division of the Cost of Living Council. While in government, I was intimately involved in the development of current oil import policies, oil price control policies and the Mandatory Petroleum Allocation Program.

I appreciate your invitation to comment on the economic impact of the Administration's energy price, tax and tariff program and on national energy policy generally. There is substantial confusion about this nation's energy policies, especially as they pertain to oil. Much of that confusion stems from the fact that our oil policies have undergone abrupt shifts in response to radical changes in supply conditions. For example, for more than a decade before 1970 U.S. policy was to keep oil prices up and supply down. Since 1970 our policy has been to keep oil prices down and supply up. Now President Ford proposes to keep prices up and supply down; but, at least some members of Congress want to keep prices down and supply down, too. Because these are each credible policy options, a little confusion is understandable. Let me explain.

PRE-1970 OIL POLICIES

Since World War II, and particularly in the past two decades, Federal and state governments have felt it necessary to maintain a major presence in the petroleum industry to influence both prices and supply. Supply conditions here and abroad have tended to be the dominant factor in shaping government oil policy, while a deep-seated free enterprise philosophy has tended to restrain government intervention into the day-to-day operations of our oil markets. The nation's fundamental policy has been to encourage the maximum interplay of free market forces limited only by the need for stable prices and adequate supplies as a matter of national interest and security.

During the long period of stability prior to 1970 there were more than ample supplies of crude oil at comparatively stable prices. These prices reflected a supply influenced by prorationing and conservation policies of the states, which limited production to meet "requirements," and the Federal program to restrict oil imports. Throughout the late 1950's and 1960's domestic crude prices were substantially above foreign crude prices. This disparity reflected not only the restraints on imports through voluntary and mandatory import quotas, but also the willingness of state regulatory authorities, particularly in Texas and Louisiana, to reduce allowable production significantly below the rated capacity of particular wells and fields. Foreign prices reflected abundant supplies from very low cost production sources especially in the Middle East, sources which were developed after World War II. They also reflected a vigorous trend toward lower per-barrel shipping costs with increased tanker size.

This, then, was a period in which government policies kept domestic prices above world price levels by keeping market supply down through import quotas and state prorationing. At the same time, Federal import policies were designed to retard the trend toward increased reliance on foreign supplies. Nevertheless, the share of U.S. oil needs supplied by imports grew as a result of a special exemption to the quota system granted for residual oil imports into the Northeast and the generally lower landed costs of foreign crudes.

The transition from a comparatively stable market to one of shortage and disruption began in the late 1960's and accelerated after 1970 through a combination of related developments, including the following:

No new major construction of U.S. refining capacity was undertaken in the period from late 1969 through 1972, a situation due largely to uncertainty over the outcome of the government's review of Federal oil import restrictions.

Domestic crude production ceased to grow and declined after 1970.

Natural gas production, which had increased rapidly during the 1950's and most of the 1960's, stopped growing significantly during the 1970's. This slackening, together with environmental restraints and declining productivity in coal, threw most of the burden of U.S. energy growth onto oil at a time when our domestic oil sources were approaching full production.

A series of interruptions in foreign production and transportation in early 1970's reduced the availability of foreign crude and increased its delivered price in U.S. ports.

Growing cohesiveness and assertiveness of the producing countries led to increased taxes and royalties on their crude exports. This in turn led to higher costs of crude oil imported into the United States.

POST-1970 OIL POLICIES

The mix of rising prices, increasing foreign dependence and declining domestic production required a shift from the old policy to hold down supply and to support prices to one of holding down prices and bolstering supply. Following an unsuccessful attempt in 1970, U.S. imports policy was re-written in early 1973 to allow the free flow of imported oil into this country under a schedule of modest license fees to encourage domestic production and refining. State prorationing ceased to be a factor and the Federal government moved to control directly the prices of oil in 1973 under the Economic Stabilization Program, which began in August 1971.

Since 1973, U.S. policy has been to allow essential foreign supplies into the U.S. to stimulate declining domestic production and to restrain prices. These new goals spawned the current Mandatory Oil Imports Program and such programs as the two-tier crude pricing system which is an attempt to both stabilize domestic crude prices and encourage increased domestic exploration and production. A complete new fabric of government policies to control oil prices was developed and the emergency created by the Arab embargo and production cutbacks of 1973–74 brought about the development of the Mandatory Petroleum Allocation Program.

POLICY CONTINUITY

What has escaped many people is that despite the abrupt shifts in U.S oil policies, the objective of our policies has been the same for the last quarter century. The objective has been stability. Although changes to adapt oil policies to changing supply conditions have been less than timely and decisions to make those changes have been somewhat agonizing, that objective has not changed. Thus, for all intents and purposes our government has been operating a stabilization program for oil, much like the Economic Stabilization Program of Phases I, II, III and IV, for more than two decades. Like the Economic Stabilization Program, oil stabilization policies have gone through phases. The current oil price control system devised under the Economic Stabilization Program is simply a variation, or a second phase, of the oil policies begun in the 1950's. The only difference is that these controls were designed to accommodate different supply conditions. Nevertheless, price stability and a vigorous domestic industry to protect us from excessive foreign dependence have and continue to be the driving forces behind our national policies and U.S. energy policy generally.

As we examine new proposals to give us added protection from becoming irreversibly dependent on foreign sources for essential supplies, we must not lose sight of the long-standing objective of oil price stability which in recent years has been pursued largely through anti-inflation policies. Further, we must continue to balance the need for oil price stability with the need to stimulate expansion of domestic exploration and production. Finally, we must hold fast to the fundamental precept that has tempered government intervention in the operations of the petroleum industry and oil markets throughout the post-war era. We must continue to encourage the maximum interplay of free market forces within a range limited only by the need for stable prices and adequate supplies, which are essential to general economic growth and stability and national security.

We are now in the throes of revising our oil and energy policies to achieve a new goal: energy conservation. We have turned to it as a further step to avoid becoming irrevocably dependent on foreign sources for our basic oil requirements. For reasons which are unclear a goal has been set to reduce oil imports by 1 million barrels per day by the end of this year. President Ford has extended that goal to include a reduction of 2 million barrels per day by the end of 1977. Two basic approaches to achieving this goal have been advanced. One by the President which involves the utilization of high prices and taxes to reduce consumption and thus imports and to allocate available supplies largely through the free market mechanism. The other approach is to reduce imports by a direct system of quotas and to allocate available supplies through a rationing system. I will discuss both of these approaches before proposing my own.

THE PRESIDENT'S PROGRAM

The main thrust of President Ford's proposed oil and natural gas tax increases is to discourage consumption and thus reduce U.S. dependence on imported oil. Higher prices are to be the driving force. The President increased import fees by a dollar per barrel on both crude oil and products on February 1. He plans further dollar increases on March 1 and April 1. He has asked Congress to levy a two dollar per barrel excise tax on domestic crude oil and a roughly BTU equivalent tax on natural gas of 37 cents per thousand cubic feet.

Under the President's proposed program oil costs would go up by more than the amount of the proposed tax increases, since decontrol of domestic old oil price is included in his proposed package. The overall effect would be to push the average crude oil price from about $9.00 per barrel to about $13.25 per barrel—a 47 percent increase. Inasmuch as there was little observed reduction in demand as a direct result of the more than doubling of domestic crude prices and the quadrupling of foreign oil costs over the past year and a half, this 47 percent increase in prices is unlikely to generate much change in demand. Nevertheless, the thesis that oil demand can be reduced substantially through higher prices is the cornerstone of the President's program. For that reason, I want to discuss the concept of demand elasticity.

RECENT EXPERIENCE

The 1973–1974 price/demand history for U.S. motor gasoline was clearly more involved with physical supply demand factors than with price generated demand elasticities. While month-to-month changes did involve random factors, the pattern of price movements and gasoline consumption between 1973 and 1974 was too pronounced to be mistaken.

The main elements of this pattern included a sharp decline in consumption in the last quarter of 1973, resulting from reduced product allocations to gasoline dealers, limited service station hours, long gasoline lines, and some hoarding. This decline continued into the first quarter of 1974, when jawboning, the 55 MPH speed limit, and individual conservation measures kept demand from drastically outpacing supply. Prices could not significantly increase until the first quarter of 1974 because cost recovery under Federal price rules limited their upward flexibility. The OPEC mandated price increases, plus the near-panic buying of crude oil by some companies at $18 per barrel and higher, pushed U.S. pump prices up to 55 cents per gallon in September 1974. This constituted a 44 percent price increase over a 12 month period.

Trying to impute demand elasticities during a period of supply stringency is clearly ill-advised. Any valid measure of demand elasticity must span a period of reasonably comparable gasoline availability. October 1973 to October 1974 probably comes closer to satisfying that condition for this analysis than any other set of dates in the 1973–1974 period. Between those two dates, pump prices increased by 44 percent, and total gasoline demand increased by 0.3 percent.

The October-to-October increase in gasoline demand was well below the postwar trend but was above what would have resulted provided any significant demand elasticity with respect to price. In addition, economic activity was declining during the period. Gasoline demand has a good positive correlation with economic activity, particularly industrial production. From October 1973 to October 1974, U.S. industrial production declined 1.7 percent. Constant dollar GNP also declined, but by only 0.1 percent.

HISTORICAL DEMAND ELASTICITY

Beyond last year's experience, post-World War II history does not support the thesis that changes in energy prices have any significant impact on energy demand.

We have carefully examined the relationship between price and demand for our most important oil product, motor gasoline; and we find no grounds in the historical record for optimism about the potential success of the President's program. Since World War II, gasoline demand has closely tracked trends in economic activity. The best year-to-year correlations have been with industrial production and constant dollar disposable personal income. Significantly, the only two years when U.S. gasoline consumption actually declined were 1974 and 1946, which were also the only two years that both industrial production and constant dollar personal income declined.

Any attempt to show a simple systematic correlation between gasoline demand and gasoline price for the period from 1946 to 1973 is doomed to failure. The data simply do not support it. The evidence in fact is slightly against a negative correlation between price and demand. Using deviations from trend growth rates, the correlation was more often positive than negative. When price went up demand went up, and when price went down demand went down in 16 of the last 28 years. In the other 12 years, the reverse was true; when price went up, demand went down and vice versa. This clearly shows there has been no significant demand elasticity with respect to U.S. gasoline prices in recent times.

A careful analysis of the data discloses a more complex and more reasonable explanation of the relationship between gasoline price and demand. Depending on the period involved, the driving forces in the market were dominated either by supply or demand. Events external to the gasoline supply/demand relationship determined which one was crucial in any period.

To be specific, in 1947 and 1948 gasoline prices rose faster than normal, reflecting efforts to catch-up following wartime price controls. Demand was sluggish until 1948, with reconversion to a peacetime economy and slow growth in auto population. From 1953 until the early 1960's both price and demand increases were below normal, reflecting the slow economic growth of that period. The next major pertubations came in the early 1970's, when several factors affected both sides of the supply/demand equation. These included lower gas mileage from new automobiles, world oil supply shortages in late 1972–1973, the 1973–1974 OPEC decreed price increases and the impact of Arab cutbacks on supply.

The structural reasons for this interaction of disparate supply/demand relationships as determinants of price—rather than the mistaken assumption that price largely determines demand—are quite straightforward. Gasoline use is essentially derived. That is, Americans buy gasoline as a minor input to the service of transportation. Since there are few substitutes for transportation, and practically no substitutes for gasoline, we should expect little causal relationship between price changes and demand.

Since the Administration has put special emphasis on an overall tax on oil, we should note that higher prices generally may inhibit oil demand overall more than in gasoline. This judgment is based on two considerations. One is that demand in the non-automotive sectors is more easily associated directly with price. Homeowners can dial down thermostats and wear sweaters. Industrial users will tighten controls on energy use and install energy-saving equipment. The second is that BTU-equivalent incentives to shift to other fuels are increased for those consumers with existing or potential dual-fired capability.

The sum of these two factors should yield a higher demand elasticity for total oil than for gasoline alone. But since gasoline currently represents some 35 percent of U.S. oil product demand, this seriously inhibits the capability of the Administration to cut overall oil consumption by a tax on oil. It is difficult to expect the relatively modest price increases proposed by President Ford to have a perceptible effect on U.S. oil demand. Short-term, without rapidly deepening recession, the results may appear to be promising. But after adjustment for changing economic activity, it seems highly unlikely that the Administration's conservation goal, i.e., a million barrel per day reduction in imports by year-end, can be achieved by the methods the President has proposed.

REVERSING THE DECLINE

In addition to its forecast elasticity effects on oil demand, the Administration assumes that the incentives provided in the President's program will halt the current decline in U.S. crude production by the end of this year. This decline is listed as 400 thousand barrels per day per year in the program, but the December 1973 to December 1974 decline was actually 900 thousand barrels per day. While it is too early to judge the medium-term effects of current exploration incentives, even the most favorable results could hardly turn around our domestic crude oil picture in less than three or four years.

DECONTROL OF PRICES FOR CRUDE OIL

Decontrol of "old oil" prices is a central feature of the President's energy proposals. The program specifies removal of price controls on domestic crude oil by April 1, 1975, subject to possible Congressional disapproval. Given the intent to increase import fees by at least $2.00 per barrel, old oil, now priced at an average $5.25 per barrel, would move directly to about $13.00–$13.50 per barrel. To prevent what might be regarded as excessive profits, the President is recommending a windfall profits tax on the increased revenues. The intention of the windfall tax is to recapture the bulk of the "excessive profits" generated by price decontrol but at the same time to leave significant incentives for expanded exploration efforts.

In this regard, the program appears to have been put together too hastily. The combination of crude oil excise taxation and the very large old oil crude price increase that would ensue would provide less incentive to find oil than does the present two-tier crude price system. While there is some ambiguity in the explanatory language issued by the White House, the wellhead pre-income tax realizations on old oil would be actually lower than they are today if the Congress also enacts the recommended $2.00 excise tax. The following tables illustrate this point.

TABLE I.—BUILDUPS OF WINDFALL PROFITS TAX, PLUS RECOMMENDED EXCISE TAX

[Dollars per barrel]

Crude price	Windfall tax	Realization after windfall tax	Recommended excise tax	Realization after both windfall and excise taxes
$5.20	0	5.20	2	3.20
$5.40	.03	5.37	2	3.37
$5.70	.12	5.58	2	3.58
$6.40	.54	5.86	2	3.86
$8.20	1.98	6.22	2	4.22
$11.25	4.72	6.53	2	4.53
$13.25	6.52	6.73	2	4.73

TABLE II.—IMPACT OF WINDFALL PROFITS TAX ON VARIOUS MIXES OF OLD/NEW OIL

	20/80	40/60	50/50	60/40	80/20
Average price per barrel	$9.84	$8.68	$8.10	$7.52	$6.36
Price per barrel in excess of base	4.64	3.48	2.90	2.32	1.16
Windfall profits tax rate	1.98+	1.98+	.54+	.54+	.12+
	.9(1.64)	.9(.48)	.8(1.70)	.8(1.12)	.6(.66)
Windfall profits tax [1]	3.46	2.41	1.90	1.44	.52
Average price net of tax	6.38	6.27	6.20	6.08	5.84

[1] Assumes December 1, 1973 old oil price plus 95 cents equal $5.20 per barrel. And new oil price equal $11 per barrel.

Moreover, it is highly unlikely in our judgment that there can be agreement on an appropriate windfall profits tax prior to decontrol. Devising an equitable tax and moving it through Congress and the Executive will very likely take months and possibly years to accomplish as a practical political matter.

QUESTIONABLE ASSUMPTIONS

Fundamentally, we believe the President's program is based on several highly dubious assumptions. These include the assumption:

That a viable recession recovery program can be financed by regressive oil and natural gas taxes.

That demand elasticity for energy is significantly negative despite the contrary evidence over the entire post-World War II period. Even the past eighteen months, while admittedly exceptional, indicate almost zero elasticity.

That U.S. domestic oil production can be quickly turned around, even though under the two-tier price system U.S. output still declined by 10 percent or 900 thousand barrels per day from December 1973 to December 1974.

That exploration incentives would still be positive with the recommended excise taxes on oil, plus the excess profits tax.

That the cake is really worth the candle. A makeshift tax package—both on the input side and on the rebate side—has been constructed to show OPEC that we mean business, to put economic pressure on foreign oil producers, despite the fact that the amounts involved are only a minor fraction of producing capacity, and to prove to our European and Japanese allies that we are willing to make sacrifices. We strongly suggest that the potential strategic benefits of these "bargaining chips" ought to be balanced against a rigorous assessment of their costs.

OVERALL IMPACTS

Full implementation of President Ford's energy program would have several major economic impacts. One is negative growth for the U.S. oil industry for the medium-term and probably longer, due to the drop in refining and marketing sales volume anticipated as a result of higher prices. Negative growth in oil may be accompanied by sharply-reduced overall economic growth. Economic activity in the U.S. has for decades been closely linked to growth in energy use. And while a reasonably-based conservation program may over the medium-term allow us to alter this close correlation, there is a considerable short-term danger that a single-minded pursuit of energy-conservation irrespective of other national goals could have disastrous consequences.

Inflationary impacts would not be confined to oil and gas prices, but would spread to competing fuels. Specifically, we could expect sharply higher spot coal prices and longer term price increases for contract coal, since the President did not propose to limit coal revenues. The rough BTU equivalent price for coal to oil at $13.25 per barrel is $52.50 per ton. Spot coal prices currently range around $40 per ton. Coal producers' eagerness to take advantage of higher spot coal prices will mean increasing lags in deliveries to contract buyers whose lower prices are protected by tight escalation clauses.

There would be an immediate increase in energy costs for major industrial consumers of oil and gas, particularly public utilities. Whether this will be a serious problem for particular industrial consumers is mainly a function of their ability to pass on increased costs to their customers. However, depending on the importance of energy to the industrial user and the competitive conditions existing at the time of the increase, these costs will take the form of higher prices to consumers for a wide range of products in a relatively short period. One of the lessons of the Cost of Living Council's Phase IV decontrol process is that a more gradual pass through, a spreading out of the price bulge if you will, can reduce the ultimate size of the increase and permit a more orderly adjustment process.

Decontrol of new natural gas prices would allow gas prices to rise to parity with oil prices. Intrastate gas prices could be expected to rise to oil parity as well. Both would mean a substantial boost in producer profits and the incentive to find more natural gas.

There would be increased incentives for growth in energy production in hydrocarbons, coal and other energy sources. However, at least initially, the President's program does not provide as much incentive for expanded crude production as does the current two-tier crude pricing system.

PROBABLE OUTCOME

If President Ford's energy program were to be implemented in its present form, we foresee a high probability of the following sequential scenario:

Several months of agonizing over whether consumption is declining enough to meet strategic import goals.

Recognition that the U.S. energy structure does not permit a quick expansion in domestic energy production.

Institution of mandatory oil import quotas to avoid "excessive dependence" on foreign supplies.

Insufficient supplies available to satisfy demand, leading to rationing for motor gasoline and stricter allocation of other major petroleum fuels.

Transition from surplus to deficit in our oil supply/demand balance, leading to a firming of oil product prices and an increase, although not a major one, in domestic inflationary pressures.

Long-term price and allocation controls, and increasing utility-type regulation of the petroleum industry.

To summarize, we have two main reactions to the President's oil tax and conservation proposals. The first is that the tax package was ill-considered. It is inflationary, regressive, uneven in its impact, and almost certain to be less than effective. While the marriage of convenience between the President's anti-recession spending program and the potential revenue from the oil and gas tax package was apparently irresistible, the fact remains that it is a bad tax program, not the least because it gives little positive incentive to expand domestic oil and gas availability.

Our second reaction is that the President's program would set a dangerously unrealistic timetable for its results. A more gradual tightening of our belts would allow more time for the necessary adjustments to be made on both the demand and supply side. I am speaking of technical improvements in energy use, improved recovery from existing reserves, and the development of new coal mines, with their associated transportation infrastructure. On the oil and gas exploration side, the economic incentives of the two-tier crude oil price system have been operating for less than a year and a half, which is hardly time to develop significant new oil. Nonetheless, I note that U.S. wildcat completions increased 25 percent in 1974 over 1973, and that another sizeable increase is forecast for 1975.

Despite our lack of enthusiasm for the President's program, his forthright presentation and support of it has provided the fundamental impetus to evolving a policy to address the nation's energy problems. If that is the kind of leadership the country needs, the President has provided it.

IMPORT QUOTAS AND RATIONING

The current alternative option to the President's program is immediate and abrupt import controls and rationing to achieve a 1 million barrels per day import reduction. Such controls would soon entail increased government involvement in all sectors of the energy industries. They would also have serious implications for the economy overall and for specific industry sectors. One important question is how much of a cutback can be sustained over a reasonable period without seriously inhibiting economic growth. This question will become all the more critical as current recessive economic trends continue into the year and political pressures grow for further government stimulation of the economy.

Installation of a program to force down oil imports by 1 million BPD would generate a requirement for tighter controls on prices and allocation of all oil supplies, including oil currently free from controls.

The most onerous aspect of this approach is gasoline rationing. An effective rationing program will require a Federal bureaucracy of 17–20 thousand persons and cost over 2 billion dollars a year to administer. Furthermore, there are serious operational difficulties associated with rationing that have not been addressed. These include the manageability of a coupon system having to serve 150 million drivers, the potential for inequities and abuses of such a system, and the inherent evils of a government deciding who is most in need of transportation.

For the producer abrupt import quotas and tighter price controls would mean a ceiling on new and stripper oil prices and probably the allocation of all uncontrolled oil. Without this ceiling, prices for uncontrolled oil would be driven up to politically, as well as economically, unacceptable levels. Allocation would be regarded as essential, once a ceiling was set for uncontrolled oil, to avoid illicit price competition for these supplies. A ceiling on new and stripper oil might well lead to an end of the two-tier system for pricing crude, with a single price for crude set at about $8 per barrel. This would eliminate the need for refiner crude cost equalization and thus would be an attractive option for Federal energy policy makers.

For the refiner, an immediate limit on imports would mean reduced growth or no growth with sharp increases in refinery margins and per barrel profits initially. As under the Arab embargo, crude availability would become more important than crude cost as price becomes a secondary consideration to consumers. Crude availability would be a function of Federal allocation and import controls. Domestic earnings also would be a function of Federal controls on prices and profits. Foreign earnings for international companies could be restricted as other consuming nations attempt to control imports and oil prices and supplies.

As for marketers, drastic mandatory import limits would mean a return to conditions experienced during the Arab embargo of last winter. Supplies will be tight, margins will be at maximum levels and growth will depend primarily on non-petroleum sales. Supplies will be especially tight for gasoline marketers, given the President's emphasis on reducing gasoline consumption. Price controls will again be a source of agitation and controversy.

An abrupt limit on imports means a limit on supplies plus higher prices for consumers. It would require long run shifts in consumption patterns and levels, with increased energy efficiency as one of the key factors to growth. Without well-developed mass transit systems to take up the slack, transportation industries would be most directly impacted, especially those dependent on gasoline availability. The leisure industries, hotel and motel trade would follow as transportation is immediately curtailed. The net effect would be serious economic disruption in these sectors with consequent impacts on lifestyle and mobility.

The most persuasive argument against this alternative in my judgement has to do with the level of government involvement in the energy industry required to make it work. A massive bureaucracy governing all segments of the energy industry would effectively snuff out what is left of the free market forces in the energy marketplace for the long term. Nationalizing the industry in this way would have dire consequences for the economy as a whole and should be avoided at all costs.

OUR SUGGESTED PROGRAM

We believe that a program that is less extreme than either the President's plan to cut consumption through higher prices or the immediate imposition of stringent import controls and rationing can both move us in the right direction and leave us the flexibility to adjust to future changes in our energy supply/demand situation. We have developed a program that is consistent with this belief. Our program has four primary elements. They are:

1. *A system of graduated import quotas* that would become gradually more restrictive over the next several years as determined by the need for tighter import controls in future.

2. *Retention of the Mandatory Petroleum Allocation Program*, which as an option appears to have widespread support, combined with a vigorous mandatory conservation program aimed at avoiding rationing and maximizing the interplay of free market forces to allocate supplies.

3. *A system of quota offsets* to maintain the viability of the oil industry by allowing prices to rise under the current oil price control system to recoup the revenues lost to them due to the decline in sales volumes forced by quota limitations.

4. *The gradual phasing out of the two-tier system* for crude oil prices, to minimize the inflationary impact of higher oil prices and to provide on a timely basis the additional capital essential for expanded exploration and production without the inequities, distortions and complexities of an "excess" profits tax.

1. A System of Graduated Import Controls

We would recommend a goal to reduce imports by 3 to 5 percent, or about 250,000 b/d by the end of this year. The nation could probably achieve this goal as a result of demand reductions caused by the current recession. However, vigorous conservation measures could offset the expected decline in domestic oil production of roughly 400,000 to 500,000 b/d. The combination of these two actions could mean a decline in total consumption in the neighborhood of 750,000 barrels per day. Achieving the goal of 1 million b/d reduction in imports, however, would require a doubling of this reduction in total consumption and result in a cutback of about 1.5 million b/d.

By the end of 1976 a target of 5 to 7 percent reduction in imports could be set providing for review of the wisdom of such an additional cutback prior to its limitation. By the end of 1977, the nation might reach for a 10 percent reduction in imports, but again only after reviewing the wisdom and necessity of such a move based on conditions that exist at that time.

Such a program would not have the drawbacks of dramatically higher prices and associated inflation nor would it require immediate rationing. It could well be a means to avoiding rationing altogether. However, it would be a direct step to reduce imports and would demonstrate to our allies and world oil producers that this nation is moving to reduce its dependence on foreign oil and is prepared to go further in the future. In addition, this approach is superior in that it provides energy producers and users alike with reasonable certainty as to the amount of energy that will be available to them for near-term planning purposes. The importance of this aspect cannot be overstated.

2. Retention of the Mandatory Oil Imports Program Combined with Mandatory Conservation Measures

A reduction in imports will require the allocation of available supplies. Combined with vigorous conservation, however, the primary purpose of an allocation program could be to assure reasonable equity and to support price stability rather than to spread the hardship of an enforced shortage.

Balancing import reductions against achievable levels of conservation would avoid rationing, or at least delay it until we have squeezed all the possible conservation out of the system. Further, gradually increasing conservation requirements is likely to produce greater conservation and far less economic distortion and dislocation than the immediate institution of rationing. Finally, it will give us time to reap at least the initial benefits of stimulative measures to increase domestic production as well as any efficiency gains we might achieve.

3. A System of Quota Offsets

Neither the President nor Congress has proposed to decontrol prices of oil products. As a consequence, any reduction in imports will reduce total industry revenues and thus reduce industry profits and opportunities for growth. The refining and marketing sectors of the industry would be hardest hit by such cutbacks since any reduction in the total supply of oil would result in a corresponding reduction in refiners and marketers' sales. These sectors are essential to the production and distribution of oil products and are normally the least profitable sectors of the industry. Any appreciable reduction in imports is certain to spell serious decline for them.

Maintenance of a healthy economy is heavily dependent on an adequate and reliable flow of oil. Therefore, any reduction in refining and marketing revenues forced by a reduction in oil imports should be offset by allowing the industry the opportunity to recoup those revenues through higher prices. Refiners and marketers should have the opportunity to raise prices and free market prices should be allowed to determine what levels of price will be sustained. Higher prices would be consistent with the President's approach to reducing consumption, but in no way would such a system of quota offsets involve the substantial inflation or recessionary prospects of the President's program.

4. Gradual Phasing Out of the Two-tier System

From virtually the moment I completed the design of the two-tier system, I have steadfastly maintained that it should be done away with. However, I have also steadfastly maintained that it should be done away with gradually, at a rate that would avoid dangerous inflation in oil prices but at the same time would provide on a timely basis the additional capital essential to maintain a level of exploration and production sufficient to avoid irreversible foreign oil dependence. In his program the President has proposed to do much the same thing but through a cumbersome and complicated "excess" tax that phases out over five years. My recommendation is that the Congress simply avoid the tax and authorize the President to phase out the two-tier system.

This approach has the virtue of striking and maintaining a balance between price stability and timely incentives for increased exploration and production. There is no question that gradually higher prices for oil would be involved. That, again, is somewhat consistent with the President's program.

Mr. Chairman, those are the basic tenets of our recommended program. I look forward to discussing them with you and the other members of the Committee. This concludes my prepared testimony. Thank you.

Testimony of Guy W. Nichols

"Modifications to the Old Oil Allocation Regulations and to the Price Regulations"

My name is Guy W. Nichols, and I am President and Chief Executive Officer of New England Electric System which, through its retail subsidiaries in Massachusetts, Rhode Island and New Hampshire, provides electric service to approximately one million electric customers. In addition, I am speaking for the New England Power Pool representing electric utilities serving some 97% of the electrical customers of New England.

Only four and one-half months ago, I testified before the Federal Energy Administration at rulemaking hearings on FEA's proposals for the allocation of old oil, two of which proposals offered both New England and other major regions of the country some short-run hopes of parity in regard to both price and supply of "fuels".

I pointed out in my testimony that the savings of such parity to New England could be several hundred million dollars and that any savings the New England electric companies incurred would automatically benefit all electric customers in our region through the operation of fuel adjustment clauses. I also indicated that a system of regulation was already in effect to assure this pass-through and that I was not sure that such a claim could be made as emphatically for any other segment of the energy industry.

The FEA apparently recognized the need for parity in price and supply of "fuels" by, in its final regulations on old oil allocation issued at the end of November, creating an entitlement program whereby some of the cost benefits of old crude oil flow to importers of certain products. While the program did not go as far as we might have wished to relieve the burden upon those regions of the country dependent on imported products, it nonetheless was a step in the right direction and exhibited an attempt by the FEA to comply with that provision of the Emergency Petroleum Allocation Act of 1973 which mandates—

"Equitable distribution of crude oil, residual fuel oil, and refined petroleum products at equitable prices among all regions and areas of the United States and sectors of the petroleum industry and among all users."

We have supported, and will continue to support, efforts by the Federal Energy Administration to carry out this equitable pricing mandate of the Emergency Petroleum Allocation Act of 1973.

In a little over two weeks, the FEA's effort to alleviate some of the economic burden borne by those regions of the country relying on imported oil, which culminated in the old oil entitlement program, has become past history. We are now back at square one, invited here today to comment upon amendments to the FEA regulations that will remove imports from the entitlement program and, by doing so, take away those benefits which were, only recently, much heralded as easing the economic burden for regions like New England. The impact of the elimination of old oil entitlements for imports, when combined with the remainder of the program for oil imports recently set forth by President Ford, will be devastating upon the economy and the people of New England.

New England is almost twice as dependent upon oil for its energy needs than the United States as a whole. Annually, it uses approximately 160 million barrels of residual fuel oil, nearly one-half of which is used in the production of electric energy, and almost all of which is imported. The President's program for oil imports means an increase in the amount of New England's annual residual fuel oil bill of over $280,000,000, $96,000,000 of which represents the loss of old oil entitlements, based on a value of 60 cents per entitlement.

The news media is replete with many other statements and statistics concerning and documenting the devastating impact which President Ford's oil import program will have upon New England. I will here only emphasize that behind the statistics are people, including electric customers, who will suffer as a result of the President's oil import program, of which the elimination of old oil entitlements for imports is but one part.

We hope that the Administration's statements concerning reducing the hardships of the program for oil imports on any geographic region are more than mere rhetoric. But, to date, those statements have not manifested themselves in any concrete form with regard to New England and other regions similarly situated. All we see is the imposition of a large supplemental fee on imports and a proposal to take away the benefits from importers of old oil entitlements. Both have a disasterous impact on New England. We ask that this concern manifest itself, that the mandate of the Emergency Petroleum Allocation Act of 1973 be carried out, and that, to address the subject of today's hearings, old oil entitlements for imports not be eliminated.

I now turn to the Federal Register notice dated January 22, 1975 concerning the proposed amendments to Parts 211 and 212. I was originally prepared to ask the Federal Energy Administration what, I believe, was a crucial question raised by that Federal Register notice relating to the "rebates" from oil import license fees. The White House fact sheet relating to the President's State of the Union Message, a page 33, spoke of these rebates being "approximately $1.00 in February, $1.40 in March, and $1.80 per barrel in April." Various other statements made by the Administration used these figures and led one to believe that the $1.80 rebate would continue beyond April. And, Presidential Proclamation No. 4341 used the rebate figure of $1.00 for February, $1.40 for March, and $1.80 per barrel for April, 1975 "and thereafter". However, the Presidential Proclamation also stated, and I should emphasize, that "the Administrator may by regulation reduce the fee payable by the following amounts, or by such other amounts as he may determine to be necessary to achieve the objectives of this Proclamation and the Emergency Petroleum Allocation Act of 1973".

There was, therefore, at least an implication that the $1.00, $1.40, and $1.80 might very well not be the figures to be used by the Administrator of the FEA. And, the four full paragraphs contained in the second column of page 3468 of the January 22, 1975 Federal Register, I believe, confirmed the fact that not only might rebates not be these figures, but might be substantially less or nothing at all. The consequences of this was that the ultimate impact of the President's oil import program could have been the total amount of the license fee, or $3.63 per barrel, in addition to the value of the loss of any entitlements. The four paragraphs I have referred to describe the manner in which the FEA was to compute the rebate. It was to be composed of two components, one of which was the current entitlements benefits and the other an amount that would equalize the impact of increased fees on products with the increased import fees on imported crude oil, taking into account also the corresponding increased price of uncontrolled domestic crude oil. If one runs through the figures, he quickly reaches the conclusion that if the price restriction was removed from old oil, the rebate would have shrunk or disappeared. The question I was going to ask of the Federal Energy Administration was this: Will the rebates be the fixed figures of $1.00 for February, $1.40 for March, and $1.80 for April and the ensuing month thereafter or will they, in fact, be determined by the language set forth in that Federal Register notice and, consequently, possibly become zero. However, the FEA has hopefully clarified the matter by, in its amendments to the Oil Import Program, announced January 28, 1975, netted the $1.00, $2.00, and $3.00 fee with the aforementioned rebates to produce fixed supplemental fees of zero for February, $.60 for March, and $1.20 for April and months thereafter. I have used the word "fixed" describing these supplemental fees and, while not conceding either their validity or their fairness as to amount, hope that the FEA also views them as fixed in the sense of being maximum fees for the term of the program and does not plan on employing the January 22, 1975 Federal Register formula, which I have mentioned, to increase their amount.

As to the proposed modifications relating to price regulations, we are pleased that the FEA has now recognized the severe economic inequity caused by the failure to accord "special product" treatment to residual fuel oil, with the result that increased costs can be and have been disproportionately allocated to this product. At the same time, we believe the proposed modifications to the price regulations fall short of providing the needed assurance that residual fuel oil will not continue to bear an unfair share of increased costs.

The present price regulations allow increased costs attributable to special products (gasoline, No. 2 heating oil, and No. 2-D diesel fuel) to be allocated to other products such as residual fuel oil. A brief look at the wholesale price index for the past two years shows that increased costs have indeed been loaded onto residual fuel oil and other products rather than placed on gasoline.

[1967=100]

	December—			Percent of 1972 price
	1972	1973	1974	
Gasoline	107.7	140.3	203.2	190
Jet fuel	[1] 100.0	118.1	210.7	210
Middle distillates	113.9	171.7	300.1	260
Residual fuel oil	158.8	281.4	514.8	320

[1] February 1973.

Under the proposed modifications to the price regulations, refiners would no longer be allowed to allocate increased costs attributable to No. 2 oils or gasoline to residual fuel oil. However, in grouping residual fuel oil together with aviation fuel and such other products as kerosene, butane, benzene, naphtha, and propane in the new category of "general refinery products" and allowing the allocation of increased costs to any product within that category, the FEA is making it likely that residual fuel oil will continue to carry increased costs properly attributable to other products. Take aviation fuel as an example. Over the past 2 years, it has approximately doubled in price—while residual fuel oil has more than tripled. Under the proposed modifications, refiners could continue to load increased costs attributable to aviation fuel on to residual fuel oil. In these times, the fact that there is a relatively inelastic demand for residual fuel oil, because voluntary conservation has already taken place, should not be the basis for unfairly loading increased costs onto this product while allowing other products with more elastic demands to carry less than their fair share of increased costs.

About 30% of each barrel of oil is used to produce the products in the "general refinery products" category—and of this 30% about one-quarter is used for residual fuel oil. Thus, there is considerable potential for loading increased costs from such other "general refinery products" as aviation fuel onto residual fuel oil, causing it a vastly disproportionate share of costs.

Accordingly, I urge that the proposed changes in the price regulations be modified so as to assure that residual fuel oil, like the No. 2 oils, will not have to bear increased costs attributable to any other product.

In conclusion, I urge that the electric consumers of New England not be asked to bear more than their fair share of the costs of any energy program and that the old oil entitlement program not be eliminated for importers of residual fuel oil.

On behalf of the New England Power Pool and New England Electric System, I thank you for the opportunity to comment on your proposed amendments and will be pleased to answer any questions regarding my remarks.

STATEMENT BY BEN H. FUQUA, SENIOR VICE PRESIDENT OF FLORIDA POWER & LIGHT COMPANY

Mr. Chairman, I appreciate the opportunity to appear before your Committee.

The electric service provided by Florida Power & Light Company is highly dependent on imported residual fuel oil, and this statement is made on behalf of the Company and its one million seven hundred thousand customers.

The present unreasonably high price of imported residual fuel is wreaking havoc on Florida's economy, working a hardship on millions of electric customers and doing violence to the financial, social and political fabric of our State.

Now, faced with even greater, and continuingly disproportionate burdens from actions taken by our own Government, the Congress and the Executive Branch must recognize Florida's circumstances and allow an exemption for our State from the proposed import levy on imported petroleum products.

There is consumed in the State of Florida upwards of one hundred million barrels of residual oil per year, of which about thirty-five million barrels will be consumed by FPL. Nearly all of this residual fuel oil is imported.

We testified and submitted a written statement at the hearing held by the Federal Energy Administration on the allocation of old oil last September. At that time, a graph (copy attached) of residual fuel costs showed that our costs per barrel had reached $11.96 in July 1974, up from $4.24 in one year. Since that time, there have been further increases, and we have just received notification that the cost of our imported residual fuel oil would be increased thirty cents per barrel effective January 25, 1975. This new increase is the result of action by the Government of Venezuela. The new delivered costs of imported residual fuel oil per barrel at various plants on our system are now at almost $13.00 per barrel, and are tabulated as follows:

Palatka	$12.93	Pt. Everglades	$12.68
Sanford	13.00	Riviera	12.72
Cape Canaveral	12.82	Ft. Myers	12.87
Cutler	12.73	Lauderdale	12.78
Turkey Point	12.7525	Miami	12.88

At the hearing last September, we stated that we had received information which we assumed to be reliable to the effect that the adoption of either Alternative No. 3 or Alternative No. 4 being considered at that time would result in lowering the price we would pay for imported residual fuel oil in amounts that were estimated from $2.00 upward per barrel. This was the so-called equalization or entitlements program. We had high hopes for some relief as a result of these proposals. However, as far as we know, there has been no relief up to this date. It is reported that our importer has received certain entitlements which it is further reported he has been unable so far to sell. Further activities are being taken to dispose of these entitlements, but the final result is unknown. It appears, however, that no relief even approaching the above estimate is in prospect. The entitlement program, as you know, was a development growing out of the Congressional mandate that product prices across the Nation should be equalized.

We appeared at the briefing on the matter of import fees on residual fuel oil held at the Executive Office Building in Washington on January 16, 1975. At that time, we undertook to describe our unhappy and deteriorating situation in Florida in respect to imported residual fuel oil which is so vitally necessary to us.

In the proposed FEA rulemaking now under consideration pursuant to the President's Order No. 3279, import fees will be raised $1.00 per barrel in February, March and April for a total increase of $3.00 per barrel. However, rebates or offsets are to be allowed so that the effective fee on imported residual oil will be zero for February, sixty cents per barrel for March and $1.20 per barrel for April. It is stated these rebates are calculated to reduce product import fees by an amount equivalent to the benefit that would have been provided under the entitlements program. This is supposed to provide some equalization for those geographical areas of the country (of which Florida is perhaps the most notable example) which are unduly and disproportionately burdened by the present outrageous price of imported residual fuel oil. While we strongly support the intent of the President's proposals for energy independence, we have an obligation to our customers to protest actions that will further burden them with disproportionate fuel costs.

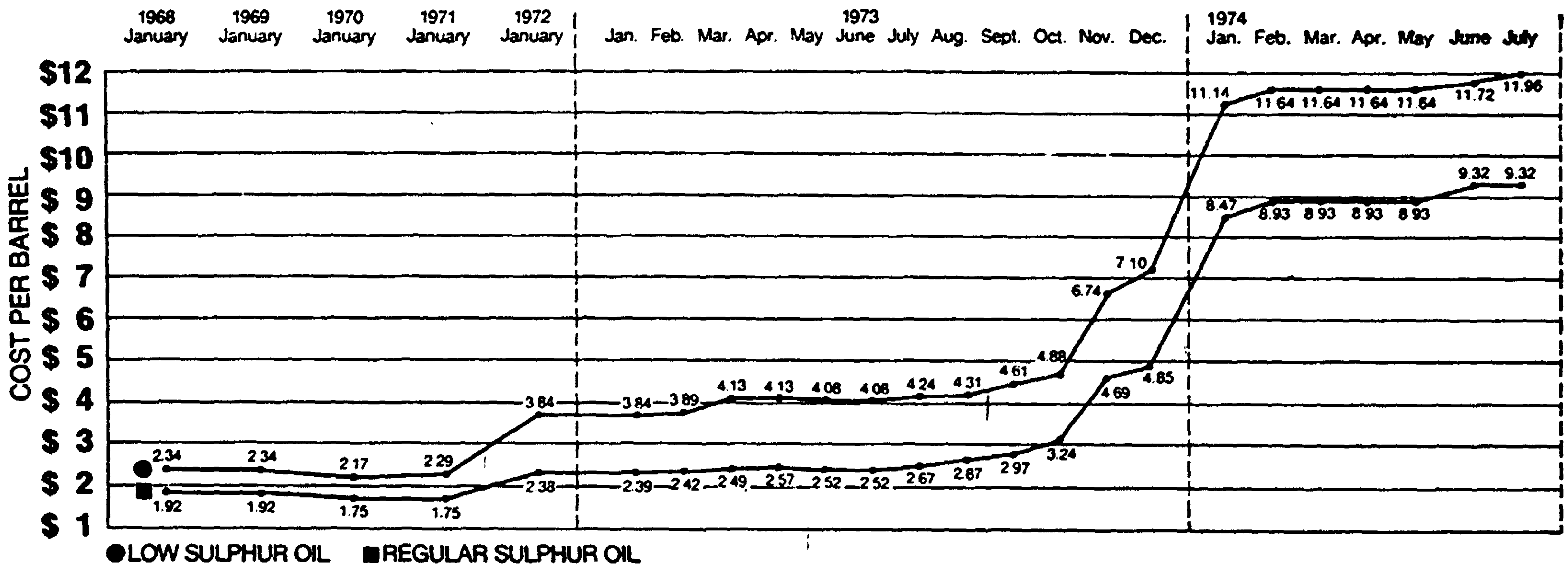
We are continuously trying to help ourselves. FPL is actually drilling for oil in Florida. We have sent teams to the Middle East and to Venezuela trying, so far without success, to work out contracts for oil at lower cost. We have been examining coal as a fuel and are studying coal supplies, both domestically and in Colombia. We have been pushing ahead on nuclear power plants to the best of our ability. We were heartened by President Ford's statement in regard to nuclear energy. We hope the licensing period can be reduced drastically, so that these much needed facilities come on the line promptly. We have two nuclear plants on the line now, one unit scheduled for 1976 and another unit for 1980. Nonetheless, we now have the high dependence on fuel oil which will continue for some time to come.

Quite obviously as we have stated before, we are opposed to the levying of the import fees on our imported residual fuel oil at all. If the $1.20 proposed for April 1, 1975, is made effective, it is seen that the delivered cost per barrel of our imported No. 6 residual fuel oil will be on the order of $14.00 per barrel, and at some plants even more than that.

Fuel costs are passed on to our already overburdened customers, many of whom are retirees and living on fixed incomes. Some of the cost is necessarily absorbed by the Company because of the time lag. During the eighteen months ending December 31, 1974, the electric bill paid by our average residential customer using 1000 KWH has increased 33%, all due to increase in fuel costs. Our average residential customer using 1000 KWH now pays a bill of $33.15 per month. If the $1.20 tariff on imported fuel oil is levied, it will increase the average residential customer's bill by $1.10 per month. The thirty cents which the Venezuelan Government levies will add another twenty-eight cents to this customer's bill.

The cost of imported residual fuel oil is so high in Florida now that it is unfair and unreasonable to add any import fee or tariff to the cost per barrel. Florida Power & Light Company serves approximately one-half of Florida with electric service. Of the many pressures and problems that beset our Company and our customers, the most burdensome load of all is the enormous cost of imported residual fuel oil. We protest any action by our own or other Governments to further add to this intolerable burden. Thank you.

FPL'S FUEL OIL COSTS SOAR



AMERICAN COUNCIL ON EDUCATION,
Washington, D.C., January 29, 1975.

MEMORANDUM

From: Charles B. Saunders, Jr., Director, Office of Governmental Relations
Subject: Impact of the President's Energy Proposals on Colleges and Other Nonprofit Institutions

To identify the potential impact of the President's energy proposals on the higher education community, the American Council on Education and the National Association of College and University Business Officers requested John F. Embersits, Director of Operations at Yale University, to conduct the study which is attached.

Colleges and universities throughout the country must do their share to contribute to the national effort to reduce energy consumption and strengthen the economy. However, the Embersits study makes clear that the President's proposals would impose particularly heavy fuel costs on institutions of higher education, as well as private schools, hospitals, museums, and other nonprofit institutions. This cost burden is unique because the President's proposals to date make no provisions for nonprofit institutions. This omission has been called to the attention of top officials in the Federal Energy Administration and other agencies of the Executive branch, who are currently studying possible amendments to their initial proposals.

In the meantime, the proposals now under review by the Congress pose the following problems for colleges and universities:

1. There is no provision for the exemption from excise taxes and import fees traditionally accorded nonprofit educational institutions.
2. Nonprofit institutions are not included in the proposals for revenue redistribution through tax refunds for individuals, corporations, utilities, and agencies of State and local government. Thus nonprofit institutions alone bear the full brunt of the proposed tariff and taxes on foreign and domestic petroleum products.
3. The tariff and tax proposals accordingly would result in staggering increases in fuel costs for colleges and universities, many of which are already in precarious financial condition and unable to pass their increased costs along to their "consumers," the students and their families.
4. The proposals are unlikely to effect significant reductions in the fuel consumption of many colleges and universities, which have already made substantial efforts to reduce their energy consumption.

The attached report also outlines a series of positive recommendations to relieve nonprofit institutions from undue financial burdens of higher energy costs, and to stimulate the search for new economies in energy consumption.

IMPACT OF ADMINISTRATION'S ECONOMIC AND ENERGY PROPOSALS OF JANUARY 15, 1975 ON NON-PROFIT EDUCATIONAL INSTITUTIONS

(By John F. Embersits, Director of University Operations, Yale University; David I. Newton, Project Analyst, University Operations, Yale University)

On January 15, 1975, in his State of the Union message, President Ford outlined programs designed to strengthen the economy and to reduce national energy consumption. Colleges and universities will be subjected to hardships unintended by those who have authored these programs; hardships which will place an excessive financial burden on non-profit institutions without stimulating further conservation activities. It is the purpose of this brief memorandum to outline the major areas of financial and energy discrimination which impact educational institutions and to suggest actions which can aid colleges and universities in working toward the President's national goal of energy independence. The serious nature of the financial pressures plaguing colleges and universities cannot be exaggerated, nor aggravated by otherwise constructive attempts to stabilize the nation's economic and energy posture.

This document will illustrate the magnitude and scope of the cost impact of the \$3.00 crude oil import fee upon educational institutions, emphasizing the absence of revenue redistribution afforded other sectors of the economy in the President's program and the lack of exemptions traditionally given to non-profit educational institutions. The failure of the current program to stimulate further energy economies in educational institutions will be highlighted as a major shortcoming. The petroleum product pricing policies as developed by the Federal Energy Administration (F.E.A.) and executed by the major oil companies have resulted in a pattern of discrimination against residual oil consumers, a major energy source for non-profit institutions. Finally, the report makes recommendations for relief to colleges and universities in ways which will reduce consumption while avoiding the financial burdens which are explicit in the current Administration proposals.

An accurate composite of the financial impact for all educational institutions is impossible to assemble in a short time. For that reason, the energy costs experienced by Yale University are highlighted as an attempt to represent those with which other institutions must contend. Yale is a complex private educational institution, with resident graduate and undergraduate degree programs, a full range of federally-sponsored research, and a medical center engaged in the delivery of health care at the research, teaching and clinical levels. As such, it represents, in microcosm, the problems facing educational institutions involved in one or more of the above-mentioned activities.

I. FINANCIAL IMPACT OF THE $3 IMPORT FEE

A new $3.00 per barrel import fee passed on to residual oil will have a significant impact on many non-profit educational institutions. Brown University estimates an increase of $420,000 should the cost of residual oil increase by $3, while Princeton predicts an increase of $600,000. Similarly, the University of California at Berkeley is burning fuel oil which costs $15.95 per barrel, thus any increase would pose serious financial problems. Even a relatively smaller secondary institution such as the Lawrenceville School estimates an energy cost increase of over $60,000 as a result of the import fee proposals. In Yale's case, this increase would cause energy bills to rise by an additional $1,700,000—$900,000 for fuel oil and $800,000 for electricity. None of these increased energy expenditures result in improvement to an institution's educational or research output.

Prior to the proposed $3 import fee, Yale's annual energy bill had risen $6,300,000—from $2,400,000 in 1969/70 to $8,700,000 in 1974/75. While a rebate system for imported refined products is proposed to offset the full impact of the import fee, it is unclear that such a system will provide relief for many institutions—especially those burning domestically refined residual oil.

Many non-profit institutions rely either solely or heavily upon residual fuel oil as a primary fuel for the generation of steam and electricity, and many sectors of the country will be increasingly dependent on residual fuel oil as an energy source due to the trend of curtailments in natural gas. Dramatic cost increases may be expected as a result of the switch from gas to oil; some institutions' energy budgets will nearly double. Those institutions fortunate enough to still receive natural gas service will be severely impacted by the imposition of the 37 cents per Mcf excise tax on this commodity.

II. FEDERAL PRICING POLICY DISCRIMINATION—RESIDUAL OIL

Government pricing regulations explicitly discriminate against institutional users of residual oil. This discriminaton is manifest in two distinct policy positions expressed in the FEA pricing regulations:

1. Gasoline, 2-D diesel fuel and #2 heating oil are artificially subsidized. FEA pricing formulae prohibit the passing of full cost increases to these "special products."

2. Major oil companies have the flexibility to allocate to residual oils all increased costs which cannot be absorbed by the "special products." As a consequence, residual fuel oil prices have grown nearly 200 percent under FEA pricing regulations, or at twice the rate of the "special products" which have been protected from full cost absorption.

The new proposed Federal Energy Administration regulations (Federal Register, Vol. 40, No. 15) do not eliminate the discriminatory policy of the past year by "limiting the proportion of increased product costs that can be passed through and reflected in prices charged for the group of products, taken in the aggregate, consisting of all covered products other than #2 oils, gasoline and crude oil." However, the proposed regulations do not address the problem of past discriminatory pricing policy, and they still allow a refiner a great deal of discretion within the category of general refinery products:

"In apportioning the total amount of increased product costs allocable to general refinery products (i.e., all products other than gasoline, #2 fuel oils and 2-D diesel fuel), a refiner may apportion amounts of increased product costs to a particular general refinery product in whatever amounts it deems appropriate."

In sum, residual fuel oil will continue to absorb a disproportionate share of refinery costs which otherwise would have been absorbed by such general refinery products as lubricants, kerosene, naphtha, and aviation fuel a situation which aggravates the discriminatory cost absorption to which this product has been exposed during the past year.

III. CONSUMPTION REDUCTION

A fundamental test of the proposed energy program's effectiveness is its ability to stimulate conservation activity. Increasing the price of residual fuel oil will not measurably reduce its consumption nor the amount of crude oil which the nation requires. Residual fuel oil represents less than 7 percent of refinery output nationally. The non-discretionary demand for this product by utilities, non-profit institutions and geographic sections of our nation impedes efforts for significant short term consumption reductions.

This is particularly true for educational institutions which rely on residual fuel oil as the basic source for lighting, space heating, research activity, health care delivery and food processing. As such, the consumption of residual fuel oil is not discretionary; it is a usage which sustains the express purposes for which educational institutions have been chartered.

Most non-profit institutions have implemented energy conservation programs which have reduced fuel consumption to optimum levels. An increase in the price of energy will not stimulate such institutions to reduce further; it merely increases cost.

For example, Yale University will consume less residual fuel oil in 1974/75 that that used in 1965/66 and less electricity than that used in 1968/69, in spite of new building additions during this period totalling 1,000,000 square feet and a loss in combustion efficiency of 9 percent due to the use of low sulfur oil as required by the State of Connecticut. It is unlikely that similar consumption reduction performance can be projected for the future, regardless of the increased price of fuel. Further consumption reduction will be effected by withdrawal of basic services to the institutions.

IV. EXCLUSION OF NON-PROFIT EDUCATIONAL INSTITUTIONS FROM REVENUE REDISTRIBUTION

The President's program calls for a redistribution of energy fees and tax revenues to various sectors of the economy through a complex mechanism of tax refunds, investment credits, reduced corporate business taxes and incentives for directed utility expansion. The exclusion of educational institutions from sharing in this redistribution of energy surcharges and investment incentives is highlighted by the following factors:

1. No portion of the $30 billion revenue from higher energy surcharges will be refunded to non-profit institutions, even though they must pay the inflated energy costs.
2. An investment tax credit program and a reduction in the corporate tax rate from 48 percent to 42 percent will have no effect on non-profit institutions.
3. Capital support or other financial incentives designed to encourage energy conservation are not offered to non-profit institutions either for past projects or future plans.
4. Federal appropriations for sponsored research have been leveled. Increased energy costs and the consequent rise in indirect expenses will continue to reduce funds available for the conduct of scientific research, thereby further diluting the output of the scientific community throughout the nation. This human resource is one which the country can ill afford to waste.

V. POSITIVE PROGRAM FOR ENERGY REDUCTION WITH MINIMUM FINANCIAL HARDSHIP

Traditionally, non-profit educational organizations which are exempt from income tax under section 501(a) of the Internal Revenue Code, have also been exempt from excise taxes imposed by Congress and from import tariffs and fees imposed pursuant to Executive Orders. The special problems which the President's energy proposals will create for non-profit educational institutions would be eliminated if this traditional tax exempt status were to be applied to excise taxes on domestic crude oil and import fees on imported crude oil and refined products.

Should the Congress and the President elect not to exempt non-profit educational institutions from the import fee, they should recognize that these institutions will be severely penalized. Most non-profit institutions, unlike utilities and many business firms, cannot pass on their energy price increases directly to customers. In the case of educational institutions, "customers" are students who already suffer heavy financial pressures due to rising tuition, and research activities with limited funds which are unable to absorb increased costs of energy.

In the absence of tax exempt status and with a recognition of the precarious financial condition of many non-profit educational institutions, a series of recommendations is offered to relieve such institutions of increased financial burdens due to high energy costs and to stimulate the search for new energy economies:

1. Residual fuel oil, as an essential non-discretionary source of energy, should be afforded the same pricing treatment as #2 home heating oil and 2-D diesel fuel.
2. An institutional import fee and excise tax waiver for demonstrable energy economies utilizing a specific time designation, perhaps two years, as a measuring period.
3. An increase to existing federally sponsored research grants and contracts to cover the rising costs of energy to those institutions which have demonstrated consistent annual energy efficiencies.
4. Special relief to those federally sponsored grants and contracts for projects which incur direct energy costs as a result of energy intensive research.
5. New research programs and incentives for capital investments which reduce energy consumption or which afford conversion to more desirable energy forms.
6. A mechanism to recognize in financial terms the efficiency of the centralized production of energy for heat, electricity and food processing typical within colleges and universities.
7. Design and construction support for the development of new buildings with innovative energy support systems which otherwise might be built with conventional but less efficient energy systems.
8. Relief for those institutions which, under local and state environmental regulations, have expended capital to convert central steam, electrical and chilled water plants to "cleaner" fuels. Many previous conversions will have to be reversed in order to return to energy sources more compatible with emerging national energy policy.
9. The establishment of a joint federal/non-profit institutional panel for the review and approval of institutional energy conservation programs and performance.
10. The formation of a joint federal and non-profit institutional committee to aid smaller institutions which lack technical expertise in energy conservation, and to disseminate and co-ordinate energy conservation activities.

Testimony of John G. Buckley

My name is John G. Buckley. I am a Vice President of Northeast Petroleum Industries of Boston and a Vice President and Director of Energy Corporation of Louisiana (ECOL) a joint-venture between Northeast Petroleum and the Ingram Corporation of New Orleans, Louisiana. ECOL is presently building a 200,000 barrels daily fuel-oriented refinery on the Mississippi River about 35 miles up-river from New Orleans. I am a former Fuel Oil Chairman of the National Oil Jobbers Council and currently on the Steering Committee of the Fuel Committee of NOJC. I am also a member of the Utility Advisory Committee to the Federal Energy Administration, Washington, D.C. and a member of the Emergency Petroleum Supply Committee of the National Petroleum Council. During the past eighteen months I have visited almost all of the major oil producing countries around the world to negotiate crude oil contracts for our Louisiana refinery. I have met with and have had many discussions with Oil Ministers and other oil and financial officials from these countries and believe I have some understanding of their goals and aspirations at this time.

Senator Jackson, I would like to start by thanking you for the leadership you have displayed on this critical matter of energy policy during the past several weeks since President Ford announced the Administration's energy plan. Of course, your concern in this area is one of long standing and we independent companies understand and appreciate the role you have played in trying to assure more equitable treatment from national oil policy for the independent sector of the oil industry nationwide. Your hearings here this morning in Washington are just another example of your concern and continuing effort to make sure that this nation does not pay a disproportionate price for the achievement of a questionable objective. Clearly the cost of achieving national objectives should be borne equally by the nation.

In my statement this morning I should like to divide my comments into two parts:

The first dealing with aspects of the Administration's program which I believe deserve support and implementation by appropriate action by the Congress; and the second dealing with those parts of the Administration's program that I believe will be inimical to New England and to the nation as a whole.

On the positive side I strongly support the following points:

1. Development of strategic storage capacity designed to enable us to react quickly to offset the disruptive force of any future embargo, cutoff or curtailment of foreign petroleum supplies.

2. The production of oil from the Naval reserves at Elk Hill in California and the use of some of that oil in filling government-owned strategic storage facilities.

3. The establishment of tougher codes of insulation coupled with tax credits to promote residential and commercial insulation in order to cut waste.

4. The establishment of appliance efficiency standards.

5. Standby authority under which this Administration or future Administrations could react quickly in the event of an embargo situation, including standby rationing authority.

6. The development of incentives, tax and otherwise to transform or shift the emphasis in the automotive industry to the production of more efficient automobiles with better miles per gallon performance.

7. Increased federal effort in research and development of alternative energy sources.

All of these measures have something in common. In combination they tend to eliminate energy waste in our society and effectively conserve available energy resources. Moreover, they are long-term in nature and not designed as a "quickie" solution to energy problems.

I would now like to turn to other parts of the Administration's program on energy and list, if I might, some of the myths and inconsistencies in the high energy cost approach to achieving certain national energy objectives. These negative comments will fall in two categories, the first dealing with our current economic situation and the second dealing with the more fundamental and philosophical question of our future foreign economic and political policy world-wide.

1. The Administration's energy program is touted as a policy, which when coupled with the Administration's tax relief policy, will have an expansionary impact on our general economic situation this year. In fact, a detailed analysis of the combined effect of both the tax and energy proposals shows that the positive contribution of the tax rebate and tax restructuring is more than offset by the cost of the energy program. The Research Office of the New England Congressional Caucus notes that the combination of tariffs and fees on imports coupled with price decontrol and new taxes on oil and gas will take between $44 and 54-billion out of the economy. The Library of Congress research study puts the energy bill at just over $50-billion annually. The point is the Administration's tax proposal looks to tax relief in the neighborhood of $24-billion. Therefore, the net effect of the total Administration tax and energy program would be, if enacted, a $20-30-billion economic drag this year. Thus, we could end up with a $45-billion federal deficit, more recession and more inflation simultaneously. This is certainly not a prescription to help the United States economy at the present time.

On the human side unemployment nationally would have to rise probably to 9% or 10%. In New England the rates would be higher—much higher—with regional unemployment perhaps at 12% and in some states, like Massachusetts, ranging from 12% to as high as 15%. This is simply too high a price to pay for the achievement of narrowly defined energy objectives.

2. The Administration's energy package, drawn liberally from the computer projections in the FEA's Project Independence Report, takes far too narrow a view of both our own domestic economy and our economic role in the world economy. The goal of the Project Independence study was to reduce oil imports. The Administration seems to be following a policy designed to achieve that objective at any cost, even at the cost of ruining our national economy.

In contrast to this narrow Administration approach the Organization for Economic Cooperation and Development (OECD) has just completed a study on energy objectives for its member countries which, refreshingly, notes that "energy is not the only thing in the world that is important." The study, citing a capital investment requirement of over $2-trillion needed to achieve a high rate of energy self-sufficiency in the member countries, states that such an effort would mean a very large shift of resources into the energy sector. This, the study says "may be in conflict with other economic objectives and may consequently be undesirable."

In fact, the Administration's energy proposal would cost our economy $50-billion annually in increased energy costs—and perhaps $75-billion if the "ripple effect" of higher prices for other products based on energy is included. It represents a commitment to divert some $750-billion of purchasing power over the next decade into high-cost energy. In addition, the capital investment required would amount to some $750-billion to $1-trillion over the same decade. With that kind of resource commitment coupled with our military budget, it is hard for me to see how any other social, economic or environmental objectives can be met during the next ten years.

3. The Administration's plan, stripped of rhetoric, boils down to putting the United States' energy economy across the board on a price basis of the present level of OPEC prices (Organization of Petroleum Exporting Countries), plus freight to U.S. ports, plus $2.00 a barrel. This means that all new natural gas, all domestic petroleum and all imported petroleum will be priced at approximately $14.00 per barrel. Inevitably, since there are no price controls applicable, coal prices will rise to roughly the same level.

One of the goals of the Administration's new energy proposal is to drive down OPEC prices. Yet by the establishment of this "high cost energy program" the United States will be unable to benefit from such lower OPEC prices, even if they are achieved. Part of the Administration's plan calls for standby authority for the President to establish quotas and tariffs apart from those already in place in order to ensure a "floor" price so that companies investing in petroleum, natural gas, shale, liquification or gasification of coal and other alternate energy supplies will be able to receive an appropriate return on their investment. Thus our economy would be insulated from lower foreign prices and would be permanently trapped into a posture of accepting higher energy costs than any other industrial country in the world. Obviously, our competitive ability will be seriously damaged, our export trade curtailed and our balance of payments plunged into deficit year after year. In effect, the Administration is calling for a policy to break OPEC prices while at the same time putting the country in a position in which we alone among industrialized countries will be unable to benefit from lower OPEC prices if they are achieved.

I would now like to turn to a number of myths, misstatements and misunderstandings relating to United States' energy policy and its interaction with OPEC. As indicated earlier one of the objectives cited by the Administration in pursuing its new energy policy is to break the OPEC cartel and cause OPEC prices to decline. Another stated objective is to destroy OPEC's ability to do "significant economic damage" to industrial economies. We shall examine these two points in detail later.

Another thought that has received wide circulation in recent weeks is the myth that OPEC's accumulation of capital will put it in a posture to undermine the world currency structure, take over all the stock listed on the New York Exchange, or in other ways prove to be so large that the existing financial system will be unable to manage the flow of funds. As a corollary to that thought is the theory that we here in the United States cannot absorb the increased OPEC prices without a crippling impact on our economy. We also hear economists and others testifying recently in Washington that the establishment of a

Federal government importing authority or the use of sealed bids will somehow break the Arab cartel—or what is called the Arab cartel rather than the OPEC cartel.

There is one final myth that permeates all the rest, that is the oft-repeated assertion that the current OPEC price problem is a separate issue and not related to the question of a Middle East peace settlement. All of these various myths and misunderstandings are creating an emotional climate in Washington and in the nation which could lead us to policies less than rational. They deserve to be analyzed and commented on one by one.

1. To understand the world as it is we must first make a more realistic assessment of OPEC in order to grasp how limited our unilateral options really are. We must understand that within OPEC there are two groups of countries. The first group—the non-Arab countries—is made up of relatively densely populated countries with high unemployment and a strong desire to industrialize. This group includes countries like Venezuela, which has already embarked on a massive long-term industrialization program; Iran, with some 26-million in population (and high unemployment) which has in place an overt government program to use all available crude oil to build new refining capacity and petrochemical facilities in Iran itself; Indonesia with over 100-million in population, and Nigeria the most populous of African countries with some 60-million people, both developing countries keen to see economic progress and a better living standard. All of these non-Arab nations believe that current price levels are not too high and that, indeed, it is about time they received a more equitable share of wealth from their natural resources, such as petroleum. I can tell you from personal experience that it is difficult for officials in such countries to identify and sympathize with what we call "sacrifices" such as turning down the thermostat a few degrees or buying a smaller car when they note the poverty, hunger and survival-oriented existence of most of their own citizens.

The second OPEC group—which includes most of the main Arab producing countries—do not have large populations and are now receiving revenues far in excess of their ability to absorb such revenues in domestic industrial development. It is this group which has a far higher degree of self-interest in making sure that the current high price level of petroleum does not drag Western Europe, Japan and the United States into a severe economic recession or depression. Such countries would much prefer industrial countries to have strong, viable, growing economies in which to invest their surplus funds. In short, it is these Arab nations to whom we must look for help in bringing down current OPEC price levels. It is also the same Arab countries who despite their economic self-interest, simply are not in a position to reduce prices sharply until and unless there is a just Middle East settlement.

2. Returning now to another of the myths and misunderstandings expressed above, I would like to comment on the oft-stated position that the key to bringing down OPEC prices is increased production and reduced consumption in the United States. We, in fact, have only a marginal impact on OPEC price decisions. Clearly, insofar as the Arab producers are concerned the United States has never been an important market. We prevented them from selling much of their oil here all through the 1960's under our mandatory oil import quota system. The Arab nations are currently producing some 18-million barrels daily of crude oil of which we import about 1-million barrels daily. We are, at best, a 5% or 6% market.

I repeat, the U.S. only buys about 5% of Arab oil production. Besides, even if we succeed in cutting oil imports most of the cuts will be imports from non-Arab countries. As you know, whether we like it or not, Canada has already decreed that it is phasing out its exports of crude oil to the United States. These exports, which were approximately 1-million barrels a day a little over a year ago, are now due to drop to 650,000 barrels daily by July 1975 and to be phased out altogether by the end of the decade. Moreover, additional cuts in imports will be likely first to back out Venezuela, Indonesian and Nigerian oil rather than Arab oil because prices for these oils are higher than prices for Middle East Arab oils.

In short, the theory that what we do here in energy policy can dramatically alter Arab pricing decisions is just that—a theory which fails to recognize political facts. No sealed bid system, no creation of a government purchasing agent to handle all imports can possibly bring about the desired results. In fact, the creation of such a government entity would do much to undermine the flexibility we now have in meeting emergency situations and would end for all time the ability of our independent companies, both marketers and refiners to negotiate lower competitive prices from foreign refiners and crude oil producers. Further, the creation of a government purchasing agency would just about end the ability of independent companies to finance new refinery capacity.

3. I would now like to comment on the theory that the United States cannot absorb higher OPEC prices without critically damaging our economy and balance of payments. Again, an analysis of our balance of payments shows this argument to be fallacious. For the calendar year 1974 just ended the United States did indeed show a staggering increase in costs for oil imports. These rose from somewhere in the neighborhood of $7 to 8-billion (in 1973) to $24-billion for the year 1974. But at the same time our exports also rose dramatically so that by year end total imports were valued at just over $100-billion while exports stood at $97-billion. This caused a $3-billion balance of payments deficit—not a small number. But had it not been for the drought in the midwest and as a result, poorer agricultural exports than expected, we could well have had a balance of payments surplus despite the rapid escalation of foreign oil prices. My point is this—this economy is so large and our export potential is so great that higher oil prices are not going to bankrupt us. In fact, in one short year—a year when the price for foreign oil was tripled—we have already shown that we can offset these added costs through additional exports. Moreover, it seems clear that as the oil producing countries develop and maintain a high level of revenues from their oil sales in the future, there is created an exciting growth market for additional exports of American managerial, financial, technical, and manufacturing skills as well as a growing market for U.S. agricultural products. Another way to look at the transfer of $100-billion annually to OPEC countries which is occurring at the present time is to look at it as a growth opportunity for U.S. business and agriculture.

4. Another popular misconception relates to the world financial institutions' ability to manage the transfer of funds that are occurring and the oft-stated fears that " the Arabs will take over the entire world economy. It is popular to note that at current stock market prices within a certain number of years the OPEC nations could buy out the whole New York Stock Exchange and own every major corporation in the United States. These simplistic and naive assertions are obviously designed to stir fear. But they are not valid.

In fact, the Administration itself has now recognized that the build-up of dollars and hard currencies in OPEC nations in the years ahead will be much lower than previously estimated. I attach a copy of an article from the New York Times of Friday, January 31, 1975 quoting Secretary of Treasury, William Simon's testimony in connection with a new and sophisticated economic analysis by the Treasury Department of the expected accrual or accumulation of funds in the OPEC countries. Mr. Simon stated that the producing countries might accumulate $200–250-billion by 1980, an amount which would level out and then decline after 1985. Mr. Simon concluded that ". . . . there is no reason that the accumulation of substantial debt by oil importing nations to oil exporters need undermine either the solvency or the liquidity of oil importers as a group." Mr. Simon also stated that these new estimates ". . . support the view that the international financial aspects of the oil situation are manageable."

5. I would now like to comment on the Administration's twin objectives of insulating the U.S. from OPEC's prices and reducing and eventually eliminating the power of OPEC countries to cause significant economic damage.

I would say as a general comment, that there objectives cannot be achieved until or unless there is a Middle East peace settlement. The whole thrust of the Administration's policy, the achieving of "Project Independence", the emphasis on "national security' 'and the goal of becoming "invulnerable" by 1985 harks back in many ways to the economic isolation policies of the 1930's. It seems to me that its emphasis on reducing Arab oil imports was conceived in semi-panic and is dedicated to the proposition that we can turn back the clock. I don't deny that the Project Independence exercise may have developed some data that will be helpful in forming a cohesive national energy policy. But as for achieving the twin objective of "insulating" ourselves from OPEC or "eliminating the power of OPEC to cause significant economic damage"—that's just wishful thinking. In short, no matter how sophisticated the technical analysis, no matter how keenly we assess the computer runs, what faces us is essentially a political problem.

It is completely unrealistic for us to look at our exposure—our ability to be independent—in the context of how many barrels a day we can cut oil imports now bought from Arab countries. That is far too narrow a context. No matter what we do, Europe and Japan cannot escape overwhelming dependence on Arab oil to fuel their basic economies for the next decade. Of our total energy supply only 43% is represented by petroleum and only about 15% of our total energy supply would be directly affected by another oil embargo or other actions by OPEC countries to deny us oil supplies. Europe and Japan, on the other hand, depend on petroleum for 60 to 80% respectively of their total energy use. Moreover, almost all of their petroleum needs are covered by imports. They have long ago built strategic stock piles of oil through a "security" storage program. Thus, Europe, and to a lesser extent Japan, can weather short-term interruptions in oil supplies. But there is no way they can do without Arab oil for any period exceeding a few months short of virtually closing their economies down tight.

Given the interdependence of our economy with those of the European countries and Japan, their vulnerability is our vulnerability. There was a time just after World War II when the popular expression was if the United States catches a cold Europe catches pneumonia. That situation has changed. Now, if they catch pneumonia we do too.

It follows that we must move forward toward a Middle East peace settlement as a first priority. Only then can we hope to negotiate lower OPEC prices. Only then can we, as the world's most skilled, diverse and technically accomplished economy, expect to earn back more dollars than we spend for petroleum imports.

There must be some recognition that this is not 1967 or 1956. The world has changed. We do not have the unilateral options we had then. And we won't have them in this decade. The golden period of roughly 25 years after World War II when the United States could afford the luxury of doing about whatever it wished to do internationally is over.

In fact, looking realistically at the world and our position in it we must conclude that the United States is today living in an interdependent world economy. The Administration, however, seems to be approaching this truth in a compartmental way. It seems to be divided into two groups, one representing the energy and economics sector and a second dealing with political questions. Senator, I suggest that the politics and economics of the Middle East are but two facets of one problem and neither can be isolated or viewed in isolation. European countries and Japan recognize this, as do the oil producing countries themselves. For the United States to keep insisting that these are two separate problems is a head in the sand attitude. We must start dealing with the facual situation that exists and as a first priority we must be on with solving the basic political problems—achieving Middle East peace.

We cannot achieve security or independence by fiddling with the number of barrels per day of oil we import. No number of new FEA computer runs will change the situation one iota. By recognizing that fact one other fact also became clear—that is the foolishness of pursuing a course of "confrontation" with OPEC.

We, and other industrial countries need a certain volume of oil. The producing countries, for their part, want to diversify their economies and improve their standards of living. Between these two groups cooperation can yield a higher level of world trade and a growth in mutual interdependence. This is far the preferable course to confrontation.

One other disturbing thought is the suggestion by the Administration that we must move now—that every day we delay is a day that increases our vulnerability.

With all due regard to the need for action, what you are looking at in Congress is an energy plan that commits our country to a basic course of action for the next 10 to 20 years. You must resist rushing into such a long-term policy without full analysis and consideration. You must not buy the Administration's program just because it is the only one offered at this time. After all it was conceived in secrecy and is already being implemented without public hearings.

The Congress need not feel under any great pressure to move in one week or two weeks or even in one or two months. There is nothing in the Administration's program that protects us from an embargo over a short time space. Moreover, even if an embargo were to be imposed during the next few months we are in far better shape today to cope with it than we were in October, 1973. Supplies of oil are ample both in the United States and around the world. There is a great deal of spare producing capacity in non-Arab countries. We have an established and operating mandatory allocation system which would avoid the regional spot shortages caused by the last embargo by spreading the available supply of oil equitably and evenly throughout the country. Finally our most vulnerable period—the winter—is well along. It takes about two months for an embargo to bite and by that time we will be into milder weather, even in New England. Thus, while no one wants a new embargo it would hurt us less than the embargo of October 1973. The Congress does have time to analyze thoughtfully the Administration's energy policy and come up with its own alternative program.

As indicated at the beginning of this paper, there are a number of alternative actions which can, at very low cost, meet the President's basic objectives of achieving meaningful conservation and lessening oil imports. But we must use a surgical tool rather than a meat axe approach. The positive programs presented by the Independent Oil Men's Association and the New England Fuel Institute contain actions keyed to conserving the two fuels that are not being conserved currently—gasoline and natural gas.

Apart from these recommended steps Congress must recognize that our greatest vulnerability to foreign oil cutoffs at present is our high dependence (particularly on the East Coast) on imported residual fuel oil. We do need and must have additional fuel-oriented refining capacity in this country to lessen this vulnerability. However, the Administration's plan discriminates against U.S. refineries and would limit if not prevent the building of any new refineries here at home. This would occur, first of all, during the so-called transitional or tariff phase of the Administration's program since product tariffs are set lower than crude oil tariffs. This obviously leads to the favoring of construction of refining capacity abroad rather than here. Moreover, the long-term Administration program which equalizes tariffs between products and crude oil nevertheless puts overseas refineries in a preferred position. Under the Administration's program foreign refineries will have lower capital costs, lower working capital needs and lower freight costs than a new U.S. fuel refinery.

There must be positive incentives to build new independent refining capacity in this country and all of the independent marketing and refining groups will, I am sure, be happy to work with you and your staff and with other political leaders in Congress to help frame out the kind of incentive program that is vitally needed.

Senator Jackson, we are at a crossroads of such importance that it cannot be overstated at this point in our national economic life. We are going to opt either for a permanent high energy cost economy which will exacerbate our recession and our inflation, or we are going to embark on a conscious policy of more moderately priced energy designed to keep our economic structure competitive in the world market.

I would like to recommend that the Congress look at the establishment of a moderate energy cost program. The Administration wants to take the 85% of the energy that we produce domestically and hook it to the price of the 15% of our energy which we import—letting the tail wag the dog. This does not insulate us from OPEC. Rather it ties pricing for our whole energy structure directly to OPEC's prices—plus, of course, $2.00 per barrel. In a very real sense our entire energy production is put under the pricing control of the OPEC countries.

There are those in the oil and gas industry (and, indeed, within the Administration) who argue that price controls should be lifted on all domestic oil and gas so that they can rise to the "free market" price. But there is no "free market" price in the world today. OPEC's prices are political, not economic. To illustrate: it costs 16 cents to produce one barrel of Saudi Arabia crude oil today; yet, today's selling price is $10.46 per barrel.

If we really wish to insulate our economy from OPEC pricing, the only logical way to do it is break away from their politically established prices by establishing prices of our own for the energy which we produce ourselves. We are uniquely able to do just that since we import only 15% of our energy needs.

I would recommend that the Congress take the two different prices which currently apply to domestic crude oil (the old crude oil price which is controlled at $5.25 per barrel and the new crude oil price which fluctuates at about the level of the landed cost of OPEC crude or, say, about $11.50 per barrel) and average these two prices thereby creating a new single price on all domestic oil. It could be set slightly lower than the weighted average of the two prices today. With a small roll-back of domestic crude oil prices there would be a deflationary effect on the economy—rather than the wildly inflationary effect of the Administration's plan.

Such a weighted average price might be set at, say, $7.00 per barrel—a reduction of perhaps 20 to 35¢ per barrel from today's weighted average price. U.S. refineries under the Mandatory Allocation Act would continue to receive their pro-rata share of total domestic oil at the new fixed price. This would promote more refining capacity, including more independent refining capacity, since refiners would be able to count on lower weighted average crude oil costs than their foreign competitors.

Once the new lower domestic oil price has been established, new natural gas prices could then be deregulated without fear of a precipitous jump in natural gas prices, since only a small volume would qualify for deregulation in the first year and since a price ceiling would be set by the new lower domestic oil price. In short, new natural gas prices would only rise to the value of the alternative energy source, i.e. oil prices. The weighted average crude cost to U.S. refiners would be about $8.50 (70% at $7.00 and 30% at $12.00).

Under the Administration's proposal, of course, deregulated natural gas prices would rise to the equivalent of $14.00 per barrel of crude oil. Similarly, the new lower domestic crude oil price would put a ceiling on price rises for coal. Yet, even with a moderate increase in natural gas prices resulting from this approach, conservation of natural gas would be increased just as conservation of heating oil during the past year has responded to higher heating oil prices.

Even at a new $7.00 price for all domestic crude oil there would still be adequate incentive to drill and develop additional oil supplies. And with new natural gas prices deregulated there would be an equal incentive, now missing, to drill for and develop additional natural gas supplies.

If an additional demand depressant is needed, and I am not sure it is, then plans such as those suggested by IOMA and NEFI could be put in place in order to moderately cut consumption of gasoline.

Such a low energy cost alternative to the Administration's plan would achieve the following:

Slightly reduce, rather than sharply raise, oil prices to consumers for all petroleum products except possibly gasoline.

Slightly raise gasoline prices, if other steps fail to curb gasoline use.

Go hand in hand with other long-term conservation measures, such as Federal taxes or high horsepower or heavy automobiles, new tougher insulation standards and tax incentives to insulate both commercial and residential building.

Provide sufficient incentive to continue drilling for new oil and increase incentive for drilling to discover and develop new natural gas supplies.

Increase incentives for the addition of new refining capacity, including new independent refining capacity, thereby reducing our dependency on foreign product imports.

Pinpoint conservation when it is likely to do the most good, i.e. natural gas and gasoline.

Continue the modest price reductions now flowing to the East Coast on imports of refined products by continuing the existing price equalization program.

Allow the tax rebate and tax reduction and reform measures to really do their job of stimulating the economy without an economic drag offsetting them from the energy sector.

Put a system into operation with the minimum of operational and administrative difficulty since allocation and price equalization regulations are already in place and functioning.

Eliminate the need for rationing, new tariffs or protective quotas.

Fit perfectly with an emergency strategic storage program designed to lessen our vulnerability to disruptions of foreign oil supplies.

Insulate our economy from OPEC price decisions whatever course they take.

Strengthen our competitive export position by providing lower energy costs to industry and agriculture than the energy costs now prevailing in other industrial countries.

Improve our balance of payments position as a result of our more competitive position in world markets.

In short, this alternative program is not inconsistent with the Administration's objectives. It does virtually everything the Administration wants to do. But it does so in a way that strengthens rather than weakens our economy in both the short and long term.

I would like to pause now at the conclusion of my remarks to try to gain perspective at this critical juncture by reflecting on a short poem by Robert Frost—a poet we like to call our own New England sage even though he was born in California. Sometimes a poet like Frost can illustrate a truth in the language of nature in a way that makes us all understand the truth a little more fully.

"Two roads diverged in a yellow wood,
And sorry I could not travel both
And be one traveler, long I stood
And looked down one as far as I could
To where it bent in the undergrowth;

"Then took the other, as just as fair,
And having perhaps the better claim,
Because it was grassy and wanted wear;
Though as for that, the passing there
Had worn them really about the same,

"And both that morning equally lay
In leaves no step had trodden black.
Oh, I kept the first for another day!
Yet knowing how way leads on to way,
I doubted if I should ever come back.

"I shall be telling this with a sigh
Somewhere ages and ages hence:
Two roads diverged in a wood, and I—
I took the one less traveled by,
And that has made all the difference."

Senator, as you may know the title of the poem is "The Road Not Taken". I would hope that when the Congress gets through fully analyzing the President's energy program that it will become The Road Not Taken.

[From the New York Times, Jan. 31, 1975]

SIMON LOWERS FORECASTS ON OPEC CASH-BUILD-UP

(By Edwin L. Dale, Jr.)

WASHINGTON, Jan. 30.—Secretary of the Treasury William E. Simon, citing a detailed new Treasury analysis, told Congress today that the buildup of petro-dollars in the oil-exporting countries would be much less in the years ahead than had been estimated last year after the sharp increase in the price of oil.

Mr. Simon said that new estimates by economic forecasters "support the view that the international financial aspects of the oil situation are manageable."

The Treasury's analysis, made public later in the day, estimates a peak "financial accumulation" of the producing countries of $200 billion to $250 by 1980 and then a leveling out followed by a decline starting about 1985. This contrasts with estimates of the World Bank last July, for example, that the accumulation would reach $653-billion in 1980 and $1.2-trillion in 1985.

The analysis also concluded that "there is no reason that the accumulation of substantial debt by oil-importing nations to oil exporters need undermine either the solvency or the liquidity of oil importers as a group."

The study was made by Thomas W. Willet, Deputy Assistant Secretary of the Treasury for Research. He referred to it at a conference here earlier this week but did not publish it until late today.

The CHAIRMAN. Governor Salmon?

STATEMENT OF HON. THOMAS P. SALMON, GOVERNOR OF VERMONT

Governor SALMON. Mr. Chairman and members of the committee, let me attempt to get in a few licks this morning from the perspective of a rural State in the Northeast. We have unemployment in one of our cities of Vermont at 20 percent. Our people are looking at an average increase under the President's program as we have evaluated it at the New England Regional Commission, and the National Governors Conference, of 35 percent.

We have some rather peculiar problems in rural America, poor rural America, that I would like to leave with this committee today. In northern New England, the increases today are double the figures that Senator Kennedy has alluded to, so we are somewhat out of wack in terms of our contiguous region. Gas costs 5 cents a gallon more in our State than it does on the national average. Our per capita income is among the lowest in these United States, and we are facing a situation now in our region that transcends this government where fundamentally we are recommending the most austere budget in modern history, and still facing the proposition, Mr. Chairman, of both level funding and the necessity to raise additional resources through new taxes in hard times.

The poor, of course, have been designated to pick up the lions share and the brunt of the President's recommendations. Those who are poor, based on some extrapolations we have done in our State, will devote as much as 16 percent of their income to energy if this program, this two-tiered program is fully implemented. The well-to-do in this society will devote no more than 2 to 3 percent of their income.

There is another important consideration that I would like to leave with you as it relates to our manufacturing structure, our manufacturing base. In the 6-month period following the embargo while industrial production in the country declined by 3.8 percent, industrial production in New England declined by 11.4 percent. There is a grotesque energy price disparity in our region as respects the rest of the country, and this is readily seen when you look at the residual fuel alone which is costing $1.81 in our region per million Btu's as opposed to a national average of 84 cents. We are 82 percent reliant on petroleum as a basic energy resource as opposed to 45 percent in the country as a whole.

This program, in addition to its devastating effect on the American consumer, holds out a special threat to our capacity to maintain the permanent, good paying jobs that we have in manufacturing in our region. The free enterprise system says essentially this, that business and industry will go where they have the best chance to make a buck. And if this program is adopted as expressed in the President's message, we face a situation of double siege. The implicit assumption in the President's message, and I read the President's message, Mr. Chairman, and I attempted to read it quite carefully, is that there is no other theory, there is no other alternative to his efforts to let a free market mechanism cure the problems of imports of foreign oil. It is our judgment that this theory is utterly incorrect.

This program came on line, of course, without any consultation with any Governor in these United States, and as I understand it, without any substantive consultation with Members of the Congress. We feel that there are other alternatives, and that is why it is so necessary in our view to buy some time here, 90 days, to put other alternatives on line. Personally, I would far prefer an approach involving volumetric reduction of imports, and the utilization of a mandatory allocation system with some degree of greater flexibility that fundamentally kept our region alive during the difficult winter of 1973 and 1974.

We hope, Mr. Chairman, as individual Governors to have an opportunity to have some input, to sit at the head table in the next alternate energy program for this country is conceived and implemented by this Congress. We have the capacity, we have the New England Regional Commission based in Boston, funded with Federal dollars that gives us capacity to make a contribution to this effort. We want to make a contribution.

And let me say that Governor Briscoe of Texas has indicated that he supports the resolution before you, and with your permission, I would like to leave the record open, Mr. Chairman, for supporting statements from other Governors.

[Correspondence of Hon. Dolph Briscoe, Governor of Texas, and Hon. Hugh L. Carey, Governor of New York, follows. A telegram of Hon. Wendell Anderson, Governor of Minnesota was entered into the record earlier and appears at page 14.]

STATE OF TEXAS,
OFFICE OF THE GOVERNOR,
Austin, Tex., February 7, 1975.

Senator RUSSELL B. LONG,
Chairman, Senate Finance Committee,
Washington, D.C.

DEAR MR. CHAIRMAN: I submit this letter to enter the record of the Senate Finance Committee in support of HR 1767. It is my personal opinion that the recovery of our economy and the stability of our national energy policy can best be served by delaying imposition of increased import tariffs until the Congress has an opportunity to act.

Sincerely,

DOLPH BRISCOE.

STATE OF NEW YORK,
EXECUTIVE CHAMBER,
Albany, N.Y., February 7, 1975.

Hon. RUSSELL B. LONG,
Chairman, Senate Finance Committee,
U.S. Capitol, Washington, D.C.

DEAR SENATOR LONG: On behalf of the people of New York, I submit the following statement for inclusion in the record of the Committee. I would urge the Committee to enact the resolution to delay the imposition of the President's tariff for 90 days.

I thank you for this opportunity to submit this statement.

Sincerely,

HUGH L. CAREY.

Enclosure.

FEBRUARY 7, 1975.

Note to: The Senate Finance Committee.
From: Gov. Hugh L. Carey of New York.
Subject: The effects of the proposed tariff on New York State.

The proposed tariff would have drastic effects on New York State. I submit the following facts.

Since October 1973:

the price of residual fuel oil delivered in New York Harbor has risen from $4.47 per barrel to $12.51 per barrel, a 180 percent increase;

the price of homeheating oil in Metropolitan New York has risen from 23.7 cents per gallon to 40.7 cents per gallon, a 72 percent increase;

the price of gasoline has risen from 43.8 cents per gallon to 57.9 cents per gallon, a 32 percent increase.

The average prices for coal and natural gas are nearly 50 percent higher in the Northeast than the national average.

According to the Federal Power Commission publication, *Typical Electric Bills 1973*, seven of the ten American utilities charging the highest rates for 500kwh of electricity are in Northeast states.

During 1974 the average electric bill in New York rose 35 percent over the average 1973 bill, while the National average bill for 1974 rose 12 percent over the National average bill for 1973.

The East coast uses more than 93 percent of the total United States import of residual oil, distillate oil, and gasoline. 90 percent of the residual oil used on the East coast is imported as opposed to 10 percent for the rest of the Nation.

In November 1974, the Entitlements Program recognized the inequities of fuel costs in the United States, and awarded the Northeastern states 60 cents per barrel of oil consumed.

The demand for home heating oil and the demand for electricity in New York have declined below 1973 levels. This unprecedented decline is the result of cost pressures, shrinking disposable income, and conservation efforts.

The rate of abandonment of buildings, by landlords and tenants who cannot pay fuel bills, utility bills, or real estate taxes, rose to 4700 multiple dwellings in New York City in December 1974.

Mass transit in New York, particularly the Metropolitan Transportation Authority system serving New York City, required more than $100 million in emergency Federal subsidies to meet increased energy costs during fiscal 1975.

New York State is dependent on imported petroleum products. We find ourselves in an intolerable position when we review the projected effects of the proposed tariff on New York State.

A tariff on imported crude oil and petroleum products, beginning on February 1st and increasing during the following three months to $3.00 per barrel on crude oil and $1.20 per barrel on products, coupled with the elimination of Entitlements, would have the following effects:

According to the New York State Public Service Commission, electricity prices would rise 6-13 percent as a result of this tariff.

The price of home heating oil would rise 10 percent as a result of this tariff.

The price of gasoline would rise approximately 4 cents per gallon as a result of this tariff.

The cost of fuel to New York State agencies and political subdivisions would rise by $4,421,000 between February 1 and July 1, 1975, and by $20,028,622 during Federal fiscal year 1976, as a result of this tariff.

The cost of gasoline and heating oil to all the citizens of New York would rise by $687,529,800 during Federal fiscal year 1976, as a result of this tariff.

The tariff would not effectively encourage energy conservation. The tariff would increase the prices of fuels for which the demand is inelastic—residual oil and home heating oil—and would increase the price of electricity used by mass transit systems by 10 percent making a transit fare increase almost inevitable.

The new impact of increased fuel and utility prices would raise the Consumer Price Index at least 3 percent, as the result of a single government action.

The increased costs of fuel and electricity will take disposable income out of the market place which is in serious recession.

According to projections by my economic advisors an immediate reduction of oil imports by one million barrels, accompanied by declining domestic production, would force a reduced demand of 1.5 million barrels of oil per day, an immediate 9 percent decline from a 1974 level that is depressed by rising prices and falling production.

Therefore, on behalf of the people of New York, I request that the imposition of the tariff be delayed, at the very least, for a length of time sufficient to disseminate to all citizens a full explanation of this tariff and its economic consequences.

Secondly, you should know that we in New York State believe very strongly that a gasoline excise tax is the only appropriate remedy for the Nation's energy problems. A gasoline tax would raise the price of the fuel which has shown the smallest percentage price rise in the past 18 months and which is the most elastic in response to price changes. A gasoline tax also gives the government the ability to redistribute the revenues to achieve full equity of pricing and adequate mass transit systems.

I respectfully submit these points to you with the knowledge that you will recognize the inequitable effects such a tariff would have on the people of New York and the other states in the Northeast, and that you will respond by postponing the imposition of the tariff.

Senator JACKSON. Mr. Chairman, I have to leave early, and may I just express to you and to the committee the deep appreciation of all of us for the expeditious way in which you have moved on this. We are most grateful.

The CHAIRMAN. Senator Jackson, I am sure you will be around on the floor to answer any questions the committee members have in mind, so we will permit you to depart if you wish.

Senator JACKSON. Senator Kennedy will answer my questions, and any others I will be glad to study and answer in writing. Thank you very much.

Senator KENNEDY. Thank you, Mr. Chairman. We are fortunate to have Attorney General Tucker of Arkansas. I think I would like to indicate that this is not something that is either for the Northern or Midwestern States as Senator Mondale has pointed out, or the Northeast, but it also affects the heartland of the country. Attorney General Tucker.

STATEMENT OF JIM GUY TUCKER, ATTORNEY GENERAL, STATE OF ARKANSAS

Mr. TUCKER. Thank you, Senator Kennedy.

Mr. Chairman, Governor Salmon, and Senator Kennedy have each given you a perspective from the Northeast, and I speak as a representative of one of your neighboring States in the South. I think there is a fairly narrow issue which you actually have before this committee. It is an issue with which I am concerned because a number of the States in New England have recently instituted litigation challenging the legality of the President's action with regard to the imposition of this tax. Arkansas will point that litigation, if need be. However, it has always been my belief that courts should be an avenue of last resort rather than first recourse. And, certainly I believe in the area of energy policy it should be the Congress and not the courts that make the determination as to the direction this country should move.

What is of such serious concern to me was touched on by Governor Salmon when he pointed out that no Governors were consulted with regard to what this tax program should be. And in that regard, I wish to point out to the committee that you have a very narrow issue before you. The issue is not, it seems to me, whether the President is going to be embarrassed or whether we like the President or do not like the President. It is not a Democratic or Republican issue. I think it is one of the most basic legal issues this country ever faced: that is the question of whether we are going to have taxation without representation. This was a tax imposed by the President and his advisers without consultation with the Governors of the States, without consultation of the Congress of the United States. I would hope that this committee would rule unequivocably that this is not the proper way to approach the energy problem, and make a determination that the Congress should have the governing voice before a new tax is imposed which will have the impact that this tax would have on the citizens of my State and the citizens of this country.

The impact will be great on the South just as it will be in New England. We in Arkansas have been particularly hard pressed by the increased prices of propane during the past year. There has been some 300, and in some cases as high as a 500-percent increase in propane prices, and this price increase occurred without any formal written economic analysis being performed by the Federal Energy Administration, and to this date the FEA does not have a written economic analysis in compliance with section 18a of the Federal Energy Administration Act.

Propane consist of 7 percent as to the total volume percentage of imports into this country, and the FEA predicts that in 1975 almost 11 percent of the propane will be imported. With the already enormous price increase that propane has experienced, this tax would only send propane prices up higher. But the impact of the tax in the South is beyond just propane. For example, many of the larger States in our country and rural States in our country are disproportionately large consumers of gasoline. Although our State has a small population, we are one of the largest per capita consumers of gasoline because we do not have mass transit systems. Our population is widely scattered, and they must travel some distance to work. The regulations in the President's proclamation which would permit the transfer of disproportionate portions of the tax on gasoline at the discretion of the importers would have a severe impact on those States that have high per capita gasoline consumption.

People in my State, Mr. Chairman, as I am sure the people in your State, do not mind suffering a hardship if they can feel assured that the hardship is one that is being suffered uniformly by the people throughout the country. But this tax and this program cannot give them that kind of confidence because it has not been reviewed by their Representatives in the Congress of the United States. I think, if we continue to pursue this policy without action by the Congress, that I can speak for many other attorneys general of this Nation when I say we will have to turn to the courts and seek our relief through litigation. I do not believe that that is the best kind of relief that this Nation is entitled to.

Thank you very much.

Senator KENNEDY. Thank you very much. Maybe now I will ask Charlie Schultze who has been the Director of the Bureau of the Budget, and then John Sawhill, to wrap up for us.

STATEMENT OF CHARLES L. SCHULTZE, SENIOR FELLOW, BROOKINGS INSTITUTION, WASHINGTON, D.C.

Mr. SCHULTZE. Thank you. Thank you, Mr. Chairman.

Let me start by stating five propositions which I think are relevant to what your committee is considering.

First, while reasonable people might indeed differ about the merits, everybody will have to agree that the President's energy program is comprehensive. His legislative program is an exceedingly complex one with large and long-lasting effects on employment, on output and prices in the economy at large, upon the energy industries in particular, and upon the competitive position of the various regions of the country. There are major questions to be considered about the effects of this legislation.

Second, unless it wishes to act simply as a rubberstamp, the Congress literally cannot conscientiously evaluate, modify, and enact such a comprehensive and far-ranging package by April 1.

Third, in the absence of congressional action by that date, the President's unilateral measures will draw substantial purchasing power from consumers by way of import fees, and the associated rise in new oil prices and competitive fuels.

Fourth, the economy is now in a critical situation. It is going downhill rapidly. In fact, in the last month, in 1 month alone we have added almost 1 million people to the ranks of the unemployed. Actions like the import fee which drain further purchasing power are bound to make things worse and to frustrate the chances for economic recovery.

Five, delaying the President's unilateral actions for a short time will not jeopardize legitimate energy policy goals. What would be gained by way of reduced imports in the 3 months or the 4 months involved is miniscule in terms of the Nation's energy demands, its imports, and the size of the world oil market. But what would be lost by way of additional unemployment and purchasing power would be large.

Let me turn just for a few moments to examine several of these propositions more carefully. As I said at the beginning, that however reasonable men might agree or disagree with the President's comprehensive energy program, it is an exceedingly complicated one, and it does have very large impact on the economy. On the surface that program takes $30 billion out of the economy by higher energy taxes and puts $30 billion back in by way of tax cuts and other measures, and therefore, one might think it is neutral.

Well, as a matter of fact, it is much more complicated than that, which again is not to say at this moment that it is wrong. It is just much more complicated and deserves tremendous evaluation. For example, in addition to the increased average crude oil prices of about $4.50 a barrel, or 45 to 48 percent, and the doubling or more than doubling of new gas prices, there will be associated increases in the prices of intrastate unregulated natural gas, and in coal prices as the prices of competitive fuels rise. Private consumers alone, as opposed to Federal, State, and local governments, will pay well over $30 billion extra; and under the President's fuel program, consumers will get back $18.5 billion of the $30-odd billion they have spent.

On the other hand, private corporations, who will undoubtedly pass on the bulk of their costs to consumers, will get a $6 billion corporate tax cut. On balance, the net effect on consumer spending is bound to be negative. What it will be on business spending we do not know.

But the main points is, it needs very careful examination before it is put into effect, and you cannot simply rely on the fact that $30 billion is taken out and $30 billion is put back in, that it is a neutral sort of thing and that we do not have to worry about it from an economic recovery standpoint.

The President's program will also have very complicated effects on the oil industry. For example, with decontrol of old oil prices, and with windfall taxes that the President proposes, the price of old oil will go from $5.25 a barrel to about $6.50 or $6.60 a barrel, the price of old oil from wells already sunk, whereas the price of new oil, which is what we want, and what we need, the prices will actually drop from about $11 a barrel to $6.60 a barrel. What will be the impact on this on the incentives to drill and refine new oil I am not suggesting I know, but I am suggesting it sure cannot be rubber stamped.

The central point, therefore, is that the President has proposed a program of truly massive size and complexity, and it is going to have vast ramifications on this economy now and in future years, for employment, inflation, the competitive situation of the various regions of the country, and for the energy industries. To pass such a program by April 1 the Congress could do no more than rubber stamp one of the most complicated and important programs that has been presented to this country and to this Congress in many years.

In the meantime, the President's unilateral action in imposing import fees, with no offsets for consumers, will clearly hinder economic recovery. By the President's unilateral actions alone the following will happen:

The price of imported crude will go up by $1 in February, $2 in March, and $3 in April. The price of imported refined products will go up in steps to $1.20 a barrel by April. The price of unregulated new domestic crude oil will go up by $1 in February, $2 in March, and $3 in April. The price of coal and unregulated intrastate natural gas will undoubtedly rise to some extent since their competitor fuels have risen. All told, by April the unilateral measures of the President will be draining $800 million a month from users of fuels, part to the Government, part to the profits of the producers. At an annual rate, that is $9 billion to $10 billion a year taken out of the consumer income stream and not put back in. Given the current economic state of the country, with unemployment at 8.2 percent and rising at a frightening rate, with output falling sharply, with sales slipping badly, it is at least in my view absolutely critical that all actions which drain off purchasing power from consumers be avoided, and that the stimulus, the Congress is now devising, the economic stimulus not be offset by an oil drain.

If the President goes ahead and the Congress deliberates on energy policy in just a reasonable manner for several months, but the President goes ahead that $800 million a month drain, it is bound to hurt employment, is bound to hurt sales, is bound to hurt output is bound to delay recovery. And it is exceedingly dangerous when the economy is falling so rapidly to take these kinds of chances.

The final point. Will a postponement of action for say 3 months, 4 months, somehow weaken the United States in its international oil policy? In any objective sense, surely not. At the present time the United States imports 6½ million barrels a day. The effect of the President's actions during this interim period on that level of imports is bound to be miniscule. If we are vulnerable to a potential embargo now, we will be equally vulnerable 5 months from now with the President's action. The strength of the United States around the world and at the bargaining table lies in getting recovery going and doing

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nothing to impede that. Impeding it will weaken, not strengthen the U.S. position at the bargaining. The U.S. strength at the bargaining table with other consumers and with producing countries is best served by a show of national unity and a considered, deliberate, longrun strong approach to energy conservation, not hasty, and unilateral measures.

Mr. Chairman, it has not been my point at this stage to take on the President's program itself. As I said, reasonable men can very well differ about it. What I think is critical is to give the Congress time to consider, evaluate, and modify this truly massive legislation and not run the incredibly dangerous risk of draining off further purchasing power from this economy in the meantime.

Thank you, Mr. Chairman.

Senator KENNEDY. Thank you very much.

Our final witness is Mr. John Sawhill, until recently, Administrator of the FEA.

STATEMENT OF JOHN C. SAWHILL

Mr. SAWHILL. Thank you very much Mr. Chairman and members of the committee. I appreciate this opportunity to appear before you to discuss and evaluate the administration's proposals for dealing with the Nation's energy problems and specifically the proposed tariff on imported crude oil and refined products.

At the outset of my statement, I would like to place the dual problems of economic recession and energy dependence in perspective. As was already pointed out, the economy is spiraling downwards into the worst recession since the Great Depression. By the end of this year, we will have experienced the first back-to-back declines in real GNP in over three decades. Unemployment jumped from 5.5 percent in the third quarter of 1974 to over 8 percent in this past month.

This situation is obviously intolerable to all of us. The costs in human and social terms of continued unemployment at such levels are profoundly disturbing. Congress must move quickly to reverse these trends not only to salvage our economy here at home but, also, to provide much needed stimulus to the economies of many of our traditional friends and trading partners overseas, some of whom are experiencing severe financial difficulties.

I have spent some time dwelling on the economy because I am convinced that—important as our energy problems are—at this time our economic difficulties must come first. A balanced energy budget is an important national goal, but not if it comes as a result of economic dislocations that would largely obliterate its benefits. And this, I fear, might be the case if the President's energy program were to be implemented exactly as presented. We simply cannot afford to drain $50 billion of consumer purchasing power out of the economy at a time when we must restore confidence, create more jobs, and get our economy turned around.

Certainly, there is much that is good in the administration's program. The measures designed to increase energy supplies such as opening up Naval Petroleum Reserve No. 1 to production, beginning exploration of NPR No. 4, exploring the Outer Continental Shelf, creating a strategic reserve, increasing the price of new natural gas at the wellhead and creating a strategic reserve are all designed to reduce our vulnerability to foreign supplies. At the same time, many of the proposed conservation measures such as thermal efficiency standards for new buildings, tax credits for insulation of existing homes and subsidies to low income groups to permit them to retrofit their homes with storm windows and doors and utilize additional insulation, are also desirable. And expended funding of energy research and development is equally important.

But having said that all those things are necessary, I must also say that the program, when viewed in its entirety, has major defects.

First, and this returns to my earlier point, it would severely aggravate our economic difficulties, which are already as acute as any we have experienced in decades. The proposed taxes and tariffs on crude oil would raise prices on the entire range of petroleum products, from gasoline to plastics, from home heating oil to synthetic fabrics. The program would result in higher costs for other fuels as well, such as coals and it would require an additional tax on natural gas that could, for example, translate into increased fertilizer costs of $4 or more per acre of cultivated land and, ultimately, into further escalation of food prices.

In short, the "ripple" effect of these proposals would eventually work its way through the entire economy.

Second, such undiscriminating increases would penalize those people who can least afford them.

Similarly, people living in certain regions, such as New England and the upper Midwest, could be forced to carry a disproportionate share of the burden.

Finally, there is no guarantee that the proposals would work. That the Arabs would not simply view this as an invitation to hike their prices again and that a Nation faced with increased costs across the board would not simply find itself, a year from now, sending even more dollars to the Middle East.

In short, the "ripple" effect of these proposals would eventually work its way through the entire economy—transportation, industry, agriculture, utilities, would all be affected. The administration projects an increase in the Consumer Price Index of approximately 2 percent—probably enough to assure continuation of double-digit inflation—but given the scope and magnitude of these "ripple" effects, that figure remains at best uncertain.

2. Second, such undiscriminating increases would penalize those people who can least afford them. Poor people and people living on fixed incomes, along with the rest of us, would have to pay those higher prices to heat their homes and feed their families. They would not have the option of closing the cottage in the mountains or postponing the vacation on the west coast.

3. Similarly, people living in certain regions, such as New England and the Upper Midwest, could be forced to carry a disproportionate share of the burden.

4. Finally, there is no guarantee that the proposals would work: That the Arabs would not simply view this as an invitation to hike their prices again and that a nation faced with increased costs across the board would not simply find itself, a year from now, sending even

more dollars to the Middle East. They did not choose to do so at their recent series of meetings, but that is no guarantee that they will not do so at some future time.

Gasoline rationing has been suggested as one alternative to the President's proposals; however, the arguments against rationing are as serious for citizens and the economy as those against the President's program. I am convinced that there is another way to reduce oil imports and curtail consumption at home, and to do so without imposing inequities or adding further disruption to an already shaken economy.

The way to achieve this is not to try to meet a conservation goal of 1 million barrels of oil per day by the end of this year, or 2 million barrels a day by the end of 1976. Our economy simply cannot afford it. We must set some lower target for this year, but make sure that we meet that target—and successively higher ones for the next several years. Only in this way, through a more gradual approach, can we hope to return our economy to health as rapidly as is necessary for our own national welfare and that of our allies.

Beyond setting the lower, graduated goals, we must take a different approach to achieving those goals. We should not raise all petroleum-related prices, for that would do little to reorder personal, industrial, or national spending priorities. Rather, we must raise the prices of those products that we, as a people, can most afford to do without.

A moderate but gradually increasing gasoline tax, accompanied by refunds to those who would otherwise suffer undue hardships, that is, those whose livelihoods are dependent upon it, and by investment in mass transit, is the best means of achieving the necessary targeted reduction in oil consumption. It could be set at 10 cents the first year, and increased by perhaps 5 cent increments over the next 4 to 5 years. This would bring about some gasoline savings immediately, but would also signal a future of gradually higher prices. Consumers and auto manufacturers would plan and act accordingly. The transition to a more efficient auto fleet and better public transportation would be steady and rapid.

To reduce the inflow of Arab oil and the outflow of dollars, we could set quotas rather than impose a tariff that, by its very nature, would result in inflationary price increases. At the same time, we should involve the Government more directly in negotiations with oil exporters, perhaps by having it require exporters to bid for access to U.S. markets.

In addition, instead of taking a voluntary approach toward development of more energy-efficient automobiles, as the President's program suggests, we should proceed to set mandatory efficiency standards which would require companies to make more efficient cars.

Further, I think the Congress should quickly, and favorably consider the President's proposals for a mandatory efficiency standard for new buildings, a tax credit to those who retrofit existing buildings with insulation and storm windows, and subsidies to low income families to make their homes more energy efficient.

In conclusion, let me summarize my position. There are some who have argued that we should accept the President's proposals because the Congress has yet to come up with an acceptable alternative. The argument is that, if we fail to do so, Congress will lapse into inaction and the country will remain without a coherent, effective national energy policy. I reject this argument.

The choice is not between the proposed program and nothing, but between the proposed program and a program more consistent with economic recovery.

The President should be commended for presenting a well-integrated program which challenges the Congress to act. And I would hope that many of the elements of the President's program will be on the agenda for congressional action this year. But given the current state of the economy, I believe that the Congress must assess the impact of tariff induced higher energy prices on the level of economic activity and employment before endorsing through inaction the President's proposals. In unilaterally raising the tariff on crude oil and imported products without congressional concurrence, the President has denied Congress the opportunity to make this assessment. It is now up to the Congress to consider the appropriateness of his action.

My position is clear. I urge the Senate to join with the House in denying the President the right to unilaterally impose this tariff, at least until sufficient time has elapsed to assess its economic impact and to consider whether the goal of reducing imports by 1 million barrels per day in 1975 is really in the national interest.

I recognize that this recommendation runs the risk of continued congressional inaction. And, for this reason, I make it somewhat reluctantly. However, I have concluded that it would be so damaging to our already weakened economy to increase energy prices across the board that I am prepared to take this risk. I hope that if the Congress decides to reject the tariff, it will not delay in developing an alternative, perhaps along the lines suggested, which will bring our Nation's energy budget into better balance.

Thank you, Mr. Chairman.

The CHAIRMAN. I would like to ask to each person be limited to 7 minutes in the first round of interrogation, and we will call on our new members first. I would like to call first on the Senator from Colorado, Mr. Haskell.

Senator HASKELL. Thank you, Mr. Chairman.

I was particularly interested, Mr. Schultze, in your analysis of the unknowns in the President's program, that is, the economic impact which you who are expert economists believe is as yet unknown. Could you elaborate a little bit more than you did on this matter. I think this is probably one of the most important considerations.

Mr. SCHULTZE. Yes, sir. Well, there are a lot of unknowns. I think I might put them into four categories.

First, there is the impact on national spending and purchases and, therefore, national employment, what it is going to do after the entire program is active, and what would the net result be in terms of consumers and business, and State and local government spending. Even though it is true that on the surface the program takes $30 billion and puts $30 billion back, there are a number of reasons why that is not a good measure of what it is likely to do.

First, given the fact that other fuels not involved in the program will rise in price, it is clear that consumers will be paying much more out by way of higher energy prices than they will get back by way of the Government's proposed tax cut. On the other hand, there is a $6 billion corporate tax cut included in the President's payback of the $30 billion. What this will do to business spending in the short run we do not know, so that when you net all of this out, I think there is a very good chance, but nobody can tell you for certain, that the reduction in spending in the American economy because of that drain in funds on higher energy prices will be greater than the income pumped back into the economy under the President's program.

Now, I do not know that, but it is something that needs much more careful investigation. I think it is likely.

The second thing is the impact on inflation and prices. The President's prepared announcement and answers to questions indicate a 2-cent price increase as a result of his action. Other independent estimates push it up to the neighborhood of 4 to 5 percent. But that is only the first round.

What happens to wage rates when prices are jacked up another 2 or 3 or 4 or 5 percent? How much of that gets its way into a new round of wage-price inflation? What do we do about it?

The third area of uncertainty is what does it do to the oil industry? It is not at all obvious to me, and I do not pase an expert on the oil industry, but it is not at all obvious to me that the combination of action of import tariffs, decontrol and windfall taxes will end up with significantly greater incentives for oil production.

My own initial judgment is that it is likely to reduce incentives because of what it does to the price of new oil, which is the oil fundamentally you get from exploration and drilling. It is going to reduce, going to reduce that substantially to producers.

The fourth question, we blankly assumed that a reduction in consumption through these higher prices and consumption of oil will come out of imports and not domestic production. That is no longer obvious.

The major people who are working to decide when consumption is cut, how much comes out of domestic production and how much comes out of imports are the major oil companies. They may, for perfectly legitimate business reasons, decide that their interests are to keep the flow of imports coming in, in order to keep their connections abroad, and to take the reduction out of the domestic production, and what does the U.S. Government need to do to insure that that does not happen. It is not addressed in the President's program.

At this moment, I do not want to argue whether he is right or wrong. What I do say is I cannot conceive—maybe I am naive—but I cannot conceive of the Congress of the United States enacting something this big and this important, with the long-range effects in a period of 2 months.

Senator HASKELL. Thank you, Mr. Schultze. Just one more question. Putting aside for the moment the effect it would have on the oil industry, which, of course, is unknown, would you concur with my thought that when you put a $3 tariff on imported oil and you decontrol domestic oil, what you really are doing is bringing oil prices, to the consumers to the neighborhood of $14 to $15 a barrel?

Mr. SCHULTZE. Well, with a minor qualification that I will not bother you with, yes.

Senator HASKELL. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. Next we will call on Mr. Brock, the Senator from Tennessee.

Senator BROCK. Gentlemen, I have been interested in the testimony, and I am generally sympathetic. I am particularly sympathetic to my friend from Arkansas, because we have the same problems. We use a great deal of propane in my State, and we have experienced the same hardships that you have. I have a considerable distaste for those actions which led to that price increase, and I consider it to be a deliberate action, because propane is not included in the cost of living formula. We allowed the refiners to load in increases there that they could not have gotten away with otherwise.

Our State, like Arkansas, uses more gasoline per capita than the Senator from Massachusetts' State by a considerable amount, because there are great distances that we have to travel, and that is what brings me to the fundamental problem that I have.

I share Mr. Schultze's concern about the impact on the economy, and Mr. Sawhill's recommendation, I support everything you have said and have for some considerable time.

But, John, you served in that office long enough to know that a lot of things you asked the Congress to do we did not do, and this is not a 2-months delay. It has been going on for a year and one-half, and nothing has happened. Nothing.

You suggested a price increase on gasoline and the Senator from Massachusetts suggested a price increase. That would tear the dickens out of the State of Tennessee and the State of Arkansas and, General Tucker, you and I both know that.

Mr. SAWHILL. Although I should point out the price increase I suggested is less than would occur as a result of the President's program.

Senator BROCK. All right.

Senator KENNEDY. And I do not support it.

Senator BROCK. But you do not support it. You see, that is our problem. This is a panel, all of which is opposed, all of you are opposed to the President's program, but there is no program from the panel. There is no agreement.

Some of you might support rationing, I doubt it, but it is possible. Not many people support rationing.

The point is that the way we are going, there is no effective effort to deal with the problem. Now, I am not sure that I want a $3 increase rise. As a matter of fact, I am quite convinced that it is not a good idea, but somewhere, somehow we have got to come up with a specific alternative. We just cannot be 'agin.' People have been complaining about this a lot longer than 2 months. I have not seen the Congress lift a finger to deal with the fundamental problem. You cannot get a natural gas deregulation bill through this Congress, Mr. Sawhill, and you know it.

Mr. SAWHILL. Well, I think there are a number of things that probably most Members can or would agree to. Thermal efficiency standards for new buildings.

Senator BROCK. That is long term.

Mr. SAWHILL. It is long term, but I think what we really need is a package of long-term measures, a package that would be credible to our Allies and the rest of the world. A package that would convince them that we are really serious about reducing the rate of growth of energy, to plan and which includes measures designed to increase supply such as opening up the Naval Petroleum Reserve No. 1.

Senator BROCK. We have been trying to do that how long, John Sawhill?

Mr. SAWHILL. Several years.

Senator BROCK. All right. And we have not done it yet?

Mr. SAWHILL. No, but I think we could have more success this year.

Senator BROCK. You mentioned natural gas increases, and we have been trying to do that a while.

Mr. SAWHILL. Of course, the price did go up substantially last year, due to the efforts of the Federal Power Commission.

Senator BROCK. Go ahead. I am sorry.

Mr. SAWHILL. No. I just said that the price did go up substantially last year, but not due to Executive action, but due to the Federal Power Commission.

Senator BROCK. My question is, gentlemen, how long do we wait for a working agreement between Members of Congress and those who are concerned about the problem before we take action? Is not the President's proposal nothing more than a forcing of action?

I do not like it, you do not like it, but until we have some mandate to require the acceptance of responsibility on the part of our public institutions, we are not going to solve the problem, and we have a problem today of $60 million a day being drained out of this Nation's natural wealth from the people of this country to pay for imported oil.

We have inflation running at 12 percent. We have a $55 to $65 billion deficit staring us in the face, and we have a massive shift of our natural wealth from the private sector to the Government.

And all we do is complain about the President's program. Now, what is the alternative?

Mr. SCHULTZE. Senator, you know I think the central question facing this committee now is if the President is going to use a political weapon at the head of the Congress, and maybe there ought to be some various weapons at the head of Congress, to try to get them to act, can this Nation afford a weapon which drains $800 million a month out of the economy?

It is like saying, "if you do not act, I am going to shoot your friend." Whatever the President should or should not do in terms of legitimate political weapons of the Presidency against the Congress to get them to act, this is not it.

What scares me is the economic impact of doing this by unilateral imposition of tariffs.

You know, we can argue, and there are reasonable differences.

Senator BROCK. Mr. Schultz, I do not argue that at all and I tend to agree with you. Can we get from those who oppose the President's action a commitment that there will be an alternative and a more reasonable course within a very specific time frame?

Governor SALMON. I would like to respond, Senator Brock, as an individual Governor. The Trade Act, which is the subject of a law suit that 10 Northeastern Governors have initiated, says, among other things, that the Secretary of the Treasury will consult with appropriate public officials before imposing a tariff, or the license fee, if you will, which brings us here today.

President Ford, when a group of Governors met with him 4 days after his taking office, indicated that we had reached a new plateau in Federal-State relationships. Now, we absolutely, as a group, Democrats and Republicans, and we even have an Independent up in Maine now, have zero imput on this program, not opportunity to sit at the head table in any way, shape, or manner.

I do not think any of us came here today to offer the net panacea kind of solution to this problem, but I think this, Senator. I think that there are other alternatives.

I think one alternative that the Congress of the United States ought to look at very, very seriously is the mechanism of the manadatory allocation system that kept us alive in the Northeast last winter, the concept of volumetric control and a rather creative, highly flexible approach to individual States utilizing less product on a basis that I outlined at a recent meeting of the New England Governors' Conference. I think this is a concept.

You fund to the level of nearly $6 million in New Engand and the activities of the New England Regional Commission were responsible for the preparation of the charge that Senator Kennedy alluded to. I sense that we have a capacity, thanks to Federal dollars, if given any reasonable leadtime to come to the Congress of the United States and make some serious recommendations for alternatives in terms of a comprehensive energy plan.

We are not here today to nay-say the President, and emulate the role of the ostrich. I think we are here to suggest we have had zero imput and we would like to be included in the decisionmaking process.

Senator BROCK. My time has expired. Thank you very much.

The CHAIRMAN. Stick around, Senator, and you will have another chance. Next we will call on Senator Packwood.

Senator PACKWOOD. I find, in going over the figures, that $55 and $60 billion are thrown around commonly as the cost of the Ford energy program, and I keep trying to look for where these estimates come from. I finally come back to this source document, called the Cost of the Ford Administration Energy Program, prepared for Senator Henry M. Jackson by somebody on the Interior Committee or the staff of the Interior Committee. It is not signed.

And I find the facts wrong, I think. John Sawhill, I want you to listen while I read something and tell me if I understand this correctly.

On page 2 of this document, the following is stated: "Each dollar OPEC raised its prices would further increase U.S. consumer cost of energy an additional $10.4 billion per year." $10.4 billion, it says here.

On the next page it says "each dollar per barrel increase in the OPEC price would increase consumers costs an additional $5.5 billion per year." Now, is that the same statement?

Mr. SAWHILL. Yes, I think so.

Senator PACKWOOD. Well, I would have thought so too. Then the fact sheet put out by Senator Jackson and Senator Kennedy reads this way: "Every $1 per barrel increase," and this is by the OPEC countries, "takes away $8 billion per year from the American consumer in higher energy costs." Is that the same statement?

Mr. SAWHILL. Sounds like it, yes.

Senator PACKWOOD. It certainly does sound like it. Let me ask the panel where are the facts on this? I do not care who answers.

Senator KENNEDY. Well, Senator, just with the overall estimates I would be delighted to go on through based upon, for the most part, Treasury figures which were worked up with the Treasury Department. The $3 tariff on imported oil, 6.5 million barrels per day times 365 days, times three is a $7.2 billion increase of price, presently controlled oil, 5.7 million barrels per day times $8.15 is a $17 billion increased price, presently uncontrolled oil is $3.3 billion, less the rebate for petroleum products $1.8 billion, increase of price of uncontrolled, intrastate natural gas, $3.4 billion plus the increase in price of coal, $3.12 billion, which comes to $32 billion.

Senator PACKWOOD. I have got——

Senator KENNEDY. Those are substantially supported by the Library of Congress.

Senator PACKWOOD. There is the Library of Congress study too. But I do not understand how the fact remains that from the Interior Committee we have a $5 billion difference in the statement from two pages. Those are big amounts to be throwing around, and you say the program costs $50 billion or $55 billion, and then you are off that far.

Mr. SAWHILL. Suppose it is wrong by $10 billion, for example.

Senator PACKWOOD. What do you mean just $10 billion.

Mr. SAWHILL. I mean, I am not sure that the point is whether it is $50 billion or $45 billion. The point is that it is draining a substantial amount of purchasing power.

Senator PACKWOOD. That is a point, John, only in this sense, I do not mind arguing the program or defending or attacking it, but I would like to have some reasonable judgment of what we are talking about. I find that by just doing a little mathematical calculation from the Interior Committee report even the multiplication is wrong.

Senator KENNEDY. Senator, as I understand it, the administration said $30 billion was the admitted direct cost of its energy program and they did not include coal. The estimate was that we added 3.1 on coal. I do not think that there is really a dispute as to the direct costs.

The question is the additional ripple effect, which the administration denies.

Senator PACKWOOD. There is a dispute in this sense with the Interior.

Senator KENNEDY. Take the economic principles of most of the distinguished economists who have appeared before congressional committees and they all expect this ripple effect to occur.

Senator PACKWOOD. The Interior Committee purports to have an analysis of the Ford Energy Program, and bases its tariff on imports of 6.5 mmbd. The Ford program presumes 5.3; there is the difference then of over $1 billion in tariff revenues. I think the facts are wrong. I would not mind it if they want to come to different conclusions, but they say this is the assessment of the President's program, and they start out with the wrong assumptions.

Senator KENNEDY. I think we used the President's own assessment of $30 billion.

Senator PACKWOOD. Well, that cuts it immediately in half.

Senator KENNEDY. The fact is they did not include any increase in the cost of coal and the best estimates of that are approximately $3 billion, so that is where at least our figures on direct costs reached $32.5 or the $32.2 billion. But we are not prepared to quibble.

The additional cost of $15 to $30 billion is the ripple effect. And we are using the formula that Data Resources Inc., the Brookings Institute economists and other leading economists have used.

Senator PACKWOOD. Let me ask you just again. In Senator Jackson's statement—and I wish he were here, but John, you can answer it—can you presume elasticity on price or not?

Mr. SAWHILL. I think there is some elasticity.

Senator PACKWOOD. How much?

Mr. SAWHILL. I do not think any of us really know. We generally estimate it at about .1 for gasoline in the first year, and maybe twice that in the second or third year.

Senator PACKWOOD. Explain that to me. I am not sure about that.

Senator Jackson's written statement says in one of his presumptions, the Ford energy program fails to limit energy consumption significantly because the demand for petroleum products is largely insensitive to price changes. Is that true?

Mr. SAWHILL. It certainly is relatively insensitive to price change.

Senator PACKWOOD. Just before that he says fuel costs increased by $1 billion in one segment of the transportation industry alone, the airlines, which could lead to a 15-percent increase in air fares or result in as many as 50,000 lost jobs. Now, what he is saying is that air fares will go up and fewer people will fly.

Mr. SAWHILL. Yes.

Senator PACKWOOD. So that is very sensitive to price.

Mr. SAWHILL. In that case it would be; yes.

Senator PACKWOOD. Well, are there some others? Now are there some other cases?

Mr. SAWHILL. Yes; I think there are probably other cases. I do not think it probably is sensitive in home heating oil, particularly, or gasoline.

Senator PACKWOOD. We cannot make a generalization that it is insensitive to price.

Mr. SAWHILL. Not all petroleum is insensitive to price.

Senator PACKWOOD. All right, now, let me go one more, and I will address this generally, I will read Senator Jackson's statement from the Congressional Record into the record first.

He says, "the Interior Committee will soon begin working on legislation I (Jackson) shall introduce to reduce our Federal oil consumption and dependence on Middle Eastern oil without huge price increases." Can that be achieved without price increases?

John, can it then be achieved without either rationing or allocation?

Mr. SAWHILL. I do not think so.

Senator PACKWOOD. Allocation is rationing, it is wholesale rationing.

Mr. SAWHILL. Yes.

Senator PACKWOOD. Do we agree that we need to reduce our consumption, or is that even a presumption that we can start with?

Mr. SAWHILL. I think that is the presumption that we ought to start with, frankly.

Senator PACKWOOD. There is no way that we will achieve that without price increases or allocation or rationing, or something of that nature, is that not right?

Mr. SAWHILL. Correct.

Senator PACKWOOD. My time is up.

Mr. SCHULTZE. I wonder if I could interject one comment. Everyone agrees that there needs to be conservation and a cut in consumption. I think there is, however, substantial disagreement that it ought to be 1 million barrels in the first year.

Senator KENNEDY. Could I just make an observation, Senator Packwood. I personally favor a mandatory allocation program. I would base it upon 90 percent of allocation, which would save us approximately 700,000 barrels of oil. It would be targeted to gasoline and would not have an increase in terms of costs. I think that could be done—reached gradually over a period of 1 or 2 years—as an intermediary measure until the full impact of the long-term conservation program can begin to be felt. This longer term program that John Sawhill and the administration have talked about in terms of fuel-efficient cars, home insulation, building and appliance energy standards, et cetera.

Senator PACKWOOD. Did you say 700,000?

Senator KENNEDY. 700,000.

Senator PACKWOOD. Targeting it toward gasoline?

Senator KENNEDY. Just gasoline.

Senator PACKWOOD. No price increase?

Senator KENNEDY. No price increase.

Senator PACKWOOD. And roughly how much diminishment in available gasoline?

Senator KENNEDY. About 700,000.

Senator PACKWOOD. Round that out.

Senator KENNEDY. 700,000 barrels a day.

Senator PACKWOOD. I understand. How much do we use today?

Senator KENNEDY. 6.7 million barrels.

Senator PACKWOOD. Of gasoline?

Senator KENNEDY. Of gasoline.

Senator PACKWOOD. OK.

Senator KENNEDY. It seems to me that we could reach the 90 percent that we saw up in our part of the country last year without the prolonged lines that were evident in January and February.

Now, let me mention in the Oil Daily newspaper, that the Independent Gasoline Marketers of America also favors a mandatory allocation program. They say at 90 percent of 1972 rates, it would save between 700,000 and 750,000 barrels.

Our studies indicate that at allocations averaging 86.4 percent, the lines began disappearing, they say, which is even a lower allocation than we have talked about here, and it seems to me that this would be a step that we ought to try. It does not have an impact in terms of increased costs. And if we set the goal for 90 percent on a gradual program, it is doing almost what the administration has asked for. It is moving down that road in a completely responsible, reasonable, cautious manner. It also has the absolute assurance that that amount is going to be saved since it would be linked to reduce gasoline and crude imports. You do not have the variables which exist in the administration's program where you do not know what the actual price elasticity will be.

As we mentioned earlier, the principal savings that are contemplated in the administration program are in distillates, where in New England there is complete inflexibility in terms of reducing home heating oil use since it is already reduced by 22 or 23 percent, and in residual oil, which is industrial and utility fuel, and where there can be only marginal reductions. So, it would seem to me that the conservation target should be in gasoline and it seems to me that we ought to try a mandatory allocation program initially. We also should move very strenuously on the other points that the President has talked about, even mandating requirements for additional fuel efficiency for cars.

There is a car, as you know, being produced by Honda, being imported by Volkswagen, that gives 37 miles to the gallon. We are completely within the possibility of technology. There can be diesels. If we went to diesel cars that are slightly more expensive, $400 to $500 more per car, slightly heavier, but they last up to 200,000 and 300,000 miles rather than 100,000, and they increase gasoline efficiency by 75 to 100 percent.

You have all of these alternatives which are available over any period of time which can achieve the elimination of wastage and duplication, and which do not have these dramatic effects which I think spell absolute disaster for the economy.

Senator PACKWOOD. I just think that we should not try to con the public, and if we are going to reduce petroleum or gasoline consumption, we are either going to have rationing or have allocation, whatever you like, or price increases. And everybody hopes that we are not going to do either one, but that we are still going to achieve the reduction, and I do not think that is likely.

Senator KENNEDY. I would say that it has been presented to us, both by the Secretary of Interior, when he met with New England Senators, and by the President, that you either have to have an increased price or a supply restriction program. We have seen in New England and in other parts of the country that the mandatory allocation program was working darned effectively, and efficiently in New England at the end of the embargo, not so in February, but in late March and April it was working fairly well. We also can insure that it would be a targeted program on gasoline without the extraordinary risk of economic impact that the administration energy program would have.

Now, maybe it would not work. It seems to me that it will work. It seems to me that its implications in terms of our economy are the least dramatic, and it certainly seems to me to be worth trying before we go into a program that threatens our chance for economic recovery.

The CHAIRMAN. Senator Mondale.

Senator MONDALE. I guess I would ask my questions jointly.

Senator KENNEDY. Mr. Chairman, I am going to have to leave in just about 3 or 4 minutes.

The CHAIRMAN. Well, we may submit you a few written questions.

Senator KENNEDY. I would rather have Charlie Schultze and John Sawhill and these other panelists answering for me.

Senator MONDALE. I would like to ask a question jointly of Charlie Schultze and John Sawhill, and maybe I will just lay out my thesis and you can comment on it.

The proposal of the President almost beyond dispute has many profound adverse economic impacts and they concede it. It will contribute to inflation—perhaps two, three or four points. It will contribute to a recession, because it is drawing more money out of the economy—10, 20 billions of dollars, nobody really knows—than it is going to put back into the economy.

It will increase the cost of doing business. It will visit the cost unfairly upon people of moderate- and low-income. It will overcome one of the major advantages which American businesses have in international trade, less expensive energy, so that no matter how you look at the program, it is a powerful blow to the economy. And I think that is pretty well conceded.

Now, the question is, why must we then mutilate ourselves in this way? And the answer is that we must because we must reduce consumption by 1 million barrels this year and by 2 million barrels by the end of 1977. The whole case of self-mutilation is based upon an assumption that we must reduce imports by 1 million this year and 2 million by the end of 1977.

Then, the question is, where did that figure come from? And, as I understand it, no representative of this administration has yet been able to say where it came from.

Joseph Kraft has asked repeatedly of Secretary Simon and others, and they all say they cannot give the reason for the million barrels and then the 2 million barrels. Well, now, if that is correct, do we not first have to have to ask ourselves by what amount we wish to reduce imports, and then second, how do we best reduce those imports and then compare that problem with the other problems we face.

And it seems to me that a lot of the questions we have heard today, a lot of the charges that the President made in this Congress, are made on the basis that we must accept those sharp reductions in foreign imports.

Mr. SCHULTZE. Senator, fundamentally I agree with that, your line of thinking. I think first the President's long-run energy goals, the quantities involved are not unreasonable. Now, you can quarrel with this part or that part, but basically the 1980 and 1985 goals are not unreasonable, No. 1.

No. 2, this is a marvelously adaptive economy. The beauty of the free enterprise system that we have is that give it time and it can adapt to a lot of changes. It has in the past and it can in the future.

But, we also know that it cannot adapt overnight. How do you adapt people's heating practices? Among other things, the kind of heating system they install, but you do not build 60 million houses a year to completely replace them.

How do you change producer's industrial processes? They can change, they can respond, but they cannot do it overnight.

So, the first proposition is the long-run goal, which I think makes some sense. Trying to get that in a hurry, in the best of times, trying to get that in a hurry threatens the economy. And now, it is really dangerous, because we are not in the best of times.

Senator MONDALE. That is the point. I agree that we need a searching, long-term program both on the supply and the demand side including many of the features that Mr. Sawhill mentioned. I think that is what we should be doing, but it is the dramatic reduction and the bluntness of the imposition of that reduction, coupled with the $3 tariff, which it seems to me gives us all of these tremendous disadvantages, and it is all based upon a target that they cannot explain.

Mr. SCHULTZE. Can I elaborate a little bit on that, Senator? One other point.

I think there is a confusion between going to an international meeting with a program, a long-run program, and going to an international meeting with something you do overnight. I do not see where we gain from the second.

I think what is important internationally is the first, and it is that big confusion that I think has engendered this.

Mr. SAWHILL. If I could just add kind of a footnote to what Charlie said, because I certainly agree that there are two reasons why we would want to cut back our imports, one is our vulnerability to the Middle East, and the second is our balance of payments problem, and I cannot think of any other reasons.

Senator MONDALE. Would you yield? Is there any guarantee that this program will do either?

Mr. SAWHILL. No; but the fact is, even if we cut our imports back by a lesser amount, we are still vulnerable .Suppose we cut out imports back by 1 million barrels a day, from 6½ to 5½ million barrels a day, the fact is we are still very vulnerable and we still have a big balance of payments problem, and I would argue, frankly, that it is probably the best thing for the world economy if the United States runs a slight balance of payments this year. If our trading partners are running very severe balance of payments deficits, they have got to finance them, and the only way they are going to finance them is if they are able to sell their exports to this country, i.e. if we run a small deficit in 1975.

So, I do not think either of the two reasons why we would want to cut back, vulnerability or balance of payments, argues for a cutback of 1 million barrels a day. And I agree with Charlie that what we need is not a big import reduction goal in 1975, but a credible, long-range program consisting of the measures that I outlined in my statement.

Senator MONDALE. In the addition to the question of the million barrel figure, there is a question of whether this does much about it. There has been a lot of testimony that we can expect a continuation of rising foreign imports even with this change.

But, I submit, Mr. Chairman, that this program is not to be explained by economics. I do not think it has anything to do with economics.

This program came from the Secretary of State, and it was designed not to help the American economy, but to help him in what he thinks he needs to be demanding. I think it is poorly conceived. I think, in fact, it will be counterproductive to his own foreign policy, because it will help further destabilize this economy, and I think we ought to have the Secretary of State up here to explain where that million-barrel figure comes from and why he thinks we must do this to our economy and to the American people to serve some end.

He is the person that is pushing this and let us hear from him why he wants it.

Senator PACKWOOD. I agree. I think that we ought to have him here next Thursday or Friday and not move at all until we have had a chance to hear his testimony.

Senator MONDALE. Let's get him up here this afternoon.

Senator PACKWOOD. Can we do that, Mr. Chairman?

The CHAIRMAN. I will do whatever this committee wants to do.

Next, I am going to call on the junior member, which in this order would be Senator Hansen.

Senator KENNEDY. Mr. Chairman, unless you had a particular question——

Senator HANSEN. No. You are too tough for me, Senator.

Senator KENNEDY. We will be over rattling around the floor there anyway, I am sure. Thank you, Mr. Chairman, and members of the committee.

Senator HANSEN. Mr. Chairman, I know that Senator Jackson had a very busy day yesterday, so I can understand why he probably would have brought up Charles Owens' testimony before the Interior Committee probably without knowing exactly what Mr. Owens said. It may be interesting to everyone to be reminded, as I am certain I need not do to him, that Mr. Owens was Deputy Assistant Administrator for Policy, Planning, and Regulation at the Federal Energy Administration up until some time not too many months ago.

In that testimony, Mr. Owens says:

> Since 1973, U.S. policy has been to allow essential foreign supplies into the United States to stimulate declining domestic production and to restrain prices. These new goals spawned the current mandatory oil import program and such programs as the two-tier pricing system, which is an attempt to both stabilize domestic crude prices and increase domestic exploration and production.

A little later on during his testimony, Mr. Owens says:

> Decontrol of new natural gas prices would allow gas prices to rise to parity with oil prices. Intrastate gas prices could be expected to rise to oil parity as well. Both would mean a substantial boost in producer profits and the incentive to find more natural gas.

I have not yet had a chance to ask Senator Jackson if he has changed his position on natural gas deregulation. Apparently, Mr. Owens is quite firm in his conviction that that would be a step in the right direction. But, let me say, on the last page of his testimony, Mr. Owens says, "From virtually the moment I completed the design of the two-tier system," and he is the guy who designed the system against which he now speaks, "I have steadfastly maintained that it should be done away with."

He continues on by saying, let's get to it gradually, so as not to upset anything, but he is damning the very system he put in, and I would hope my good friend, Senator Jackson, might find time in the next week or two to read exactly what Mr. Owens said.

Mr. Chairman, let me quote from the testimony of Frank Zarb before the Interior Committee, under the glare of blazing TV lights on January 31, 1975, when he said:

> The plain facts are that while we have been talking ourselves into no action or rationalizing some of the approaches to a hard problem, our vulnerability to political pressures from other nations has grown. The price of 40 percent of

the oil we use continues to be set by the cartel and has no relationship to a free market. And what is more important, the threat to our national security grows more each day. To those who say action is too extensive, they should also reflect on the cost of the new embargoes within the next 3 years if we do nothing.

I was impressed with the statement that the attorney general from Arkansas, Mr. Tucker, made, when he said that this is taxation without representation. Those words, of course, ring down through the corridors of time, and I think they may have started around Boston. The point is, and we ought to keep this in mind, the President has not done anything that has not been authorized by the elected Representatives of the people of the United States.

This committee, as you know, Mr. Chairman, passed the Trade Act of 1974, and all the President has done, I submit, is in full compliance with that law.

Now, he has proposed many other things that the panel does not like, and let me join the panel and say I do not like many of them either. I think there are definite disincentives insofar as the domestic oil industry is concerned, and I say that before these proposals by the President are going to be enacted into law, that you can be certain that Chairman Long will convene the committee, and we will go over those proposals, and I suspect we will call, in addition to Secretary Kissinger later this week or next, others who may have been able to defend some of the proposals. I do not think by any means they all ought to be adopted into law, but the fact remains that when Senator Jackson says he is proposing legislation, he surely is.

That is an old record. He has been proposing it for several years. I am on the Interior Committee, and we have been so busy on that committee for the last Congress, the 93d, that I had to introduce myself to the chairman of this committee. He did not remember me, I had been gone that much, working on the energy proposals.

We have worked on more legislation than you can possibly imagine, and we have studied and we have had testimony and we have had occasional TV lights. But we do not get down to basic solutions to the problem.

I do not propose for a moment to say that what the President has proposed ought to be passed in toto, but I do say that it is a step in the right direction.

And I need not remind people from the Midwest, from Ohio, as an example of what I am saying, that about 3 weeks ago, United States Steel, which has a little plant in that State, laid off 1,200 people, and they later laid off about 600 more at the end of the week. And if I could just finish this statement, Mr. Chairman, let me say that the significance of that plant in the total overall economy of the United States is that while only 1,800 people were put out of work, and maybe you can multiply that by four if you want to get the full impact of the number of persons directly affected, that plant made casing and collars and valves and other things needed desperately by the domestic oil industry today.

So, because we have tried to keep prices low, because we have not wanted to face up to the tough problem that we should have done a long time ago, we have denied the domestic industry the ability, through the discouragement of a regulated natural gas price and a regulated two-tier oil price that was designed by Mr. Owens, the ability to come to grips with the problem.

The CHAIRMAN. Thank you very much, Senator.

Next we will call on Senator Byrd.

Senator BYRD. Thank you, Mr. Chairman.

Mr. Schultze, you said that the President's proposal is very complicated and very complex, and I certainly agree. It seems to me it is quite inflationary.

Would you comment on that aspect of it?

Mr. SCHULTZE. Yes, sir. It raises prices in one way we know about and one way we do not. Or we do not know very much about.

First, it directly raises the price of fuel and energy products throughout the economy. That we know. And while there are quarrels, we can calculate roughly what that is. And it ranges somewhere I think, from 3 percent to 4 percent.

Second, it has a second-round impact, because that will go to increase wage demands. If price indexes rise because of this by 3 to 3½ percent, will that not mean additional wage increases, and then a second round of price increases, and this has nothing whatsoever to do with energy.

Do not get me wrong, Senator, I do not know how much that will be and I do not think anybody really does, except some escalation clearly will happen. So yes, on two grounds it will raise prices.

And then you have to ask yourself to what extent is it worth it, under current circumstances. Some price increases may be worth it. Under the current circumstances, I think it is too much, and it is not worth it.

Senator BYRD. What do you regard as an appropriate energy conservation program?

Mr. SCHULTZE. Without dealing in numbers year by year, I would regard an appropriate energy program as one which took the President's 1985 goal of getting imports down to something in the neighborhood of 4 to 5 million barrels a day, against which we could cover ourselves through stockpiling, and then have a currently legislated program, currently legislated, which would get our consumption and production to the point where by the mid-1980's, we are down to what the President aims for.

Senator BYRD. Yes, but we are talking about 1975, now. Can we wait as long as 1985?

Mr. SCHULTZE. I do not think you can wait to legislate it. I do not think you can wait to legislate. I think it should be legislated this year.

But I do not think, Senator, you gain anything by trying to get a million-barrel-a-day reduction this year, instead of aiming for 200,000 or 300,000 barrels a day this year, 300,000 or 400,000 barrels a day the year after, and then gradually increase it to where the President wants to go. I see nothing magic about 1 million barrels a day this year. But I think it is important to get legislation this year.

Senator BYRD. Well, then, is your opposition on his program based on the million-barrel-a-day figure, or is it based on opposition in increase to the tariff?

Mr. SCHULTZE. Let me say, Senator, I think there are three points to my opposition. One, whatever you think about the President's long-range comprehensive program, whatever you think, even if I agreed with that program, I think it would be a big economic mistake to impose the tariff unilaterally before the Congress enacts it. So my major concern at the moment, quite apart from the President's legislative program, is his unilateral steps to impose the tariff before the program goes into effect, because that is going to hurt the economy.

Senator BYRD. Go ahead, sir.

Mr. SCHULTZE. Then second, I do have problems with the program itself. Although I think that may be less relevant for the immediate bill at stake, I do have problems with the program itself, and they are the same problems that Mr. Sawhill stated.

One, I have just indicated earlier, the legislative program tries to get there too fast, and it is going to harm the economy by going in the right direction too fast.

Second, on a more detailed level, I think it attempts to get where we ought to go by putting too much emphasis on heating oil, and public utility use, and not enough on gasoline. So I have problems within detail of the program also. But it is that central point of trying to get to where we ought to go in a hurry, which I think is bad.

Senator BYRD. The point you make about the home heating oil is the point that gives me the greatest concern about the program that we are considering. As I visualize it, there does not seem to be any good solution to the problem which Congress and the administration and the country is groping with.

You have the President's plan, which all here are testifying against, and which I am not inclined to favor too much either. Or you could have a program where you cause a very sharp increase in gasoline prices.

May I ask this, would it take, if you were going that route, would it take a tax of about 40 cents to 50 cents a gallon to reduce by any reasonable extent the amount of gasoline usage?

Mr. SCHULTZE. If that is all you were willing to do, if that is all you were willing to do, I do not know if that is the right number, but it probably would be in that ball park.

Senator BYRD. And that is not a very good program either.

Mr. SCHULTZE. I do not think either Mr. Sawhill or I are suggesting that.

Senator BYRD. No, I understand. I am trying to understand the alternatives.

Mr. SAWHILL. One alternative is not to try to reduce by a million barrels a day in 1975. What we are arguing for is not do nothing, and not to reduce by 1 million barrels a day, but to reduce by somewhat less than 1 million barrels a day.

Senator BYRD. Well, do I take that to mean then that you are not particularly against the President's program, except that you think that the million barrels a day is too much.

Mr. SAWHILL. I think that is one thing wrong with it, and I think the second thing wrong with it is that it results in price increases across the board. I think we can afford to have a small price increase in gasoline.

To answer your specific question, about a penny increase in the price of gasoline would decrease consumption by 25,000 barrels a day, so if we had a 5 cent increase, we would be talking about 125,000 barrels a day, and a 10 cent increase would be 250,000 barrels a day.

Senator BYRD. Could I have just 1 minute to follow up my third point?

Then the third possibility would be rationing. Do either of you favor rationing?

Mr. SAWHILL. I certainly do not.

Mr. SCHULTZE. Except, of course, under embargo conditions, but apart from that, I do not favor rationing.

Senator BYRD. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Hartke.

Senator HARTKE. I think the American people are probably very confused. Let me just demonstrate what the situation is here today.

On the one hand you are saying that you want to cut back on the importation of oil because of vulnerability, is that right, Mr. Sawhill?

Mr. SAWHILL. Yes, sir.

Senator HARTKE. And the second is because of balance of payments, is that right?

Mr. SAWHILL. Yes.

Senator HARTKE. Mr. Simon says we can stand a balance of payments problem, right?

Mr. SAWHILL. He may have said that. I do not know.

Senator HARTKE. Now, the vulnerability problem assumes there is going to be a war in the Middle East, does it not?

Mr. SAWHILL. Not necessarily.

Senator HARTKE. You mean they are going to cut off the oil supply otherwise?

Mr. SAWHILL. We are not only vulnerable to a cutoff, but we are also vulnerable to arbitrary price increases.

Senator HARTKE. I understand that, but that is the balance of payments problem again. What you are really advocating here is going to some type of rationing or allocation on the one hand, or some type of an increase in the cost of oil through a tariff on the other. And you are putting an embargo on, a self-imposed embargo, rather than an embargo from outside.

In other words, it is a self-inflicted wound.

Mr. SAWHILL. I am not advocating this—you did not understand that I was advocating this?

Senator HARTKE. I would have a great deal more faith if I could see something in the background to give me some justification. As I recall, Mr. Schultze, you were in President Eisenhower's administration, is that correct?

Mr. SCHULTZE. A very lowly staff member in the Government.

Senator HARTKE. Were you not on the Council of Economic Advisers?

Mr. SCHULTZE. I was a staff member.

Senator HARTKE. And then you came to be the Director of the Budget under the Johnson administration?

Mr. SCHULTZE. That is correct.

Senator HARTKE. At that time we went from a balance during the period when you were there, we went from a balance of trade situation of $7 billion surplus to practically nothing.

Is that correct?

Mr. SCHULTZE. I do not remember the numbers, but I assume that is correct.

Senator HARTKE. That is fair, is it not?

Mr. SCHULTZE. I assume that is correct.

Senator HARTKE. At that time, we had a request for a 10-percent tax surcharge, is that correct?

Mr. SCHULTZE. That is correct.

Senator HARTKE. At that time also, we saw a steady increase in inflation, is that correct?

Mr. SCHULTZE. That is correct.

Senator HARTKE. Now, what bothers me with all of this is that I do not understand exactly what you are trying to say here, and I do not think the American people do, when you say you do not approve of a million barrel cutback, and I do not either, but you think it should be something less than that, and you do not approve putting on additional costs, and I agree with that. You want to go back to some type of austerity in America here. If you cut back on the consumption you are going to cut back on the productive capacity of America without regard to cost.

You agree to that; do you not? You have been saying that?

Mr. SAWHILL. Yes, I agree. I think we can cut back consumption without cutting production.

Senator HARTKE. And you are falling right back to the old Eisenhower philosophy of 1952, which gave us the Democratic controlled Senate, and I was one of the lucky beneficiaries of that policy from 1955 to 1958.

Now, I am not going to excuse this administration, because all they have done is accelerate that policy. All I can tell you is that I do not know any reason to take those alternatives, but rather we should just go ahead and ditch both of these policies by increased production in the United States, and get on with the business of trying to increase the available sources of energy which we will need.

Now, all I can say to you is you are not advocating that?

Mr. SCHULTZE. That is correct.

Senator HARTKE. You are advocating an austerity program. What you are really saying is you can do more by doing less, and that has been the fallacy of the Johnson administration from 1965 on, and the fallacy of the Nixon administration and the Ford administration, and ultimately you will make us become so ashamed of ourselves that we will not be able to hold our heads high anyplace.

Mr. SCHULTZE. Senator, it is clear that we agree on the issue at the moment, and it is clear that we disagree on how simple the world is.

Senator HARTKE. I do not think that it is simple. You say everyone agrees that there is a need to cut back in consumption. I do not.

Mr. SAWHILL. The issue at the moment is the bill before us.

Senator HARTKE. No; the bill before us, I am going to vote against it. I mean, very simply, I am going to vote against it for a number of reasons, but that is something else.

You see, the reason you vote against it is one thing, and what you are saying here is another, and I would not want to put myself in a position of ever endorsing what I consider to be a very contradictory statement of policy which is not in any way any better than Ford's statement. And both of them, I think, ought to be put down where they belong.

That is, let us get America back and go ahead producing, because if you produce you can reduce costs, and if you cutback in production you increase costs, and what you propose would make the costs increase and would increase the unemployment, increase the balance of payments deficits and do all these things that have caused all of the trouble in the past.

And the only cut that I find more reprehensible, or maybe I should not say more, but equally reprehensible, is the policy of tight money and high interest rates.

Mr. SCHULTZE. Senator, just so the record would be straight, neither Mr. Sawhill nor I, or any of the witnesses, have been arguing for proposals which would increase unemployment, which in some sense would decrease production.

Senator HARTKE. Let me say when you were Director of the Budget, we had a steady decline in industrial employment, did we not?

Mr. SCHULTZE. We did not.

Senator HARTKE. From 1965?

Mr. SCHULTZE. I am sorry, Senator, you have not looked at your statistics. Certainly, during the period——

Senator HARTKE. Industrial employment from 1965 on went down.

Mr. SCHULTZE. Employment rose from 1961 to 1969.

Senator HARTKE. Industrial employment?

Mr. SCHULTZE. Senator, how do you define industrial employment?—

Senator HARTKE. By the same way as the Bureau of Labor Statistics does.

Mr. SCHULTZE. And which is what?

Senator HARTKE. They use it in the system, and I do not know here where——

Mr. SCHULTZE. They have private, nonagricultural employment, which rose, manufacturing employment during the period did not rise very much, but it is not industrial employment, Senator.

Senator HARTKE. Well, I just do not agree with the reasons, and I think I have made that pretty clear. And if I have not, I will just use the word perfectly clear.

Mr. SCHULTZE. Yes, sir.

The CHAIRMAN. Are you through with your questions, Senator?

Senator HARTKE. I am done.

The CHAIRMAN. I want to ask one or two questions.

In the first place, Mr. Sawhill and Mr. Schultze, I have had the pleasure of working with both of you two gentlemen down through the years when we had to try to face up to some rather difficult and sometimes unpopular decisions—in your case, for example, Mr. Schultze, trying to pass a debt limit bill, never a popular bill, but something that has to be done from time to time. We have tried to do some things to keep the economy moving, and also trying to do some of the things that might not have been too popular, but were in the Nation's interest during the difficult responsibilities you carried for many years around here, working as best you could for your Government, Mr. Sawhill.

I am inclined to agree in large measure with the argument that you two have made. But I find myself, at least at this point, doubting your conclusion, even though I agree with your argument.

Now, let me just get this straight in my mind, if I can. What percentage of overall energy reduction, Mr. Sawhill, does 1 million barrels a day amount to?

Mr. SAWHILL. Well, it represents about 3 percent.

The CHAIRMAN. That is about what I would assume.

Now, it would seem to me that the President's action will necessarily be very unpopular with the people of this country, and I am also convinced that it would be easy enough to put some program into effect that would be much more popular, or to put it more correctly, much less unpopular than what the President is proposing. I think that what he is suggesting in his approach is that he would use the powers available to him to put into effect a program that would be exceedingly unpopular, and therefore, make it easy for Congress to pass something which is likely to be much more acceptable to the American people and which he would recommend.

Now, it is not likely that we are going to pass the program that he recommends, but you have a Democratic group meeting right today trying to work up what they believe to be a substitute for his program. My guess is that if we just try to put that substitute into effect it will be a very unpopular thing, and I would hope the Democratic substitute would incorporate all of the suggestions that you have made here, for example, Mr. Sawhill, and there are some additions to that that could be made. But it would be a lot easier to enact if it were done to take the public out from under what the President's action, rather than act and put it into effect in a vacuum.

For example, there is a suggestion to bar those under 18 years old from driving. You know how popular that will be with the young people and their parents.

Senator BROCK. It would not be so unpopular with the parents, I think, at least this one.

The CHAIRMAN. It would involve a whole number of things, such as the suggestion to strictly enforce the 55 mile speed limit, or to close most filling stations on Sunday, and that will be unpopular with everybody in the hotel and motel business. It would seem to me, Senator, that if you had the President's actions in effect, it would put a lot of pressure on the Congress, and at the same time, be a great deal easier to put into effect the program that would conserve energy by striking down the President's action substituting another, than it would if the Congress had to assume the burden of putting into effect the program which, while not as unpopular as the President's program, would nevertheless be unpopular.

Now, what is your reaction to that?

Mr. SAWHILL. My reaction, Senator, is the President has done the Nation a real service by putting the Congress in a position already where they have to act. And the very fact that you have a group meeting today concerned with coming up with an alternative energy program is testimony to that.

The President, by coming forth with a comprehensive program, has put the monkey on Congress' back. So I do not think you have to permit this tariff to go through, which I feel would have a devastating effect on the economy, in order to keep the monkey on Congress' back.

I think it is already there. I think the Congress will come up with an alternative.

The CHAIRMAN. It has been my experience that my constituents appreciated me a lot more if I saved them from something they had actually experienced than if I saved them from mere conversation. If it is something we are talking about that never happened, it is difficult to explain to them how bad things would have been if we had not acted in the fashion that we did.

Mr. SAWHILL. Perhaps you are right.

The CHAIRMAN. I take it that you at least understand my view on that subject.

Mr. SAWHILL. Yes, sir. But I would say this, you and I have had many conversations about the energy industries, and we have talked a time or two about the depletion allowance, and I remember your saying to me many times in the past, John, if we eliminate that depletion allowance, what's going to happen is the oil industry is going to have to raise their prices, and then that is bad for the American people. And I think that this is an analogous situation here.

If we permit this tariff to go through, it is going to increase energy prices, and it is not going to result in any additional production, it is not going to provide any additional incentive, and it is going to further aggravate the economic situation.

The CHAIRMAN. I am all for the incentives, and I think that you and I could not agree more fully than we do in that regard.

I believe that we should be able to agree that gas rationing does not necessarily prevent an increase in the price of a product, whether you have an unlawful market, or whether you have a lawful market for rationing coupons. They still are going to be sold and they are going to be at a much higher price than they would be if you did not have a rationing system at all and you had plenty of supply.

Do you agree with that?

Mr. SAWHILL. I agree.

The CHAIRMAN. Mr. Schultze, I see that you agree with that also?

Mr. SCHULTZE. I agree.

The CHAIRMAN. I would like to pursue the matter further, but I will obey my own time limit and call on Senator Brock.

Senator BROCK. Mr. Chairman, I would like to pursue that point, because I think the Chairman is on the right point now insofar as what our real objectives are. When you look at the alternatives that we have previously agreed to, rationing or allocation or increased price, I think it is fair to say, and I do not know if any of you want to disagree, and if you ~~do~~, please do, that under allocation or rationing, you have no supply effect.

Is that not a fair statement to make?

Mr. SAWHILL. Yes. But, also it is a fair statement to say that under a higher tariff you have absolutely no supply effect at all.

Senator BROCK. I do not disagree with that. I find fault with both positions. I am sorry that Senator Kennedy had to leave for he came out very strongly for allocation. John Sawhill, you tried to allocate in this country and it is not possible.

Mr. SAWHILL. No, I would not favor allocation, but I am not sure, you know, you have to get back to the basic premises. That is, do we want to cut a million barrels a day, and I say no.

Senator BROCK. All right. I personally am in agreement with you and particularly Charlie Schultze on this point. I question the million barrels a day more than I do some of the other things.

But, it does not matter whether you are talking about 500,000, 700,000 or a million. We first have to make a distinction between our short-term problem of conservation and our long-term problem of supply.

And gentlemen, I have not heard from you any suggestion today on how we can increase supply without a change in the price mechanism; specifically, the two-tier price system as it affects oil and the deregulation of natural gas.

Mr. SAWHILL. I should point out that the two-tier price system does have an incentive for new oil. After all, it is selling for $11 a barrel and you are permitted to release an old barrel when you discover a new barrel, that is newly discovered, so that in effect that gives the person who funds a new barrel about $17 for that new barrel.

My statement outlined other actions to increase supply.

Senator BROCK. But permit me to point out, if you go for rationing or allocation you are going to reduce the high-priced fuels and increase the proportion of the low-priced.

Mr. SAWHILL. I am not favoring rationing or allocation. But I also do not favor decontrolling prices and putting on windfall profit taxes, and in effect rolling back the new oil price to $6.60. And I cannot believe Senator Hansen would agree with that either.

Senator HANSEN. I am on the record, Mr. Sawhill, as being opposed.

Mr. SAWHILL. Thank you.

Senator BROCK. I would much prefer to see a phased lifting of oil price controls and the deregulation of natural gas and get away from this tax concept, because that is taking the resource and putting it in the hands of the Government, which is not a productive investor under any circumstances.

Mr. SCHULTZE. We can quarrel on the edges.

Senator BROCK. One final point, Mr. Chairman.

I am sorry that the Senator from Virginia is not here, for I worry about the continued desire to load all of our efforts against gasoline. Maybe I am sensitive because Tennessee's third largest industry is tourism, and there is $600 million worth of my State's income involved.

And in Virginia it is the largest industry, I think. But in Tennessee, in Arkansas, Virginia, the rural States, and Vermont, Governor, you must be heavily dependent upon gasoline with your skiing. And I love to ski. But people have to drive up there. They surely do not have any air service into your State, unfortunately.

Mr. SAWHILL. I do not think we are talking about loading a lot of increase on anything. I think we are suggesting that perhaps a gradually increasing tax, which would give people time to adjust and give them opportunities to——

Senator BROCK. But, you keep coming back to the question of what? What?

You say you want to gradually increase this tax, say a nickel a year for 5 years, or 10 cents for 5 years. Now that is somewhat different from what you were suggesting before you left the Energy Office.

Mr. SAWHILL. Correct.

Senator BROCK. Accepting that premise, you know, and I know that that will not affect demand to the extent of 700,000 barrels——

Mr. SAWHILL. I know that it could not and I do not want to reduce demand by 700,000 barrels. I do not want to do it by allocation, or rationing or taxes or anything. I just do not think we need to cut that much out of demand.

Senator BROCK. Then we are back in agreement, because I question whether or not we can take the economic impact of a million-barrel reduction.

Mr. SAWHILL. We cannot, and that is why we should not embark on this tariff right now.

Mr. TUCKER. Senator, what bothers me through all of this discussion, and I am certainly not an economist or an expert in energy, as Mr. Sawhill, but all of us have been sitting here this morning and admitting that we do not know how much of a reduction in fuel imports we really need. We really do not understand fully the problem, and yet it appears that a great many members of the committee are willing to accept a substantial increase in price, being imposed on citizens of this country by fiat of the President, whether it was delegated to him by the Congress, or without knowing those facts, and it is difficult for me to understand how the committee could justify allowing prices to go up not through market demands, but through just the order of the President.

Senator BROCK. General, may I say for this particular Senator that I am not interested in following that course of action. There is only one element in the logic to the President's case, and that is an enforcement, to force action by the Congress, and I have been in this Congress too long, and heard too much rhetoric about the fat cats here and the fat cats there, and nobody ever gets down to the point of what do we do to develop a supply.

We have not opened up Elk Hills, we have not opened up Naval Pet No. 1, and we have not opened up Cook Inlet. We have done nothing to increase the supply of natural gas, and that is what closed down that plant up there in Ohio.

Mr. SAWHILL. Senator, I would say I think you are keeping the monkey on Congress, and I said this to Senator Long, too, because this bill provides for a 90-day period in which the Congress has either got to do something or then I think the President will be justified in moving forward with his program. So I think you are keeping a very tight time line in the Congress by passing this bill.

Senator BROCK. Thank you.

The CHAIRMAN. Senator Haskell.

Senator HASKELL. Mr. Chairman, I would like to make a statement for the record.

The Senator from Tennessee says the Congress has done nothing in this area. I disagree with that statement. I do agree with John Sawhill that the President has put the monkey on our back, but just briefly, let us review the conservation side of the Senate's record.

In the fall of 1973, the Congress passed an Emergency Energy Act which contained conservation measures, and it was vetoed. In the summer of 1974, the Senate passed a Conservation Act that contained such things as you were talking about, Dr. Sawhill, such as telling Detroit to achieve certain efficiency standards on the supply side. And, the Congress has formed ERDA, has passed an energy research and development bill, and has funded ERDA to explore new energy sources.

And on the third aspect of this, although Dr. Sawhill disagrees with it, I do not imagine the Governor does, but Congress has passed the Mandatory Allocation Act which I would suggest saved the independent sector of the industry. This is merely a statement for the record, not a question.

Mr. SAWHILL. The only point that I was making on allocation is, I do not think that is the solution to reducing oil consumption. I think it is a solution to managing a shortage, and it was helpful last winter.

Senator HASKELL. It is short range.

Mr. SAWHILL. It did keep the independents in business, as we all know.

The CHAIRMAN. Senator Packwood?

Senator PACKWOOD. I would still like to follow up, Mr. Chairman, on Senator Mondale's comments about the necessity of a million-barrel-a-day reduction and ask Secretary Kissinger to come and justify it, if that is where the statement came from. And I hope that the committee will move and will have a chance to get him to come up here and tell us why that presumption should be made.

Let me ask the panel, we are all assuming the $3 tariff is going to be paid by the companies, and immediately passed on to the consumers. Is that a necessary conclusion?

Mr. SCHULTZE. I think it is close to necessary. It will not be passed on in 1 month.

Senator PACKWOOD. It cannot be passed on in 1 month. Are you assuming they would pass along the entire cost, and if so, why do you assume that?

Mr. SCHULTZE. Yes, sir. It seems to me, on the average, it is going to come out, they pass it along, the entire cost, and that is everything that you look back at through history, what happens to raw material prices when they go up and they are not expected to come down—if they go up and they are going to come down in a month or two, that is another matter—but in general, they will get passed on.

In some areas they will get passed on with the markup, and in some areas they will not get fully passed on, and when you run through the calculations, it is a little bit on one side or the other, but I do not think there is anything in history which would point to assuming that it would not get passed on.

Mr. SAWHILL. I would say to the extent they do not get passed on, they have to come out of the oil company profits, and that is going to hurt the efforts which we need to resolve in our longrun solution, and that is stimulating additional production and exploration.

Senator PACKWOOD. Let me ask you this, and I am not an economist, but is it fair to assume that corporations generally then will pass along in full value any imposed cost we place on them, any tariffs or minimum wages, anything else?

Mr. SCHULTZE. Pollution controls. Yes, it is a fair statement.

Senator PACKWOOD. So, not only on this subject, but when we get down to general tax reform later this year and start talking about socking it to the corporations, we are simply talking about adding to consumer costs?

Mr. SCHULTZE. No; I think there would be some distinction. I don't know the answer.

When you tax a company's net profits, it is generally agreed that the impact of that is much more complicated, harder to determine than when you, in effect, tax a cost or increase a cost. To be honest, the economics profession is fairly divided on precisely how a profits tax is or is not passed on.

But when it comes to a tax on payrolls, or materials or anything——

Senator PACKWOOD. Any kind of direct costs. So if we were to mandate a national health service, 3 percent of payroll or taxes, then this will just be passed on?

Mr. SCHULTZE. They will pass it on.

Senator PACKWOOD. No other questions.

The CHAIRMAN. Senator Hansen?

Senator HANSEN. Thank you, Mr. Chairman.

I do not have the precise figures before me, but as I recall, I think in 1972 we were spending for imported oil between $3 billion and $5 billion and in 1973 about $9 billion, and last year in the neighborhood of $25 billion?

Mr. SAWHILL. That is correct, approximately correct.

Senator HANSEN. Let me say this to you, Mr. Sawhill, would you feel that we can continue not to address the problem of the increasing cost of these imports?

Mr. SAWHILL. No. I think we do have to address that problem. There is no question about it, although I think we should also recognize that the price of our exports have increased in the same period as well, so that all of that increase has not gone against our balance of payments.

Senator HANSEN. I realize that. Let me say I do not consider you an unfriendly witness.

Mr. SAWHILL. Thank you.

Senator HANSEN. I feel kindly toward you. Do you subscribe to the objectives that have been espoused by the administration generally, in trying to bring together all of the consuming countries of the world in unified action that may help address the energy problem?

Mr. SAWHILL. Yes, sir. And I testified to that, in fact, last week, before the Joint Economic Committee.

Senator HANSEN. Would you agree that if the United States were to take an action which would be hailed by the domestic energy industry, including oil and gas and coal, and whatever else—oil shale, geothermal steam—stimulate a greater effort within this country, that that would, indeed, be beneficial not only to this country, but to other nations of the world as well, whose cooperation we are searching for?

Mr. SAWHILL. Yes; and that is why I would be quite concerned about a program which in effect rolls back new oil prices and puts an excise tax on natural gas.

Senator HANSEN. Rolls back new oil prices, you say?

Mr. SAWHILL. Yes; because with decontrolling the prices and slapping on the windfall tax, that means the new oil barrel, after tax, only gets $6.50 return.

Senator HANSEN. You say you would be opposed to that?
Mr. SAWHILL. Right.
Senator HANSEN. Yes. Yes. I am opposed to it, too. I think it goes the wrong way.
Now, before that could be done, would not legislation by this Congress be required before the President could do that?
Mr. SAWHILL. Yes. Yes, it would.
Senator HANSEN. So, in effect, there is no real threat posed to the domestic energy industry as contained in the President's proposals that were made until Congress gives that authority to the President, which he does not now have? Am I correct?
Mr. SAWHILL. Except to the extent they are getting a signal from the White House that there is, you know, concern about, apparently concern about the amount that they are receiving for new oil right now.
Senator HANSEN. I know there is great concern, but I think you have made the response that I would like to underscore, and that is they may read all sorts of signals, but presently the President does not have the authority?
Mr. SAWHILL. No.
Senator HANSEN. To do those things to the domestic industry which it is fearful of now?
Mr. SAWHILL. He certainly does not have authority to enact his program. He, of course, would have the authority to roll back prices.
Senator HANSEN. Would you feel that the $30 billion, in round numbers, that is being proposed to being added on to the cost of energy by virtue of the impact of these total taxes, when we go the full length, will be returned in one way or the other to the consumers in this country?
Mr. SAWHILL. Well, I think the problem is the timing, how it will be returned, and the method by which it will be returned. I think that is a difficult thing to tell.
Senator HANSEN. But, there is no question, I mean there has been a lot of talk about how much we are taking out of the consumer's pockets in this country. Probably, while we may argue about the precise implication of it, there is not any question about that $30 billion will be going back into the taxpayer's pockets, or to those who do not pay taxes?
Mr. SAWHILL. I will defer to Mr. Schultze. I think he had some concerns about that.
Senator HANSEN. Yes.
Mr. SCHULTZE. I think there are problems with paying it back. That is, consumers will get back less than they pay, if you take the full amount.
Senator HANSEN. Why will they, if you could answer that?
Mr. SCHULTZE. Yes. The reason is that first the President's proposals, taking into account the associated impact on intrastate gas and coal and making a very conservative estimate, not as big as Senator Jackson's at all, a conservative estimate——
Senator HANSEN. What you are saying is Senator Jackson is not too conservative?
Mr. SAWHILL. You would agree with that.
Senator HANSEN. I would not want to infer anything you did not mean to imply.

Mr. SCHULTZE. In any event, it seems to me a conservative realistic estimate of how much consumers will pay will be in the neighborhood of $30 to $32 billion—consumers, not State and local governments or the Federal Government, and consumers will get back from the President's program $18.5 billion.

Senator HANSEN. Let me ask you, what happens to the dollars that may be snatched up by State and local units of government? What happens to those dollars?

Mr. SCHULTZE. Well, as I understand the President's program, he has estimated that State and local governments will pay $2 billion more in higher fuel charges, and he in turn will pay out, through additions to general revenue sharing, $2 billion to make that up.

Senator HANSEN. Now, when those dollars have been collected by State and local governments, and then spent, who eventually gets those dollars? Are they consumers or is it someone else?

Mr. SCHULTZE. No, I think in that case the consumer nets out, that is on the one hand, the consumer, if the President did not pass it back, would have to pay higher State and local taxes, but he is not, because the President is passing it back, so it nets out zero for consumers.

Senator HANSEN. We have about 211 million people in this country. Are there any of us who are not consumers?

Mr. SCHULTZE. As far as I know, I have not met any yet.

Senator HANSEN. I have not either, and I just wondered.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Hartke.

Senator HARTKE. Mr. Schultze, you said you were on the Council of Economic Advisers at one time; is that right?

Mr. SCHULTZE. I was a staff member of the Council of Economic Advisers.

Senator HARTKE. You are familiar with the organization?

Mr. SCHULTZE. I am somewhat familiar.

Senator HARTKE. You said there is no identification, and I do want to apologize. I said it came from the Bureau of Labor Statistics, and I now am talking from the staff report which was the economic report of the President of January 1972, on page 277, which shows manufacturing employment and gives the whole period from 1945 to 1972. I do want to tell you it shows that, in 1965, there were 18 million employed in manufacturing and that rose to 19 million—1.4. I will point out that the percent of the total in manufacturing in relation to the work force, however, decreased from 1965 to 1970 from 30 percent of the work force down to 27 percent of the work force.

Mr. SCHULTZE. That is right; it has been going down for 20 years. That is correct, sir.

Senator HARTKE. That is right, and I just also call attention to a chart where they do identify very vividly—to me, at least—they identify it as manufacturing employment, which you said they did not identify.

Mr. SCHULTZE. I said industrial. Excuse me, I may have misspoke, but I said they did not have a category called industrial.

Senator HARTKE. All right. I will change my phrasing. Maybe I misspoke. I did not mean manufacturing.

I might point out, however, that the difficulty here—I think this is where I agree with Senator Long. In other words, there is an attempt here to use scare tactics in the hope that somehow you can make these people of the United States feel that, somehow or another, they have to be afraid of the future, and they have done a pretty good job—I mean that they have scared most people half to death.

I do not think there is any good purpose served by it, but the basic premise of everything that is being said by the President, and the basic premise of what you are saying here today, is that you are going to have either an embargo from without or an embargo from within.

Now, I just want to point out to you, and I think Mr. Sawhill, that you will agree at least, whether the rest of them do or not, that you say there will be an increase in the cost of fuel?

Mr. SAWHILL. Yes.

Senator HARTKE. Under either circumstance, which in turn will be passed on by making our products in the United States less competitive than they are worldwide today; is that not fair?

Mr. SAWHILL. Well, I am not sure, because the products of other nations are experiencing the same thing, and as a matter of fact, that is one of the concerns I have. If we increase our cost, we are making our manufacturers less competitive by virtue of the fact that we are adding a tariff on to their other costs, and so on.

Senator HARTKE. Well, I quite agree. But the same effect is caused by rationing?

Mr. SAWHILL. Well, I agree. I am not for rationing.

Senator HARTKE. I agree. You see, this is where I am saying to you, how can you really say that this country is going to put itself out of this hole, get itself out of this economic recession by increasing costs?

Mr. SAWHILL. I am not suggesting that.

Senator HARTKE. Who says we are really in this type of a trap today? I tell you, I go to Indiana and they are starting to give away things to purchase gasoline, and they are talking about building bladders and sinking them into the bottom of the ocean to store gasoline, and they have hanging demurrage on the Ohio and the Mississippi Rivers because they do not have any place to store it.

And we have Arab tankers over there, and if you had a tanker come, do you think you could get it up to the point—they have undestined loads of oil in the Arab ports today, do they not?

Mr. SAWHILL. I am not really familiar.

Senator HARTKE. Is there really a shortage at this moment?

Mr. SAWHILL. There is no shortage of oil in the world; no.

Senator HARTKE. No shortage of oil. When I talk to people in Indiana and say that there is no shortage of oil, they look at me in stark disbelief, and they say, well, the President said so, and if the President says so, it has to be true.

And I think from experience that we should know by now that when the President says so, we ought to look at it.

That is all.

The CHAIRMAN. Let me just get one thing straight in my mind and see if you agree with this, Mr. Sawhill.

Look at the tremendous dislocation that took place when the embargo was imposed against the United States. Automobile dealers would ask me, if just that small cutback in oil imports could do this much harm to our economy and to our Nation, what would it be like if they cut all of those oil imports off? I believe at that time it was only about one-third of the imports that were cut off; is that not correct?

Mr. SAWHILL. Approximately; yes, sir.

The CHAIRMAN. Now, recognizing all of the havoc that that did to our Nation and to our economy at the time that it happened, I wonder if you agree with me that we ought to have a skeleton of rationing-allocation program ready to put into effect if those people decide to put a real blockade on us, that is, cut all oil exports to us?

Mr. SAWHILL. Absolutely.

The CHAIRMAN. It seems to me that that is essential. Do you agree with that, Mr. Schultze?

Mr. SCHULTZE. Absolutely.

The CHAIRMAN. It seems to me we can live with a cutback of, let us say, 18 percent in our energy, if it is evenly shared among the Nation. But if we have to have people standing in automobile lines 10 blocks long, using up 2 gallons of gas just to get up to the gasoline pump—that kind of confusion we had some time ago—it could be devastating to this country.

But I am satisfied that we could, in a proper way, cut back 18 or 20 percent in our energy consumption without just bringing everything to a halt, the way it would appear, based on the confusion that occurred when we had a mere 6 percent cutback. It wrought havoc over the country.

Mr. SAWHILL. I could not agree more.

The CHAIRMAN. Well, I think that that ought to be a part of any program that we come up with.

Now, I also believe that what has been suggested here by you, Mr. Sawhill, that repealing the incentive to go out and find new oil, and substituting as a result in place of that increases in the price of old oil, does nothing to help solve the problem.

Mr. SAWHILL. No.

The CHAIRMAN. I am led to believe that there might be in some cases a reluctance of producers to bring forth all of the old oil that they could pump out of their wells, or that would be produced if they opened them up to their maximum efficient production. But if that is a problem, it seems to me we could get to it other ways, either through the taxing tools or through some other procedure.

Mr. SAWHILL. I think so. I have in my own studies not found that to be a serious problem.

The CHAIRMAN. You have not found that to be a serious problem?

Mr. SAWHILL. No. Old oil production has actually increased since the imposition of the price controls.

The CHAIRMAN. I did not hear you mention in the suggestions you had in mind for saving energy a proposal that makes so much sense to me, and that is just reversing the order in which you charge for the high and low unit for utility units. That was suggested to me by the chairman of the board of a major utility company. In other words, you could just take a man's gas bill or electric bill and just reverse it, and instead of having the expensive unit come first, have the expensive units come last. That would place a much greater premium on conserving energy.

Mr. TUCKER. May I just speak to that? In Arkansas, we have just completed hearings in our Public Service Commission in Arkansas for a 38 million rate increase by the Arkansas Power & Light, which is part of the mid-south system which serves your State, and while we are not advocating a total reversal of the pricing system, you could obtain an enormous savings in energy in this country if the utilities would adopt some kind of a peak pricing method which penalized persons, or industry, or individual residents for use of energy at times of greatest demand, and at the same time it would reduce the overall cost to the consumer in his bill.

The CHAIRMAN. I think that would help, but let me state that I think we ought to do this. Let us assume a person is using 2,000 units of any given source of power you want to designate, and the pricing system works so that he pays 10 cents a unit for the first 1,000 units and 5 cents per unit thereafter, which is a program that has been conducted down through the years to encourage people to use more of it. It actually has been one to encourage people to install appliances and to encourage people in Florida to even take out their solar heating system for water, for example, and replace them with a premium to put in electric heaters in their place.

If we did it that way around, instead of the fellow advertising that if you insulate your attic it is going to save you $173 a year, he would be telling you that it would be saving you $346 a year. And I simply would submit that by reversing those rates, it would place a much greater incentive on people to conserve energy in their homes.

Mr. SCHULTZE. Senator. I used to think that, and maybe I still do, but I want to point out one problem that we have got to consider. We use about 3½ million barrels a day for residential and commercial heating. Now, the only real alternative to using oil for residential and commercial heating—they cannot use coal, natural gas is short—is to go to electric.

And ultimately, if you want to push people in residential homes toward getting away from using oil when you are building new homes, there is a problem if you switch those rates as to what you then do to keep them in oil and out of electricity. Electricity uses coal, you cannot use coal directly to heat your home, but you use it indirectly to heat your home by electricity; you cannot use coal directly to heat your home anymore, so I agree with you, but I think it ought to be looked at carefully as to what the cost for the substitute of electricity for oil in heating would be. And you may have to make some distinction in various types of use.

I am not sure how you would do it, and maybe it cannot be done.

The CHAIRMAN. In my part of the Nation, and I know it may be true in other parts of the Nation, practically all of your heating is done either by gas or it is done by electricity, heating and air conditioning, and if you simply structured your rates in such a fashion that the more expensive units come last, rather than first, there would be a tremendous incentive on people to save. That is just one of the things that has occurred to me as something we ought to do.

Now, of course, we ought to also find a way to step up making buildings and homes energy-efficient. The President suggested that we do that over a period of 10 years.

I do not, for the life of me, see why we cannot act as though we have an emergency on our hands, which he seems to think we have, and do it over a period of 2 or 3 years. What is your reaction to that?

Mr. SAWHILL. I agree with that. He proposed a 15-percent tax credit. I think it ought to be 50 percent, at least. This is one way that we can save energy and stimulate the economy at the same time, because we will stimulate the construction industry, which certainly needs it.

The CHAIRMAN. Right. Well, thank you very much, gentlemen.

Governor, you were making a note or two. Do you have a comment that you would like, or do you have something else in mind you would like to add to the record?

Governor SALMON. No; I would just comment, Senator, that this has geen a remarkable education for a country lawyer from up in the wilderness of the Northeast, and I am very pleased to have been able to participate at this head table.

The CHAIRMAN. Thank you very much for being with us, gentlemen, and we appreciate your help.

The committee will meet again Monday at 10 a.m.

[Whereupon, at 12:35 p.m., the hearing was recessed, to meet Monday, February 10, 1975.]

SUSPENDING PRESIDENTIAL AUTHORITY TO IMPOSE OIL IMPORT FEES; $531 BILLION DEBT LIMIT

MONDAY, FEBRUARY 10, 1975

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 10:05 a.m., in room 2221, Dirksen Senate Office Building, Senator Russell B. Long (chairman of the committee) presiding.

Present: Senators Long, Nelson, Mondale, Haskell, Curtis, Dole, Packwood, and Brock.

The CHAIRMAN. The hearing will be in order.

Today the committee continues its hearings on H.R. 1767, a bill to suspend for 90 days the President's authority to impose oil import fees, and on H.R. 2634, a bill to increase and extend the temporary debt limit.

Our leadoff witness this morning will be Treasury Secretary William E. Simon. We would also like to welcome James Lynn on his first appearance before the committee as Director of the Office of Management and Budget. We would also like to welcome Frank Zarb, Administrator of the Federal Energy Administration. I would like to ask all three gentlemen to summarize their testimony first and then the committee will proceed to the questioning.

Secretary Simon, Mr. James Lynn, and Mr. Zarb, you may proceed as you see fit.

STATEMENT OF HON. WILLIAM E. SIMON, SECRETARY OF THE TREASURY

Secretary SIMON. I speak of the initial goal of conservation and the ultimate goal and the desire and indeed the great need to achieve greater self-sufficiency.

Again the options are to do nothing; rations which indicates more Government mechanisms; or third; the market application, the tremendous market mechanism which every other country in the world uses to such great advantage.

If you will notice, the article in the Wall Street Journal this morning, the front page, about how much other countries have conserved. They just do not believe we are serious about conservation. We talk a great deal about what they call and what we have called giveaway prices; we will never achieve significant savings, and natural gas is just one of the very fine examples of that, the policies of the past 20 years, which, Mr. Chairman, you are only too familiar with.

Then I speak of the $1 a barrel and $2 a barrel, and $3 a barrel that the President has recommended and how we designed this program, that the economic impact and the stimulus as it is carefully balanced with our tax package would be positive, not only in the second, third, and fourth quarters of this year, but also through 1976. But the major impact, of course, is in the third and fourth quarters as far as the positive stimulus is concerned on the phasing and collection and redistribution of the import fees.

The inflationary impact idea as far as the 2 percent is concerned, and I know there has been great debate on the issue of the inflationary impact, and our studies have shown that the 2 percent one time consumer price index impact was after our careful analysis, and I know, and it seems to me that there is also great currency paid in this country to the worst forecast; people want to believe the worst. They are not willing to look at supporting the facts, and I think if we can go back to $1 bread and $1 gasoline and $1 a lump sugar and the collapse of the international finance system, that all of these things were predicted by the so-called experts in the past year, and when one tries to put out a measured judgment carefully balanced on both sides, saying these figures are just not balanced on both sides, this is just laissez-faire. This is what we have tried to do in general and the Treasury Department was to try to explain after very careful analysis that this was just not true.

The Consumer Price Index, I might also add, does not reflect the fact we are rebating the moneys to the people that we are taking away.

The bill that recently passed in the House, the Grenn bill, which is similar to the bill that is facing you in the Senate, and I will speak at some length with the comparisons and the reasons behind the President's desire to act and act immediately, because this energy problem we have talked about a great deal for the last several years and the time for action, my President and we believe, is now, and we urge the Congress to cooperate with us in this venture, so together we can provide the leadership that this country needs.

Thank you, Mr. Chairman.

[Mr. Simon's prepared statement follows:]

STATEMENT OF HON. WILLIAM E. SIMON, SECRETARY OF THE TREASURY

Mr. Chairman and Members of this Committee:

I welcome the opportunity to testify before this distinguished Committee on the pressing problem of Petroleum imports. Since two of my colleagues in the Administration, Mr. Lynn and Mr. Zarb, will also be speaking to you this morning on this subject, I will confine my opening remarks to the legal and economic justifications for the President's plan for oil import fees and I will also touch briefly on the Green bill, H.R. 1767.

LEGAL AUTHORITY

As you know, the President recently signed Proclamation No. 4341 authorizing increases in the fees on imported oil. His authority for signing that proclamation is contained in Section 232 of the Trade Expansion Act of 1962, as amended by the recently enacted Trade Reform Act of 1974.

Section 232 provides that if the Secretary of the Treasury, after appropriate investigation, finds that an article is being imported in the United States in such quantities or under such circumstances as to threaten to impair the national security, he should promptly advise the President of that fact. Unless the President determines to the contrary, he must "take such action, and for such time, as he deems necessary to adjust the imports of such article and its derivatives so that such imports will not threaten to impair the national security."

As you can tell, this is a broad grant of authority that includes the authority to impose quotas, license fees and other types of import restrictions.

Section 232 also provides that the Secretary of the Treasury shall, if it is appropriate and after reasonable notice, hold public hearings or otherwise afford interested parties an opportunity to present information and advice relevant to a national security investigation. Treasury Department regulations, implementing the national security provision, allow an exception to procedures for public comment when, in the judgment of the Secretary of the Treasury, national security interests require that these procedures be dispensed with.

On January 4, in accordance with Treasury Regulations, I directed Assistant Secretary for Enforcement, Operations and Tariff Operations, David R. Macdonald, to initiate an investigation to determine the effects on National security of imports of petroleum and petroleum products, I also determined that it would be inappropriate to hold public hearings and that national security interests required that the procedures for public comment under the regulations not be followed. I decided to proceed in this manner because I believed that the national security required an immediate determination and action with regard to petroleum imports. In addition, a number of public investigations and hearings on the effect of petroleum imports had already been carried out during the past year, and the results of these investigations had been made generally available to the public. The Attorney General, whose opinion I requested, concluded that to proceed without public hearing was fully consistent with both the spirit and the letter of the law.

As you know, the authority of the President to issue the Proclamation and my authority to proceed with the investigation and report without public hearings has been challenged in the courts. Since the matter is properly before the courts, it would not be proper for me to discuss it any further here.

Based on the report that I received from Mr. MacDonald after his investigation as well as my own knowledge of the situation, I reported to the President that crude oil and petroleum products are being imported into the United States in such quantities and under such circumstances as to threaten to impair the national security.

NATIONAL SECURITY

As I have noted, the test which must be met under Section 232 of the Trade Expansion Act of 1962, in order to authorize such trade restrictions, is that petroleum "is being imported into the United States in such quantities or under such circumstances as to threaten to impair the national security." In making a determination under the statute, the Secretary of the Treasury takes into consideration a number of factors, probably the most important of which is that the economic welfare of the country is closely tied to the national security of the country.

The facts which, in my view, amply justify the national security finding in this case are these:

(1) Petroleum is a unique commodity, entering into almost every facet of our economy, either as the fuel for transportation of goods and people or as the raw material for a myriad of products like fertilizer and petrochemicals. It is hardly an exaggeration to say that petroleum has become the lifeblood of our economy.

(2) Because our demands for energy have been outstripping the growth in domestic production, we have become increasingly reliant upon foreign sources of oil. We are now importing about 40% of our total petroleum consumption; by 1985, if present trends continue, we would be dependent on foreign nations for more than half of the oil we consume.

(3) Only a small portion of these imports can be deemed to be secure from interruption in the event of a political or military crisis, and recent history strongly indicates that such a crisis is by no means a remote possibility in an area where two-thirds of the world's known petroleum reserves are located.

(4) Most of the countries which export the oil that we import are organized into a cartel which has managed to raise international oil prices to a level four times above that which prevailed prior to the 1973–74 embargo.

(5) The outflow of U.S. funds to those oil-rich countries greatly enhances their economic and political power and weakens our own and that of our allies. In 1970 our total bill for foreign oil was $2.7 billion. In 1974, that figure shot up to approximately $24 billion, and unless we act to restrict imports, the bill will rise within a short time to over $30 billion a year.

(6) At the present time, we cannot safely stop the import of all petroleum to this country. We can, however, reduce our imports by one million barrels a day without significantly damaging our economy.

Mr. Chairman, after reviewing these facts, it was clear to me—as it is to most Americans—that immediate action was needed to reduce our reliance on imported petroleum and that a failure to take prompt action would indeed severely threaten our national security.

POLICY IMPLICATIONS

Underlying all of the difficult economic and energy decisions required in preparing the President's program has been the need to turn away from the policies that have helped to create our current difficulties. We must reduce imports of expensive and insecure foreign oil and increase the production of our own resources so that by 1985 this Nation will no longer be vulnerable to an energy embargo. The President's initial goal is to reduce our oil imports by one million barrels a day by the end of 1975 and by two million barrels a day before the end of 1977.

He is calling for swift action so that we can prove our willingness and capacity to act decisively in the face of our national security threat, thereby regaining control of our economic destiny.

While the process of attaining greater self-sufficiency will require the long-term development of various energy resources, we must rely heavily upon conservation in the short-run. It will take years to develop many of these potential energy sources—too long a period for us to wait to reduce our reliance on foreign supplies.

The President recognized that we face essentially three choices in the field of conservation.

First, we could continue along our present course of doing nothing, but as I have said, that option is clearly unacceptable.

A second choice is to ration fuels, but this also presents intolerable objections. The basic problem with rationing is that it cannot be done fairly and practically. Every family, every car and motorcycle, every store, school, church, and business—everything and everybody—would have to obtain a permit for gasoline, electricity, and natural gas. Those allocations would have to be changed every time someone was born or died or moved or got married or divorced, and every time a business was started, merged, or sold, and even when the church or school added a room. When we consider the problems of just getting the mail delivered, are we really ready to trust an army of civil servants—however able and well-intentioned—to decide who gets what? Rationing may be appropriate for temporary emergencies arising from a war, but it is hardly suitable for the 5–10 year period that would be required to meet the current oil challenge.

The third choice is to employ the pricing system as a mechanism for both discouraging consumption and encouraging production. This is the alternative the President has chosen—wisely so, in my judgment. The President made this decision with full recognition that energy prices would increase and we would suffer a small, one-time rise in the rate of inflation, but he has coupled the price increases with changes in the tax structure that should compensate most energy users, especially low- and moderate-income families, and should also prevent energy producers from realizing windfall profits. This is a sound, thoughtful approach, and I hope that the Members of the 94th Congress will ultimately recognize its wisdom.

Under the proclamation recently signed by the President, an increase of $1 a barrel in the fee on imported crude oil went into effect on February 1. That fee will be increased to $2 on March 1 and to $3 on April 1. Increases of up to a maximum of $1.20 per barrel are being imposed on refined oil, or what is known as petroleum products. It is estimated that these fees will increase average petroleum prices by about 3½ cents per gallon. It is also assumed that these fees would be reduced to $2 a barrel when the President's legislative package is acted upon.

It is worth asking what economic risks, if any, are created by the decision to increase the import fees on crude oil and petroleum products. Possible risks include: (1) That the increased taxes might constrict the entire economy by reducing the available purchasing power of individuals and businesses; (2) that the timing of the tax collections and the offsetting reductions might not be coordinated properly; (3) that geographic or specific industry inequities might result; and (4) that the increased fees might significantly increase inflationary pressures. Let me address each of these problems in turn.

Our best estimate, based on various economic projections, is that the President's total energy package would raise energy costs by about $30 billion. However, the program should effectively overcome any depressant effects by returning that entire amount back into the economy. Of this sum, $19 billion would be returned to individuals, $6 billion to businesses and $2 billion to State and Local Governments. The final $3 billion represents increased costs of the Federal Government. The proposed changes in taxes for individuals are designed to favor low- and middle-income families. In fact, those who pay no income taxes will receive $2 billion in benefits.

Nor is the phasing of the collection and redistribution of the import fees an insurmountable problem. As indicated in Table 1, the import fees are expected to total only $200 million during the first three months of 1975. The fees would increase to $400 million under the administrative authority and $700 million under the new legislation requested by the President. Fees of $900 million are projected for the third and fourth quarters of 1975. The redistribution of these fees through the income tax system can begin in June of 1975 if the necessary legislation is enacted quickly. Therefore, the potential collection of fees prior to getting the redistribution started should not be a major problem. As shown below, the net effect of the entire energy tax redistribution and temporary tax cut proposed by the President is clearly stimulative in every quarter after the first (in which the amount is negligible in a $1500 billion economy):

[In billions of dollars]

	Timing of direct budget impact, 1975			
	I	II	III	IV
Energy taxes	+0.2	+4.1	+12.6	+7.6
Redistribution and temporary tax cut	0	−9.8	−20.2	−10.8
Net effect	+.2	−5.7	−7.6	−3.2

Note: Negative figures indicate amount of stimulus to the economy.

As to the third risk involving geographic and industry sector inequities, the President and his energy advisers have repeatedly emphasized that they will work to even out such distortions wherever possible. The meetings that have been held with various governmental and industry representatives are good examples. More specifically, the "Old Oil Entitlements" program of the Federal Energy Administration will be utilized to spread price increases on crude oil among all refiners and to lessen disproportionate regional effects, as in New England, or in any specific industries or areas of human need where oil is essential. In order to overcome any severe regional impacts in areas which are especially dependent on imports, imported products will receive a fee rebate corresponding to the benefit that would be obtained under the "Old Oil Entitlements" program.

The fourth problem that I raised is the question of the inflationary impact of the energy package. There can be no doubt that the possible effects on prices are difficult to determine. Our most reliable estimate is that the entire energy package is expected to cause a one-time increase in the consumer price indexes of approximately 2 percent. This estimate combines the direct and indirect effects of the entire $30 billion energy conservation taxes and fees package. It assumes that all of the increases in fees and excise taxes are passed through to the final users of energy (both businesses and consumers) and, further, that there are no secondary effects in the form of increases in profit margins or increases in wages.

The 2 percent figure is, of course, an estimate, and thus an uncertain figure, but we believe that it is reasonable. In calendar year 1975 the import fees are expected to total $3.1 billion or 12.7 percent of total energy tax receipts in that year. In calendar year 1976 the import fees are projected to be $4.1 billion or 13.6 percent of the total. Therefore, the potential inflationary impact of the oil import fee part of the energy package is small.

I recognize that the 2 percent estimate has been widely challenged. Some say it is too low, others claim it is too high. Those who believe the inflationary effect will be less than two percent contend that the rise in energy price is a relative price increase only—that is, because the energy part of the President's program does not change some of the basic determinants of inflation (such as the overall operating rate of the economy, or fiscal policy, or the money supply), prices of things other than energy will have to rise less than they otherwise would, which will partly offset the overall inflationary impact of the energy package.

Those who believe the price impact of the energy policy actions will be more than 2 percent believe that there will be substantial secondary effects—in other words, that a pyramiding of profit margins will take place as the excise taxes are passed through the refining and distribution system. Moreover, they foresee that the energy price increases will cause wage settlements to escalate further, and the higher wage costs will then feed back through the system in the form of higher prices.

We believe, on the contrary, that there will be little margin pyramiding and little effect through the wage side. Let me explain why. First, with unemployment at 8 percent or more this year and the product markets comparably weak, economic conditions are not at all conducive to either a further escalation in the wage trend, or a pyramiding of margins. Second, since for the economy as a whole the individual and corporate income tax reductions offset the excise tax increases, the typical employee and the typical corporation are left no worse off than before and, thus, do not feel pressures that might cause them to demand higher profit margins or still larger boosts in pay.

Furthermore, I think it is very important to stress that this price increase is a one-time event. The great bulk of the increased energy prices will be felt within this calendar year. No further inflationary effect will take place in future years. The ongoing rate of inflation, therefore, should not be permanently affected by this policy.

H.R. 1767

In conclusion, Mr. Chairman, I would like to comment on H.R. 1767, the bill recently passed by the House, H.R. 1767 would effectively rescind the President's oil import proclamation, and for 90 days after its enactment would also abrogate the authority of the President to use Section 232 of the Trade Expansion Act, or to use any legal provision, in order to "adjust imports of petroleum or any product derived therefrom." In other words, by enacting H.R. 1767, the House of Representatives, without any assurance that Congress would adopt a conservation plan to counteract the problem of petroleum imports, would strip the President for 90 days of all his authority to take any action whatsoever on behalf of the country to solve the import problem.

The bill passed by the House of Representatives does preserve the right of the President to act "under certain circumstances involving the United States armed forces engagement in hostilities." But armed warfare is not the crisis that now faces us. What if the oil exporting countries were to impose a selective embargo on some consuming nations only, or increase the price of oil by 50 percent over its present level, or take some other unforeseen action? Unless the Congress were to immediately rescind this bill, it would paralyze the President from responding to any kind of additional threat short of armed hostilities. In other words, H.R. 1767 replaces leadership with vacuum.

We have already delayed for well over a year in finding a solution to a problem that we all knew existed. Each day of additional delay drains our strength and our capacity to act effectively. Each day of delay leaves the OPEC nations with a knife at our throat. To delay for at least 90 more days without solid assurance of a viable energy program at the end of that period is unconscionable.

Finally, our failure to take affirmative action in this situation must be viewed by allies and adversaries alike as a demonstration of American vulnerability and weakness, due to domestic divisiveness in the face of a new kind of foreign policy challenge. Decisive action is essential. We have signalled our intention to move toward energy self-sufficiency and have demonstrated with action the strength of our commitment. We urge the Congress to cooperate with us in this venture, so that together we may provide the leadership that our country needs at this critical hour.

TABLE 1.—DIRECT BUDGET IMPACT OF THE PRESIDENT'S ECONOMIC AND ENERGY PROPOSALS

[In billions of dollars]

	Calendar years—							
	1975				1976			
	I	II	III	IV	I	II	III	IV
Energy taxes:								
Oil import fees	+0.2	+1.1	+0.9	+0.9	+0.9	+1.1	+1.1	+1.0
Oil excise tax		+1.3	+1.6	+1.6	+1.8	+1.8	+1.8	+1.8
Natural gas excise tax		+1.7	+2.1	+2.1	+2.0	+2.2	+2.2	+2.4
Windfall profits tax			+8.0	+3.0	+2.9	+2.4	+2.4	+2.3
Subtotal	+.2	+4.1	+12.6	+7.6	+7.6	+7.5	+7.5	+7.5
Return of energy tax revenues to economy:								
Tax reduction		−3.2	−9.0	−9.0	−5.6	−7.9	−6.3	−6.4
Nontaxpayers			−2.0				−2.0	
State and local governments		−.5	−.5	−.5	−.5	−.5	−.5	−.5
Federal Government			−.8	−.7	−.8	−.7	−.8	−.7
Temporary tax cut		−6.1	−7.9	−.6	−.8	−.9		
Net effect	+.2	−5.7	−7.6	−3.2	−.1	−2.5	−2.1	−.1

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Feb. 6, 1975.

Secretary SIMON. I will now turn to Mr. Zarb.

STATEMENT OF HON. FRANK G. ZARB, ADMINISTRATOR, FEDERAL ENERGY ADMINISTRATION

Mr. ZARB. Mr. Chairman, I ask my statement be received in the record, and I would not go through it in its full text. I will briefly summarize its content.

The President's program is designed to achieve one primary purpose; that is, to reduce our vulnerability by the year 1985 so that we no longer can be susceptible to the kind of activity which this Nation faced at the end of 1973 or early in 1974.

To achieve that goal and the goals of the later 1980's that he articulated, the President has submitted two different strategies.

The first is to limit our consumption levels to a more efficient use of our available oil energy, thereby reducing over the near term our vulnerability with respect to the OPEC nations; and second, going into the 1980's, demonstrating that we have the capability of using energy for its real value.

The second part of the President's program reaches toward the areas of bringing on new oil supplies and new alternative energy supplies. Now, that portion of the program which comprises 70 or 80 percent of the total package has come under a little discussion and debate. There seems to be fairly substantial agreement on the strategies to develop additional oil supplies in the way of nuclear coal conservation and so on.

In addition, there seems to be little concern regarding some of the other mandatory measures of conservation which the President has put forward, mandatory standards for building, assistance to consumers for the acquisition of storm windows and installation and assistance to poor homeowners who cannot afford to avail themselves of a tax credit provision.

An emergency storage program whereby this Nation can store a year's worth of consumption at the rate of 3 million barrels per day or almost the equivalent of 6 months of imports. The discussion thus far has surrounded the techniques that the President has put forward to achieve a more efficient use of our energy supplies. It is stated that we should attempt to achieve a 1 million barrel savings by the end of 1975 and 2 million by 1977. He has said these savings should come from the levels at which we would be if our current projections of consumption and economic activity prevail.

Mr. Chairman, this Nation has one-sixth of the world's population. It uses one-third of the world's energy. There seems to be little debate that we as a nation should start to endeavor to use oil energy supplies with recognition of its real and true value.

The question of one million barrels a day in 1975 has been raised, and I would say that that goal was established when we first examined what it is going to take to get from here to invulnerability in 1985, and the decision was made that we should begin now with substantial action to achieve our consumption savings as well as our new source development.

The technique has been questioned with respect to using market forces as compared to some form of management by the Government. Two principles were used in exploring these various alternatives. The first was effectiveness. The second was equity for people. In our determination and our analysis that is available to this committee, we determined that neither rationing nor an import quota or an allocation system would pass those two tests and, therefore, we selected the market mechanism.

The current discussion, Mr. Chairman, about our economic activity, that perhaps we should delay or rethink the question of having a national energy program, seems to be inconsistent with what the Nation has been saying for the last year. The economic activity problems we face today will be overcome. The economy will turn up. At that point in time we should have in place an active program to insure that we begin the process of using lesser imported oil and also begin the process of bringing on additional oil and alternative supplies.

That is all for my summary, Mr. Chairman.

[Mr. Zarb's prepared statement follows:]

STATEMENT OF FRANK G. ZARB, ADMINISTRATOR, FEDERAL ENERGY ADMINISTRATION

I appreciate the opportunity to appear before you today to discuss the Administration's proposals for dealing with the Nation's energy problems.

Last winter's oil embargo demonstrated the distressing vulnerability of the United States to foreign supply cutoffs. The embargo was one result of years of energy policy neglect which left the economy and its relationship with other nations subject to foreign influence, sudden disruption and devastating price increases.

The energy situation requires broad, decisive and prompt Government action to prevent continued erosion of our economic vitality and national security.

The scope of the task suggests its wide-ranging and long-lasting significance. The lives of the American people—indeed, those of the people of much of the world—will be seriously affected by what we do, or fail to do, in the days ahead. And they will not be affected just for five or ten years, but for generations to come.

Our economic system is strong and resilient. However, the impact on other countries much more dependent on oil imports has been correspondingly greater.

The United States can be profoundly affected by severe economic crisis abroad. We must show our leadership among the industrialized nations and demonstrate our willingness to take the hard and expensive steps in energy conservation and development of new energy resources. The President's program is an outstanding example to other countries of America's determination to reverse the trends towards dependency. Reducing our vulnerability to supply interruption and price manipulation must be given the highest priority.

The President has prescribed tough action to cure our energy ills. He has outlined three, time-phased goals.

One: In the short-term, a cut in our oil imports of 1 million barrels per day by the end of this year and of 2 million barrels per day by the end of 1977.

Two: By 1985, imports of no more than 3-5 million barrels per day—and the capability of immediately replacing that amount from storage and standby measures in the event of a supply disruption.

Three: Accelerated development of energy technology and resources so that the United States can meet a significant share of the energy needs of the free world by the end of this century.

ACTIONS TO MEET THE SHORT-TERM GOAL

In the first crucial years, there are only a limited number of actions that can increase domestic supply. We must develop and increase production from the Elk Hills, California, Naval Petroleum Reserve. The President has submitted legislation for this purpose.

The Administration has also submitted a set of comprehensive amendments to the Energy Supply and Environmental Coordination Act of 1974 to ultimately increase the number of oil burning facilities that can be converted to coal in the coming years.

These are the only supply actions that can have much effect during the next two to three years. Therefore, we must rely heavily on energy conservation and it is clear that voluntary conservation is not sufficient. We cannot wait months or years for long-term conservation measures to achieve our national goals. Therefore, as you know, the President has raised the cost of all imported petroleum products by imposing a $3 per barrel import fee as a first step to reducing demand. This fee began February 1 and will be applied in three consecutive monthly $1 increments. The revenues raised thereby will be returned to the economy through the President's recommended tax program.

I want to emphasize that these increased import fees are only temporary and will be adjusted to $2 when Congress enacts the President's comprehensive tax legislation, already described by Secretary Simon, which includes an excise tax of $2 per barrel on all crude oil and petroleum products.

To ease the impact on regions heavily dependent on imported petroleum products, such as New England and the Northeast states, the President's program provides for a much lower fee rate on products than on crude oil.

In addition, a proposed excise tax of 37¢ per thousand cubic feet on all natural gas would approximate the $2 oil excise tax and would, with deregulation of natural gas as proposed by the Administration, serve to reverse the trend of dwindling natural gas reserves. Unemployment due to curtailments, and prevent industrial switching from oil to already scarce natural gas.

Further tax changes under the program include:

A windfall profits tax. The President will take steps to administratively decontrol the price of old domestic crude oil on April 1. Accordingly, Congressional enactment of the windfall profits tax by that time is urgently required to prevent excess profits accruing to the industry. However, care must be taken not to inhibit the needed amount of capital required to find and develop new oil and other energy sources.

A program of income tax reductions and rebate measures to return to the economy the roughly $30 billion estimated to be raised this year through these provisions. Most of this money is to be restored directly to consumers, with special measures to provide funds for the poor.

The use of import fees and excise taxes to foster large-scale energy conservation has attracted much attention and criticism.

I would like, therefore, to spend a few moments discussing alternatives. First, there is the alternative of doing nothing. No action only postpones the tough decisions we have to make. Without conservation, our tab for imported oil, which was $3 billion in 1970, and $24 billion last year (1974), would reach $32 billion in 1977. A brief respite of a year or so will only increase the vulnerability of the world to a crippling embargo by the producers.

The Arab Embargo of 1973 resulted in a significant drop in our Gross National Product and the unemployment of perhaps one-half million members of our labor force. Yet today, even more of our imports are coming from Africa and the Middle East than did a year ago. Now over half of our petroleum imports come from sources outside of the Western Hemisphere. And, unless we do something, this dependence on African and Middle Eastern sources will continue to grow. By 1977 imports will reach 8 million barrels per day, as compared with 6 during the last embargo. Because all of the increase will come from insecure sources, we may well be just as vulnerable as we were last winter. This is simply unacceptable.

Every month we hesitate will make it that much harder to achieve our 1985 goals. Those who say action is too expensive should reflect on the future cost to the nation if we do not act expeditiously.

There are those who believe that raising prices of energy at home will not help us cut back on consumption. They are wrong. While a comparison of our present consumption with that of last year's shows that we are actually using slightly more now, more importantly, we are using much less than we would if prices had not risen 400 percent in the last year. This is a clear demonstration of price elasticity of demand, or consumption of certain items decreasing as their prices rise relative to other prices. Present consumption would have been at least 1 million barrels a day more if prices had not risen so sharply. Furthermore, although the cartel has cut back on production by about 9 million barrels a day, there is still a surplus of oil on the world market. There is concrete evidence all around us that price is indeed effective in reducing demand.

The other alternative to inaction is the greater use of government controls—whether import quotas, allocation systems or rationing, or on another level, Sunday closings of gasoline stations, no driving days, etc. We looked at all of those last year during the embargo. We chose some and rejected others. And our reasoning was good for a short-term crisis. We now face a longer-term one. Each of these alternatives would involve some form of self-imposed shortages as well as built-in inefficiencies, burgeoning bureaucracies and regulatory proliferation and disruptions in the lives of all American citizens. And remember, to be effectve controls must be in place for a long-term of up to ten years. I doubt that the American people would be willing to put up with such alternatives nor should we subject them to this long lasting pervasive control over almost every aspect of their lives. Furthermore, most of the controls would involve higher costs to everyone. Gasoline taxes, for example, would have to be increased about 40¢ per gallon to save 1 million barrels of oil per day. Instead, the crude oil price increase, distributed across all of the products from a barrel of oil will raise the price of gasoline about 10¢ to 15¢ per gallon. This seems a more effective and more equitable solution.

I think it's unnecessary for me to dwell on this at any greater length. Suffice it to say, we should allow the free market to work to the maximum extent possible. This is what the energy conservation taxes and fees would do. And the rebates would assure no significant loss of consumer purchasing power or economic impact.

MID-RANGE (1976–85)

The second of the goals addressed in our energy program is the elimination, by 1985, of our Nation's vulnerability to economic disruption by foreign suppliers. In other words, by then our petroleum imports should amount to only 3–5 million barrels per day of our consumption, and we should be able to implement standby emergency measures and draw from storage enough to offset a complete cutoff of these remaining imports.

To attain such a goal, we must start immediately to remove constraints and provide new incentives for domestic production and conservation because most of the measures will take 5–10 years to reach fruition after the necessary laws are enacted. And all of these things must be accomplished through a single program that has the balance to bring about the required reduction in our energy use, the necessary increase in our domestic production, and—equally important among our naitonal goals—the continued economic well-being, environmental quality, national security, and social welfare that the American people demand and deserve. There is no piecemeal program which can provide the balance that is required. Hard decisions must be made from the very outset within the framework of our overall structure.

The President has reaffirmed the intent of this Administration to move ahead with exploration, leasing and production in those frontier areas of the Outer Continental Shelf where the environmental risks are judged to be acceptable. He has also asked the Congress to authorize oil production from the largest of the nation's Naval Petroleum Reserves, NPR-4 in Alaska, to provide petroleum for the domestic economy, with 20% earmarked for military needs and strategic storage. According to our estimates NPR-4 could produce 2-3 million barrels of oil per day and commensurately large quantities of gas by 1985.

But, in addition to finding more oil and gas, we must take advantage of our most abundant energy resource, coal. The President vetoed the surface mining legislation passed by the last Congress, but it remains a valuable piece of work. The President has submitted a bill which builds upon S. 425 in such a way as to make it acceptable to the Administration. I and others in the Administration are prepared to work with the Congress to arrive at a sound surface mining law.

The Congress must also act on the Administration's amendments to grant the Environmental Protection Agency authority to suspend emission limitations for powerplants until low sulfur coal can be obtained or stack gas scrubbers can be installed. The nation would thus be permitted to reap the enormous benefit of increased use of domestic coal under appropriate environmental safeguards.

The Congress should also amend the Clean Air Act to deal with the issue of "significant deterioration" of air quality. In this case, as in that of the strip mining legislation, we want Congress, rather than the courts, to make the essentially legislative decisions that are required.

To assure rapid coal production from existing leases and to make new, low sulfur supplies available, the President has directed the Interior Department to adopt legal diligence requirements for existing Federal coal leases and to design a new program for accelerated leasing of Federal coal lands.

Of course the market for coal, as well as the availability of all electric power, depends upon the health of the electric utilities industry, and we must address its problems. In recent months, utilities have cancelled or postponed more than 60 percent of planned nuclear expansion and 30 percent of planned additions to non-nuclear capacity. The delays and difficulties this industry is currently experiencing could well lead to higher oil import needs and inadequate supplies of electricity 5 to 10 years from now.

The President has, therefore, proposed legislation to assist the electric utilities through higher investment tax credits; mandated reforms in State Utility Commission practices; and other measures. And to rejuvenate our drive toward more effective use of the potentials of nuclear power we have markedly increased our budget request for nuclear waste disposal and for continued improvements in safeguards.

As we take these actions to increase our energy supplies, we must be aware of some potential problems. Before we achieve our goals of energy sufficiency, actions of oil producing nations, or economic conditions, could result in lower—but unstable—price levels that could weaken our continued commitment to greater self-sufficiency. The Federal Government must take actions to encourage and protect domestic energy investment in the face of significant world price uncertainty. To foster such investment, the President has requested legislation to authorize and require the use of tariffs, import quotas or other measures to maintain energy prices at levels that will achieve full national capability for self-sufficiency and protect our energy industry and jobs.

All of the actions I have mentioned would have the effect of increasing our available domestic supplies of energy. Oil production could reach 13 or 14 million barrels per day versus approximately 9 million today, coal production could double and nuclear generation could increase from a 4 to 30% share of our electric generation capacity by 1985.

But, as in the short-term supply actions are not enough. We must dramatically cut our historical demand growth. We have signed agreements from major domestic automakers to improve gasoline mileage by 40% on average by 1980, as compared to 1974 model cars, provided that the Clean Air Act automobile emission requirements are modified for five years.

The Energy Resources Council is developing energy efficiency standards for major appliances and will seek agreements from manufacturers to achieve an average 20% improvement in efficiency by 1980. At the same time, draft legislation has been submitted that would require labels on automobiles and major appliances disclosing energy use and efficiency. To move quickly where the problem hurts most, the Federal Government will provide money to the States for the purchase of insulation and other energy conserving devices in homes owned or occupied by low-income citizens, who might otherwise not be able to have such improvements made in their homes. The President's Program also sets forth proposals to mandate thermal efficiency standards for all new buildings in the United States. Since energy savings are even greater for existing homes it also includes a proposal to institute a 15% tax credit for insulation investments up to $1,000.

These numerous proposals and actions taken together, can reduce our dependence on foreign energy supplies to 3 to 5 million barrels of oil per day. While this does not seem much less than current consumption, it is down substantially from the 12–13 million which we would have to import if we did not act. To ensure that we could meet any supply disruption of the remaining imports we must establish legal authority for emergency measures that can be readily implemented to guarantee the equal sharing of shortages and the equitable allocation of supplies at home, and to meet our obligations under the International Energy Agreement abroad. We must also begin as soon as possible to develop a strategic storage capacity of 1 billion barrels of oil for domestic use and 300 million barrels for military use. Only by taking such precautions can we act responsibly both at home and in the international community in a time of future supply interruptions.

ACTION TO MEET THE LONG-TERM (POST 1985) GOAL

For the longer term, our goal is to sustain a position of energy independence, and to enhance it so that the United States will again be capable to supplying a significant share of the Free World's energy needs.

This means that, as a Nation, we must reaffirm our commitment to a strong energy research and development program, aimed not only at developing the capability to tap all our major domestic energy resources but also at improving the efficiency of energy utilization in all sectors of our economy.

Last year, the United States committed itself to a five-year, $10 billion energy-R&D effort. Our 1975 energy R&D budget was twice that of 1974 and three times that of 1973. In 1976, this accelerated effort must continue, and the President has pledged to seek whatever funds are needed for future R&D activities.

Now that we have an Energy Research and Development Administration, a Federal Energy Administration and an Energy Resources Council, we have, for the first time, both the unified Federal organization and the financial commitment to get the job done.

But energy R&D funds and organization are not enough; we also need new incentives to assure that emerging technologies are not only developed in the laboratory, but brought into use in the marketplace. Therefore, the President has announced a National Synthetic Fuels Program which will assure the equivalent of at least one million barrels per day in synthetic fuels capacity by 1985. It will entail a program of Federal incentives designed to reduce price uncertainty, raise capital and overcome unnecessary delays in bringing existing or nearly developed technologies into commercial use. The program will result in the commercial application of technologies of several types and the construction of major new plants, using both oil shale and coal resources.

CONCLUSION

The program the President put forward is a comprehensive one. It will reach the goals the President set forth and which I think the American people want. I have heard much talk and criticism in recent weeks on elements of it, but I have seen no constructive alternative. We all want an easier way to reach our goals. This program does require sacrifice by all, but it is also equitable. Finally, its impacts are far outweighed by the important benefits it will achieve.

Thank you.

Secretary SIMON. That is all, Mr. Chairman, on the subject. We could go into the debt ceiling or finish this subject.

The CHAIRMAN. Why do we not close this subject first, and then we will go to the debt ceiling.

Mr. Secretary, I want to ask you the question which from my point of view is a $64 problem at this moment.

Now, I know very well that the administration feels, and I think they are correct in feeling, that it is urgent that this debt limit bill be passed. Without it the Government is not going to be able to continue to operate. I also know that there are a majority of Senators committed to the Kennedy-Jackson resolution to suspend the President's action with regard to oil imports and with regard to the pricing of petroleum products.

Now, if those people do not have a legislative opportunity to vote on that matter sometime in the near future, I do not see any doubt at all about it that they will be impelled to offer that as an amendment on this debt limit bill, and I think that could lead to all sorts of problems.

It is my feeling that this committee should report both of those two bills. I do not think I am for the Kennedy-Jackson resolution, but I would propose to vote it out of this committee so that it could be considered on the Senate floor.

I would like to have your views. Do you think there is anything to be gained by bottling up any one of those two bills in this committee?

Secretary SIMON. No, sir, Mr. Chairman; I certainly do not. As you know, we have long favored a clean debt ceiling bill and I would like that moved most expeditiously.

The CHAIRMAN. It is my feeling that to meet the requirements of this Nation we will have to report both of those two measures out, and insofar as the chairman of this committee is concerned, I am going to urge that the members of this committee make both of these measures available to the Senate at the earliest opportunity. I do not mean they should be denied the opportunity to express their views or to make their views clear to the Senate or write minority views or whatever the majority of this committee wants to do, but I do think both sides are entitled to have a decision on the Senate floor at an early date. If you are willing to accord the other people the same opportunity I believe they should accord you, I believe we can resolve that matter in fairly short order.

Secretary SIMON. Thank you, sir.

The CHAIRMAN. There is one other question I want to ask about, and this could take some additional time.

I was led to believe that this 1 million barrel reduction figure is a result of international negotiations at which Mr. Kissinger and those representing the executive branch of this Government seemed to have arrived at some sort of a tentative agreement with other consuming nations, our friends and allies, that the free world should try to make a reduction of 2 million barrels per day in the amount of oil that they were consuming during this next year, and that the United States should try to absorb half that cut on the theory that we are probably the biggest waster of energy, is that true or not?

Secretary SIMON. Not entirely, Mr. Chairman. Let us just say it is partially complete.

The CHAIRMAN. In view of the fact I did not get it directly from the horse's mouth anyway, I believe that is about a reasonable myth.

What is the reason for that 1 million barrels.

Secretary SIMON. Let me attempt to explain what our policies have been as far as conservation, which is the only thing we can do, recognizing it takes 3 to 5 years to bring on additional sources of gas.

In an attempt to obviously put pressure on the international price of oil, conservation is important, and while the world has had significant conservation in the past year and there is indeed some pressure on prices as one takes a look at some of the discounts being given now through the delayed payment mechanisms, 8½ million or close to 10 million barrels a day are shut in as far as OPEC production is concerned.

Now, we believe that somewhere in the area of 3 million barrels a day, and this number is yet to be negotiated as far as international energy agency and the consuming nations of the world are concerned, could be served and what the U.S. share of that is yet to be negotiated. negotiated.

Our million barrels a day reduction of imports by the year 1975 was arrived at because that was an amount that could be reduced safely without any significant economic impact, recognizing we have a declining economy at this point. The measures that the President put forth as far as reduction through the price mechanism would achieve that reduction this year and give us a reduction also in 1977, giving people time to buy more automobiles and insulate their houses and do more permanent things. The intermedia and long term elasticity is greater, of course, and this is where the numbers came from, Mr. Chairman.

Of course, it does have foreign policy implications, because we are attempting to get all the consuming nations to cooperate, not only in conservation, but research and development and alternate sources. If we want to do that as evidenced by the energy conference held here last February, then we have to recognize as leaders that we must do it ourselves. We just cannot talk.

The CHAIRMAN. I am going to ask each Senator to limit himself to 10 minutes.

May I suggest that we proceed to call on Senators by the Curtis rule; that is, we call on Senators in the order in which they entered the room. So I will call on the Senator from Nebraska, Mr. Curtis.

Senator CURTIS. I thought my rule was one they called on if they agreed with us.

Go ahead.

The CHAIRMAN. Senator Mondale.

Senator MONDALE. Mr. Secretary, the policy that we are discussing today, as I understand it, is designed because we have made a decision to reduce imports by a million barrels a day this year, and by 2 million barrels a day by the end of 1977. I think it is pretty well agreed, at in least the testimony we have had here and before the Joint Economic Committee, that the plan is very dangerous economically. It will produce higher unemployment in the midst of a disastrous unemployment picture. It will contribute further to inflation—2 percent, according to your figures, but that does not include the ripple effect—possibly 3, 4 percent, or even higher.

It will overcome one of our American businesses' major advantages in trade, namely, less expensive energy, therefore presumably affecting our balance of trade or at least our standard of living.

So that the problems resulting from this policy economically are very tough. I think that is why Arthur Burns the other day said as much and John Sawhill, formerly of this administration, said the same.

On the other hand, the growing evidence is that the problem you are dealing with is not quite as bad as we originally imagined. The other day you testified that the balance-of-payments problem was proving to be more manageable than we anticipated. The capacity of the cartel countries to buy and use money was greater than we expected. The stability of the financial institutions to manage this money was better than we expected. New discoveries have soared. I think there have been 80 billion barrels of proved resources added to the world's proven resources in the last 15 months. Oil and energy exploration worldwide has proved more price responsive than we expected, and energy usage is not rising as expected.

So that we have a situation in which the results of the administration's policies from an economic standpoint may be disastrous, and the problem we are dealing with is not as serious as we once expected. Yet the whole reason for the policy is that we must reach the million and 2-million-barrel target.

Now, why?

Secretary SIMON. Senator Mondale, I would like to clarify one thing I said when I said that the balance of payments situation was bad. I was talking at some length in my testimony the other day about the accumulative reserves of OPEC nations about 1980 in the study we did.

Senator MONDALE. That is what I meant to say.

Secretary SIMON. Our balance of payments is the important reason we want to get this under control.

We spent last year, $25 billion for imported oil versus $3 billion in 1970. If we allowed our dependency on these foreign sources to continue at this level and grow, by 1977 it will be over $30 billion. In our judgment our exports and otherwise can not keep up, and this further weakens our dollar.

The price of imported oil compacted by a group of countries has an economic impact. Fortunately, in the United States it is not as great as other nations, but still an impact. If we have to pay as much as other nations then you do not have money to spend for expansion and productivity capacity.

The level of dependence—and we look at the level of dependence in two ways, an economy way and also one must look at it in a political and military way as well. If we are dependent on 40 percent of our needs now for foreign oil we subject ourselves to a cutoff. In our considerations and in my recommendation to the President I took always into consideration that in the event of a worthwhile political or military crisis it is not impossible to expect there would be a cutoff from these insecure prices and in that event the total U.S. production of about 11 million barrels a day would be insufficient to supply the needs of a wartime economy.

We have talked about it a couple of years now and now it is time for action. We have looked at the three options of do nothing and going through the allocation or rationing and further bureaucracies. For the long term it will take less to get on our energy feet in the third option.

No one likes higher prices, Senator Mondale, I agree with you, and I also agree, and I am beginning to get some people to agree that we did our homework on this subject, that it is not a long term problem stretching out well into the eighties, that there is a tremendous amount of exploitation and discovering going on in this world. But we have to worry about our tremendous dependency and growing dependency for the foreseeable future.

Senator MONDALE. You say three options, one status quo, two, your plan, and three, rationing.

Is there not a fourth option being discussed, and that is a more gradual but legislatively mandated policy of moving toward greater independence by the President's target of 1985, instead of risking the immediate, abrupt and disastrous effects that could follow from this million barrel, then two million barrel target—whose derivation I have yet to see defined—which might just throw this economy into a tremendous tailspin. Would it not make more sense to sit down and say all right, we agree on the objectives, but instead of this incredibly abrupt wrenching of the economy, let us do it with some kind of stable but agreed-upon, long term policy which can assure a growing, stable economy but do so toward these long term objectives?

Secretary SIMON. I agree, that would be a method to implement the price mechanism, doing it gradually. There again, we do not agree that there are disastrous consequences involved, you know, when the original DRI forecast came out it was given all the headlines of a 4-percent impact, approximately, on the Consumer Price Index, and I am told at the end of last week that they made an error in the numbers that they cranked in, and now they agree with ours that the impact will go to 1.2. The word also agrees with our 2-percent impact without the ripple effect.

Senator MONDALE. There will obviously be a substantial ripple?

Secretary SIMON. That is where we have some disagreement based on what occurred last year that otherwise from the producer to you, the consumer of the product, these increased prices are eaten, if you will, through the gasoline station, the jobber and the marketer all the way through and results in lower profits.

Senator MONDALE. If you agree there is a fourth option and it is acceptable to the administration, I think we ought to sit down and work out a gradual program and get around these abrupt costs.

Secretary SIMON. I agree that is an option.

Senator MONDALE. When you have Arthur Burns saying you are creating havoc with the economy you are left with a fairly small band of economists on your side, are you not?

Secretary SIMON. No, I think we outnumber them.

Senator MONDALE. Can you think of one, not in the government, that is on your side? I have not met anybody yet who thinks it is a good idea economically who is not in the Government.

Mr. ZARB. Senator, I thought perhaps——

Senator MONDALE. I thought we ought to have the name of one economist.

Secretary SIMON. Alan Greenspan.

Mr. ZARB. I would like to add to Secretary Simon's response to your question.

We had calculated that our imports from the Middle East primarily would probably be expanded to an additional 2 million barrels a day by the end of 1977, maybe 1978, if you take a more pessimistic look at economic recovery—that, plus the possibility of the OPEC nations increasing their prices substantially over the next 3 years. Sure, we could have a different goal. However, each goal that we have lesser than a million barrels or 2 million barrels by the end of 1977 is an absorbtion of additional risk. We have to value that additional risk we are willing to take as a nation during this period and the additional prices we are willing to pay and the additional pressures which may be brought to bear on us because of our expanding vulnerability during this period and weigh national security and other issues against whatever price we have to pay over the long term.

The CHAIRMAN. Senator Packwood.

Senator CURTIS. I want to ask some questions, but I will wait.

Senator PACKWOOD. I will direct this to you, Frank.

You all read the papers and you know what Senator Mondale is driving at. There is a great reluctance in this Congress to do anything. We thought about rationing for a while and it is not a very palatable project, but that has been discarded.

Allocation is slightly more palatable. Congress does not want a price increase. They have come to the conclusion by eliminating unpalatable options that we will reduce our overseas consumption gradually, and I think that is the major argument you will have to hit and discount.

I wonder if you would run through again why that is not acceptable to the administration.

Secretary SIMON. We have been phasing in on the collision course in our energy policy for 20 years on this position and it is time to have a turnaround. It is not a disastrous impact, because this kind of thinking bases their assumptions on the fact that what we are proposing is a disaster. This proposal is designed to be neutral, return money to the economy, to make energy relatively more expensive than other goods and services and promote conservation.

Senator PACKWOOD. I am concerned with those people who want to do anything but cut consumption. John Sawhill was talking about a 5 and 10 cent gasoline surtax every year. That is I hope a plan for reduction, but could the administration stand that? Assuming that we in Congress came up with a plan that would do it, would a surtax be a satisfactory way to get down to 20-million barrels over 10 years or even in the next 6 years? Without the program right now, we face a very difficult problem.

Secretary SIMON. Yes, we do, and we face it over the next 3 to 5 years until the supply side of the equation, assuming again we get the needed legislature to remove the impediments to bring on the additional supply in this country. We are not proposing anything that is draconian in nature. It is designed to do a million barrels of oil a day, which isn't that great when one considers we are consuming 17½ million barrels a day.

Senator PACKWOOD. I agree. When you were Federal Energy Administrator concerned with the problems that some independent industries had with getting petroleum, we were worried about getting jobs and having energy shortages. The argument is raised if we drop a million or two barrels a day that there will be industries operating on part shifts even if they have demands because they cannot get supply.

Secretary SIMON. That is not true. We are offering them a mechanism that gives them the great freedom of choice instead of cutting down on their energy consumption is concerned. If we went the allocation route I could show you a severe economic impact.

Senator PACKWOOD. Again to emphasize the arguments I know you will have to meet—because I can see the emphasis is shifting from a month ago—FEA has some good reports on industry's reduction in the use of energy without reducing costs. I don't think you can automatically say because industry uses X barrels of oil, you give them X minus 10, and they will have to cut employment, X−10.

Mr. ZARB. If we eliminated for the moment the issue of a possible embargo in 1977 or 1978, when we would be really vulnerable, if we eliminated the possibilities of political pressures and if we eliminated the possibility of substantial price increases by OPEC nations, then we are only left with assurances of industry that we would be independent by 1985. Each of the President's measures has a value. The value is in barrels of oil and the payoffs is in 1985.

Now, he has calculated into the total program 10 years of decisionmaking, 10 years of decisionmaking by the homeowner who will buy storm windows and insulate and who has previously not done so. Believe me, there is vast opportunity for improvement there. Ten years of decisionmaking by automobile buyers who will buy more efficient automobiles and demand more efficient automobiles, 10 years of efficiency by industry who will make the investment in more efficient rather than more wasteful equipment. That will get us to independence by 1985.

So if you eliminate the short-term aspect and conclude there is no need to be independent by 1985 or invulnerable, then we can stretch out reductions to 1982 and then some of those arguments might prevail.

Senator PACKWOOD. The lobbying of some of the New England senators concerning the administration's proposals, makes me think they are still convinced that New England will come out on the short end of this. First run over the differential in tariffs, and secondly why that would give New England the short end.

Secretary SIMON. They pay zero of the first month's dollar and pay 60 cents the second month and 60 cents the third month when implemented. So basically they are paying $1.20.

Mr. ZARB. Senator, two questions with respect to short-term administrative actions that should be recognized.

First, the initial dollar placed on February 1 will not be felt in the consumer economy until late March or early April. So we will have ample time before any impact is felt, and it will be about a penny a gallon.

Now, let us assume that we go all the way to $3 and $1.20 for production, as Secretary Simon has indicated. New England consumers, if you mentioned all consumption together—new oil and old oil—New England consumers would be paying an additional $1.40 per barrel. While the rest of the Nation will be paying an additional $1.65 per barrel. So there is an offset. The reason for the offset is that particular area of the Nation is completely dependent upon foreign oil for its energy. It used 85 percent of oil for energy as compared for 50 percent throughout the Nation, and the bulk of that comes from abroad. They start from a very high base and have suffered the most difficult consequences as a result of the OPEC increase in prices.

But there is the essence of our problem. Here is a major sector, an independent industrial sector of our Nation that has been hit awfully hard by unilateral actions of the OPEC nations. This program is designed to get us off that hook. If we do not start now, 2 or 3 years from now an embargo will put New England completely out of business.

Senator PACKWOOD. Part of the President's program will be decontrol of the old oil. First, what do you expect the price to rise to, and second, what will be the effect if Congress vetoes his decision on decontrol but we have managed to maintain the tariff?

Secretary SIMON. I think you have to look at the entire program rather than just single aspects of the decontrol. You have to look at the windfall profit tax and the balances of it.

The decontrol of old oil at $3.25 a barrel would presumably move to the world market of approximately $11 a barrel and the windfall profit tax which operates, as you know, from 15 percent to 90 percent based on an adjusted base period, would effectively remove the windfall from the producer element of the industry and return that to——

Senator PACKWOOD. Let me ask you for sure. It will raise the world oil price. There would not be any moderating of old oil and new oil prices in this country rounding out to 9.5 a barrel?

Secretary SIMON. No; my judgment is that it would move to the new price, in an internationally traded market. That is the way the price mechanism works, or the market works, in the absence of any Government controls.

Again, I say and I emphasize, there is pressure on the world price and that is shown in the discounts given through delayed payments today by the OPEC nations. They recognize too, that this oil that has been discovered in the past year, as Senator Mondale said, 30 billion barrels by our reports in the past year, will be 13½ million barrels a day by 1980. Exploration is going on at a frenzied pace in response to this price. I am very optimistic on the longer term, but we are in a dangerous position at the present.

Senator PACKWOOD. I have no other questions right now, Mr. Chairman.

The CHAIRMAN. Mr. Haskell.

Senator HASKELL. Thank you, Mr. Chairman.

Mr. Secretary, we are dealing with two bills today; one is the debt limit, and the other is H.R. 1767, a bill to suspend for 90 days the President's authority to impose oil import fees. The latter bill, of course, seeks 90 days to permit a legislative energy tax program to be worked out and hopefully negotiated with the administration. Why do you think it is inappropriate to give the Congress 90 days?

Secretary SIMON. Senator, the President felt that the time for action was now, and in putting this very comprehensive program before the Congress the import fee was the only thing the President could do in the absence of legislation, and that the time to start was right now for both domestic as well as international reasons.

Mr. ZARB. May I add to that.

The President's program has a built-in time delay. The first dollar will not be felt until late March or early April. The second dollar has the same kind of time delay. The total impact would be about 3 cents per gallon.

The time before some of the difficulties could take place there, which some project, and we do not agree with, and there is ample time to develop some of the issues and some of the options and alternatives that may evolve from the Congress.

Senator HASKELL. I would disagree with you, Mr. Zarb. After all, once you have initially inflicted that 10-, 20-, 30-cent bite on the energy economy, you have created an inflationary effect that you cannot reverse.

But let me respond in another way to Secretary Simon's answer. The President apparently says now is the time to do something.

Secretary Simon, I would like to point out that in 1973 the Senate, and subsequently in 1974, the House passed S. 1283, designed to increase the utilization of certain conventional sources of energy, such as coal, designed in short to stimulate the supply side of the energy problem. This eventually resulted in a bill to set up ERDA and provide an appropriation along those lines.

So I would say Congress has addressed the supply side of this problem.

Moreover, in the fall of 1973, the Congress passed an energy conservation act that dealt with mandatory conservation measures. This had a low impact on new oil prices—somewhere in the neighborhood of $7.10. Our bill was vetoed, but, as I understand it, your windfall tax program would probably roll back oil prices to that level now.

But be that as it may, after the veto, there not being sufficient votes to override the veto, the Senate again passed a very comprehensive mandatory conservation bill, which, for example, told Detroit that it would have to develop and produce more efficient automobiles by specified times.

Then, third, the administration now makes a great—and Mr. Zarb just alluded to it—a great demand for a strategic reserve. In either 1973 or 1974 we introduced a bill that was proposed by a committee of which I am a member. I distinctly remember the administration opposing that bill on expense grounds.

Now, I think I can anticipate your answer, so I will not put it in the form of a question. But it seems a little bit disingenuous for the administration to say Congress has done nothing on the energy question. I would submit that it has been the Congress working on this problem, not the administration until very recently. Now the administration apparently sees the necessity of doing something and is proposing a program which I think is immensely complex. We had witnesses the other day who described certain unknown economic effects of the program. I do not consider it unreasonable in light of those unknown economic results and in light of the Chase Manhattan Bank charge that the program is recessionary while certain prominent economists predict the program will also be immensely inflationary, for the Congress to ask for a 90-day delay. Do you have a comment?

Secretary SIMON. Sure, our program is complex, and of course, so is the problem complex. We have been discussing this. I have testified on the subject of energy in the Congress probably 100 times in the last 2 years.

The bills that you talk about, the ERTA bill, was a good one. It is paying off, of course, as far as future coal conservation, which comes really in the next decade.

The conservation that talked about rollback and rationing was not, in our judgment or the President's judgment, the way to attack the problem.

Senator HASKELL. I may say that bill had a great many other features.

Secretary SIMON. Our windfall profits tax, while in the short run could take on the appearance of rollback, has a distinct phaseout which does not discourage production, which is what we need. I was not familiar with the automobile bill passing the Senate.

Senator HASKELL. I think my 5 minutes have been used.

The CHAIRMAN. You have 10 minutes, Senator.

Senator HASKELL. Well, under those circumstances, I do have a few more questions.

One thing you mentioned—I forget whether it was the Secretary or Mr. Zarb—was that there really would not be a major ripple effect. I think this was in response to the Senator from Minnesota's question. And you talk about an increase of 3 cents on the price of gas, but how about residuals—how about airline fuel? Have you looked at the effect on the airline industry, for example? We had testimony in another committee that it would probably double the price of jet fuel, that the alternative, of course, was for the airlines to absorb this increase, which means either massive layoffs, or fare increases somewhere in the neighborhood of 20 percent.

The opinion of the gentleman who testified, and it was extremely well-prepared testimony, was that under those circumstances, because of the price elasticity in the airlines, based upon historical patterns, the airlines would have to cut back on routes, lay off employees, and have standby or idle equipment.

How about the effect on such things as utilities, houses, colleges? Florida Power & Light came in, for example, and showed us a chart on the increase of their fuel costs which they passed on to their customers. I question whether the economy or segments of the economy can stand this type of increase, and I would also wonder what your responses would be to this testimony—you have heard it from me secondhand, but I assure you it was accurate on the airlines and also on the increase in utilities costs. Do you have any comment on that?

Secretary SIMON. Yes, I will let Frank elaborate on it because he has met with a lot of these affected industries. We have studied this in the Economic Policy Board.

The fact residual oil comes in almost entirely from imported sources is the reason we are attempting to attack this problem as far as our domestic supply is concerned.

Again, when we talk about what noted economists agree with our economic forecasts and what the effects are going to be, DRI, in working again agree with us when we designed the package so that it would have a positive stimulus in our economy with the tax rebates and the rebates carefully put into effect that it would not have a negative effect, and that I think is important.

Senator HASKELL. If I may pursue this with you, Mr. Secretary, I find it difficult to see how raising the total price of oil in the United States to the consumer—and I am not just talking about your tariff—to a level of $14 or $15 a barrel, which would happen, since in response to Senator Packwood's question, you agreed that a deregulation of old oil in the United States would push it to the imported price—we are using about 65 percent of our own oil, and probably of that 65 percent somewhere in the vicinity of 40 percent is old oil—will have anything but an inflationary effect.

Secretary SIMON. Well, that is an inflationary effect of approximately 2 percent, a one-time inflationary effect seemingly, short-term contradictory or conflicting policies, in order to get at a long-term goal. Basically, what we are attempting to do is to raise the price now to have a lower price later, recognizing if OPEC quadrupled the price last year when we are depending on 33 percent, if our oil continues to grow in the future, what is to stop them from raising the price in the future.

I want Frank to address the utilities and airlines as well.

Senator HASKELL. May I ask one more question of you, Mr. Secretary?

What makes you think that putting a $3 tariff on imported oil is going to have the slightest impact on the policies of the OPEC countries?

Secretary SIMON. You have to look, Senator, at the entire program, not the $3 tariff. The $3 tariff becomes a $2 tariff along with the tax on natural gas and excise tax on domestic production, and it equalizes the price of oil.

Senator HASKELL. Mr. Secretary, I think you were saying that the President's program would have an effect on foreign imports in that we woul import less from foreign countries. I assume that was your response?

Secretary SIMON. We would consume less in this country, and therefore, less, we would import less.

Senator HASKELL. Well, we have shifted grounds. Why would we consume less?

Secretary SIMON. Because there has been shown what economists call an elasticity of demand for petroleum based on the past year's experience, and again I refer you to what the other countries in the world have done and the Wall Street Journal this morning—we are at the bottom of the heap in the world in what we have conserved in energy. Look at the price of gasoline in all the other countries, it is from a $1.25 to $2.25. The paper this morning, an unknown source, contends we continue to give our products away.

Senator HASKELL. That is the end of my questioning, Mr. Chairman.

I would merely like to observe that over the weekend I read an article asserting that when the last big jump in the price of oil came, there was a 3-percent decrease in the use of gasoline, that we now have made up that 3 percent and indeed are now using more. I will seek that article out, Mr. Secretary, and we will trade——

Mr. ZARB. Senator, that was my quote.

The CHAIRMAN. Might I just suggest that we let the witness answer this question, and then we will come back to you for a second round, Senator Haskell.

Mr. ZARB. I would just answer two parts of your question quickly.

I pointed out that when gasoline went up as high as it did in its peak last summer, our consumption rate was about 3 percent below the previous year, adjusted for all kinds of things. As soon as the supply became more abundant and consumption went down, margins were squeezed, and even in this area gasoline was down from 7 to 10 cents from the peak, and as soon as that squeeze occurred, the 3 percent went back to almost a comparable number. Now, 3-percent lesser is a lot lower than our normal consumption rate, which had been increasing rather dramatically each year, so price did have its effect.

With respect to airlines and other specialized industry, I would just point out, Senator, that regardless of what program we selected, unless it was no program at all, if we went to a gasoline tax, Florida would be talking to us about tourism and not residual oil. If we went to rationing, we would have the same kinds of problems. If we went to allocation and created a shortage and the inconvenience and so on, we would have those kind of issues industry by industry, and we ought to look at that with whatever program we go forward with and be sure that we resolve those individual situations.

The point is, this seems to be the one program that has the least number of those problems to deal with.

Finally, we have said right along, we have the authority to adjust the passthrough of these increases on various petroleum by products and that our intent was to pass a greater part of the increase on to gasoline and a lesser amount to products such as heating oil and residual oil.

Senator HASKELL. Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Dole.

Senator DOLE. Mr. Secretary, do you have a contingency plan in case everything else fails?

Secretary SIMON. The President has said that if all else fails and we do not achieve the targets that we desire, the demand, that other measures would be taken. There are other measures, but we believe the program that the President has put forth will accomplish what it is designed to do.

Senator DOLE. I am thinking about the event that the tariff suspension bill is adopted by the Senate, and a veto is overridden. Are you not yet publicly making any statements on an alternate plan, then?

Secretary SIMON. I believe that through these sessions and the dialog that always occurs in the Congress that we will arrive at a sensible policy as the President put forth, Senator Dole.

Senator DOLE. I have read your statement. I came a little bit late, but what is the source of this conservation goal of 1 million barrels and 2 million barrels?

Secretary SIMON. I have a chart I believe prepared by FEA which I will submit for the record which specifies how much will be saved with each product, gasoline, residual No. 2, et cetera.[1]

Senator DOLE. What countries would it affect the most?

Secretary SIMON. Oil being an extremely pungentable product, it is extremely difficult to trace cutting off. Somebody suggested we save the million barrels purely from this one source, but there are so many transhipments involved, it is very difficult to pinpoint it. I know the great difficulty I had last year in attempting to trace the product as it was being shipped.

[1] At presstime, Feb. 17, 1975, the material referred to had not been received by the committee.

Senator DOLE. I want to ask Mr. Zarb a question. Of course, we all have somewhat different interests. Our Governor made a statement recently that certain portions of proposed rule changes could result in permitting higher financial burdens being imposed on some sections of the country. We take New England versus the Midwest, for example, to show the regional inequities. According to Kansas' figures it would annually cost the average Kansas about $101.79 while costing the average New Englander about $74 more, assuming a $3 per barrel tax on all crude oil passed through only on gasoline. We want to help the New Englander, but I am not sure we want to help that much.

Mr. ZARB. Senator, you are correct in that the burden would be felt more in some of the areas of the country with respect to gasoline and that New England would not be at the top of the list with respect to burden.

However, I think we do have to recognize that New England does start at a very, very, very high level because of their total dependency on oil as opposed to the rest of the country and almost totally on foreign oil.

I have seen the bumper stickers in Louisiana and Texas that relate to that issue and suggest perhaps they have gotten themselves into that bind and they should not have this kind of entitlement. I think in view of the fact that there are people in those houses that pay for fuel oil, and particularly those people that have been responsible for the current state of affairs, that we really should as a Nation impose whatever program that we finally decided upon so that it is properly balanced. I think the program as the President put forward does properly balance the situation, so that undue hardship is not felt anywhere.

Senator DOLE. There was also some discussion with regard to Hawaii.

Mr. ZARB. Our analysis of Hawaii, which we discussed with the delegation from Hawaii, concluded that at this point they do not require special consideration. The President specified that any part of the country suffering undue hardship should be considered. We do not think we need to have a special program there.

Senator DOLE. Well, there has been some suggestion rather than to strive for the million barrel per day cutback that we reduce that goal, which would in turn reduce the economic impact. I presume that is one possible alternative kicking around somewhere.

Is there any real reason for a conservation goal of 1 million barrels per day this year and 2 million by the end of 1977?

Mr. ZARB. Senator, I have not seen a proposal that suggests a different kind of phase period or that we save 1 million by a year from today or 18 months from today. I think we ought to examine any proposal that is put forward on that basis. In each case we ought to look together at what we might be trading off. If we elongated our period of exposure or extended our period for invulnerability to achieve invulnerability that is something Congress should come to agreement on. But I have not seen a program that would demonstrate we would achieve independence or have some kind of program for phaseout.

Senator DOLE. What are your comments about the argument that you are in effect taking money out of one pocket and putting it into another? This $30 billion from the energy taxes, if and when it does happen, as I understand, would go for tax reductions, both temporary and permanent. Do you have any comments on that statement?

Secretary SIMON. Our program was designed to be neutral in its effect on the economy, recognizing that we are in a sliding economy and any effort to raise taxes or raise the price of a commodity will have an economic impact just left to itself. So, therefore, we turn not only to business and Government, but also through the tax system, but the people who pay no taxes at all, the approximate amount of money that they would be paying additionally for this increased price is called for during this period of declining economic activity. But this means that they are going to save more as far as energy is concerned and therefore be able to have more money to spend for other goods and services.

Senator DOLE. Are there any plans to take care of those who cannot pass the cost on? I think farmers, and they are very important in the economy today, could end up on the short end of the stick. If the excise tax on natural gas takes effect, the price of fertilizer per ton would probably rise about $15 a ton, and there is no way for the farmer to pass on that cost. In the State of Kansas alone the added cost of fertilizer would be, according to figures, and I understand they are conservative, but about $64 million dollars per year. That additional cost would come out of any profit the farmer might expect to have.

Is there any plan afoot for rebates to those people?

Mr. ZARB. Senator, the President has directed that we work out a mechanism to rebate to the farmer because of his inability to pass through and because of the food situation. We have been working with Secretary Simon's people for the last week and hopefully we will have an arrangement completed very shortly.

Just one part of the last question you asked which I did not get to answer. We talked about elongating our time table for achievement. We also ought to keep in mind if we go from $24 billion of outflows as compared to $3 billion in 1970, and then go to $32 billion by 1977, that that is lost American wealth and American jobs, and I think we ought to trade off exactly how much of that we will allow to happen for how long.

Senator DOLE. Thank you.

The CHAIRMAN. Senator Brock.

Senator BROCK. Mr. Secretary, if I understand your logic, there are three essential reasons for this particular action. The first is to raise the cost of energy relative to other sectors of the economy.

Second, in order to increase revenues so that you could have the means by which to motivate through tax incentives greater conservation, for example, home insulation.

And third, to set the price of energy high enough to induce the development of alternatives. Is that a fair summation of the three?

Secretary SIMON. Yes, it is, Senator.

Senator BROCK. All right. Then we have got to face, either separately in the Congress or jointly with you, the question that has been asked time and again at these hearings what will be the economic impact of the program in the short term? Can we achieve these three objectives with a somewhat different, perhaps more slowly phased in program?

The question we have faced time and time again is whether or not the economic impact would not so devastate the economy with 2 diget percent inflation, but more than that, dislocation so as to set back our total economic recovery and perhaps make it worse; if not make it worse, certainly delay it for a period of extended time.

I would like you to comment on that question, because that is the one that bothers me more than anything else.

Secretary SIMON. Yes, Senator Brock.

No single part of this program did we spend more time on than designing the fiscal impact as far as taking this large amount of money out of the economy and simultaneously turning it back in, recognizing the lags.

There is a table attached to my prepared statement[1] which shows the energy taxes, when levied, the amounts levied by quarter, and how it is returned. We specifically designed, if you will notice, the windfall profit tax does not begin to be collected until the third quarter of 1975, because if it had been collected much earlier it would have done just as you say in giving us a negative impact. As you will see, the positive impact is concentrated in the second and third and to a lesser degree the fourth quarter of calendar 1975 and to a lesser degree during all of calendar year 1976. So we think we have done that.

Now, we have not designated as far as the Consumer Price Index the 2 percent; no. But I will say the Consumer Price Index does not take into consideration that fine, we are raising the price of a commodity. When the price goes up it is illustrated in the rise in the Consumer Price Index. The Consumer Price Index does not take into effect the fact we are giving the money back. If one wants to say, well, you are taking it back out of one pocket and putting it in the other, well, why are you doing it. Well, Senator Brock, if you raise the price of oil and gas relative to the other commodity we are going to save that and that is the purpose of the exercise.

Senator BROCK. Would not it be possible, instead of going $1 per month for 3 consecutive months, to phase it in over a couple of years and achieve the same end result? You might reduce your savings from 1 million barrels to 700,000 barrels this year, but would not your ultimate saving be the same?

Secretary SIMON. Yes, Senator Brock; you could phase it in over whatever period you would like to phase it in. You have to weigh that, after the economic analysis of the impact of not doing it and attempting to reach a conclusion versus the alternatives and what the exposure is during this period of time while we continue to be so reliant on foreign crude.

You know, it is very difficult, because you can get economists who will give you their analysis, and they do it in great good faith and with great expertise, but we have in this country, as we do around the world, economists for all seasons. We can find any answer, really, that you would like.

Senator BROCK. You are going back to statistics and statisticians, are you not?

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[1] See page 99.

Secretary SIMON. Yes.

Senator BROCK. The thing I am reaching for, and I am enormously sympathetic with what you are trying to accomplish and agree with the end product of the program, but I just wonder if you have anything to trade to the Congress for some fairly fundamental changes. We have been trying for as long as I can remember in the Senate to deregulate natural gas with no success whatsoever. It seems to me that—maybe I am particularly sensitive, because Tennessee has just been hit with another curtailment in December that has shut down industries, costs us thousands of jobs. It is going to get worse before it gets better. We are one of the five most seriously affected States. The Congress is talking about rationing instead of increasing supply of natural gas. This is ridiculous. We are about as rationed as you can get right now and we have people out of work, and I just wonder if there is not some possible trade-off here to get quicker action from the Congress on the supply side in exchange for reduction in the cost impact on the tax side?

Secretary SIMON. Well, I always believe in flexibility, Senator Brock. I am not speaking of certainly the President's willingness to compromise, but we would be willing to see any comprehensive program the Congress comes up with.

I agree with you on natural gas, and we are at that point that anything we do on natural gas will not forestall the tremendous problems we have in natural gas over the next couple of years.

Senator Dole brought up the fertilizer problem. We talk about fertilizer shortages where a vast amount of our nitrogen fertilizer comes from natural gas and they are down under 10 percent from 24 percent with what they were when we first started to control the price and at a ridiculous level, and at the same time paying five times that for the equivalent Arab oil. I do not understand that kind of arithmetic.

Senator BROCK. Neither do I. Maybe I can divert you to a better conversation.

Are we going to have an adequate supply of fertilizer this year? Are we in the same mess we were in last year?

Secretary SIMON. It is going to be short, Senator Brock. In looking forward in the future, if our natural gas situation remains the same it will be shorter and shorter and shorter. There are some industries that use natural gas that cannot use alternative sources. It is causing massive layoffs. I am well aware of that in my own State of New Jersey right now.

Mr. ZARB. Senator, where we are running short we have been allocating in propane and some cases oil for conversion. The oil we are allocating as a substitute is a further irritant on the import levels of our oil.

Senator BROCK. One final question for Mr. Zarb, if I may.

The way the tax breaks out it looks to me as though if this program is adopted in total as suggested by the administration, that it could result in a rather serious disincentive for domestic refineries. Is that an unfair statement, and if so why? Is there adequate motivation for the refining of petroleum products in this country under the proposed plan before us?

Secretary SIMON. I went through this debate in the Ways and Means Committee in—I do not remember—March of 1973 when, as Chairman of the Oil Policy Committee for the President, we invoked section 233 to change the old import quota system to a fee system whose primary design and justification was to build refinery capacity and stimulate refining capacity to make sure oil products would not come into this country at a lower price than our domestic supply. It immediately increased the announcements of new refining capacity in this country to a significant degree.

If we are going to monkey around with the oil fee, in my judgment, it is going to be very counterproductive.

Senator BROCK. Thank you very much.

Senator NELSON. Would the chairman like to ask a question?

The CHAIRMAN. I suggest the acting chairman go ahead and take his turn.

Senator NELSON. Thank you, Mr. Chairman. Senator Curtis.

Senator CURTIS. Is the effect of the Kennedy-Jackson proposal and the Green proposal in the House, are they the same?

Secretary SIMON. Yes.

Senator CURTIS. A vote for either one of those, will it carry a plan of meeting our problems in the area of petroleum?

Secretary SIMON. No sir, it does not. It just, again, postpones for further consideration any action in this area, and as Frank so accurately said, this program was designed to phase in the dollar, does not have an effect for at least 30—and probably much longer—days, the $2 and the $3 the same way. That gives us plenty of time to have the dialog we are having right now to get a program into place.

Senator CURTIS. I think it is important these hearings show, both for Members of the Senate and the public, that the issue is not one of the choice of two plans, but it is to stop at least for 90 days the only plan that is before us. Is that right?

Secretary SIMON. Yes, Senator Curtis.

Senator CURTIS. Now, I would like to have explained to me how the application of the tax would work. When we talk about an import fee of $1 a barrel how does that work out on the retail level, on the various components such as heating oil and gasoline and other products?

Secretary SIMON. Our estimate is approximately a penny a gallon across——

Senator CURTIS. A penny a gallon on all types?

The heating oil and gasoline would, and the industrial uses would come out about the same, a penny a gallon?

Mr. ZARB. Well, Senator, the first $1 is relatively small in impact. We have said, as the President's program was enacted, to a total of zero, that the total program would be 10 cents per gallon average, that we would use our authority to roll through somewhat more on gasoline and less to heating oil and other less elastic products.

For example, with a 13- to 15-cent change in gasoline, 7- to 8-cent change in heating oil

Now, in this interim period while we are going through the administrative phase—we have the abilities to phase in this increase so that it affects one product more than the other. We have not as yet come to a determination as to whether that is required, but we certainly can.

Senator CURTIS. Well, now, if the application of the import fee of $1 amounts to 1 cent a gallon additional in cost to the consumer, what are the other parts of the proposal that would give it the price increase that you have just referred to?

Secretary SIMON. The President's administrative actions, of course, only affect imported crude oil, and when you mix it all together that is all you get to the 1 cent per gallon I just described, in case there is some questioning how we get to that number. But you mix domestic and imported together and that is the way our rules would have these prices roll through the economy.

The total program, if enacted, would have a $2 tariff rather than the $3, which administratively would come off. A $2 excise tax, decontrol of old oil, decontrol of new gas and a 37 cents per thousand cubic feet of natural gas excise tax. That would have the net effect of increasing all petroleum products an average of 10 cents per gallon, and it is that which we would administratively direct that a higher incidence of that would flow to perhaps gasoline and in the oil area, residual oil or heating oil.

Senator CURTIS. Now, those subsequent steps all require legislative action, do they not?

Mr. ZARB. Yes, that is correct, except decontrol. That requires legislative action. Decontrol has 5 days during which the Congress can veto the President's action.

Senator CURTIS. So in a sense that is a limited legislative action?

Mr. ZARB. Yes.

Senator CURTIS. In other words, if the President's import fee is allowed to go in, it is going to have an impact of 1 cent per gallon on consumers?

Mr. ZARB. The first month.

Senator CURTIS. Yes, on the basis of 1 cent per gallon for each dollar of the import fee, that is what it amounts to?

Mr. ZARB. The first dollar's effect will be felt in late March or early April. Then the second dollar is levied March 1, and the third dollar on April 1.

Senator CURTIS. So if we come up with something that can be enacted into law, in the meantime all that is involved in the Kennedy-Jackson proposal is to prevent a 1 cent a gallon for each dollar of the import fee from going into effect. Is that not correct?

Mr. ZARB. Yes, that is correct.

Senator CURTIS. There is no proposal involved in that particular vote that is going to have any drastic or far-reaching effect upon the consumers unless the Congress provides the necessary legislation. Is that not correct?

Mr. ZARB. Yes.

Senator CURTIS. Is it true that what we are faced with in meeting our problems of energy is sort of twofold. One, to encourage full domestic production, and the other to discourage reliance on foreign products. Is that what it amounts to?

Mr. ZARB. Yes.

Senator CURTIS. Do you agree that it takes a full consumption of energy to have our economy and our employment going full capacity or as near that as possible?

Mr. ZARB. Yes.

Senator CURTIS. Is it not true that we also are not deciding between some new proposal and going back to the old days of low-cost oil from the Middle East?

Mr. ZARB. That is correct, Senator.

Senator CURTIS. And what is the outlook in reference to the cost of domestic production. Is that apparent to be high for sometime?

Mr. ZARB. It certainly is going to continue to increase as the cost of exploration and development increases, Senator.

Senator CURTIS. Well, I heard a member of this committee who is very knowledgeable in the field of oil, because he comes from one of our major oil States, Senator Bentsen, point out that the future cost of producing oil any place, domestically, off our own shores, for the North production, the English and Norwegian production and elsewhere, is going to call for massiv e amount of capital and a high-cost drilling operation. Is that the Government's opinion that some of those factors are likely to be present?

Mr. ZARB. Yes.

Secretary SIMON. Not only that, Senator Curtis, but as we have said so often, we have moved from a low cost abundancy base to a high cost scarcity base. We have found all the oil and gas we will find in this country and we must move to more hostile climes, the secondary and tertiary techniques. They will obviously cost us more. OPEC oil costs more to produce. We will see something in the area of $2.50 a barrel before transportation to produce in the North Slope and perhaps some even higher than that. But it still will not reach the levels of the current world price, and that is the point, that by giving all those incentives and a comprehensive program in the short run to reduce our dependency and utilization of energy in this country and to bring on the super abundancy of natural resources in this country we are going to bring the price down.

Senator CURTIS. The balance of my questions I will wait until my second time around. I hear the bell.

But I will propound one that does not call for an answer now, but to supply for the record. If the figures are available, fine.

I would like to know what our annual consumption of petroleum and all petroleum products has been and how much of it has been domestic and foreign, going back as many years as statistics are available, fine.

I would like to know what our annual consumption of petroleum and all petroleum products has been and how much of it has been domestic and foreign, going back as many years as statistics are available. I would like to go back to World War II. But I do not want to make a request for the assembling of a great deal of statistics that are not available.

Mr. ZARB. We will provide that for the record, sir.

Senator CURTIS. I will reserve the balance of my questions until later.

[FEA subsequently supplied the following information:]

TOTAL U.S. PETROLEUM SUPPLY 1945-74 [1]

[In millions of barrels]

	Imports					
	Crude	Refined products	Total imports	Domestic production	Total new supply	Imports as percentage of total new supply
1974	1,277	945	2,222	3,816	6,038	37
1973	1,184	1,080	2,264	3,988	6,252	36
1972	809	922	1,731	4,083	5,814	30
1971	613	819	1,433	4,072	5,505	26
1970	483	765	1,248	4,123	5,371	23
1969	514	641	1,156	3,952	5,108	23
1968	472	566	1,038	3,883	4,921	21
1967	412	514	926	3,730	4,656	20
1966	447	492	939	3,496	4,435	21
1965	452	449	901	3,290	4,181	22
1964	439	388	827	3,209	4,036	21
1963	413	362	775	3,154	3,929	20
1962	411	349	760	3,049	3,809	20
1961	382	318	700	2,984	3,684	19
1960	372	293	665	2,915	3,580	19
1959	252	297	549	2,896	3,445	16
1958	348	273	621	2,744	3,365	18
1957	373	201	574	2,912	3,486	16
1956	342	184	526	2,911	3,437	15
1955	285	170	455	2,766	3,221	14
1954	239	144	383	2,568	2,951	13
1953	236	141	377	2,596	2,973	13
1952	210	139	349	2,514	2,863	12
1951	179	129	308	2,453	2,761	11
1950	178	133	311	2,156	2,467	13
1949	154	82	236	1,999	2,235	11
1948	129	59	188	2,167	2,355	8
1947	98	62	160	1,990	2,150	7
1946	86	52	138	1,852	1,990	7
1945	74	39	113	1,829	1,942	6

[1] 1974—FEA, "Weekly Petroleum Statistics Reports," and "Petroleum Situation Reports," for 1974, 1945-73—Bureau of Mines, Mineral Industry Surveys "Petroleum Statements."

TOTAL U.S. PETROLEUM DEMAND 1945-74 [1]

[In millions of barrels]

	Total [2] domestic demand	Total imports	Imports as a percentage of total demand		Total [2] domestic demand	Total imports	Imports as a percentage of total demand
1974	6,057	2,222	37	1959	3,450	549	16
1973	6,298	2,264	36	1958	3,315	621	19
1972	5,974	1,731	29	1957	3,219	574	18
1971	5,554	1,433	26	1956	3,213	526	16
1970	5,364	1,248	23	1955	3,088	455	15
1969	5,160	1,156	22	1954	2,832	383	14
1968	4,788	1,038	22	1953	2,775	377	14
1967	4,481	926	21	1952	2,664	349	13
1966	4,325	939	22	1951	2,570	308	12
1965	4,125	901	22	1950	2,375	311	13
1964	3,959	827	21	1949	2,118	236	11
1963	3,851	775	20	1948	2,114	188	9
1962	3,736	760	20	1947	1,990	160	8
1961	3,579	700	20	1946	1,793	138	8
1960	3,536	665	19	1945	1,773	113	6

[1] 1974—FEA, "Weekly Petroleum Statistics Reports," and "Petroleum Situation Reports" for 1974; 1945-73—Bureau of Mines, Mineral Industry Surveys "Petroleum Statements."
[2] Note that total domestic demand is the disappearance of product from primary supply. It does not equal total consumption.

The CHAIRMAN. Senator Nelson.

Senator NELSON. Maybe you addressed yourself to this question before I arrived. If so just say so and we will skip it.

What price level does the old oil and all new oil go to when you put $3 a barrel on imported oil?

Secretary SIMON. I did address that, Senator. It is our judgment that the—when we decontrol old oil it will go to the world oil price and, of course, the taxes would go on top of that.

Senator NELSON. And when the old oil is decontrolled, what will its price be?

Secretary SIMON. It will be approximately $13 a barrel.

Senator NELSON. $13 a barrel.

Presently the price of controlled oil is $5.25, isn't it?

Secretary SIMON. Yes.

Senator NELSON. So that will go up $7.50 a barrel?

Secretary SIMON. Approximately.

Senator NELSON. And all new oil will be at the world price, also?

Secretary SIMON. $2 of that, of course, will be taxes.

Senator NELSON. Again, this may have been asked before I arrived here this morning, but what precisely is the purpose of the tax? How would you describe the specific purpose of placing a $3 a barrel tax on imported oil?

Secretary SIMON. Well, it is ultimately going to be a $2 tax. It is a demand restraint tax.

Mr. ZARB. I would like to add to that, if I may, Senator.

The purpose is to put oil energy at a level of values within our economy different from its current level of value to promote over a period of time the kinds of consumption and investment decisions which would have us use energy for its truer value as a scarce commodity.

If we had 10 years of investment in a home—I mentioned this earlier—for insulation or storm windows and caulking and more efficient heating equipment, if we had 10 years of activity which had the automobile driver make different selections with respect to the efficiency of his automobile and demand that from the seller, and 10 years worth of investment in the plant which would have the plant manager select a piece of equipment which was more energy efficient as compared to one which was not, although that one may cost a little bit less, that kind of activity over a period of time could have a measured affect on the way this society uses energy. There is no question but what we as a nation per capita, based upon our standard of living, uses energy far in excess of other nations with an equal standard of living per capita.

Senator NELSON. So the purpose of the tax is not, as has been at sometimes reported, solely to reduce the importation of oil. It is also to make the price of all oil so dear, and therefore, as a policy matter, as a decision of the Federal Government to just arbitrarily raise the price to force a reduction in consumption. Is that correct?

Mr. ZARB. Well, that is both effects, Senator. It does indeed backout imported oil and if we are able to use less oil per unit of work done in our economy, we are going to backout imported oil. So that is both effects.

Senator NELSON. That is why I raise the question. If the objective were, as a number of stories I read stated it to be, simply to reduce imports to help the balance of payments and so forth, it would seem to me it would be more sensible simply to limit imports, period, without adding this heavy burden of an additional tax on the consumer.

Mr. ZARB. Senator, the scheme of import quota and allocation was one we examined very carefully and we ought to share with you some of our analysis. It had several problems.

First, it did nothing in the way of incentives with respect to future development. We put that aside.

It meant that the Government had created a shortage. If the Government did not create a shortage there would be no savings. Now, we would not have the Arabs to blame or OPEC to blame. This could be a Government imposed shortage.

Now, then, the Government could not let the shortage go by its own devices because of the way things would be affected. We would have to manage that shortage, similarly during our approach to the embargo, although we have gained some additional expertise since that point.

It would mean the Government would have to make decisions with respect to who got 90 percent, who got 100 percent, who got 80 percent, and then insure that each of these decisions, day in, day out, which company could expand, which company could not expand, which company could start brand new, which company could not start brand new. The Government could make all these decisions perfectly. Economists tell us this would have a disruptive effect on our economy.

If the Government were capable of doing that perfectly across the board that would not be the net result.

We concluded that is the kind of system that is not accepted in our free society and, over a long period of time, would not prevail and get the job done in an equitable way, but it certainly is one of the alternatives.

Senator CURTIS. The question before us, Mr. Chairman, is just the debt limit, as I understand it, and the 90 days. So on a later date the Committee will be hearing the tax proposals and the energy conservation proposals. I have a number of questions that are beyond what is before us, so I will hold those. They involve energy conservation.

Thank you.

The CHAIRMAN. I believe we offered everybody a chance to ask questions the first time around.

Mr. Secretary, I would like to make my position clear. I suppose I am the most isolated man in this hearing at this moment, because I do not go along with all the President's program by any means, and I do not go along with all the Democratic program, if we ever get around to determining what it is going to be. I find there are good points and bad points in all these suggestions, and I would hope we take the best of what everybody has to offer and try to improve on those suggestions that are not so good and dump out those that are not good at all.

It does seem to me there is a need for statemenship in the operation of this Government, especially with a Republican President and a Congress overwhelmingly Democratic. I think we would do well to drop out all this needless self-righteousness on both sides. We have heard a lot from some of our Democratic colleagues about how we sent a bill down to the President which had some of the same provisions which you are recommending to us, and the President vetoed it. If I recall correctly, when that was done, you were the Energy Administrator and you were advocating against one provision in that bill which you thought made it counterproductive. You were willing to support a rollback in the price of oil, but you felt that to go beyond a certain point would be counterproductive and result in a lot less energy, rather than a lot more. I thought you had put those of us on the Democratic side of the aisle on notice that if the bill went down in that fashion, you would feel compelled to urge the President to veto it.

To me the logical thing to have done when the bill was vetoed and the President indicated he would go for a rollback at a certain point and no further, would have been to send that bill down there in a fashion that the President would sign it. At that point it seems to me those with the power took the view that if the President would not sign the bill on their terms, that they were not going to send anything back to him. What that not about the way that was played out?

Secretary SIMON. I do not remember the President ever saying he would support a per se rollback, because he felt very strongly that the windfall profits tax with a phaseout would do the job of removing the windfall from the price of a barrel of crude oil and at the same time not remove the incentive to bring on additional supply in this country. The minute you start monkeying around with price incentives——

The CHAIRMAN. The issue is pretty much the same. It had to do with the profits that the companies were permitted to make. The administration had one approach to it which would limit the profits the companies could make, and the prevailing view among Democrats seemed to be somewhat different than that. But in either event, you were recommending a proposal that would limit the profits of the oil industry, although not the same proposal the Democrats were recommending.

Secretary SIMON. Yes, you are correct in that the President asked me to tell you that if the measure comes down in a rollback form, that he would recommend a veto, which, of course, he did.

The CHAIRMAN. My suggestion is that those things in that bill the President was recommending should have been sent back to him at that time without the provision that required him to veto that measure in following his conscience. We should have taken as many of the things we agreed upon at that point as we could, and not left ourselves in the ridiculous position of failing to do anything simply because the Republicans wanted to control oil profits one way and the Democrats wanted to do it in a different way. It seems to me that is a failure of statesmanship. I do not think the Democrats can escape responsibility for that any more than the Republicans, and I believe that is what we are facing now.

You are going to have some good suggestions, Democratic and Republican. You have some good suggestions made by the President.

If we sent a bill down to the President and he thinks there is something there he can't sign, then send it back.

Secretary SIMON. Couldn't agree with you more. I don't sit downtown and point my finger at the Congress and say if they would do this and that, we would be well off. The people in America, when we look at Government, they don't think of Congress or the executive branch. We are their Government. We ought to be able to hammer out differences of opinion. We are delighted to do that.

I don't think the importation of a dollar and the great lag that exists in the dollar, $2, $3, it is a start in the right direction. Let's hammer out together what the balance is going to be.

The CHAIRMAN. Let me just get to one of the aspects of the President's program that I find some doubt about.

It would seem to me that the large amount of revenue that you would raise with your so-called windfall tax, ought to be directed toward producing more energy to provide adequate capital to get this job done, opening new mines, opening new sources of energy, drilling in the Atlantic, whatever it takes, before that money is directed to other purposes.

As I understand it, about $60 million were spent on exploration and development 10 years prior to the energy crisis in this country. That sounds like a great deal of money, about $6 million a year. My impression is it should have been twice that much during the same period of time, and we never would have found ourselves in this fix.

Now, why shouldn't we direct all the revenue that can be raised from energy to finding more energy from whatever source, be it shale, coal, atomic, anything else, solar, up until we have this problem licked, before we direct that money into other forms of tax relief in other areas?

Secretary SIMON. Here again, with the declining economy that we presently have, if we took that amount of money out of the economy, $30 billion, and just devoted the entire amount or whatever portion you wish to devote to further energy resources, it would have a significant economic impact and for that reason it was designed to be neutral to return as nearly as we could to all categories of users, recognizing they are going to pay a higher price, so it would be neutral.

We are spending $10 billion over the next 5 years for research and development, which is aimed to do just as you say. The current price of oil is giving tremendous incentive for increased exploration, all over the United States; indeed, all over the world. That is adequate incentive at the present.

Mr. CHAIRMAN. Here is my second major problem.

President Nixon was talking about Project Independence with a target date of 1980. Now you are talking about 1985.

You have been around here with both of these Presidents. Why can't we get this job done by 1980 or by the end of 1980?

Secretary SIMON. In designing a program to attempt to accomplish in that short period of time everything that has to be accomplished, to do this, it would put too severe strains on labor and resources in this United States in that short a period of time.

Mr. CHAIRMAN. Well, I hope we can discuss that and talk about it in the future, because with all the people we have out of work in this country right now, it seems to me that would be a good area for employment. I am not just talking about energy, but some of the things you are recommending. For example, weather proofing more homes—why don't we get that done in 2 years rather than 10 or opening up these new mines—just an off-hand calculation, this will involve about $7 billion. Why can't we do that in 2 years rather that 10? Can't we open those two mines up in 2 years?

Mr. ZARB. First of all, the use of coal is not supply limited for the most part. It is demand limited, which means, we can't right now burn coal in many areas that perhaps burn it. Some of that is related to environmental laws on the books. Some of that we are asking for relief with Clean Air Act amendments.

Second, there are places where we can open those mines and get the coal up on the ground, and we can't put it anywhere, because we haven't developed transportation systems and we have let the railroads decline.

There is a lot of work to be done to create the demand for coal, provide the ability to mine it, and transport it, and get it to where it can be burned.

We tried to be somewhat conservative but also honest in what we can accomplish. We can't put a nuclear plant up short of 8 to 10 years in this Nation because of the procedures that are now designed and developed. Some of them are absolutely essential, some can perhaps be streamlined.

But the fact is, it takes many, many years to bring these things on line and get them developed.

Mr. CHAIRMAN. My time is up. I just want to make this statement. It seems to me this is just a matter of urgency and priority. It depends upon what degree of urgency and what degree of priority. Frankly, I think we ought to look at it as a far more important matter and try to get it done a great deal sooner than that.

Senator Mondale.

Senator MONDALE. Thank you, Mr. Chairman.

I was interested in the chairman's suggestion that we compromise and come up with an economic measure to serve all America, and I agree with that.

It seems to me, however, the key point in compromise is whether the administration is willing to negotiate over its foreign import fee, the $2 tax, and whether it is willing to give some on the abruptness of its 1 and then 2 million barrel figures.

Let me quote what Arthur Burns says to show this is not a partisan matter. The other day Arthur Burns said, "I find the President's energy proposals extremely complicated and some parts of it are extremely hazardous at times like these." Then we went on to say that, "any reduction in imports of oil must be phased in, not concentrated as the President suggested."

In other words, it seems to me there is a rising number of prominent economists and officials, including Mr. Sawhill, formerly with your administration, who are saying the identical thing—that, while there is nothing wrong with the long-terms targets, it is the abruptness and the shock of the tax which creates the problem.

Now, in the spirit of the chairman's suggestion, is the administration willing to sit down and open up again the question of that tariff and of those immediate reductions in imports, or is that not a part of the matters to be negotiated?

Secretary SIMON. Well, the chairman, Senator Mondale, also said we ought to be acting quicker in all these things and move ahead, and that, of course, means move ahead on both fronts, demand restraints and also the supply side.

As far as our attitude, I can assure you we will be delighted to discuss and cooperate with any alternative proposals.

It sort of reminds me of our business, a bid and ask. We have our bid out but we don't have an ask. I don't know what compromise is in.

Senator MONDALE. In other words, you are willing to negotiate and open the question of the 1 and 2 million barrel import reduction goals, and you are willing to open up the question of the tariff which the President has unilaterally proposed?

Secretary SIMON. Of course, the very purpose of these hearings is a constant opening of this proposal and in the absence of you passing, I have to convince you, here are the reasons why we continue to do it. We believe the economic impact is minimal for 2 million barrels a day, realizing there will be other economists who will reach another conclusion.

Senator MONDALE. All right. Going past the question of what Arthur Burns sees as the extremely dangerous implications of your proposals—a view shared by Mr. Sawhill—let's go to the question of whether it is going to work. Your program assumes that once it is adopted your objective of reducing imports by 1 million barrels, this, and by 2 million barrels by the end of 1977, will be accomplished. What is the basis for that assumption?

Secretary SIMON. It is a combination of what we are doing as far as coal switching and supply problems, it is removing supply constraints and also the simple demand elasticity that is attached to increase in price, Senator.

Senator MONDALE. What do you say figures will be in the reduction of imports next year as the result of those policies?

Secretary SIMON. At the end of this year, the assumption, and I want Frank to correct me if something is wrong—we go from 69 to 59.

Senator MONDALE. Mr. Zarb, are you convinced your figures are solid, and if you are given what you ask we will reach those targets?

Mr. ZARB. Well, there isn't anything I would say without any doubt, Senator.

Senator MONDALE. Do you think it is probable?

Mr. ZARB. I think it is more than probable. I think it is very likely. Let me point out the three areas which we get our main barrels. We will achieve about 260,000 barrels by virtue of Elk Hills and with natural gas decontrol, an additional withdrawal of natural gas shortage, and the remainder based upon demand constraint.

We believe that we will achieve those goals. The only analytical challenge to that number thus far has come from the Wall Street Journal using their models, we only get to 800,000 barrels.

The President has said, let's assume we only fall short 800,000 barrels, we would use his authority with a kind of minor allocation system as opposed to a full allocation system to make sure the job got done.

Senator MONDALE. Are you sure you will meet the 2 million barrel goal by 1977?

Mr. ZARB. Yes. We are quite sure. We have a paper that FEA has available that demonstrates the exact elasticity factors in all the analytical work that brought us to that number.

Senator MONDALE. The second part, since we are trying to reduce the out-flow of American dollars affecting the balance of payments, is whether we have any guarantee that the Arabs would not simply raise their prices. This is the point Mr. Sawhill made and I quote "Finally, there is no guarantee the proposal would not work, that Arabs would simply view this as an invitation to hike their prices and a nation faced with an increase across the board would not find itself a year from now sending more dollars to the Middle East."

Secretary SIMON. We disagree with that, Senator Mondale. Number one, OPEC doesn't need an excuse to raise the price. They have already riased it without any economic justification. It bears no rationale as far as the cost of production or alternate sources of energy, which, of course, is what the ultimate price of oil will be.

Number two, OPEC has already agreed that the prices will be frozen until I believe September of this year at their recent meeting and the statements by Sayed Marei are consistent with what he has been saying for some months now.

Senator MONDALE. You are not using him as a support, Sheik Yamani?

Secretary SIMON. I am talking about his comments over the weekend.

Senator MONDALE. Did not he once say prices were going down?

Secretary SIMON. He said two things as reported by the paper or by radio. He did not tell me directly, although he has said in my presence that he would hate to see oil ever used again as a political weapon and the price of oil should be lower. That is a reduction of the price at 10 million barrels a day and further conservation on the consuming nations will put further pressure on these countries to decide who shares and how they share further production cuts when the internal demand for funds, as you said Senator Mondale, is greater than any anticipated.

Senator MONDALE. I come from the upper Midwest where we have several so-called Canadian-dependent refineries. They have no other alternative source of crude oil. They are not partly dependent on Canadian oil, they are completely dependent.

Under the President's proposals we will be taxing the importation of Canadian oil on the theory that, I guess, its importation threatens the national security. This will add, we estimate, between $100 and $200 million to the cost of living in Minnesota alone next year. Would not it make sense to be more selective in this tariff if we are going to have it, and discourage the importation of oil from countries that have proven to be unreliable sources of energy? Why slap that $3 tariff on a source of energy that is totally reliable, that is essential for a crucial area of the country, and which provides oil for which we have much need? Would it not make sense not to apply that to the Canadians?

Secretary SIMON. What we are doing, the price equalization, the entitlements program will make sure a disproportional burden is not born by the Midwest or any other portion in this country. We are trying to have a one-price system in the United States. Canada has already announced that some time in the early 1980's they intend to use all of their domestic production. They are building the Montreal Zarnia pipeline—so they won't have to rely on insecure foreign oil prices. So that again gives us an the upward tier of the United States additional reason why we have to get going on alternative sources so we can provide the Midwest with the energy they require when Canada is no longer a supplier, period.

Senator MONDALE. Mr. Secretary, it is not that simple. We have some profound issues of natural gas and the rest under negotiations. It seems to me that this tariff is sort of our way of saying we do not need your oil.

Mr. ZARB. Senator, may I just add two parts to the answer.

First, we keep talking about 2 million barrels in a year. The President's program calls for a saving of 2 million barrels, at the rate of 2 million by the end of 1977, which brings it out to 3 years.

Secondly, with respect to the Arab reaction, or the OPEC reaction, while we don't believe that that reaction would occur, it is not unusual that we worry about the technique or strategy which the United States might have within one of its domestic policies because we are concerned with the reaction with a set of other nations, and that is the predicament we are trying to substract ourselves from.

With respect to the northern tier, and we have talked about that before, we will do everything in our power, and I think we can minimize that situation both short term and long term.

Senator PACKWOOD. I have no further questions.

Senator CURTIS. Bob.

Senator DOLE. No.

Senator CURTIS. Just briefly, what was the date of the imposition of the embargo by the OPEC countries.

Secretary SIMON. That is in October 1973, Senator Curtis.

Senator CURTIS. Now, did the administration recommend a windfall profits tax, had it been enacted by Congress, would have been effective at least in part in calendar year 1974?

Secretary SIMON. Yes, in September 1973 we submitted a windfall profits tax.

Senator CURTIS. How much revenue would that have produced.

Secretary SIMON. Would have to get that number and supply it for the record, Senator Curtis. It would have been a significant amount.

Senator CURTIS. If you will supply the figure, please.

Secretary SIMON. I certainly will, sir.*

Senator CURTIS. It seems to me that part of our solution is going to be in the area of substitution of fuels, because fuels mean energy and it takes energy to have full employment and expanding industries. I am not for conserving energy beyond preventing ways.

Is coal a more economical source of fuel for production of electrical energy than petroleum.

Secretary SIMON. It most certainly is, and that is part of our program, not only the amendments to the clean air account, but switching to coal utilities for those who can do it.

*The material referred to had not been received at presstime, Feb. 17, 1975.

Senator CURTIS. Is there any figure or percentage that would indicate the relative cost between petroleum and coal.

Secretary SIMON. $7 a barrel if my memory serves me correct, is equivalent to $30 a ton coal. Your long term contracts are around $12 to $13, in that general area. It is 16. So as you can see, it is significantly cheaper.

Mr. ZARB. Just the sheer amount of supply that we have, Senator, if it can be made and transported, would have a significant effect on the long term price with respect to utilities. Both coal and nuclear can develop energy more cheaply than oil can.

Senator CURTIS. Well, conversion to coal is quicker, is it not.

Mr. ZARB. It is quicker than building a nuclear plant, yes.

Secretary SIMON. We achieved a good deal of this during the embargo, about 5,000 barrels a day, but as soon as the embargo ended people preferred to go back to oil again.

Mr. CURTIS. During those days of embargo, I had some figures submitted to me, one great city like Chicago, if it used no petroleum to generate electricity would have released enough petroleum production to run all the trains and more, and that was at a time when trucking and train transportation was being curtailed because of fuel.

Do you concur in this thought: that our problem would not be solved even if there were to be a drastic reduction in the price of oil immediately from the OPEC countries—I recall attention to the fact that that could change over night. But even though we might have arrangements, and agreements by responsible individuals, governments can change over night, and that until we tackle the problem of less dependency on foreign production, expanded production at home plus substitution of other fuels, that both our economy and our national defense could be subject to immediate danger any time; is that correct?

Secretary SIMON. I agree with that. That is the only answer, Senator Curtis.

Senator CURTIS. What portions of our domestic production of oil comes from stripper wells or low producing wells.

Secretary SIMON. About 13 percent, Senator Curtis. That is my recognition.

Senator CURTIS. A 13-percent shortage in any commodity creates havoc, does it not.

Secretary SIMON. Yes.

Senator CURTIS. Nebraska is not, by any means, an important oil producing State.

But we have about three or four counties in Nebraska that produce some oil. It is not a high producing area. It is a small amount of oil. It is true that drilling is not nearly as expensive as elsewhere. Back in the days when we were running our economy geared to the low price oil coming from the Middle East a good many of those wells shut down entirely, and when the various forces caused the price of oil to go up in this country, just in a matter of weeks there were a hundred of those wells in use.

Do you regard the overall petroleum policy that we should adopt should include something to assure that the oil that is available in these stripper wells and other low producers should be recovered?

Secretary SIMON. Yes, I do, Senator Curtis. I bring up a good point, and I wholeheartedly endorsed the exemption of the strippers from price controls, recognizing the costs of an awful lot more to produce six, seven, eight barrels a day, or one or two even to the larger producer wells. You cannot only take Nebraska, but in any State. I believe they have 5,400 oil wells in New York State, and I believe effectively all of them are stripper wells. If we role back the price or do lots of other things you are going to effectively force those to shut down again just as they did in earlier times.

Senator CURTIS. I dislike doing anything or seeing anything happen that raises the cost of any commodity to any household or any user. But on the other hand, I do not think that we can restrict an expanding petroleum program in an effort to solve all the problems of our general inflation by adopting an unsounded and economic petroleum policy.

Now, I yield.

Mr. CHAIRMAN. Mr. Haskell.

Senator HASKELL. Thank you, Mr. Chairman.

I guess we have gotten pretty far afield from the 90-day delay bill, but since we have, one of the aspects that I would like to hear a little more about is the matter of rebates. I gather that part of the administration program is to rebate to people who pay more for petroleum products a portion of the increased costs; I am correct in that assumption?

Secretary SIMON. Yes.

Senator HASKELL. How is that going to work? Let me be very parochial. I lived 10 miles from my law office in Denver. There are people at the Climax Mine in Leadville who commute 60 miles a day. Now, how are we going to work out equitable rebates.

Secretary SIMON. First of all, nothing. And it is not related directly to that. When you take a look at roughly what each class of the economy, business, industrial, local Governments as well as the Federal Government, individuals, and attempt to do that and weigh it, and it was weighed on the low- and middle-class, as you can see by the tables, which I will also put into the record, where these people were actually in the aggregate overcompensated for the additional price of oil. The people at the upper end of the scale and the people that you say, the miners, or what you people must drive to work a longer distance than people who live in New York, there is really no way to be that precise, Senator.

Senator HASKELL. I see. Then there would be no way, for example, under your system, to take care of the speeial needs of universities and the like on residual oil costs.

Secretary SIMON. No, that could be on an exemption basis that could be taken care of.

Mr. ZARB. I will add two things. First, in all the programs we looked at there were inequity potentials of significant magnitude.

The one program which had the maximum ability to deal with those was one that did correct these revenues and give the Government an opportunity to redirect those in ways to provide the treasury with an opportunity to restructure the tax tables so that middle- and lower-income people could get a correction for distortions which inflation have created in the tax tables.

So our intent was to deliver more back to middle- and lower-income people in our Nation than people in the higher brackets so that they would get more back than their increases in energy could conceivably be.

Now, any program, allocating, rationing, all gave us the same subset of potential equities. This one program, because of its revenue return devise, gave us a better handle on redressing them.

Senator HASKELL. I see your method.

Just one more question. I think, Mr. Zarb, in answer to Senator Nelson's question as to why your program will reduce imports—really, I wonder whether it will—you say imports will be backed out and domestic oil will be used. I don't know what the transportation profit might be on not having to bring oil from the Middle East. For all I know, if I were running an oil company I might find that even with an increase of $3 a barrel it is still more profitable to buy oil from the Mideast. I don't know.

Mr. ZARB. The Secretary reminds me that economics are working in our favor, and we believe it will occur that way.

But I answered this question last week when it was raised and the possibility we would be backing out domestic production rather than imports, and if that is all that stood in our way to coming to an agreement, then we could find various legal forces—we could find a way to prohibit that from occurring, and would.

Senator HASKELL. Thank you very much.

Secretary SIMON. The oil companies' profits, as far as that goes, have been reduced drastically because their oil has been nationalized and taken over and a relatively low cost per barrel, I believe 30 cents.

Senator HASKELL. My question, Mr. Secretary, is this: If I were an international integrated oil company, what percentage of my profits would be from transportation, what percentage from offshore or foreign subsidiary companies? Do we really know that this program is going to back out imported oil or will it back out domestic oil, given the unknown profit structure of the major corporations?

Secretary SIMON. We believe that having studied it that yes, it will back out the more extensive imports versus domestic production when you take into consideration the transportation and the other insecure supplies.

Senator HASKELL. Do you have figures you can submit for the record?

Secretary SIMON. Yes; we will submit that for the record; yes.[1]

Senator HASKELL. Thank you very much.

The CHAIRMAN. Senator Dole.

Senator DOLE. Just two questions.

Senator Curtis was asking about the stripper wells, and in our State about 95 percent of all our wells are stripper wells, and about 60 percent of the State's oil production comes from stripper wells. There are about 42,000 oil wells in Kansas which produced about 66 billion barrels of oil in 1973. There has been increased exploration activity, which reverses a decline in drilling activity over the past several years. The number of active rotary rigs increased from 25 to 48 during the past 2 years. So there is this incentive that is working.

[1] The material referred to had not been received at presstime, Feb. 17, 1975.

One fear we have, not in the first step, but down the line with the excise tax and the windfall profit tax, is that prices received on oil from stripper wells are going to drop almost in half. Is there any likelihood some special provisions may be made for wells that produce less than 10 barrels a day? They produce a total of over 1 million barrels a day across the country.

Mr. ZARB. Senator, the small independent producers have made what appears to be a compelling case for the problems which might be created at the lower end of the producing spectrum. We have asked that hearings will be held to that specific subject in both Houses so that producers could lay on the table their particular cash flow problems.

From the energy standpoint, we will support a balanced program while getting maximum oil development in the years ahead, because in our view we desperately need it.

Senator DOLE. I know the effort is being made, because there has been a decline in other States——

Secretary SIMON. It leveled off last month. You cannot go on a 1-month basis——

Senator DOLE. But when consumption was going up our production was declining.

The hearing was called for the 90-day tariff suspension bill and I would like to touch on that briefly.

The Kennedy-Jackson proposal was introduced on January 23, and it has already been 17 of 18 days. Assuming it is passed out of this committee, and it should be passed out, and debated at some length on the Senate floor, and I am not certain what the strategy will develop, but finally passed and sent to the President and vetoed and sent back for action by the Congress, it seems to me we will have used up most of that 90-day period in any event. It just seems to me, and certainly it is a concern expressed by the chairman, that rather than become involved in a partisan confrontation that there is probably some very valuable time right now that could be used.

But in the event the efforts to take away this authority from the President for 90 days succeed, how much will that cost the Government? We are collecting this tax. Does it have to be rebated?

Secretary SIMON. Yes, it would. We would have to go ahead and rebate the tax for everything that has been selected.

Senator DOLE. So there is some expense involved?

Secretary SIMON. Yes.

Senator DOLE. And a great deal of work involved?

Secretary SIMON. Yes.

Senator DOLE. And then if nothing happens from the date of enactment, that of course would extend that 90 days; but if nothing happens in the interim, if they cannot come up with a plan—and I do not believe they can—then I assume the President could proceed under the authority he has now under the Trade Act. Is that correct?

Secretary SIMON. I would agree with that unless Congress decided——

Senator DOLE. There has been a great deal of emphasis about a $3 tax. It may never reach $3 if Congress acts as Congress should act, expeditiously. Three dollars would be the high point. I think by count we are in our 523d day of doing nothing in the Congress, and if we continue on that road I can understand there could be some problems.

I say even though there is rather sharp disagreement in my State as to the President's plan, at least he has one, and I think the others have an ambition and the President has a plan. I would hope that Congress in its wisdom would either come up with something or permit the President to proceed, although it may need to be changed through compromises, and certainly most everyone is willing to compromise, including the President.

Mr. ZARB. Senator, we have every inclination to work with whatever vehicle the Congress may put forward to analyze what the President has looked at before coming to his decisions. We are prepared to go over with any group or staff group that you may put forward to look at our work, why we value this program more than we did an allocation or rationing system, why we think we must make progress now and what kind of timetable we see before us. We are certainly more than willing to work in this period with any congressional group who would like to sit down and review the President's program or answer questions or accept suggestions.

Senator DOLE. It appears to me there are alternatives, but they are not painless. Rationing is good to talk of as a balanced program, but it just appears to me that some people may say they like it in a poll because they have not had it. Everybody understands what a tax is and when you mention import taxes, people are generally opposed to taxes. Rationing, since we have not had it for quite a while, might appeal to a great many people, but I think many who talk about it really don't want it.

The CHAIRMAN. Senator Nelson.

Senator NELSON. Well, I would like to observe about Senator Dole's comments—was the 535 days——

Senator DOLE. I did not count the Lincoln recess.

Senator NELSON. 535 days of doing nothing. You know, one of the problems has been the quarterback, he has been calling signals for the team and gets the team running in all directions. It was only 2 months ago that the President was denouncing the Congress for not adopting his surtax. Now he is criticizing Congress for not reducing taxes. Six weeks ago he vetoed the bill to ship oil on American bottoms, on the grounds it would be highly inflationary because it would cost 12 cents a barrel, and now he is asking to place a $2 fee on imported oil. So let us not get mixed up about who is delaying.

Senator DOLE. He never was a quarterback.

Senator NELSON. We do not know what quarterback we have——

Senator CURTIS. In the interest of trying to work something out, who is quarterback in the Congress?

Senator NELSON. Well, the quarterback was in the White House, then he left, then we got another quarterback and he has not got his game plan memorized yet.

Secretary SIMON. I am very encouraged, Senator, by this debate we are witnessing here in recognition of the President being the quarterback and calling the signals. He has set a rather comprehensive game plan up here to win this game plan and if the tackles and guards and lonely ends want to do something else, let us hear about it, but we have not seen anything yet.

The CHAIRMAN. Well, I want to referee this game. I want to insist that the question be directed toward the witnesses and that the witnesses respond to the questions rather than the Senators.

Senator NELSON. Well, I might have been mixed up, but Senator Dole was testifying.

The CHAIRMAN. I am not talking about how the ball got out of bounds, all I am trying to do is get it back in the playing field.

Senator NELSON. It would seem to me that it is a kind of an unfair demand to insist that the questions be relevant.

The CHAIRMAN. I did not insist on it.

Senator NELSON. I had one question that raises a fundamental issue. Maybe there is not any answer to it.

The concept of raising the price by an import fee, and decontrolling all old oil which would raise to the new price, as I understand it, a level based upon a market price concept with the objective to reduce consumption, to make other alternative sources feasible and to develop alternative sources of energy.

One of the things that puzzles me about it is that the market price is not a true market price, it is a cartel price, as you have said many times yourselves. It is not based upon the costs of production, transportation, reasonable return, et cetera. It is just a cartel, monopoly price.

Nevertheless, we accept that as the market price, then add $2 on top of an outrageous price with the objective in mind being to do as you have said, reduce consumption and develop alternative sources.

What makes you believe that it is necessary to go that high, in other words, to escalate the price over and above the cartel price, which is an outrageous price, in order to reduce consumption and in order to develop alternative sources, considering also that the greatest supply of energy available is coal, and it probably could be on the line at half the price?

Secretary SIMON. And that will be an important criteria when we are finally able to burn it in independent industries and utilities and utilize it, and that requires some change in the Clean Air Act, which is another portion of it.

But this increase in price and further reduction in demand worldwide, and believe me, Senator Nelson, we talked about a higher tax and we looked at the alternatives and how much we would save.

We want to reduce the price of oil, and the world price is too high. That is one of the purposes, but let us talk about reduction because we know the increased price will create great activity as far as bringing on additional supplies in 3, 4, and 5 years.

The OPEC nations have about 67 percent of the world's proven reserves. Saudi Arabia has 25 percent of all of the OPEC reserves. It is in their best interests to have an assured long-term market, again looking as Senator Mondale said before, about their internal ~~demand for~~ funds in their country, their desires for the—the social desires and dreams of their people, the industrialization and diversification to the ends they have an assured market to sell their oil at reasonable prices.

What a reasonable price is, one can make different definitions. The more pressure that can be put through in the short run through reducing our demand for this commodity is going to either have them cut back production to keep equilibrium or again to sell at what the market will pay for it, recognizing these additional markets are coming onstream. It is a deep belief that the market ultimately works on supply and demand. In the short run, fine, they have got us, because they have 67 percent of the world's proven reserves, but we can assist through reduction of demand at this point and the crash programs to bring on additional supply using the price mechanism where we have freedom in our market to do that and the oil price is going to come down. It is not a matter of whether, it is a matter of when. But we know the actions we can take to bring this price down.

Senator NELSON. One more question based upon a question that I think Senator Haskell raised. There are a number of serious problems that I know you are aware of, and in imposing this additional costs, and therefore you are attempting to work out as equitably a rebate program as you can. Senator Haskell raised the question about colleges and universities. I assume there are other nonprofit organizations who have similar problems, but specifically to that one, every university, public and private all over the country, almost all of them, are in serious financial difficulties, and there are heavy cutbacks in universities' budgets because of the erosion of the income base of the State governments, or in the private sector, the people's capacity to contribute.

I have been told that some of the universities are simply saying that the energy costs alone are just busting their budgets. I understand that one medical school out West is planning to close its doors, part of it due to this economic cost squeeze. I know a number of others who consider the energy squeeze a burden they cannot handle. They do not have the money.

Are you specifically going to address yourselves to alleviating that burden with the taxes that you raise?

Mr. ZARB. Senator, the President has directed us to look at individual sectors that are particularly hurt by this program. It is clear that the nonprofit institutions are one of those sectors and we have a task group now working on their particular problems in an effort to come up with recommendations on which the President can act, nonprofit institutions, the ones you have just described.

Keep in mind, please, that which ever program we looked at, we had a series of those affected which would be relatively more impacted than others, whether rationing or allocation, we always had a stackup of particular exceptions which we had to *x*, and in this particular case we are looking at a particular sector plus two or three others.

Senator NELSON. Thank you.

That is all I have.

The CHAIRMAN. Mr. Secretary, there is one additional point that troubles me somewhat, and this is perhaps a situation with regard to both this Nation as well as other producing nations. That is the failure of perhaps both sides to understand the other fellow's side of the argument. Now, the late Richard Newberger made a contribution in this city by pointing out that we should keep in mind that the other fellow might be right. These things are not so much a matter of black and white as a shade of gray that we are trying to choose. Of course, it offends me to think we would pay $10 a barrel for some oil that a fellow in Saudi Arabia might have produced for 10 cents. That offends me. I do not like that. It seems to be all together too much. Those people take the view that oil is worth a great deal more than that, and if they are ever going to have anything for their people they are going to have to get a lot more than 10 cents a barrel for it. They want to look at what it costs us to produce it here. That is what it costs you to produce it, that is what you will have to pay us.

You will have to negotiate with them. I do not know how you will come to terms, but it does concern me every time a country is able to produce enough energy so that it can export something that that country is then going to take the attitude that the price for which it will sell the product is the price that the fellow who does not have energy would have to pay to produce it. I do not know how that would solve the world's problem. But it seems to me we will have to find some meeting ground between the producing and consuming countries and we cannot do it on the basis of the assumption that we are right and they are wrong. How are we going to do that?

Secretary SIMON. The ultimate is to allow the market to set price, not curtailing products, allowing a price clearly lower in the absence of curtailment; to set it and to allow the market to set a price for this commodity we must find additional sources of energy and alternate sources of energy and bring them on stream all over the world. That is our response.

In the interim dialogs do go on, and they are going on now. We are going to have a producer-consumer conference. That does not mean we are not talking to these people constantly.

The CHAIRMAN. You are not going to advocate what people want to read in Secretary Kissinger's statement that we invade those countries to get the oil, are you?

Secretary SIMON. I have never suggested that.

The CHAIRMAN. I don't think the Secretary suggested that.

How do you propose to put pressure on those people or prevail upon them to sell oil at a more reasonable price?

Secretary SIMON. I want to say one thing and then Frank wants to add something.

I think the best argument you have in any discussion you are having where there is a difference of opinion, as I said a few minutes ago to Senator Nelson, to convince them it is in their longer term best interest for a lower price of oil and we sincerely believe that and they have been intrigued by our analysis of the situation, yes.

Mr. ZARB. Mr. Chairman, it would seem to get the other fellow's attention to demonstrate we as a nation had a plan we all enforced and subscribed to, to have us independent of an inordinate supply from their lands. If we can reach an agreement and have the U.S. Government policy that we can all subscribe to, it seems to me our negotiators would be more stronger sitting around the table than they presently are.

The CHAIRMAN. Any further questions on that subject, gentlemen?

I would take it that concludes our hearing with regard to the import question.

Now, with regard to the debt limit measure, I would suggest, Mr. Secretary, that you submit your statement and that Mr. Lynn submit his statement and you make any additional statement that you want to make on that subject.

Secretary SIMON. Well, even if I had all morning to do it, I had not intended to submit a 40-page testimony which I have, which I encourage you to read, because it not only deals with the arithmetics of the debt ceiling where the temporary limit is $495 billion and goes back to $400 billion on March 31. We bumped the ceiling on February 18, and I came up originally asking, which was consistent with the Budget Reform Act, that we get an extension through fiscal 1976 which moves it from $495 to $604 billion, a rather staggering figure. This would carry us through fiscal 1976.

Then I have tables and charts that traditionally come with debt ceiling requests, including some additional charts that we have not put out before. I ask you to look at some of these charts.[1] They deal with the Federal Government broken down by sector, Federal, State, and local percentage of the capital markets through the years, and then, because people thought that that didn't show the true story, I also had included in the total financial area, which includes mortgages, residential, farm, as well as short-term business loans—I always thought it was more appropriate to not compare apples and oranges and compare the market that we borrow in, but I have done both here. I think the numbers are quite significant of the total in the financial area, mortgages, residential and farm and consumer credit, short-term loans foreign, everything, the Federal Government percent of total is 44 percent.

Senator PACKWOOD. What is this in the back?

Secretary SIMON. This is with my testimony. There is about seven or eight charts there. This is table 6, the one that shows Government as a sector of security.

Then I raise some points that while I am not predicting anything, I am recognizing some clear dangers involved in financing and deficit financing of this size, the possible danger of extensive monetary expansion to accommodate this as well as other private demands when the economy begins to pick up again, the disadvantaged, the illiquidity of nonfinancial corporations in our economy today as a result of declining profits over a prolonged period of time, and of course the extraordinary inflation that we have had for a period of time.

But that is a very capsuled summary written testimony, Mr. Chairman, and I guess Jim would like to say something and then we would be delighted to answer any of your questions, but I would urge you to read some of the fears that I express in here and that is what they are, they are just fears, not predictions, and they are based on my experience in the banking business as well as what I have seen occur in Government, only right now with much bigger numbers for a longer period of time.

[The prepared statement of Secretary Simon relative to H.R. 2634, follows. Oral testimony continues on p. 156.]

[1] See page 150ff.

STATEMENT OF HON. WILLIAM E. SIMON, SECRETARY OF THE TREASURY

Mr. Chairman and members of the committee: In the second portion of my testimony today, I would like to discuss with you another subject of immediate concern: the need to raise the Federal debt ceiling.

As you know, the current limit on the Federal debt is $495 billion. That is a temporary limit which will expire on March 31; in the absence of legislation, the limit will revert on April 1 to $400.

Our current estimates show that the Government will exceed the temporary limit of $495 billion on February 18—less than 10 days from now. Thus, there is a genuine need for immediate action on the part of the Congress.

Just over two weeks ago I presented to the House Ways and Means Committee the Administration's proposal to raise the debt ceiling to $604 billion. Barring unforeseen developments, that new ceiling should be adequate to carry us through June 30, 1976, which would be the end of fiscal year 1976. I also pointed out that if the ceiling were extended only to the end of fiscal year 1975, it would have to be set no lower than $531 billion. Our estimates are based on the conventional assumption of a $6 billion cash balance and a $3 billion margin for contingencies.

The House last week approved a bill authorizing a temporary debt limit of $531 billion through the end of the current fiscal year, at which time the limit would revert to the permanent ceiling of $400 billion.

Our request for a higher figure carrying us through fiscal year 1976 was consistent with legislation passed by the Congress last year, the Congressional Budget and Impoundment Control Act. In that law, the Congress set up a timetable for spending and revenue decisions. When that timetable takes effect, the Congress by May 15 of each year is to have completed action on the first concurrent resolution providing new budget authority, setting revenue figures and establishing the public debt limit for the fiscal year beginning that October 1. A second concurrent resolution and reconciliation bill, if needed, must be enacted by late September. Thus, prior to the new fiscal year, the debt limit will be set for that entire fiscal year. This is essentially the idea that we are asking the Congress to approve for fiscal year 1976, and we strongly urge your support for this proposal.

For your background, I am submitting to the committee today four tables which usually accompany our discussion of the debt ceiling:

Table 1 shows actual operating balances and the debt which is subject to limit through December 31, 1974. It also shows the estimated debt subject to limit at the end of each month through the end of fiscal year 1975.

Table 2 extends these estimates through fiscal year 1976.

Table 3 shows the budget estimates for fiscal years 1975 and 1976, providing you with the basis for the figures in the earlier tables.

Table 4 presents our tentative revenue estimates for fiscal years 1975 and 1976.

As all of you know, the rapid downward slide of the economy has reduced the Federal revenues below our original expectations in January of 1974. As a result, Federal deficits are mounting rapidly and are causing the current squeeze on the debt ceiling. A slowdown in the economy had been anticipated, but the current recession is steeper and will probably last longer than first expected.

We have thus been required to reduce our fiscal year 1975 estimates of individual income taxes by $6.7 billion, reflecting higher unemployment, shorter work-weeks, less overtime, and fewer second jobs. We have also reduced our estimates of corporate income taxes by $3.7 billion, due in large measure to the decline in corporate profits.

Most of you are aware that a number of corporations are switching their inventory accounting methods from "first in, first out" to "last in, first out." LIFO accounting methods exclude a large portion of the effect of inventory price increases from the calculation of business profits and thus lessen corporate tax liability. This trend toward LIFO accounting methods in fiscal year 1975 is expected to reduce our total revenues by $3–4 billion. I should point out that in first estimating revenues for fiscal year 1975, we anticipated reductions in revenue of approximately this size from companies switching to LIFO, so that it has not been a factor in changing our predictions.

The changes in forecasts that we are making this year are similar in nature to those that were made in past recessions. In the recessions of 1969–1970 and 1960–61, corporate and individual income tax collections fell well below estimates. On one of those occasions, fiscal year 1962, an increase in the debt ceiling was also needed prior to the expiration of the one then in effect.

The new debt ceiling we are requesting today incorporates our tentative estimates for both Federal revenues and expenditures, based upon our projections for the economy over the next 17 months and upon the economic and energy proposals that the President has presented to the Congress. As I noted earlier, it also includes the traditional $6 billion cash operating balance and the $3 billion margin for contingencies. It does not take account of new spending programs which might be enacted.

Let me point out that the debt figures also include Treasury borrowing to finance the Federal Financing Bank. The Bank has one marketable issue fo $1.5 billion now outstanding and maturing at the end of March. In the future, I believe that the Bank should borrow from the Treasury rather than going into the market. The Bank's cost of borrowing is somewhat greater than Treasury's, and the additional interest costs which result are inappropriate. Moreover, we can already anticipate that large budget deficits projected for fiscal years 1975 and 1976 will put some upward pressure on interest rates. Federal Financing Bank market borrowing would be likely to put somewhat more pressure on rates than the equivalent Treasury borrowing. In order to minimize costs to the Government and the taxpayers, it would thus be prudent for the Bank to borrow from the Treasury.

Some Members of the Committee may think that the new debt ceiling is too high and the deficits too big. I would emphasize that there is no one in Washington today who feels more strongly than either the President or I that deficits of the magnitude we are now facing are horrendous. We believe that many of the economic troubles we have today are rooted in more than a decade of excesses in fiscal and monetary policy. To continue the rapid upward momentum of Government growth over an indefinite period would erode the very foundations of our economy and could threaten us with social ruin. But we also recognize that because of the recession, receipts are inevitably going to be lower than we would like and we believe that in order to stimulate the economy, we must temporarily—and I stress the word temporarily—cut taxes and leave more money in the private spending stream. Big Federal deficits in fiscal years 1975 and 1976 are thus a result of both the recession and the cumulative cost of the many Federal spending programs that have been enacted in recent years.

Other Members of this Committee may feel that to the contrary, Federal outlays should be increased significantly this year so that the deficits and, therefore, the debt ceiling should be much higher than we propose. The President strenuously opposes this view. If we open up the sluice gates on Federal spending during the coming year, we could seriously overheat the economy and insure that further down the road we will be riding the tiger of inflation once again—and inflation then would be even more virulent and powerful than what we have had over the past year. That is why the President has proposed a moratorium on all new spending programs outside of the energy field and why he intends to veto bills which violate that moratorium.

IMPACT OF DEFICITS ON THE CREDIT MARKETS

A second reason why the Administration wants to hold the line on massive new spending programs is in order to preserve the private credit markets.

There is a considerable dispute among economists and market specialists on this question. My own view is that the deficits anticipated by the President's program will cause some strains in the markets, but those strains could be manageable. However, in the event that the Congress is unwilling to accept the strong discipline the President is trying to impose upon the Federal spending, the higher deficits that will result will certainly threaten the private credit markets with intolerable burdens. We could quickly clog up those markets and create genuine havoc in the Nation's financial system.

The anticipated deficits already exceed the upper limit of demands that the Government should place on the financial markets. Normally, financial conditions ease substantially in a recession, and normally they remain easy for sometime after the recovery gets underway. This slackening occurs because private demands for credit fall off at the same time that the Federal Reserve moves to maintain or increase the rate of growth in money and credit. We have seen some evidence of this easing in recent declines in business loans and in the Federal Reserve discount rate. Under such conditions, interest rates decline and credit becomes more readily available—all of which is part of the process by which the economy pulls out of a recession and regains the road to prosperity.

A decline in interest rates, in both the short-term and long-term markets, has in fact been underway for several months. There are reasons to question, however, whether the decline in interest rates will continue.

In the first place, current pressures on the financial markets from private business are heavier than normal for a recession. The borrowing needs of only a few sectors have moderated, and the financing of oil consumption both were and abroad as well as the external financing needs of business have remained extraordinarily large. As businessmen will readily confirm, the inflationary forces of recent years have helped to produce a marked decline in profits and have seriously eroded the liquidity base of both households and businesses. As a result, huge amounts of credit are needed in the private sector just to sustain existing levels of economic activity. Moreover, with the stock market so low that many issues are selling well below book value, new equity financing is not a feasible source of funds. Therefore, the demand from the private sector for new long-term debt issues is unusually high—unusual at least for this stage of the business cycle.

The Members of this Committee have probably read that borrowing demands are declining in the private sector and therefore, according to some analysts, Federal borrowing should not present a problem in the credit markets. Private short-term credit demands are indeed declining, but the point is that they are not declining as much as we would expect in a normal recession, and corporate bond issues are running at levels considerably above the totals of any other previous year. Our latest projections show that net new corporate bond issues, which rose from $12½ billion in 1973 to $25 billion in 1974, will advance even further to some $30 billion or more in 1975. In addition, while some slowing in business demand for short-term credit is underway, total short-term credit for 1975 is still expected to be one of the highest yearly totals on record.

A second reason why interest rates may not continue their decline lies in the borrowing needs of the Federal Government. Under proposed programs, we estimate that the Treasury during this calendar year will be coming into the capital markets for almost $70 billion of net new financing, of which $65 billion will be marketable securities (Table 5). Federally sponsored agencies may account for another $14 billion in borrowing. Total borrowing of net new money attributable to the Federal Government will thus come to an enormous sum—more net new funds, in fact, than have ever been borrowed before by both the private and public sectors combined.

I have frequently attempted to provide some perspective on the enormity of the Government's financing requirements, and I have pointed out that borrowing for all federal programs has ranged between half to two-thirds of the total amount of funds borrowed by all issuers of securities in the U.S. capital markets in recent years.

In the attached Table 6 we have charted the level of Government borrowing in the debt capital markets over a period of more than two decades. This table clearly illustrates the progressive domination of the private capital markets by the Federal Government. In fiscal years 1955–59, the Federal Government accounted for 20 percent of net funds in the capital markets; in fiscal years 1970–74, the Federal share grew to 45 percent. In fiscal year 1976, we anticipate that even with the moratorium on new spending and other spending control measures proposed by the President, total Federal borrowing will account for 68 percent of the capital markets, and if we add to that amount the anticipated borrowing by State and local governments, total government borrowing during the coming fiscal year will be 80 percent of the capital markets. Only 20 percent will be left to private industry in a financial market that has always been the centerpiece of our free enterprise system.

Some observers have suggested that those figures are misleading because they do not take into account the full range of borrowing in our financial markets. For instance, they do not encompass the mortgage market. My staff has recently been working to develop measurements of the entire financial markets. This project poses many difficult analytical and data collection problems, but we have developed preliminary data for current years, and in the near future we hope to have a more comprehensive presentation which will show these borrowing activities for earlier years. The preliminary data is included in Tables 7A, 7B, and 7C. These tables measure the levels of borrowing in all of our financial markets for fiscal years 1972 through 1976 and show the impacts of Federal and Federally-assisted borrowings on each major sector within these markets. Included here are the markets for debt securities, mortgages, securities, business loans, and consumer credit.

These are remarkable tables, and I would urge that at your leisure each of you spend a few moments examining them. The tables show that the estimated Federal share of funds raised in all sectors of the economy increased from less than one-fourth in fiscal year 1974 to almost one-half in fiscal years 1975 and 1976. The growing domination of the Government in our credit markets represents an alarming situation, reflecting the even more alarming growth of Government in this country.

It is startling enough to realize that we reached the point in recent years where the Federal Government's stamp was on 1 out of every 4 dollars of credit flowing in this country. But we are now entering a period in which 1 out of every 2 credit dollars must be blessed by Washington.

There are several ways in which the strains created in the private capital markets by Federal borrowing could be eased this year. For instance, the deficits could be financed without difficulty and interest rates could decline even further if the recession becomes deeper than we expect, if inflation subsides more than we anticipate, if the OPEC nations put a larger amount of their accumulated funds into investments in this country, or if the American people save more and spend less of their rebate.

Some financial analysts expect such developments even with a set of economic projections similar to our own. We cannot, however, be sure that any one of these events will occur so that it would be foolish to base our policy decision upon such assumptions.

Moreover, we must be aware of what might happen if the Federal Government does begin to elbow other borrowers out of the market:

Housing, for example, is always at the end of the line in the credit markets and thus the first sector to be crowded out. We now expect that a recovery in housing starts will get underway by mid-year, but we cannot overlook the continuing danger that excessive Government borrowing, coupled with a high demand coming from a private sector that is suffering from illiquidity, could drive up interest rates and seriously disrupt this recovery or even abort it at an early stage.

Business firms of marginal financial strength, especially small businesses, would also be cut off from the supply of credit if the Federal Government completely dominates the capital markets. This would further weaken the creditworthiness of such firms. Lenders would then intensify their preference for high quality debt issues, and marginal firms would be unable to obtain enough credit. Their ability to expand would therefore be limited and bankruptcies could result.

Let me stress that I am not predicting these events. I am only suggesting the scenarios that could unfold if we ignore the President's call for fiscal discipline and increase Federal deficits beyond their projected levels. It is too early to tell precisely what will happen this year in the credit markets, but we do know that Government will pre-empt most of this market and we must constantly be alert to the possibility that unrestrained Government borrowing could drive the economy into an even worse mess than it is today.

Some observers suggest that it would be easy to avoid these difficulties—at least for now—if the Federal Reserve were to adopt more aggressively easy monetary policies. In other words, to prevent the Federal Government's demands from crowding others out of the market, the Federal Reserve would make the market larger by increasing the total supply of money and credit. This approach, however, is a sure formula for still higher inflation rates when the recovery gets into full swing—if not sooner. It does not solve our problems, it only postpones them, and when they recur they could be much worse than they are today. By now, like the man who gives up drinking because he can't stand the hangovers, we should have learned that short-term binges with easy money and excessive spending are no substitute for the long-term virtues of savings, investment and moderation in our monetary and fiscal policies.

This dilemma, I would hope, emphasizes for all of the Members of this Committee the fundamental importance of a tough policy to restrain the growth of budget outlays by reducing less urgent programs and postponing new initiatives that are not included in the President's package of economic and energy policies. We already have enough problems on our hands—many of them created by irresponsible Government policies over the past decades—so that we should be sensible enough to avoid the shoals of even more serious troubles.

Let me review for a moment the staggering size of the deficits that are already contemplated. Under the budget program submitted by the President the deficit estimated for fiscal year 1975 is close to $35 billion and in fiscal year 1976 the estimated deficit is the biggest in peace time history—almost $52 billion. That's a total of approximately $87 billion over two fiscal years, an amount that hardly anyone can welcome gladly. But I would remind you that even these deficits are significantly below what will happen without the cap that the President is seeking to impose on Federal expenditures. Six billion dollars will be saved by limiting Federal pay increases to five per cent through the end of fiscal year 1976 and by placing a similar limit on those Federal benefit programs like social security, that increase automatically with the cost of living. In addition, we can realize savings of $14 billion through the budget reductions requested or planned by the Administration for fiscal years 1975 and 1976. Thus, overall the President's proposed actions would save $20 billion in expenditures. If the Congress ignores this call and overrides the President without making savings in other areas, the additional $20 billion in deficits would make the combined deficit figure for fiscal years 1975 and 1976 well over $100 billion—more than the total deficits of the previous ten years combined.

Unfortunately, even these deficits do not tell the full story of Federal borrowing, for they do not include the borrowing for off-budget programs or the myriad of obligations issued by Federally sponsored agencies or Guaranteed by Federal agencies. For fiscal years 1965–1974, the cumulative deficit of the unified budget was $102.9 billion. During that same period, the cumulative borrowing for off-budget programs was $137 billion.

I cannot over-emphasize the dangers that may be created by such mammoth deficits at the Federal level, nor can I urge upon you more strongly a plea for maximum fiscal discipline during the life of the 94th Congress. It is absolutely imperative that during the 1970's we turn this country's fiscal policies around.

THE CAPITAL INVESTMENT CHALLENGE

If time permitted today, I would very much like to discuss with you in greater detail the impact that the growth of Government has had upon our free market system:

The way that irresponsible fiscal and monetary policies stretching back to the mid-1960's and earlier have created strong, underlying forces of inflation in our economy, forces that we must contend with for many years to come;

The way that excessive governmental regulation has discouraged new production and growth in many of our industries, particularly in the fields of agriculture and energy;

The way that the wage and price controls of the early 1970's disrupted the economy and have left us a residue of troubles that are still working their way through the system;

The way that the Government's policies have encouraged consumption at the expense of adequate savings and investment;

The way that broad Government domination of many of the industries in this Nation has stifled individual initiative and spawned a new breed of business managers who seem more eager to rely upon the judgments of a GS-16 in Washington than upon their own judgments and competitive instincts. To me, there is nothing more distressing than to see businessmen trade their economic freedoms to the Government in exchange for what they falsely perceive to be financial security.

Rather than dwelling further on this point, however, I ask you to consider the net result of kind of Government growth as well as other social forces which have gained favor in the United States.

The net result, I would suggest, is that we have tilted our great economic machine in the wrong direction. Instead of continually renewing and enlarging our economic foundations, we have allowed them to rust and crumble while we have enjoyed a long binge of over-spending and over-consumption. The bills are coming due today, and unless we soon reverse these trends, the bills can only grow larger in the future.

Once again, let's look at the facts. From 1960 through 1971, as an accompanying table shows (Table 8), annual capital investment in this country averaged approximately 18 percent of our gross national product—the smallest figure of any major industrialized nation in the Free World. In Japan, for instance, annual capital investment averaged over 38 percent of the GNP, while in Germany it averaged 26 percent and in France, 25 percent. Thus, the amount of its annual income that the United States was willing to put back into new plant equipment was smaller than in most of the Nations with whom we compete.

The recent figures that are available for international comparisons—figures showing investments in 1973—indicate an even bleaker investment picture for the United States. In that year, our investment in private industry sank to 14.9 percent of our GNP, lower than any other major industrialized nation except Italy.

Higher rates of capital investment do not guarantee lower rate of inflation. Japan, for instance, has the highest rate of inflation among the countries mentioned, even though it has also had the highest level of capital investment. But there is a close correlation between the rate of capital investment and the increase in a nation's productivity. The annual growth in productivity during the 1960's and early 1970's averaged more than 10 percent in Japan, almost 6 percent in Germany and France, and only 3.3 percent here in the United States. As you can see, the U.S. had the lowest level of capital investment among those countries and also the lowest rate of growth in productivity. I need not explain to this Committee that it is growth in productivity which determines how much of an increase in living standards that the American people can achieve over time.

In the future, we are going to have to do better. The capital requirements of the American economy over the next decade will be enormous. We will need up to a trillion dollars for energy alone. Beyond that, we will need extremely large sums for control of pollution, urban transportation, and rebuilding some of our basic industries where new investment languished over the past decade. In addition, there are the more conventional, but still mammoth, requirements for capital to replace and add to the present stock of housing, factories and machinery.

Yet in the face of these massive requirements, we are not providing adequate incentives for new investment. Over the past decade the inflation has led to high effective rates of business taxation and low rates of profitability, which in turn have greatly eroded the incentives for capital formation.

It is not unfair to say that we are in a profits depression in this country. Nonfinancial corporations reported profits after taxes in 1974 of $65.5 billion as compared to $38.2 billion in 1965, an apparent 71 percent increase. Those profit increases are an optical illusion created by inflation and outmoded accounting methods. When depreciation is calculated on a basis that provides a more realistic accounting for the current value of the capital used in production and when the effect of inflation on inventory values is eliminated, after-tax profits actually declined from $37.0 billion in 1965 to $20.6 billion in 1974—a 50 percent decline. A major factor contributing to this decline is that income taxes were payable on these fictitious elements of profits. That resulted in a rise in tthe effective tax rate on true profits from about 43 percent in 1965 to 69 percent in 1974.

Corporate profits normally provide the foundation upon which corporations build for the future. They are not only a source of investment funds in themselves, but they also permit corporations to attract or borrow other funds which may be used for capital investment and which in turn create more jobs.

The decline in profits therefore has grave implications for capital formation and growth. That is perhaps seen best in the figures for retained earnings of nonfinancial corporations, restated on the same basis to account realistically for inventories and depreciation. It is the retained earnings that corporations have available to finance additional new capacity, as distinguished from the replacement of existing capacity. In 1965, retained earnings totalled $20 billion. By 1973, after eight years in which real GNP had increased more than 35 percent, the retained earnings of nonfinancial corporations had dropped 70 percent to $6 billion. And for 1974, our preliminary estimate for retained earnings is a minus of nearly $10 billion. That means that there was not nearly enough even to replace existing capacity, and nothing to finance investment in additional new capacity.

It is a simple but compelling economic fact of life that increases in productive performance are required over time to support a rising standard of living. Yet, as a Nation, we are rapidly expanding public payments to individuals but neglecting to provide adequate incentives for new investment. Since 1965, in real terms, economic output has increased by one third while government transfer payments to persons has more than doubled. On the other hand, private investment expenditures—upon which the economic future of all of us inevitably depends—have failed to keep pace, rising by approximately one fourth.

It is imperative that we make better provision for the future. This means that we must place much greater emphasis upon saving and investment and much less upon consumption and government expenditure. Today, recession and inflation dominate the discussion of economic events and policy. We must take determined action to deal with these interrelated problems and I believe we shall. At the same time, however, we must begin to shift the long-run balance of domestic priorities away from consumption and government spending and toward investment and increased productivity.

I believe history will judge us, not on how we handle our short-run problems such as recession, but on our ability to deal with the more fundamental problems of the allocation of resources and capital formation. If, as a Nation, we fail to address these problems, we will fail to attain the prosperity and the rising standard of living that the American people can achieve. I hope that the recession has taught all of us the folly of pursuing a "no growth" policy, as some figures once argued. Our goal should be to enlarge the economic pie, not just to redistribute it.

CONCLUSION

While many of the challenges of the economy must be solved primarily in the private sector, the Federal Government has a positive responsibility to help, and there are a number of ways that I believe we can help:

First, we can and must take steps to prevent the recession from deepening to intolerable levels.

Second, we must not abandon the more long-range fight against inflation, for inflation is a bitter enemy of savings and investment and exacts a heavy toll on economic growth.

Third, we must enact legislation that will create greater incentives for capital investment and will allow our financial institutions to operate more flexibly.

Fourth, we must lift the heavy hand of Federal regulation from the many areas where it restricts the efficiency and growth of the free enterprise system. Competition is still the best route to an efficient and productive economic system, and that in turn remains the best means we have of fighting inflation and creating more jobs.

Fifth, as we emerge from the recession, we must restore a reasonable balance to the Federal budget and even seek to achieve budgetary surpluses in better years so that we can keep up a maximum amount of capital for savings and investment.

Finally, even as we recognize that the Government should provide strong leadership, let us also resist those who would have us turn to the Government for solutions to all of our problems.

Considering the severity of our economic troubles today, it is easy to understand why there are so many who look to Government for instant answers. Many want to take the easy road, which means letting Government intrude more and more into our daily lives. We should understand by now that whenever we allow the Government to do something for us that we can do for ourselves, we must surrender some of our own freedom. In these difficult times, there is a continuing danger that temporary security may become so attractive to many Americans that they may become not only willing but eager to give up more of their liberty in return for security.

If we have neither the strength nor the wisdom to say "no" to those who call for further Government domination over our affairs, we will set this nation on the road to a planned economy and the destruction of the free enterprise system that has preserved our liberties and given us the highest standard of living man has ever known. I do not want that for my children, and I am sure you don't want it for yours. Let us recognize, then, that each of us must accept the risks of freedom so that we may preserve its rewards.

Thank you.

TABLE 1.—PUBLIC DEBT SUBJECT TO LIMITATION FISCAL YEAR 1975, BASED ON ESTIMATED BUDGET RECEIPTS OF $279 BILLION, OUTLAYS OF $313 BILLION, AND DEFICIT OF $35 BILLION

[In billions of dollars]

	Operating cash balance	Public debt subject to limitation	With usual $3 billion margin for contingencies
ACTUAL			
1974:			
June 30	9.2	476.0	
July 31	6.5	475.6	
Aug. 31	5.4	482.1	
Sept. 30	8.7	481.7	
Oct. 31	2.2	480.5	
Nov. 30	3.1	485.7	
Dec. 31	5.9	493.0	
1975: Jan. 31	5.9	494.5	
ESTIMATED			
1975:			
Feb. 28	6.0	502.0	505
Mar. 31	6.0	507.0	510
Apr. 30	6.0	510.0	513
May 31	6.0	522.0	524
June 30	6.0	528.0	531

TABLE 2.—PUBLIC DEBT SUBJECT TO LIMITATION FISCAL YEAR 1976, BASED ON ESTIMATED BUDGET RECEIPTS OF $298 BILLION, OUTLAYS OF $349 BILLION, AND DEFICIT OF $52 BILLION (ESTIMATED)

[In billions of dollars]

	Operating cash balance	Public debt subject to limitation	With usual $3 billion margin for contingencies
1975:			
June 30	6	528	531
July 31	6	532	535
Aug. 31	6	538	541
Sept. 30	6	544	547
Oct. 31	6	551	554
Nov. 30	6	558	561
Dec. 31	6	567	570
1976:			
Jan. 31	6	571	574
Feb. 29	6	577	600
Mar. 31	6	583	586
Apr. 30	6	584	587
May 31	6	596	599
June 17 (peak)	6	601	604
June 30	6	596	599

TABLE 3.—BUDGET SUMMARY

[In billions of dollars]

	1974 actual	Estimated 1975	Estimated 1976
Receipts:			
Federal funds	181	186	199
Trust funds	105	119	127
Interfund transactions	−21	−26	−28
Total budget receipts	265	279	298
Outlays:			
Federal funds	199	229	254
Trust funds	91	110	123
Interfund transactions	−21	−26	−28
Total budget outlays	268	313	349
Surplus or deficit (−):			
Federal funds	−18	−43	−55
Trust funds	14	8	3
Total budget	−4	−35	−52

NOTE.—Figures are rounded and may not add to totals.

TABLE 4.—ESTIMATED UNIFIED BUDGET RECEIPTS, FISCAL YEARS 1975–76

[In billions of dollars]

	Current estimate including proposed legislation, fiscal years— 1975	1976
Individual income tax	118	106
Corporation income tax	38	48
Employment taxes and contributions	75	80
Unemployment insurance	7	7
Contributions for other insurance and retirement	4	5
Excise taxes	20	32
Estate and gift taxes	5	5
Customs duties	4	4
Miscellaneous receipts	8	11
Total budget receipts	279	298

NOTE.—Figures are rounded and may not add to totals.

TABLE 5.—TREASURY MONEY MARKET BORROWING[1]

[In billions of dollars]

Calendar year	1st half: Gross new issues[2]	Maturities[3]	Net new money	Peak increase in borrowing	2d half: Gross new issues[2]	Maturities[3]	Net new money	Peak increase in borrowing
1970	$22	$24	−$2	$4	$31	$15	$16	$16
1971	27	24	3	3	37	15	22	22
1972	13	15	−2	7	21	7	14	16
1973	17	16	1	10	20	15	5	5
1974	17	22	−5	4	32	18	14	14
1975 (estimated)	45	17	28	31	48	11	37	37
1976 (estimated)	49	23	24	28				

See footnotes at end of table.

TABLE 5.—TREASURY MONEY MARKET BORROWING [1]—Continued

[In billions of dollars]

Calendar year	Full year: Gross new issues [2]	Maturities [3]	Net new money	Peak increase in borrowing
1970	$53	$39	$14	$14
1971	64	38	25	25
1972	34	22	12	13
1973	37	31	6	6
1974	49	40	9	9
1975	93	27	65	65

[1] Including foreign nonmarketable securities.
[2] Includes increases in regular bills.
[3] Includes paydowns in regular bills.

TABLE 6.—NET FUNDS RAISED IN THE CAPITAL MARKETS BY MAJOR SECTOR

[Fiscal years, billions of dollars]

	U.S. Treasury and financing bank	Federal and sponsored agencies	Total Federal sector	State and local	Corporate and foreign [1]	Total securities	Federal sector as a percent of total securities	Government sector as percent of total securities [2]
1954	$3.6	$1.7	$5.3	$5.5	$3.4	$14.2	37.4	76.0
1955	1.7	—.1	1.7	5.4	2.6	9.7	17.4	73.1
1956	—4.3	.6	—3.7	4.6	3.3	4.1	....	21.0
1957	—3.6	.9	—2.7	4.0	5.7	7.0	....	18.6
1958	6.3	.8	7.1	5.1	6.9	19.2	37.1	63.9
1959	8.0	1.4	9.3	5.7	4.7	19.7	47.5	76.4
1960	.8	2.0	2.8	5.7	3.5	12.1	23.5	70.7
1961	2.0	.1	2.1	4.9	5.0	12.0	17.7	58.5
1962	8.8	2.4	11.2	6.0	5.5	22.7	49.4	75.6
1963	6.4	1.1	7.6	5.5	5.5	18.6	40.7	70.3
1964	2.7	1.5	4.2	5.2	3.8	13.2	31.8	71.4
1965	3.1	2.2	5.4	6.9	5.2	17.5	30.8	70.4
1966	—1.0	6.7	5.7	7.3	9.2	22.2	25.8	58.9
1967	.6	2.6	3.3	6.0	12.2	21.5	15.2	43.3
1968	18.2	5.5	23.8	7.2	15.1	46.1	51.6	67.3
1969	—1.9	5.7	3.8	12.0	14.7	30.5	12.4	51.8
1970	6.8	8.1	14.9	9.7	14.8	39.4	37.9	62.4
1971	20.5	2.7	23.2	15.0	23.0	61.3	37.9	62.4
1972	19.6	8.7	28.2	15.6	15.8	59.7	47.2	73.5
1973	18.5	14.3	32.8	12.6	10.5	55.9	58.6	81.2
1974	2.1	21.3	23.3	16.7	15.6	55.6	41.9	72.0
1975 [3]	43.9	17.6	61.5	12.5	26.3	100.3	61.3	73.8
1976 [3]	63.7	14.7	78.4	14.6	22.7	115.7	67.8	80.4

[1] Bonds issued by nonfinancial corporations.
[2] In these State and local as part of Government sector.
[3] Assumes adoption of President's budget program, with budget deficits of $35,000,000,000 in fiscal year 1975 and $52,000,000,000 in fiscal year 1976.

Source: Fiscal year 1954-74 data based on FRB "Flow-of-Funds."

TABLE 7A.—FEDERAL AND FEDERALLY ASSISTED CREDIT AS PERCENT OF TOTAL FLOW OF FUNDS IN U.S. FINANCIAL MARKETS, BY TYPE OF CREDIT, FISCAL YEARS 1975 AND 1976 PROJECTED[1]

	Fiscal 1975			Fiscal 1976		
Net funds raised	Total (billions)	Federal Government (billions)	Percent total	Total (billions)	Federal Government (billions)	Percent Federal
Long-term funds:						
Mortgages:						
Residential	$35.3	$10.4	29.5	$43.7	$8.5	19.5
Commercial	7.9			8.7		
Farm	4.6	6.9	150.0	5.2	3.8	73.1
Total	47.8	17.3	36.2	57.6	12.3	21.3
Corporate securities:[2]						
Bonds	29.1	2.0	6.9	26.9	1.6	5.9
Stocks	5.3			7.9		
Total	34.4	2.0	5.8	34.8	1.6	4.6
Total, long term	82.2	19.3	23.5	92.4	13.9	15.0
Government securities:						
U.S. Government	43.9	43.9	100.0	63.7	63.7	100.0
Federal agencies	17.6	17.6	100.0	14.7	14.7	100.0
State and local governments	12.5	2.2	17.6	14.6	1.9	13.0
Total	74.0	63.7	86.1	93.0	80.3	86.3
Other funds:[3]						
Business credit	36.8	6.1	16.6	41.1	7.9	19.2
Consumer credit	3.2	.1	3.1	7.0	.3	4.3
Security credit	−.4			1.0		
Other loans, including foreign	1.9	4.0	210.5	9.2	5.3	57.6
Total	41.5	10.2	24.6	58.3	13.5	23.2
Total funds raised	197.7	93.2	47.1	243.7	107.7	44.2

[1] Based on Federal Reserve flow of funds (through 3d quarter 1974) and Special Analyses C. & E., U.S. Budget, fiscal year 1976.
[2] Including foreign.
[3] Includes bank term loans and long-term Federal credits.

TABLE 7B.—FEDERAL AND FEDERALLY ASSISTED CREDIT AS PERCENT OF TOTAL FLOW OF FUNDS IN U.S. FINANCIAL MARKETS, TYPE OF CREDIT, FISCAL YEARS 1973 AND 1974[1]

Net funds raised	Fiscal 1973 Total (billions)	Fiscal 1973 Federal Government (billions)	Fiscal 1973 Percent Federal	Fiscal 1974 Total (billions)	Fiscal 1974 Federal Government (billions)	Fiscal 1974 Percent Federal
Long-term funds:						
Mortgages:						
Residential	$55.7	$10.9	19.6	$45.3	$12.9	28.5
Commercial	16.7			15.9		
Farm	3.3	3.2	97.0	4.5	2.1	46.7
Total	75.7	14.1	18.6	65.7	15.0	22.8
Corporate securities:[2]						
Bonds	15.5	.2	1.3	17.4	.6	3.4
Stocks	12.2			7.1		
Total	27.7	.2	.7	24.5	.6	2.4
Total long term	103.4	14.3	13.8	90.2	15.6	17.3
Government securities:						
U.S. Government	18.5	18.5	100.0	2.1	2.1	100.0
Federal agencies	14.3	14.3	100.0	21.3	21.3	100.0
State and local governments	12.6	2.2	17.5	16.7	1.9	11.4
Total	45.4	35.0	77.1	40.1	25.3	63.1
Other funds:[3]						
Business credit	53.1	4.5	8.5	72.3	6.8	9.4
Consumer credit	23.3			16.3	.1	.6
Security credit	−4.8			−3.7		
Other loans, including foreign	13.2	3.2	24.2	13.8	2.4	17.4
Total	84.8	7.7	9.1	98.7	9.3	9.4
Total funds raised	233.6	57.0	24.4	229.0	50.2	21.9

[1] Based on Federal Reserve Flow of Funds Accounts and Special Analyses C. & E., U.S. Budget for fiscal years 1975 and 1976.
[2] Including foreign.
[3] Includes bank term loans and long-term Federal credits.

TABLE 7C.—FEDERAL AND FEDERALLY-ASSISTED CREDIT AS PERCENT OF TOTAL FLOW OF FUNDS IN UNITED STATES FINANCIAL MARKETS, TYPE OF CREDIT[1] FISCAL YEAR 1972

Net funds raised	Total in billions of dollars	Federal Government in billions of dollars	Percent Federal
Long-term funds:			
Mortgages:			
Residential	43.7	11.2	25.6
Commercial	12.6		
Farm	2.6	2.3	88.5
Total	58.9	13.5	22.9
Corporate securities:[2]			
Bonds	21.6	.2	.9
Stocks	15.5		
Total	37.1	.2	.5
Total long term	96.0	13.7	14.3
Government securities:			
U.S. Government	19.6	19.6	100.0
Federal agencies	8.8	8.8	100.0
State and local governments	16.2	1.9	11.7
Total	44.6	30.3	67.9
Other funds:[3]			
Business credit	26.7	3.3	12.4
Consumer credit	15.2		
Security credit	9.5		
Other loans, including foreign	9.4	2.9	30.9
Total	60.8	6.2	10.2
Total funds raised	201.4	50.3	25.0

[1] Based on Federal Reserve flow of funds accounts and special analyses C&E, U.S. Budget for fiscal 1974.
[2] Including foreign.
[3] Includes bank term loans and long-term Federal credits.

Source: Office of the Secretary of the Treasury Office of Debt Analysis.

TABLE 8.—INTERNATIONAL COMPARISONS OF INVESTMENT AND PRODUCTIVITY, 1960 THROUGH 1973

	Average private investment as percent of GNP (excl. defense expenditures)	Average annual growth in productivity (output per man-hour, percent)
United States	18.0	3.3
Canada	22.4	4.3
Japan	33.4	10.7
France	24.9	5.9
Germany	26.2	5.8
Italy	21.4	6.2
United Kingdom	18.9	4.2
OECD less United States [1]	24.2	6.3
All OECD [1]	20.5	4.8

[1] Figures in the 1st column for the OECD country groups represent private investment as a percent of GNP including defense expenditures and cover the 1960–71 period only.

Sources: OECD and national sources; Bureau of Labor Statistics.

TABLE 9.—SUMMARY RECONCILIATION OF DEBT LIMIT NEED IN FISCAL YEAR 1975 AND 1976 WITH BUDGET AND OFF-BUDGET ACTIVITY

[In billions of dollars]

	1975	1976
Debt subject to limit end of prior year	$476	$531
Adjusted to $6.0 cash balance	473	531
Plus:		
Unified budget deficit	35	52
Trust fund surplus	8	3
Off-budget agency spending financed by Treasury	14	11
Allowance for contingencies	3	
Less: Change in checks outstanding (assumed flow of tax rebate checks)	2	−2
Equals debt subject to limit end of year	$531	$599

STATEMENT OF HON. JAMES T. LYNN, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. LYNN. Mr. Chairman, I likewise have a statement. It has been delivered to the committee. It presents the material in the usual pattern, showing budget total figures, a breakdown of receipts and outlays, the budget by fund group, and then on page 7 a table titled "Debt Subject to Limit." This table shows the adjustments that have to be made to go from the unified budget deficit to the debt subject to limit.

I don't believe that anything would be served in my repeating the narrative that is contained in that statement. In the main, it explains the highlights of these figures. For every page in this statement, there are over 40 pages in the Budget and some 120 pages in the Budget Appendix. Rather than trying to summarize all that, let me answer specific questions here or provide the answers for the record.

[Mr. Lynn's prepared statement follows:]

STATEMENT OF JAMES T. LYNN, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. Chairman and members of the committee: Thank you for the opportunity to appear before you today in support of the request for an increase in the statutory debt limit. I will discuss the budget outlook and its effect on the public debt subject to statutory limitation.

BUDGET TOTALS

The fiscal year 1975 deficit is now expected to be about $35 billion, with outlays of $313 billion and receipts of $279 billion. The estimated deficit for fiscal year 1976 is expected to be about $52 billion. Total 1976 outlays are estimated at $349 billion, and receipts are estimated to be $298 billion.

BUDGET TOTALS

[Fiscal years; in billions of dollars]

Description	1974 actual	1975 November 26 estimate	1975 Budget estimate	1976 budget estimate
Receipts	264.9	293.0	278.8	297.5
Outlays	268.4	302.2	313.4	349.4
Deficit (−)	−3.5	−9.2	−34.7	−51.9

RECEIPTS

The receipt estimates include the effect of the President's recent tax proposals to stimulate the economy and to hold down energy consumption. The effect of these proposals on 1975 and 1976 receipts is shown in the following table.

EFFECT OF THE PRESIDENT'S TAX PROPOSALS ON BUDGET RECEIPTS

[Fiscal years; in billions of dollars]

	1975	1976
Estimate excluding proposals	283.8	303.9
Tax cuts to stimulate the economy	−6.1	−10.2
Individuals	(−5.1)	(−7.9)
Business	(−1.0)	(−2.3)
Energy taxes	4.3	35.3
Excise taxes and import fees	(4.3)	(19.0)
Windfall profits taxes	(...)	(16.3)
Tax offsets to energy program	−3.2	−31.5
Individuals	(−1.4)	(−24.9)
Corporations	(−1.8)	(−6.6)
Net effect of proposals	−5.0	−6.4
Current estimate	278.8	297.5

Since these tax proposals were not contemplated in November, about $5 billion of the drop in estimated 1975 receipts from the November estimate is due to the President's tax proposals. The remaining $9 billion decline is due largely to lower individual and corporation incomes resulting from a weaker economy than earlier anticipated.

Receipts in 1976 are estimated to rise by almost $19 billion over 1975. This increase is based on a projection of an economic upturn beginning in the second half of this calendar year. Again, receipts would be larger—by some $6½ billion—in the absence of the President's proposals.

OUTLAYS

The estimate of 1975 outlays has increased from the November estimate of $302 billion to a current estimate of $313 billion. The major factors responsible for this increase are:

	(Billions)
Aid to the unemployed	$3.5
Decreased receipts from offshore leases (counted as an offset to outlays)	3.0
DOD—Military and military assistance	1.6
Health, Education, and Welfare	1.4
Veterans programs	.9
Energy tax equalization payments (proposed legislation)	.5
Other	.3
Total	11.2

Aid to the unemployed, which includes both benefit payments and public service employment, increases largely because unemployment now is expected to be higher than previously was forecast. The lower offshore oil receipts stem from slower leasing than had been anticipated. The delays result, in part, from assuring that proper environmental considerations have been taken into account. The increase in defense reflects current spending rates that are higher than were forecast, partly due to higher operating costs. Outlays for HEW increase because benefit levels and participation rates are higher than were earlier anticipated in public assistance, medicaid, and medicare programs. Veterans programs rise primarily because of congressional action overturning the President's veto of the veterans education bill.

The President's budget recommendations will result in 1976 outlays of $349 billion, $36 billion above the 1975 level. The following table indicates the source of major increases.

MAJOR CHANGES IN OUTLAYS, 1975–76

Increase, fiscal years 1975–76

	(Billions)
DOD—Military and military assistance	$8.0
Social Security Administration trust funds	7.7
Allowance for energy tax equalization payment	6.5
Aid to the unemployed	3.5
Interest	3.1
Special petrodollar fund	1.0
Other	6.2
Total	36.0

The increase for defense and military assistance reflects the need to maintain defense preparedness and preserve personnel levels in the face of rising costs. This $8 billion increase takes into account the President's proposal to limit pay and other automatic benefit increases to 5%. Without these actions, total Department of Defense outlays would reach $94.6 billion rather than the $92.8 billion now estimated. The $7.7 billion increase for Social Security Administration trust funds also takes into account the proposal to limit automatic benefit increases. Energy tax equalization payments serve the goal of compensating those who will face increased fuel prices as a consequence of the President's energy proposals. While most of the increased costs can be returned through changes in personal and corporate income tax rates, the allowance will finance payments to individuals and to sectors of the economy not affected by the income tax reductions. These include non-taxpayers, State and local governments, and Federal agencies. The growth of aid to the unemployed reflects increased outlays for unemployment insurance and for public service employment. Increases in interest on the public debt result largely from the need to finance the 1976 level of government debt.

Last year, the President sent a number of messages to the Congress outlining actions to restrain spending. Including the effect of those messages, the budget outlines $17 billion in planned reductions. Of this total, $6 billion would be realized by limiting Federal pay increases to 5% through the end of fiscal year 1976 and by placing a similar limit on those Federal benefit programs that increase automatically with the cost of living. To the extent that the Congress fails to approve these limits, or overturns more of the President's earlier savings proposals than it already has, or does not endorse other rescission and deferral recommendations, the 1976 outlay total—and the deficit—will increase.

One way of looking at the debt is in terms of the debt held by the public as a percent of the GNP. I have attached a chart that shows this figure for the years 1950–1976.

THE BUDGET BY FUND GROUP

Most Federal debt subject to statutory limitation arises from activities of the Federal funds part of the unified budget. For this reason, changes in the debt subject to limitation are more closely related to the Federal funds surplus or deficit than to the unified budget surplus or deficit. With your permission, Mr. Chairman, I would like to insert the following table into the record:

BUDGET TOTALS BY FUND GROUP

[Fiscal years; in billions of dollars]

	1974 actual	Budget estimate 1975	Budget estimate 1976
Receipts:			
Federal funds	181.2	186.0	199.3
Trust funds	104.8	118.7	126.5
Interfund transactions	−21.1	−25.9	−28.3
Total	264.9	278.8	297.5
Outlays:			
Federal funds	198.7	229.0	254.2
Trust funds	90.8	110.3	123.4
Interfund transactions	−21.1	−25.9	−28.3
Total	268.4	313.4	349.4
Surplus or deficit (−):			
Federal funds	−17.5	−43.0	−54.9
Trust funds	14.0	8.3	3.1
Total	−3.5	−34.7	−51.9

In addition, as of 1975 the off-budget agencies begin to have an important effect on the debt subject to statutory limitation. The following table explains the relationship among these various items and the proposed debt limit of $531 billion for the end of the current fiscal year that was approved in the House of Representatives' bill.

Debt subject to limit—Fiscal year 1975

	Billions
Unified budget deficit	$34.7
Trust funds surplus	8.8
Federal funds deficit	43.0
Effect of off-budget agencies on debt subject to limit	13.7
Total to be financed	56.8
Means of financing other than borrowing, and other adjustments	3.9
Change in debt subject to limit	52.8
Debt subject to limit, beginning of year	476.0
Anticipated debt subject to limit, end of year	528.9
Adjustment for the usual $3 billion margin for contingencies and for rounding	2.1
Debt limit, end of year	531.0

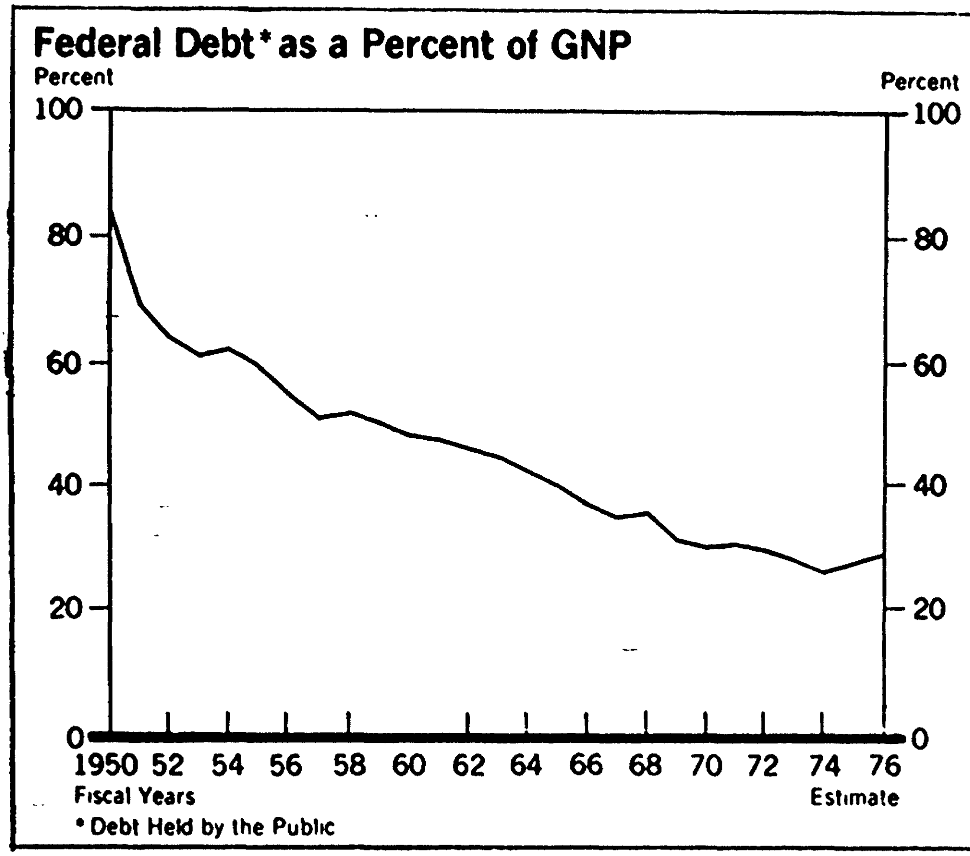
CONCLUSION

The deficits anticipated for fiscal years 1975 and 1976 are substantial. They are not, however, the result of massive increases in discretionary spending programs of the Federal Government. In fact, they assume that reductions of existing programs by $3 billion and $17 billion will be achieved in fiscal years 1975 and 1976, respectively. These reductions are essential if we are to limit the long-run growth of the budget so that, with economic recovery, the budget may return toward fiscal balance. Again I stress how important it is for the Congress to avoid increasing the deficits by adding new spending or by failing to accept the President's proposed reductions.

The deficits for fiscal years 1975 and 1976 are directly related to the economic recession. Aid to the unemployed, including the special measures proposed by the President and enacted—with some modifications—by the Congress, will be $9 billion larger in 1975 and $12½ billion larger in 1976 than it was in 1974. In addition, the softening of the economy will result in substantially lower tax receipts. Tax receipts would be $30 billion larger in 1975 and $40 billion greater in 1976 if the economy were as fully employed as it was during 1974. Finally, the President's economic stimulus proposals—which are a response to the recession—will also contribute to the deficit, decreasing receipts by $6 billion in 1975 and $10 billion in 1976. In the absence of these factors, the budgets for 1975 and 1976 would be in surplus.

I urge prompt enactment of the requested increase in the statutory limitation on the public debt.

Mr. Chairman, I will be pleased to answer any questions members of the Committee might have.



The CHAIRMAN. All right. I have traditionally asked for a series of charts, which I think are helpful in placing this entire problem in context, and I would like to make the request that that information be updated to the present time for the record and our committee record.[1]

Now, in addition to that, I wish you would provide us with a chart that shows what the gross national product is and what it has been over a period; convert that to constant dollars, and put it on a per capita basis, with the final column showing what the percentage change is from year to year. I think that that not only will place in perspective what has been happening in the growth of the economy or the business cycle, but I think it would also tend to indicate the fact that at this moment we must depart from the balanced budget concept because of the economic conditions that exist in the country. I don't think you would have any difficulty putting that together for us.

Secretary SIMON. No; I wouldn't, Mr. Chairman.

If I could briefly make a comment on that, because where the analytical and theoretical argument raises between the GNP and the size

[1] See tables attached to Mr. Simon's prepared statement at pp. 150ff.

of deficits, and this makes an assumption there is a correlation between the size of the economy and the size of deficits or surpluses. I don't believe in this relationship, but let's look at it just a little bit closer. We make these comparisons based on a recessionary year and find a deficit is not only unavoidable but desirable for the reasons you say as far as stimulus is concerned.

The deficits in prospect for 1975 and 1976 and indeed 1977 are roughly comparable in relative size to those of 1959 and 1968. The 1959 deficit occurred really after we had begun to pull out of the recession due to the decline in the corporate profitability during that time.

But, and here is the big "but" that nobody pays any attention to, each time after those deficits we swing in to surplus the following year. Let's look at the accumulative effect of a deficit of this size and present the dangers that I point out in my testimony. We are not talking about swinging back into surplus after the recession is over, and once private demand starts to pick up again what happens when we bump head on into the resurgence of private demand, long demand, long corporate demand, and you take a look at where corporate demand is and it is extraordinarily high. Everyone in the private sector is projecting a record year.

Does our term jeopardize a decline in the interest rates before we start all over again before the demand increases, and indeed if that is correct, left with an inordinately high demand—are we starting at a higher base and take off with higher interests and what happens to housing and economic recovery? I know there is difference of opinion on this subject and I can bring financial economists in here who can speak quite eloquently to this and you get sources and uses of funds from many companies. My former company, Solomon Brothers, has put out a very extensive one that will be out tomorrow that I recommend to your reading because they see a real danger in the numbers aborting economic recovery. That is a real danger. And also to monetary expansion that might be a responsibility, once business starts to pick up, because this is exactly what happened in 1971 and 1972, pulling out of the expansion we expanded the monetary supply and look where we are. So this is something we have to pay very close attention to.

So when I do submit this chart, which I have one for percent of GNP and percent of financing to GNP, I am going to point out in brackets, the recessionary years and what followed these and what we are doing now and the potential impact, who we are crowing out, what happens as far as illiquidity if some of these lesser advantaged companies, the less advantaged if you will.[1] The people today, with the risk ratio, the price premium they are paying today is still extraordinarily large.

Senator CURTIS. Mr. Chairman, I will try to be brief because of the hour, but I think it is important that we clarify the issue that is before us in this particular piece of legislation.

We refer to it as a debt ceiling. Actually it is not an effective device which prevents the Congress from voting additional appropriations, additional authorizations and additional authority to spend, is it?

Secretary SIMON. It is not.

Mr. LYNN. It is not.

Senator CURTIS. So, regardless of where the debt ceiling is fixed, it is not an effective instrument on which the American people can rely that our debts won't go any higher?

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[1] At presstime, Feb. 17, 1975, the material referred to had not been received by the Committee.

Secretary SIMON. No, sir.

Mr. LYNN. It is not. It is, I would say, a rather rough effort by the Congress of the United States to set an overall limit on activity for the year. But that rough effort is not an effective tool against the things you have just mentioned.

Senator CURTIS. I am not sure that it even is that. It is a limit on the amount of money that the Treasury can borrow to pay the debts for the spending that Congress and the Executive already authorized; isn't that right?

Secretary SIMON. Yes, sir. I think the best thing about it, there is only one really good thing about the whole debt concept, and that is the ability to come up and debate with the Congress on the basic merits and demerits of Federal spending.

Senator CURTIS. I have not been ready to accept the idea that we should do away with the debt ceiling and just borrow what is needed. The present system means that periodically it is called to the attention of the public and to the Congress, as to where we are headed in our fiscal policies. Debts are created when we spend money, debts are created when Congress authorizes a program that will call for future costs. Debts are created when we vote for programs which offer to our citizens, our States, and municipalities grants of money. Debts are created when we take other actions which cause money to flow out. If somebody can come up with a real debt ceiling, I will be the first champion.

We are faced now with a ceiling that limits the ability of the Secretary of Treasury to borrow enough money to pay for the past sins of the spenders; isn't that right?

Secretary SIMON. Yes, sir.

Senator CURTIS. Thank you.

Senator PACKWOOD. Last week the Wall Street Journal carried Chairman's Mahon's testimony of our borrowing, his political assessment. George Will had references to it in the Post today, and I saw it on the west coast over the weekend.

Assuming that Congress will turn down the 5-percent limit, on Social Security, military, and Government retirement policies and that our deficits are likely to run $15 to $20 billion higher than you are projecting, what is your real assessment as to what this will do to interest rates 18 months to 2 years down the road, and specifically what will it do to borrowing for home building?

Secretary SIMON. We are right now in the fortunate position of having raw declines and interest rates that is concentrated on the short end of the yield curve, like the money market rates, and this is causing a reflow of money in our thrift institutions. Of course, the housing permits went up and this is the first harbinger of the recovery. The behavior of the people who buy houses, I believe a high mortgage rate is a great deterrent, and the former assistant of housing and urban development is a great expert, and I won't comment any further.

But if it is to be $30 billion this year and perhaps go as high as 36—let me give you a measurement of that. During the month of January, and here we are in one of the steepest recessions post-war, certainly it will be measured in my judgment as the steepest recession, and you had borrowings long term in the marketplace of about $3¼ billion. The previous record was $2¼ billion. That pretty well tells the story.

When they are coming down how far down is down? When private demands which are off, and they will be off until the turnaround comes, again pick up and bump headon with what the Government is demanding, well, everybody can make different judgments, and Solomon Brothers have $50 billion being the outside limit of what can be demanded this year and the danger of aborting an economic recovery, aborting a housing recovery, A: starting from an economic recovery, an inflation rate that will keep long term rates at a high level, starting into the next recovery is a very dangerous thing.

Senator PACKWOOD. In your estimate if we borrow substantially between now and October 1, 1976, are we going to see a prime rate of 12 to 14 percent?

Secretary SIMON. Of course, your prime really is not used to that, Senator. That is pretty much on the private demand. I have great trouble with $170 billion. We made some assumptions when we put our borrowing demands that Congress would act on the references and decisions totaling $20 billion in fiscal 1975 and 1976 and would enact no new spending plans. Of course, we are watching both those things in some disappointing fashion, also Outer Continental Shelf leasing, $300 million for our program here where we had expected to get $5 billion during this fiscal year and it will obviously fall quite short of that, which indeed enlarges our deficit.

In using that $50 billion market—but U.S. Trust predicted $40—right now we are looking at new money demands for this calendar year of $65 billion, gross demands of $93 billion. I suggest gross demands are pretty important in the market price because economists like to talk about net new demands because they make the assumption they catch the same buyer in the same net, because expectations change. I have to maintain sloping yield curve.

Senator PACKWOOD. I see some economists saying and testifying the deficit is not big enough and will not pull us out of the recession and what is needed is a much greater magnitude of deficit spending. The State of Oregon, because of lumber, is dependent upon housing. We are going to amputate housing by raising interest rates which may or may not get us out of the recession. But we guarantee the 92 percent of people working plus the 8 percent of unemployed face 10–20 percent inflation high interest rates if we go anywhere beyond what I believe is the expanded deficit rate you submitted to us——

Secretary SIMON. I believe, as Dr. Paul McCracken said a few weeks ago, that economists in general have been very slow to understand the financial implications of deficits of this size and the effect on the capital market and the illiquidity that exists. These dangers are not going to be fully recognized, that is, unless the recession is much deeper than anyone predicts or inflation comes down farther than anyone predicts. That is a pretty dangerous hope to base assumptions on, that we will not have problems if we increase expenditures beyond these extraordinary and I hope temporary levels.

Senator PACKWOOD. I have no other questions, Mr. Chairman.

The CHAIRMAN. Thank you very much, Mr. Secretary.

The committee will meet in executive session 10 o'clock tomorrow morning.

[Whereupon the committee was adjourned until February 11, 1975.]

Appendix A

Communications Received by the Committee Expressing an Interest in these Hearings

LET'S END INFLATION

(By Dr. Fred Schulman, chairman, Trade-Energy Information Center)

Today's inflation is sapping the vitality of the United States and the free world and has put the free enterprise system on the defensive everywhere. Clearly it must be stopped and, fortunately, it can be, and at much less pain than is commonly prescribed.

Today's inflation is not conventional, and it will not yield to conventional remedies of tight money, balanced budgets, unemployment, or reduced expenditures. For example, lumber and food prices took off for the stratosphere, after large contracts were signed with Japan and the Soviet Union. Similarly, prices of oil and of all products and services using energy were raised dramatically as a result of actions by the Arab producing countries encouraged, as we know, by Soviet broadcasts and propaganda. These price increases affected everyone here immediately, both individual consumers and business and industry, thereby setting in motion further price increases based on higher costs and compensatory labor demands for off-setting wage increases. Notice that these very significant inflationary increases originated in actions not subject to domestic controls of tight money, government expenditure, unemployment, or other conventional economic countermeasure to inflation. The remedy then, is to isolate the major root causes of our terrible unconventional countermeasures, and finally, and most important we must find the courage and determination to apply the most effective specific countermeasures to the specific root causes of our inflation.

It is obvious that this is a complex subject and all relevant contributory causes cannot be considered in a brief analysis such as this. Nevertheless, without affecting the basic conclusions, only two prime unorthodox causes of the present inflation and world economic chaos will be discussed and solutions suggested. Other more conventional causes and remedies have been ably discussed by World Bank economist Irving S. Friedman in his book "Inflation, a World-Wide Disaster" and by many other leading economists.

First, we have not yet realized that the Organization of Petroleum Exporting Countries, (OPEC), has, in effect cartelized world prices of ALL commodities involved in world trade—not just oil, but also food. metals, raw materials and manufactured products. In today's world of instant global communication and multinational corporations, all the world except the non-market countries is one global interdependent economic market. In other words, because of the West's yielding to embargoes and quadrupling of oil prices by OPEC and the relative inflexibility of the high OPEC oil price, the prices of everything else must inexorably rise throughout the world to restore the *Equivalence of Value* of these products with oil. Therefore, if the West, and particularly the United States, does not show leadership in opposing the Arab-Soviet cartel, the prices of most goods must rise to an inflationary level far higher than at present. In the U.S. alone, wholesale fuel prices rose 64.6% during the past year and are still rising. Industrial wholesale prices rose 25.1% and are now rising faster. Wholesale prices for the month of July 1974 rose a fantastic 3.7%, equivalent to an additional annual rate of 44.4%. This continuous rise in the rate of inflation is assured, unless we begin to use our considerable strength in food, technology, trade, and diplomacy to firmly oppose the Arab OPEC stranglehold on Western economies and policies.

Regarding high intertest rates, the need of American industry for vastly increased amounts of capital to pay for the inflated costs of new or improved facilities, has stretched the capacity of American capital markets almost to the breaking point. For example, the current industry estimate of needed capital for the utility-energy industry alone in the period 1974–1985 is a staggering $1,000 billion. This compares with the $350 billion estimate for the period 1970–85 reported to the Secretary of the Interior in 1971 by his Industry Advisory

Committee. Yet, despite this desperate shortage of available capital, it was announced recently that Occidental Corporation has signed a $20 billion deal with the USSR for fertilized facilities to be built in the Soviet Union. Occidental must raise the $20 billion in the U.S. capital markets thus further increasing stress on the limited available capital and forcing up the interest rate. This process has been repeated by many companies during the past nine months and has forced the prime rate continuously upward until in July it hit a record of 12–12¼%. Such misuse of detente could force interests rates even higher in the future. Yet projects for energy, fertilizer, plastics, chemicals, computers, machinery, bearings, satellite communication equipment, etc., announced recently by Houston Offshore Drilling, Control Data, General Tire and Rubber, International Paper, Union Carbide and many others, for high technology facilities to be built in the USSR and the Soviet bloc, are only the forerunner of many more projects that will cost the U.S. perhaps hundreds of billions of sorely needed Capital. It should be understood that exports of capital to the Soviet bloc forces the prime rate up by competition for scarce capital at a time of unprecedented huge domestic capital needs. Tight money policies of the Federal Reserve Board does not create the problem but adds to it by shifting the emphasis from some expensive domestic projects to Soviet projects where low subsidized or guaranteed loans and interest rates can be obtained through detente policies. If we are serious about reducing interest rates, then export of capital to the Soviet bloc should be reduced or stopped until inflation is controlled. It is surely known that Soviet trade has political and strategic objectives. Should we do less?

From this brief discussion, it can be seen that the two root causes of today's excessive unorthodox inflation are:

1. Export of materials without domestic allocation.
2. Uncontrollable high interest rates caused in part by unusual and unexpected and unplanned for export of capital to the Soviet bloc during the present period of intense world capital shortage and need.

When these two root causes of today's double-digit inflation are remedied, then the classic economic forces can moderate any remaining inflation, if needed. But if we do not recognize these two root causes of our massive inflation, or fail to have the courage and determination to remove them, then don't be surprised if inflation continues to rage onward until the full equivalence of value with oil is reached and economic chaos threatens the stability of both the United States and friendly Western governments.

Effective anti-inflation counteraction requires the following actions as soon as practicable:

1. Reserve domestic supplies to cover needs.
2. Reduce capital exports, guarantees and subsidies and relate them to resource imports and political objectives.
3. Use exportable surpluses as a quid-pro-quo to assure resource source availability and national political objectives.

These suggestions are offered merely as ideas which I believe merit further discussion and analysis. Today's inflation is gnawing at the heart of the nation. I believe that further analysis will show that these suggestions can help bring us back to the economic health and stability that we all deeply desire.

Position of the New England Fuel Institute on H.R. 1767

Mr. Chairman: The New England Fuel Institute, an association of 1300 independent retail and wholesale home heating oil distributors throughout the six state region wishes to state its position and indicate its support for delay and/or discontinuance of the crude oil and refined tariff and supplemental fee program, as proposed by the President in his state of the union message.

New England is especially vulnerable to, and will be adversely affected by, the President's tariff and supplemental fee program. Further, its economic situation will be disadvantageously affected by the loss of the entitlements program due to the proposed decontrol of the price of old crude, as well as by the proposed tariffs and supplemental fees on imported crude and refined products.

During the last quarter of 1973, New England home heating oil consumers reduced their consumption, adjusted for the weather, by 12%. In addition, during the last quarter of 1974, New England home heating oil consumers again reduced their consumption another 8.2%. This brings the total reduction for the last three months of 1974 to 20% adjusted for the weather, as compared to the base period year 1972.

Tariffs on imported home heating oil and residual oil will impose an unjust economic burden on the New England consumer. New England, with 5.8% of the population, consumes 21% of the heating oil and will pay 16⅔% of the total Federal income tax rebate of $14,000,000,000 that has been proposed by the Administration. In face of the unusual savings due to conservation, New England will be doubly burdened by rationing through taxation, which will confiscate a substantial portion of the region's income.

Increases alone, due to home heating oil tariffs, along with losses of the entitlement program, will add $75,000,000 to home heating oil bills, or $30 for every oil-heated home in the region. The tariff on heating oil and residual oil combined, will result in a minimum increase in cost of $41 for every person in New England, and about $152 for every family, according to these New England Fuel Institute figures. We wish to emphasize that the economic burden will be much greater, as gasoline and other petroleum products are not included in these statistics. Further, the tariff on residual oil will increase electric bills by 30% to 34% beginning the first of May. Rationing through taxation is not the answer.

There is a solution to our energy problem. The New England Fuel Institute Program is one that can be put into effect immediately. Without undue hardship on the consumer, who can stand it least, this program will take care of the immediate problem.[1]

Down the road, statesmanship must be exercised. We must separate conservation from taxation; we must de-regulate new natural gas; we must explore the use of all energy forms and develop them to the utmost; and, we must allow the free market to create the capital necessary for the exploration and development of existing forms of energy.

The imposition of added tariffs and supplemental fee costs of $75,000,000 per year, to the New England home heating oil economy where over 2,350,000 consumers heat their homes by oil, and where 71% of all of the buildings and 74% of the population, and 92% of the schools and educational institutions are heated by oil, will impose a financial hardship that almost boggles the mind.

In addition to the $75,000,000 supplemental fee increase for imported home heating oil, there will be an additional increase for the 147,000,000 barrels of residual oil that are imported into the area each year, of $442,000,000. With heating oil and residual oil combined, these tariffs and supplemental fees impose $517,000,000 of increased annual costs upon an economy embracing slightly more than 12,000,000 people, 71% of the $442,00,000 residual oil increase will be borne by Massachusetts alone, an amount exceeding $300,000,000 starting April 1st. On an annual basis for residual imported product alone, the results will be catastrophic for this single state. In addition, it will affect adversely the entire New England economy in relation to residual and other petroleum products costs.

As stated previously, this will boost electric bills 30% to 34% as electric utilities would pick up $221,000,000 of the residual oil tab. This can only be passed on to consumers.

Because of this, any delay in implementing the President's program would be advantageous in helping the already overburdened New England economy.

Not only must the implementation of the tariff and supplemental fee program, with its loss of entitlements be postponed, it must be set aside forever, and substituted for it, should be the Mandatory Allocation Program which is in effect at the present time and which the President has full authority to adjust and amend at this time.

In conclusion, we are submitting a copy of New England Fuel Institute's Position Paper, which in detail presents a counterproposal with a minimum taxation.

Thank you very much.

[POSITION PAPER]

PROPOSED PROGRAM TO REDUCE IMPORTS BY 1,600,000 BARRELS PER DAY AS OPPOSED TO THE PRESIDENT'S PROPOSAL FOR TARIFFS AND EXCISE TAXES THAT WOULD REDUCE THE VOLUME OF IMPORTED CRUDE OIL AND FINISHED PRODUCT BY 1,000,000 BARRELS PER DAY

The New England Fuel Institute, an association of 1,300 independent wholesale and retail heating oil distributors throughout the region wishes to state its positive position and program presented in rebuttal of the President's proposed

[1] The New England Fuel Institute Position Paper is attached to this statement.

tariff and excise tax approach to the problem of reducing the volume of imported crude oil and refined products.

The New England Fuel Institute has argued strongly against the proposed tariff and excise tax program because of the inordinate economic burden that will be placed upon New England consumers of oil, gas and electricity. The Institute wishes to state that it is unalterably opposed to any excise taxes on domestic petroleum products, further, it is adamantly opposed to any tariff on imported crude oil, imported residual oil, imported heating oil and other imported petroleum products.

The President's proposal of a tariff of $1.20 per barrel affecting the 25,000,000 barrels of No. 2 home heating oil imported into New England each year is deceptive, as the program will phase out the 60¢ per barrel entitlement expected for January, and will further eliminate the full incremental value of $1.20 per barrel that the product entitlement would have reached in the future. Therefore, the actual tariff of $1.20 per barrel, the loss of the present entitlement of 60¢ per barrel, plus the loss of the full value of the entitlement for the future, will amount to about $3.00 per barrel for the 25,000,000 barrels of home heating oil imported annually into New England. As a result, $75,000,000 will be added to present home heating oil bills of New Englanders and this substantial figure does not include the increased cost of heating oil that will be produced from imported crude oil that will bear the full $3.00 per barrel tariff.

Further, the $3.00 per barrel increased cost of home heating oil due to the tariff ($1.20 per barrel), plus the loss of the present 60¢ per barrel entitlement, plus the loss of the future full value of the entitlement, applied to the average 147,300,000 barrels of residual oil imported into New England annually, will increase residual oil costs for the region by $442,000,000 per year. One-half of this will be borne by consumers' electric bills after April 1st. Also, at the present time, NEFI is very strongly opposed to the decontrol of the price of domestically produced "old" crude oil.

This Institute strongly supports the erection of at least two refineries in New England and favors the immediate commencement of East Coast off-shore drilling as soon as possible. Further, regulations of the Environmental Protection Administration must be suspended during this time of crisis in a prompt and efficient manner that will prevent New England from suffering undue economic hardship.

After lengthy consideration, the Institute proposes a five point program which will reduce consumption by 1,615,000 b/d during its first year of operation, rather than the 1,000,000 barrels per day that the President's program now projects. Further, the NEFI plan will achieve this reduction in imports at a minimum cost to the New England economy. Since foreign oil prices are higher than domestic, every barrel of reduction in domestic consumption will result in a corresponding reduction in import volume. Therefore, the NEFI proposal will achieve a 1.6 million barrel per day reduction rather than the one million proposed by the President. In fact, this Institute doubts that the President's proposals will result in the projected one million barrel reduction. It will be considerably less.

It is the firm opinion of this Association that the use of taxes and tariffs to reduce consumption is inequitable and unjust, and completely unfair to lower and middle income groups. It is rationing by economic hardship despite any disclaimers.

As the President already has the power to allocate oil under the authority granted him by the Mandatory Allocation Act passed in November, 1974, there is no reason that the present policy of economic confiscation of a large portion of New England's income through an inequitable imposition of tariffs at the present time, should continue.

In place of the Administration's plan, the New England Fuel Institute proposes the following program be adopted by the Congress and/or implemented by the President:

	Barrels per day
1. An immediate prohibition on the importation of gasoline. (Gasoline importers to be assigned domestic suppliers with an adjusted base period to be 1972). This will result in an approximate reduction of imports of	165,000
2. A mandatory 55 mile per hour speed limit with penalties such as two warnings and then loss of license. This to be instituted on Federal and State Highways as well as at the county, city and town levels. This will result in an approximate reduction of imports of	100,000
3. An immediate mandatory reduction of prime suppliers' allocation fraction by 10% to a maximum reduction of 90% on gasoline, distillate and residual oils, with 1972 as the adjusted base period year for gasoline and distillate, and 1973 for residual oil. This will result in an approximate reduction of imports of	700,000
4. Equal treatment on mandatory reduction of consumption for natural gas and electric users. This reduction by electric users will result in an import reduction of	250,000
5. In opposition to gasoline rationing, New England Fuel Institute instead supports a maximum 10¢ per gallon tax on gasoline. This tax could be refunded to low and middle income taxpayers. This will result in an import reduction of	400,000
Total reduction	1,615,000

STATEMENT OF EDWARD FALCK, ENERGY CONSULTANT AND FORMER DIRECTOR, OFFICE OF WAR UTILITIES, WAR PRODUCTION BOARD

I believe that the President's proposed tariff on oil imports and proposed excise tax on domestic oil and gas should be rejected by the Congress.

As has been stated very well by distinguished Senators and other witnesses in these proceedings, President Ford's tariff and tax proposals are (1) regressive, (2) inflationary, and (3) a blow to our already depressed economy. I would like to add a fourth point, namely that this tariff and excise tax program is entirely negative—it does nothing to stimulate exploration, development and production of additional energy resources.

What are the alternatives?

If indeed it is necessary to cut imports for reasons of foreign policy and military security, then we should impose volumetric quotas on the importation of crude oil and petroleum products. Such a quota system would achieve the precise quantitative reduction required without imposing an unnecessary economic burden on the entire energy consuming public.

I agree that consideration should be given to a relatively small Federal tax on gasoline subject to future gradual escalation. Federal revenues derived from any such fuel tax should be plowed back into assisting development of both traditional and non-traditional new energy resources.

I am wholly in accord with the philosophy expressed by Chairman Long during the hearing on February 10 when he said in his opinion the revenue that may be raised by the Government from energy taxes should be directed toward producing more energy and to providing adequate capital for new mines and opening up new sources of energy from shale, coal, atomic, solar or anything else. Senator Long also made an impressive point when he stated we should be able to do the necessary job in two years rather than 10. We have good, hard practical experience to support the assumptions and philosophy of Senator Long's position. During World War II, when the Congress gave the President the necessary war powers which he in turn delegated to the War Production Board and the Petroleum Administration for War, this country was able within three or four years to create and complete the Manhattan Project for the manufacture of the components needed to make the first atom-bomb; constructed a brand new synthetic rubber industry to replace the raw rubber supplies that had been cut off; constructed the Alcan Highway to Alaska; completed both the Big Inch and the Little Inch oil pipelines; and produced unprecedented numbers of war planes, ships, tanks, guns, munitions and communications equipment. This entire program was carried out with the cooperation of experienced industrial and business executives, engineers, scientists and Government administrators working together for a common cause. The operations of the War Production Board were always under the surveillance of a watchdog Senate Committee—the celebrated Truman Committee.

There is no practical reason why this country cannot do as well today in coping with the energy shortage. In order to accelerate the schedule, it may be desirable for Congress to consider establishing a new agency similar to the War Production Board with broad planning and coordinating responsibilities including the legal authority to schedule production of equipment and the authority to break bottlenecks that are interfering with the progress of any authorized energy project or program. Such an agency should be able to issue necessary directives to other Government departments that may be delaying the commencement of any new energy project. While such an agency would, of course, be a part of the Executive Department, it should be subject to close supervision of a Joint Committee of the Senate and House of Representatives.

I recommend this concept as an affirmative and positive alternative to take the place of the President's tariff and tax proposals.

NATIONAL RETIRED TEACHERS ASSOCIATION AND THE AMERICAN ASSOCIATION OF RETIRED PERSONS,
February 7, 1975.

Mr. MICHAEL STERN,
Chief Counsel, Committee on Finance, U.S. Senate,
Washington, D.C.

DEAR MR. STERN: On behalf of the 8-million members of our affiliated organizations, I wish to submit for inclusion in the record of the February 7th and 10th hearings on Administration's energy program a copy of the enclosed statement.

As advocates of the aged, our Associations cannot ignore what is currently happening to the economy nor what can be expected to happen if the Administration's program is implemented.

It is our conclusion that the consequences of the Administration's tariff, excise taxes, and "new" natural gas and "old" domestic oil deregulation package would be: accelerated inflation, continued recession, increased portions of consumer budget devoted to energy, another massive shift of wealth from the consumers to the energy industry and permanent energy prices wholly unjustifiable by the supply response.

In our view, inflation-recession is the most serious threat to the income security of the poor and fixed income at the present time and is seriously jeopardizing the financial integrity of the income maintenance structure on which millions of them are dependent. It is clear that the extortionately high prices artificially established for oil, both at home and abroad, have been responsible for much of the current situation; the Administration's program will substantially aggravate that situation and will distribute disproportionately its adverse consequences among the poor and the aged—the very groups who have already suffered the most.

Sincerely,

PETER W. HUGHES,
Legislative Representative.

STATEMENT OF THE NATIONAL RETIRED TEACHERS ASSOCIATION AND THE AMERICAN ASSOCIATION OF RETIRED PERSONS ON H.R. 1767 AND THE ADMINISTRATION'S ENERGY-TAX RELIEF-BUDGETARY PROPOSALS

As advocates for the aged, our Associations cannot ignore what is currently happening in the economy nor what can be expected to happen if the Administration's energy, tax relief and budgetary programs are implemented. The interests of the aged cannot be separated from the interests of the population as a whole, nor can the systems upon which the aged are so dependent for a substantial portion of their income security be considered out of the context of the performance of the economy in which they exist.

Let it be understood at the outset—inflation-recession is the most serious threat to the income security of the poor and the fixed-income aged at the present time and is seriously jeopardizing the financial integrity of the income maintenance structure on which millions of them are dependent. Let it also be understood—the extortionately high prices artificially established for oil, both at home and abroad, are responsible for much of this current situation.

It is our conclusion that the Administration's program (including the tariff, excise tax, "new" natural gas and "old oil deregulation, tax relief and budgetary cutbacks) will substantially aggravate that situation and will distribute disproportionately its adverse consequences among the poor and the aged—the very groups that have already suffered the most. We are therefore opposed to the tariff, recently imposed by Executive proclamation on foreign imported crude oil and derivative products. We are in favor of the enactment of H.R. 1767, the bill to negate the preemptory action taken by the President on January 23rd and to provide the Congress with a reasonable period of time within which to develop an energy demand reduction policy that will be the product of full and free discussion and careful deliberation, and will reflect a truly national consensus.

A. INFLATION-RECESSION AND THE AGED INDIVIDUALS

For the poor and fixed-income aged, the combination of inflation, recession, and unemployment during 1974 was catastrophic. With less purchasing power to begin with, it was these groups that suffered the most from inflation. While the magnitude of their dollar income decline may not have been as great as that of other groups, the decline was from a level that was, at best, marginally adequate. We are not suggesting that all the aged are poor. We wish to point out, however, that older family units now tend to be concentrated more in the lower and less in the upper extreme of the national income distribution.[1] Although recent increases in OASDI benefits have reduced the number of the aged in the poverty class to under 3.7 million, the incidence of poverty and low income is still substantial. Because of the higher rates of inflation with respect to necessaries such as food[2] and housing, on which the poor and fixed-income aged tend to spend far higher portions of their total income,[3] they suffered a relatively greater loss of purchasing power than other groups in 1974.

The impact of the recession has rendered even more difficult, if not impossible, any moderation of the impact of inflation through increased income from active employment. Even in the best of times, the aged encounter a formidable combination of barriers to employment.[4] With an increasing number of workers competing for a diminishing number of jobs, the employment alternative, as a means of sustaining purchasing power, is for the most of the aged, out of the question.

B. INFLATION-RECESSION AND THE INCOME MAINTENANCE SYSTEMS

If our Associations are concerned with the impact of inflation-recession on the aged individual, we are equally concerned about its impact upon the financial viability of the income maintenance programs upon which the aged are so dependent.[5] With the trust funds sufficient to continue benefit payments for only nine months in the absence of a continuing influx of payroll and self-employment tax revenues, and with social security cash benefit levels subject to automatic increases that are directly related to the cost of living, performance of the economy is indeed important.

Workers who are unemployed are not paying social security taxes. High rates of inflation trigger automatic benefit increases which, in turn, must be financed by contributions from a diminishing number of active workers. Such circumstances cannot fail to aggravate the three percent, long-range deficit that is already projected for the system.[6]

Since the projections of the revenue needs are based on assumptions that are dynamic with respect to demographic changes and future rates of inflation, our

[1] See Table I in the Appendix.

[2] The Joint Economic Committee reported that food price inflation in the past 18 months has added twice as much to the cost of living of the poor as to that of the average urban worker. (Joint Economic Committee, "Achieving Price Stability through Economic Growth," H. Rept. No. 93–0000, 93d Cong., 2d Sess.) (Dec. 23, 1974) (Hereinafter referred to as J. Eco. Com. Rept.)

[3] See Table II in the Appendix.

[4] The combination includes: labor union restrictions, mandatory-retirement policies and the social security retirement test.

[5] See Table III in the Appendix.

[6] See Table IV in the Appendix.

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Associations are concerned when we discover that those assumptions may be dangerously understated. We have been advised that the difference in projected cost to the system as a result of a four rather than a three percent assumed long-term rate of inflation is in the area of 40 percent. The future of the social security system (or of any other primary retirement system) is critically dependent upon the maintenance of a reasonably low rate of inflation and a reasonable high rate of employment.

Our Associations cannot remain silent while the Administration proposes and proceeds to implement a program that will destabilize the economy further and aggravate, over the long term, the economic problems of our constituency.

C. MACRO AND MICRO ECONOMIC EFFECTS OF HIGHER ENERGY PRICES

According to the Joint Economic Committee, about one-fourth to one-third of the total 12.2 percent increase in consumer prices in 1974 was attributable to higher energy prices.[7] Although this coincides with conclusions of the Congressional Research Service,[8] the C.R.S. also found that the "ripple effects" emanating from these primary price increases could have caused 35 to 50 percent of 1974's inflation.[9]

Certainly, our Associations have no doubt that soaring energy prices have resulted in an enormous transfer of purchasing power from consumers to domestic and foreign energy producers and have left the domestic consumer with substantially reduced real disposable income.[10] We therefore agree with the general consensus that, in order to reduce our reliance upon foreign imported crude oil, and our vulnerability to international trade disruptions, a comprehensive energy policy must be formulated that will reduce demand for energy, promote conservation and stabilization of energy prices, and still provide the incentives necessary to encourage the efficient development of the vast energy potential of the United States.

With these objectives, the Administration's energy program is supposedly in accord. Our Associations expect, however, that the actual consequences of the proposed program would be: accelerated inflation, continued recession, increased portions of consumer budgets devoted to energy, another massive shift of wealth from consumers to the energy industry, and permanent energy prices at levels wholly unjustified by the supply response. Moreover, as we shall indicate below, we feel the Administration's program is founded upon premises wholly at variance with the evidence with respect to the oil-natural gas industries.

Since mid-1973, prices for gasoline, home heating oil, and residual fuel oil have increased by 37, 66 and 143 percent respectively.[11] If the Administration's entire energy package were implemented, a 77 percent increase in overall fuel costs by next heating season is expected to occur.[12]

The Administration's estimates of the direct and indirect impact of its proposed energy program on average family expenditures range from $275 to $345. The increased fuel expenditure impacts in terms of dollars and percentages of total income for the poor and the lower, upper-middle, and high income resulting from the program are estimated to be $82 (3.3 percent), $129 (1.6 percent), $189 (1.3 percent) and $225 (.9 percent) respectively. The direct and indirect impact of the proposed program is expected to produce a 2 percent increase in the Consumer Price Index over what would have otherwise obtained.

The Congressional Research Service, on the other hand, estimates that the increased energy costs for the poor and the lower, upper-middle, and high income, would be $341, $530, $694, and $1,017 respectively or an average cost for a family unit of $720, taking into account both direct and indirect cost increases. Moreover, the CRS concluded that these measures could increase the 1975 estimated rate of inflation of 6 to 7 percent to 9 or 10 percent—even before considering the "ripple effects." [13] If these indirect effects are included, double-digit inflation is likely to continue.

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[7] J. Eco. Com., 93d Cong., 2d Sess. 104 (1974).
[8] See Lawrence Kumins, Cong. Research Service, Library of Congress, "Administration's Energy Tax Proposals and Related Measures," 2 (January 23, 1975) (Hereinafter referred to as CRS Rept.)
[9] Id.
[10] See Table V in the Appendix.
[11] Washington Post, January 19, 1975, C–2, Col. 5.
[12] Energy, January 20, 1975, vol. 3, no. 3, at 1.
[13] C.R.S. Rept. 5.

D. THE IMPACT OF THE TAX RELIEF PROPOSALS ON THE POOR AND FIXED INCOME AGED

While we have commented separately with respect to the energy proposals, our Associations recognize that the Administration's tax relief and $80 payment proposals are an integral part of the same package. According to Administration estimates,[14] the tax rebate will offset the average increase in direct energy costs of the poor and the upper middle income families, and significantly offset the costs of the lower middle-income group.

Since the tax relief program lacks a negative income tax aspect (availability of the intended tax relief is conditioned solely upon the presence of income tax liability), the poor and the non-poor living on non-taxable income can expect to receive the $80 payment but no tax relief.

Since only 4.5 of the 6.8 million returns filed by the aged in 1971 (the last year for which comprehensive statistics are available) were taxable returns, only about 5.8 million persons (66⅔% of 8.7 million) had some federal tax liability.[15] It should be clear that the aged who are taxpayers are a distinct minority within their own age group and a very small minority within the total population; they can expect to receive a disproportionately small share of the intended tax relief.

In evaluating the merits of any proposed tax relief mechanisms, our Associations will object to a mechanism that conditions the availability of relief solely on tax liability. We will also object to any mechanism which disproportionately benefits those in higher income tax brackets.

With respect to our first criterion, we fully appreciate the policy significance of a tax relief mechanism that is in the nature of a negative income tax. However, it is the poor and the fixed income aged who have suffered the most through inflation. Moreover, since the purpose of tax relief is to stimulate demand and create jobs, the relief dollars should be placed in the hands of those most likely to spend them—the poor and the aged. This could not readily and efficiently be done in the absence of such negative tax devices.[16]

With respect to our second criterion, we wish to point out that a tax benefit distribution of the Administration's tax rebate proposal would probably benefit more those in higher income tax brackets and could not therefore have our support.[17]

Considering both the energy and tax-relief aspects of the Administration's package, we believe that the results will be with respect to the poor and many of the fixed-income aged, higher prices and no tax relief. While for some population groups, the program would mean a "taking" with one hand and a "giving" with the other, for much of our constituency, the program would simply mean a "taking."

E. THE FIVE PERCENT COST-OF-LIVING LIMITATION

Perhaps the consequences of the Administration's program would be less severe with respect to the poor and fixed income aged if the Administration were willing to allow the automatic cost-of-living adjustment features of the primary retirement and welfare systems to operate in their statutorily pre-

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[14] See Table VI in the Appendix.

[15] Derived from tables IX & X in Appendix.

[16] Certainly it would be possible to channel increased income to some of the poor and fixed income aged who have no federal tax liability through existing programs such as Aid to Families with Dependent Children and Supplemental Security Income. But these programs do not reach all of the poor nor do they reach all of the aged who are not poor but have no tax liability. Indeed the Supplemental Security Income program is, according to the Joint Economic Committee, presently providing benefits to less than one-fourth of the estimated 1.2 million potentially eligible individuals.

Although our Associations have consistently urged welfare reform (taking into account what has already been done with respect to the substitution of the SSI program for the former federal-state adult assistance programs), we cannot realistically expect comprehensive welfare reform, despite the need therefore, to be achieved in time to enable the aged and non-aged poor to benefit from the proposed tax relief. Since these groups cannot be fully reached if relief is contingent solely upon liability we recommend a mechanism to provide both permanent tax relief to taxpayers who have, in the absence of such relief, federal income tax liability, and temporary relief to persons who would have no liability. The temporary period should be sufficient to provide the Congress ample time within which to determine upon the comprehensive program of welfare reform that would coordinate the "needs" programs with the federal income tax system and with the primary retirement systems such as OASDI, railroad retirement and civil service.

[17] See Col. 5 of Table XI in the Appendix. The referred amounts for different income categories projected as percentages of "adjusted gross income" tend to support the disproportionate distribution we expect.

scribed manner. However, as an additional feature of its economic-energy package, the Administration has proposed the imposition of an absolute five-percent limitation for one year on cost-of-living increases otherwise applicable with respect to these programs.[18]

Our Associations reiterate what we said at the White House Inflation Summit last autumn: "We will vigorously oppose any reduction in benefit payments from, or any delays in scheduled cost-of-living increases under, income maintenance programs such as OASDI and SSI."

F. RATIONALE FOR THE ADMINISTRATION'S ENERGY PROPOSALS

Not only are we opposed to the structure of the Administration's program, but we are unpersuaded by the rationale for it. While our Associations believe that it is important to provide the price and profit incentives necessary to expand domestic production of oil and gas, we also believe that excessive concentrations of market power in these interrelated industries may produce high prices and profits without any reasonable supply response unless policies designed to restore workable competition to these industries are undertaken simultaneously.

With imported, "new" domestic and "old" domestic oil selling in the marketplace at about $12, $11, and $5.25 per barrel respectively, and with oil industry profits at record levels, we do not believe that immediate higher prices are justified or necessary as a stimulus to increase domestic production. Moreover, with constraints in the capital goods markets, higherpricesfordomestic
over, with constraints in the capital goods markets, higher prices for domestic
oil will add nothing to the supply incentive but will add to inflationary pressures within the economy.

With respect to natural gas, our Associations have already expressed our support for the Natural Gas Production and Conservation Act. We feel that it will provide adequate price incentives to elicit the natural gas supply increments necessary to eliminate the current shortage while simultaneously continuing price ceiling regulation to prevent oligopolistic pricing practices.

In order to promote competition, facilitate entry into the oil and gas market and thereby increase domestic production to ultimately moderate the current high prices of domestic fuel, our Associations have expressed support for legislation to break up the vertical integration existing in these industries and prevent control over multiple energy energy. Concomitantly, we have urged the establishment of an independent public corporation to explore for and develop oil and natural gas reserves in the federal domain in order to stimulate competition and provide a much-needed yardstick with which to measure profits, costs, and production techniques. Furthermore, we believe that it will be necessary for the Department of the Interior to substitute a "royalty bidding" policy for its present "bonus leasing" procedures which tends to preclude entry into the federal offshore production areas by small producers. Finally, the Congress must prohibit the practice of extending off shore leases beyond five years after original lease sales without requiring production and assure that forfeiture is strictly enforced.

It is the failure of higher prices for domestic oil and gas to elicit a reasonable supply response that indicates to us an absence of workable competition and excessive market power in the hands of a few corporate entities. In a market dominated by a few producers, where cooperation rather than competition prevails, the principles that operate in competitive markets do not apply. In an oil-gas oligopoly, higher prices for gas are likely to be used to justify even higher prices for oil, coal, and other energy products—thus accelerating the current inflation and generating precisely those disastrous consequences for the poor and fixed-income aged that our Associations seek to avoid.

Producers and the Administration seem to agree that the artificial prices established for OPEC oil should be used as the basis for new natural gas and old domestic oil prices. Since it is the cost of finding, developing, and producing gas and oil that should be determinative of field prices, this argument is further indication of industry non-competitiveness. It is the cost of production (plus the going rate of return) that is the basis for a competitive supply price.

The higher energy prices that the Administration is seeking would restrain demand, but would not likely be driven back down over the long run because of the substantial barriers to energy market entry. Extra high prices and profits would likely continue with no reasonable supply response.

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[18] See Table XII in the Appendix for the programs to which the limitation would apply.

Our Associations urge that in considering policies designed to reduce energy demand and increase domestic energy supply, the Congress reject the Administration's proposed program and the false assumptions upon which it is founded and proceed to develop a comprehensive program of its own.

G. A REASONABLE POLICY TO REDUCE ENERGY DEMAND

In order to decrease the domestic demand for foreign imported petroleum and refined oil products, the prices for which are administered (set without reference to world supply and demand) by the OPEC nations, our Associations have examined six basic policy options: (1) import tariffs on oil and oil derivatives; (2) import quotas; (3) a mandatory allocation system for oil products; (4) removal of domestic price controls from "old" oil; (5) taxes on gasoline and automobiles; and (6) gasoline rationing.

We have concluded that a reasonable policy response to excess reliance on artificially priced foreign petroleum imports should include: (1) a phased-in, graduated excise tax on new and used automobiles and pleasure craft (based on vehicle weight and horsepower); (2) a white market gasoline rationing system or a rebatable gasoline tax; (3) a stand-by, mandatory fuel allocation scheme; and (4) if necessary, an import quota.

1. Policy options with direct consumer impact

Since the automobile accounts for over 50 percent of fuel consumption in the transportation sector, which itself consumes 25 percent of all energy, a reduction in gasoline consumption (where demand is relatively more elastic) would do more to reduce petroleum consumption, and would do it with less consumer and economic hardship, than reduction in the consumption of any other petroleum product. We therefore support the following combination.

First, we urge the imposition of a steeply-graduated excise tax on automobiles (including used automobiles) and pleasure craft on a basis of weight and horsepower in excess of minimum prescribed levels. We believe that vehicle engine efficiency must be monitored and that mileage standards must be prescribed for new automobiles until they reach, by 1980, a required minimum average of 25 miles per gallon on the range of automobiles offered for sale by a manufacturer. If the choice is between less size, comfort and "extras" in the automobile or less heat in the home, our Associations would prefer the former. The longer a shift to fuel-efficient automobiles is delayed, the more difficult will be the task of managing future fuel shortages.

Second, our Associations would be prepared to support either a white-market gasoline rationing program or a properly-designed gasoline tax with redistribution of revenues. While we prefer the former, we recognize that they both can be made to be equally equitable.

A simple, across-the-board distribution of rebates from the tax or of coupons under the rationing program to all adult persons seems to us to be the only fair approaches.

While we believe that a rebatable gasoline tax or a white-market gasoline rationing program is clearly preferable to less direct forms of demand reduction (although a mandatory allocation scheme must be devised and kept on a stand-by basis for use in case of an emergency) we agree that either of these policy options could be used in combination with an import quota. If the direct options are not enough, such a quota should be added.

2. Mandatory fuel allocation

Our Associations believe that a stand-by, mandatory fuel allocation program must be established in order to deal with any emergency shortage of petroleum and petroleum products. The goal of such a system is, of course, to distribute resources geographically and among various sectors of the economy in order to insure that all share the shortage in a reasonably equitable manner. While we believe that such an allocation system must always be ready, we also believe that to the extent that other conservation options work, an oil allocation system will not be needed. If oil demand can be reduced by taxes or rationing, no shortages need develop; the traditional supply and demand distribution of the market would be entirely adequate. However, should an oil embargo precipitously cut oil imports, a stand-by allocation program is necessary to distribute resources until other tax and/or rationing policies can be established.

3. An import quota

With respect to an import quota, which would restrict the amount, either in quantitative or monetary units which may be imported, the result of such a quota system would, standing alone, mean an increase in domestic energy prices to that level where domestic supply and demand balance, given the fixed quantity of imports. The presence of price ceilings with respect to some domestic oil could cause shortages such as occurred during the winter of 1973–74 or require allocation of petroleum products.

To us, it seems that an import quota can only be a sensible policy option when combined with some other energy-conserving policy option such as a rebatable gasoline tax or a gasoline-rationing scheme. However, a quota on imported oil is a good way to guarantee that energy saving is realized in terms of decreased domestic production.

4. Other considerations

In selecting a policy option or a combination of options, the Congress must take into account a number of moderating factors. First, in considering a desired level of reduction in imports of foreign petroleum and petroleum products, the Congress should take into account the impact of any such reduction on the available supply of fuel and the rates of inflation and unemployment.

Second, it must also consider the impact of any excise tax on automobiles and any rebatable gasoline tax or rationing scheme on the depressed condition of the automotive industry. It might be desirable to phase-in such taxes and/or rationing system over a period of time during which stimulative fiscal and monetary policies could take effect and revive the depressed automobile industry.

Third, regulations with respect to any fuel allocation or rationing system, if instituted, must be sufficiently flexible to permit consideration for the needs of the aged and the poor and to provide waivers in circumstances where health and special needs require. (Regulations should clearly spell out a simple procedure whereby persons in voluntary organizations with special needs can apply for increased allocations or rations of fuel, with reasonable appeals procedure.)

In order to further perfect the energy demand reduction program, our organizations believe it desirable to prepare and promulgate thermal efficiency standards for new buildings and structures renovated with the assistance of federal funds or loan guarantees. We also believe that the Department of Housing and Urban Development should be authorized to provide low-cost loans for housing insulation and that the Department should develop special energy conserving designs for HUD-assisted housing.

Finally, we believe that the energy efficiency of home appliances should be monitored and that these appliances should be labeled accordingly.

H. CONCLUSION

In conclusion, our estimates of the Administration's energy, tax relief and budgetary proposals are as follows.

First, the energy proposals will mean substantially higher prices for fuel which will result in a substantial increase in direct consumer costs. The burden of these increased costs will devolve disproportionately on the poor and fixed-income aged. Second, higher prices for fuel will percolate through the economy and accelerate the 1975 projected rate of inflation and virtually assure a repetition of the double-digit inflation experienced last year. Third, the Administration's tax relief proposals would benefit, not the poor and fixed-income aged, but higher income groups.

Finally, the proposed 5 percent limitation on cost-of-living adjustments in the primary retirement and welfare systems would reinforce the increasingly desperate situation of our constituency.

The poor and fixed-income aged have suffered a great deal from the inflation-recession experienced during 1974. The income maintenance systems upon which they depend for a substantial portion of their income are threatened by this combination. The Administration's program will aggravate their situation and the situation of those systems. Last year's hardships for these consumer groups will be exacerbated.

In the giant shell game that is the Administration's energy, tax-relief and budgetary proposals, the poor and the fixed-income aged will be very big losers. Our Associations therefore urge the Congress to reject these proposals, to take the initiative in developing a comprehensive economic and energy program that takes into account the interests of all population groups, and to enact that program even over the flurry of Executive Branch vetoes that must be anticipated. In these efforts, Congress will have the aide and counsel of our Associations and the nearly 8 million persons they represent.

TABLE I.—FIFTHS OF FAMILIES RANKED BY SIZE OF MONEY INCOME BY AGE, 1952, 1962, AND 1972

FAMILY INCOME

Age of head in years, total in years	Total			Lowest fifth			2d fifth			3d fifth			4th fifth			Highest fifth			Top 5 percent		
	1952	1962	1972	1952	1962	1972	1952	1962	1972	1952	1962	1972	1952	1962	1972	1952	1962	1972	1956	1962	1972
Total	100.0	100.0	100.0	100.0	100.0	100.0	100 0	100 0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
14 to 24......	5.2	5.5	7.7	7.1	8.4	13.2	8.0	8.5	12.4	6.0	6.0	7.5	3.7	3.4	3.8	1.3	0.9	1.6	0.3	0.2	0.5
25 to 34......	23.6	19.3	22.0	13.8	13.5	17.1	26.1	21.9	23.7	29.5	26.3	27.7	28.7	22.4	24.5	19.7	12.7	16.8	9.2	7.3	9.4
35 to 44......	23.8	24.4	19.7	15.7	14.8	11.7	22.2	20.8	16.0	25.2	26.0	21.0	28.4	30.8	24.3	27.7	29.3	25.6	24.8	26.7	24.5
45 to 54......	19.8	20.8	20.7	16.1	14.1	11.7	17.0	17.3	14.9	18.6	18.9	19.4	21.0	22.8	25.8	26.5	30.9	31.7	29.7	33.1	36.3
55 to 64......	14.6	15.6	15.9	17.2	14.9	13.5	14.0	14.4	15.3	12.9	14.7	16.4	11.9	14.7	16.0	17.0	19.0	18.4	25.2	22.4	22.6
65 years and over.......	13.0	14.5	14.0	30.1	34.3	32.8	12.7	17.1	17.6	7.8	8.0	7.9	6.4	5.9	5.6	7.9	7.2	5.9	10.9	10.2	6.8

Source: U.S. Bureau of the Census, Current Population Reports, Series P-60, No. 90, "Money Income in 1972 of Families and Persons in the United States," U.S. Government Printing Office, Washington, D.C., 1973, p. 40.

The Consumer Price Index makes no distinction among subgroups, assuming that all consumers, rich and poor, consume the same market basket of goods and services. This is obviously not the case, for the rich by choice spend a higher proportion of their income on luxuries, while the poor have no choice but to spend a higher proportion of their income on such necessities as food and shelter. In order to assess the impact of inflation on such dissimilar groups of consumers, it is necessary to develop price indices based on the different market baskets that are consumed.

Such market baskets were developed in R. G. Hollister and J. L. Palmer's analysis of "The Impact of Inflation on the Poor." They created market baskets for both rich and poor families from the 1960–61 Survey of Consumer Expenditures, which in turn were used to fashion both a Poor-Person's Price Index (PPI), and a Rich-Person's Price Index (RPI), that approximate the true price indices for these different groups. These market baskets are split into eight major categories, with the importance of each category to the rich and poor consumers identified in the following Table.

TABLE II.[1]—WEIGHTS OF MAJOR CATEGORY EXPENDITURES

Item	Poor persons' index	Rich persons' index
Food	0.349	0.219
Housing	.356	.278
Apparel	.078	.118
Transportation	.051	.160
Medical care [2]	.058	.062
Personal care	.033	.027
Recreation	.034	.077
Other	.041	.059

[1] J. Eco. Com., "Inflation and the Consumer in 1973, 93d Cong., 2d sess. 34-35 (1974).
[2] For the aged, the weight for medical care would generally be higher.

TABLE III.[1]—SHARES OF AGGREGATE INCOME

Income	Social security	Earnings	Private pensions	Public pensions	Asset income	Other
MARRIED MEN AND THEIR WIVES, 1970						
$500 to $1,499	82	8	1	1	4	3
$1,500 to $2,499	69	16	2	2	6	5
$2,500 to $3,499	57	21	7	3	8	4
$3,500 to $4,499	48	22	12	6	9	4
$4,500 to $5,499	40	25	14	6	10	4
$5,500 to $6,499	34	27	17	6	12	5
$6,500 to $7,499	29	27	18	8	13	4
$7,500 to $8,499	25	31	17	10	13	4
$8,500 to $9,499	23	33	18	8	14	4
$9,500 to $12,499	17	39	15	7	16	5
NON MARRIED MEN, 1970						
$500 to $1,499	77	8	0.005	1	4	10
$1,500 to $2,499	62	15	3	3	6	12
$2,500 to $3,499	46	19	10	6	9	11
$3,500 to $4,499	37	18	19	8	9	8
$4,500 to $5,499	29	18	26	9	12	6
NON MARRIED WOMEN, 1970						
$500 to $1,499	77	9	1	1	4	7
$1,500 to $2,499	62	16	4	3	8	8
$2,500 to $3,499	45	23	9	5	8	8
$3,500 to $4,499	35	25	14	7	13	6
$4,500 to $5,499	29	23	14	11	17	6
$5,500 to $6,499	23	24	12	14	23	5

[1] Social Security Administration, Office of Research and Statistics, "Preliminary Findings from the Survey of New Beneficiaries," report No. 10 (June 1973).

TABLE IV.[1]—ESTIMATED ACTUARIAL BALANCE[2] OF OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE SYSTEM AS PERCENT OF TAXABLE PAYROLL,[3] DYNAMIC ASSUMPTIONS[4]

Item	OASDI	DI	Total
Average cost of system	11.97	1.92	13.89
Average rate in present tax schedule	9.39	1.52	10.91
Actuarial balance	−2.58	−.40	−2.98

[1] 1974 Trustee Report on OASDI, H.R. Doc. No. 313, 93d Cong., 2d sess. (1974).
[2] As measured over the 75-year period, 1974–2048.
[3] Payroll is adjusted to take into account the lower contribution rates on self-employment income, on tips, and on multiple-employer "excess wages" as compared with the combined employer-employee rate.
[4] See text for a description of the assumptions.

As the following table shows, the decline in real disposable income during the current recession is almost twice as large as that which occurred during any other post-war recession.

TABLE V.[1]—CHANGES IN INCOME AND TAX BURDENS DURING POSTWAR RECESSIONS

Recession years	Percent decline in real disposal income[2]	Taxes as a percent of personal income: Including Government transfer payments		Excluding Government transfer payments	
		Peak	Trough	Peak	Trough
1948–49	−1.9	10.4	9.5	11.0	10.1
1953–54	−.7	14.2	13.2	14.9	14.0
1957–58	−1.3	13.8	13.4	14.7	14.4
1960–61	−.7	14.6	14.5	15.7	15.8
1969–70	−.8	18.1	16.9	19.8	18.8
1973–74	−3.1	17.8	18.4	19.9	20.8

[1] Source: Bureau of Economic Analysis, Department of Commerce.
[2] Percent changes based on those quarters during which peak and trough months occurred, as defined by the National Bureau of Economic Research.

TABLE VI.—CURRENT ENERGY COSTS WITHOUT THE PRESIDENT'S PROGRAM[1]

	Poor average, $2,500	Lower middle average, $8,000	Upper middle average, $14,000	Well-off average, $24,500
Gasoline	$140	$349	$627	$736
Heating oil	66	66	66	83
Natural gas	91	108	117	140
Electricity	160	203	259	319
Coal	16	16	16	16
Total	473	742	1,085	1,294
Percent of average income	18.9	9.3	7.8	5.3

[1] Source: WCMS Survey for 1972–73, adjusted for price increases to September 1974.

TABLE VII.—ENERGY COSTS WITH PRESIDENT'S PROGRAM[1]

	Poor	Lower middle	Upper middle	Well off
Gasoline	$166	$415	$746	$876
Heating oil	83	83	83	105
Natural gas	120	142	154	184
Electricity	170	215	275	338
Coal	16	16	16	16
Total	555	871	1,274	1,519
Percent of average income	22.2	10.9	9.1	6.2

[1] Estimated by applying percent price increases for each type of energy from table 1 to the energy costs in table 3.

TABLE VIII.—NET ENERGY COSTS OF PRESIDENT'S PROGRAM

	Poor	Lower middle	Upper middle	Well off
Average increase in energy costs	$82	$129	$189	$225
Average rebate	97	311	253	183
Net energy costs	458	560	1,021	1,336
Percent of average income	18.3	7.0	7.3	5.5

TABLE IX.—RETURNS WITH AT LEAST 1 TAXPAYER AGE 65 OR OVER: ADJUSTED GROSS INCOME, TOTAL DEDUCTIONS, EXEMPTIONS, TAXABLE INCOME, AND TAX ITEMS BY MARITAL STATUS, SEX, AND AGE

[All figures are estimates based on samples—data are in thousands]

Marital status, age exemptions by sex of taxpayer	Number of returns (1)	Adjusted gross income (2)
All returns, total	6,761	$55,265,581
Joint returns of husbands and wives, total	3,847	37,731,364
Both 65 or over	1,909	18,629,417
Man 65 or over; woman under 65	1,647	16,178,292
Woman 65 or over; man under 65	291	2,923,656
Separate returns of husbands and wives, total	125	657,216
Men	77	408,191
Women	47	249,025
Returns of heads of households, total	125	949,635
Men	47	373,726
Women	78	575,909
Returns of surviving spouses, total	22	101,234
Men	7	60,173
Women	14	41,061
Returns of single persons, total	2,643	15,826,131
Men	670	4,397,537
Women	1,973	11,428,594

TABLE X.—ALL RETURNS AND RETURNS OF TAXPAYERS AGE 65 OR OVER, 1969, 1970, AND 1971

[All figures are estimates based on samples—data are in thousands]

Item	1969 (1)	Percent change, 1969-70 (2)	1970 (3)	Percent change, 1970-71 (4)	1971 (5)
All returns, total	75,834	−2.0	74,280	+0.4	74,576
Taxable	63,721	−6.9	59,317	+1.0	59,916
Nontaxable	12,113	+23.5	14,962	−2.0	14,680
Returns of taxpayers age 65 or over, total	7,181	−3.7	6,913	−2.2	6,761
Taxable	4,637	−4.0	4,452	+1.2	4,507
Nontaxable	2,544	−3.3	2,461	−8.4	2,254

TABLE XI.—EFFECT OF THE TAX REFUND—ILLUSTRATED FOR A FAMILY OF 4

Adjusted gross income	Present tax	Proposed refund	Percent saving	Percent of adjusted gross income
$5,000	$98	$12	−12.0	−0.24
7,000	402	48	−12.0	−.68
10,000	867	104	−12.0	−1.04
12,500	1,261	151	−12.0	−1.21
15,000	1,699	204	−12.0	−1.36
20,000	2,660	319	−12.0	−1.60
40,000	7,958	955	−12.0	−2.39
50,000	11,465	1,000	−8.7	−2.00
60,000	15,460	1,000	−6.5	−1.67
100,000	33,340	1,000	−3.0	−1.00
200,000	85,620	1,000	−1.2	−.50

TABLE XII

Programs affected	Outlays	Ceiling	Ceiling	Difference 1975-76 (with ceiling)
Social security	64.5	74.3	71.8	+7.3
Railroad retirement	3.0	3.4	3.3	+.3
Supplemental security income	4.7	5.5	5.4	+.7
Civil service and military retirement payments	13.5	16.2	14.9	+1.4
Foreign service retirement	.1	.1	.1	(1)
Food stamp program	3.7	3.9	3.6	−.1
Child nutrition	1.3	1.8	1.6	+.3
Federal salaries:				
Military	23.2	23.1	22.5	−.7
Civilian	35.5	38.9	38.0	+2.5
Coal miner benefits	1.0	1.0	1.0	(1)
Total	150.5	168.2	162.1	+11.7

1 Less than $50,000,000.

TESTIMONY OF JOHN G. BUCKLEY, VICE PRESIDENT, NORTHEAST PETROLEUM INDUSTRIES, INC.

My name is John G. Buckley. I am a Vice President of Northeast Petroleum Industries of Boston and a Vice President and Director of Energy Corporation of Louisiana (ECOL) a joint-venture between Northeast Petroleum and the Ingram Corporation of New Orleans, Louisiana. ECOL is presently building a 200,000 barrels daily fuel-oriented refinery on the Mississippi River about 85 miles up-river from New Orleans. I am a former Fuel Oil Chairman of the National Oil Jobbers Council and currently on the Steering Committee of the Fuel Committee of NOJC. I am also a member of the Utility Advisory Committee to the Federal Energy Administration, Washington, D.C. and a member of the Emergency Petroleum Supply Committee of the National Petroleum Council. During the past eighteen months I have visited almost all of the major oil producing countries around the world to negotiate crude oil contracts for our Louisiana refinery. I have met with and have had many discussions with Oil Ministers and other oil and financial officials from these countries and believe I have some understanding of their goals and aspirations at this time.

Senator Long, I would like to start by thanking you for the leadership you have displayed on this critical matter of energy policy during the past several weeks since President Ford announced the Administration's energy plan. Of course, your concern in this area is one of long standing and we independent companies understand and appreciate the role you have played in trying to assure more equitable treatment from national oil policy for the independent sector of the oil industry nationwide. Your hearings here this morning in Washington are just another example of your concern and continuing effort to make sure that this nation does not pay a disproportionate price for the achievement of a questionable objective. Clearly the cost of achieving national objectives should be borne equally by the nation.

In my statement this morning I should like to divide my comments into two parts:

The first dealing with aspects of the Administration's program which I believe deserve support and implementation by appropriate action by the Congress; and the second dealing with those parts of the Administration's program that I believe will be inimical to New England and to the nation as a whole.

On the positive side I strongly support the following points:

1. Development of strategic storage capacity designed to enable us to react quickly to offset the disruptive force of any future embargo, cutoff or curtailment of foreign petroleum supplies.

2. The production of oil from the Naval reserves at Elk Hill in California and the use of some of that oil in filling government-owned strategic storage facilities.

3. The establishment of tougher codes of insulation coupled with tax credits to promote residential and commercial insulation in order to cut waste.

4. The establishment of appliance efficiency standards.

5. Standby authority under which this Administration or future Administrations could react quickly in the event of an embargo situation, including standby rationing authority.

6. The development of incentives, tax and otherwise to transform or shift the emphasis in the automotive industry to the production of more efficient automobiles with better miles per gallon performance.

7. Increased federal effort in research and development of alternative energy sources.

All of these measures have something in common. In combination they tend to eliminate energy waste in our society and effectively conserve available energy resources. Moreover, they are long-term in nature and not designed as a "quickie" solution to energy problems.

I would now like to turn to other parts of the Administrations' program on energy and list, if I might, some of the myths and inconsistencies in the high energy cost approach to achieving certain national energy objectives. These negative comments will fall in two categories, the first dealing with our current economic situation and the second dealing with the more fundamental and philosophical question of our future foreign economic and political policy world-wide.

1. The Administration's energy program is touted as a policy, which when coupled with the Administrations' tax relief policy, will have an expansionary impact on our general economic situation this year. In fact, a detailed analysis of the combined effect of both the tax and energy proposals shows that the positive contribution of the tax rebate and tax restructuring is more than offset by the cost of the energy program. The Research Office of the New England Congressional Caucus notes that the combination of tariffs and fees on imports coupled with price decontrol and new taxes on oil and gas will take between $44 to 54-billion out of the economy. The Library of Congress research study puts the energy bill at just over $50-billion annually. The point is the Administration's tax proposal looks to tax relief in the neighborhood of $24-billion. Therefore, the net effect of the total Administration tax and energy program would be, if enacted, a $20–30-billion economic drag this year. Thus, we could end up with a $45-billion federal deficit, more recession and more inflation simultaneously. This is certainly not a prescription to help the United States economy at the present time.

On the human side unemployment nationally would have to rise probably to 9% or 10%. In New England the rates would be higher—much higher—with regional unemployment perhaps at 12% and in some states, like Massachusetts, ranging from 12% to as high as 15%. This is simply too high a price to pay for the achievement of narrowly defined energy objectives.

2. The Administration's energy package, drawn liberally from the computer projections in the FEA's Project Independence Report, takes far too narrow a view of both our own domestic economy and our economic role in the world economy. The goal of the Project Independence study was to reduce oil imports. The Administration seems to be following a policy designed to achieve that objective at any cost, even at the cost of ruining our national economy.

In contrast to this narrow Administration approach the Organization for Economic Cooperation and Development (OECD) has just completed a study on energy objectives for its member countries which, refreshingly, notes that "energy is not the only thing in the world that is important." The study, citing a capital investment requirement of over $2-trillion needed to achieve a high rate of energy self-sufficiency in the member countries, states that such an effort would mean a very large shift of resources into the energy sector. This, the study says "may be in conflict with other economic objectives and may consequently be undesirable."

In fact, the Administration's energy proposal would cost our economy $50-billion annually in increased energy costs—and perhaps $75-billion if the "ripple effect" of higher prices for other products based on energy is included. It represents a commitment to divert some $750-billion of purchasing power over the next decade into high-cost energy. In addition, the capital investment required would amount to some $750-billion to $1-trillion over the same decade. With that kind of resource commitment coupled with our military budget, it is hard for me to see how any other social economic or environmental objectives can be met during the next ten years.

3. The Administration's plan, stripped of rhetoric, boils down to putting the United States' energy economy across the board on a price basis of the present level of OPEC prices (Organization of Petroleum Exporting Countries), plus freight to U.S. ports, plus $2.00 a barrel. This means that all new natural gas, all domestic petroleum and all imported petroleum will be priced at approximately $14.00 per barrel. Inevitably, since there are no price controls applicable, coal prices will rise to roughly the same level.

One of the goals of the Administration's new energy proposal is to drive down OPEC prices. Yet by the establishment of this "high cost energy program" the United States will be unable to benefit from such lower OPEC prices, even if they are achieved. Part of the Administration's plan calls for standby authority for the President to establish quotas and tariffs apart from those already in place in order to ensure a "floor" price so that companies investing in petroleum, natural gas, shale, liquification or gasification of coal and other alternate energy supplies will be able to receive an appropriate return on their investment. Thus our economy would be insulated from lower foreign prices and would be permanently trapped into a posture of accepting higher energy costs than any other industrial country in the world. Obviously, our competitive ability will be seriously damaged, our export trade curtailed and our balance of payments plunged into deficit year after year. In effect, the Administration is calling for a policy to break OPEC prices while at the same time putting the country in a position in which we alone among industrialized countries will be unable to benefit from lower OPEC prices if they are achieved.

I would now like to turn to a number of myths, misstatements and misunderstandings relating to United States' energy policy and its interaction with OPEC. As indicated earlier one of the objectives cited by the Administration in pursuing its new energy policy is to break the OPEC cartel and cause OPEC prices to decline. Another stated objective is to destroy OPEC's ability to do "significant economic damage" to industrial economies. We shall examine these two points in detail later.

Another thought that has received wide circulation in recent weeks is the myth that OPEC's accumulation of capital will put it in a posture to undermine the world currency structure, take over all the stock listed on the New York Exchange, or in other ways prove to be so large that the existing financial system will be unable to manage the flow of funds. As a corollary to that thought is the theory that we here in the United States cannot absorb the increased OPEC prices without a crippling impact on our economy. We also hear economists and others testifying recently in Washington that the establishment of a Federal government importing authority or the use of sealed bids will somehow break the Arab cartel—or what is called the Arab cartel rather than the OPEC cartel.

There is one final myth that permeates all the rest, that is the oft-repeated assertion that the current OPEC price problem is a separate issue and not related to the question of a Middle East peace settlement. All of these various myths and misunderstandings are creating an emotional climate in Washington and in the nation which could lead us to policies less than rational. They deserve to be analyzed and commented on one by one.

I would now like to turn to a number of myths, misstatements and misunderstandings relating to United States' energy policy and its interaction with OPEC. As indicated earlier one of the objectives cited by the Administration in pursuing its new energy policy is to break the OPEC cartel and cause OPEC prices to

decline. Another stated objective is to destroy OPEC's ability to do "significant economic damage" to industrial economies. We shall examine these two points in detail later.

1. To understand the world as it is we must first make a more realistic assessment of OPEC in order to grasp how limited our unilateral options really are. We must understand that within OPEC there are two groups of countries. The first group—the non-Arab countries—is made up of relatively densely populated countries with high unemployment and a strong desire to industrialize. This group includes countries like Venezuela, which has already embarked on a massive long-term industrialization program; Iran, with some 26-million in population (and high unemployment) which has in place an overt government program to use all available crude oil to build new refining capacity and petrochemical facilities in Iran itself; Indonesia with over 100-million in population, and Nigeria the most populous of African countries with some 60-million people, both developing countries keen to see economic progress and a better living standard. All of these non-Arab nations believe that current price levels are not too high and that, indeed, it is about time they received a more equitable share of wealth from their natural resources, such as petroleum. I can tell you from personal experience that it is difficult for officials in such countries to identify and sympathize with what we call "sacrifices" such as turning down the thermostat a few degrees or buying a smaller car when they note the poverty, hunger and survival-oriented existence of most of their own citizens.

The second OPEC group—which includes most of the main Arab producing countries—do not have large populations and are now receiving revenues far in excess of their ability to absorb such revenues in domestic industrial development. It is this group which has a far higher degree of self-interest in making sure that the current high price level of petroleum does not drag Western Europe, Japan and the United States into a severe economic recession or depression. Such countries would much prefer industrial countries to have strong, viable, growing economies in which to invest their surplus funds. In short, it is these Arab nations to whom we must look for help in bringing down current OPEC price levels. It is also the same Arab countries who despite their economic self-interest, simply are not in a position to reduce price sharply until and unless there is a just Middle East settlement.

2. Returning now to another of the myths and misunderstandings expressed above, I would like to comment on the oft-stated position that the key to bringing down OPEC prices is increased production and reduced consumption in the United States. We, in fact, have only a marginal impact on OPEC price decisions. Clearly, insofar as the Arab producers are concerned the United States has never been an important market. We prevented them from selling much of their oil here all through the 1960's under our mandatory oil import quota system. The Arab nations are currently producing some 18-million barrels daily of crude oil of which we import about 1-million barrels daily. We are, at best, a 5% or 6% market. I repeat, the U.S. only buys about 5% of Arab oil production. Besides, even if we succeed in cutting oil imports most of the cuts will be imports from non-Arab countries. As you know, whether we like it or not, Canada has already decreed that it is phasing out its exports of crude oil to the United States. These exports, which were approximately 1-million barrels a day a little over a year ago, are now due to drop to 650,000 barrels daily by July 1975 and to be phased out altogether by the end of the decade. Moreover, additional cuts in imports will be likely first to back out Venezuela, Indonesian and Nigerian oil rather than Arab oil because prices for these oils are higher than prices for Middle East Arab oils.

In short, the theory that what we do here in energy policy can dramatically alter Arab pricing decisions is just that—a theory which fails to recognize political facts. No sealed bid system, no creation of a government purchasing agent to handle all imports can possibly bring about the desired results. In fact, the creation of such a government entity would do much to undermine the flexibility we now have in meeting emergency situations and would end for all time the ability of our independent companies, both marketers and refiners to negotiate lower competitive prices from foreign refiners and crude oil producers. Further, the creation of a government purchasing agency would just about end the ability of independent companies to finance new refinery capacity.

3. I would now like to comment on the theory that the United States cannot absorb higher OPEC prices without critically damaging our economy and balance

of payments. Again, an analysis of our balance of payments shows this argument to be fallacious. For the calendar year 1974 just ended the United States did indeed show a staggering increase in costs for oil imports. These rose from somewhere in the neighborhood of $7- to 8-billion (in 1973) to $24-billion for the year 1974. But at the same time our exports also rose dramatically so that by year end total imports were valued at just over $100-billion while exports stood at $97-billion. This caused a $3-billion balance of payments deficit—not a small number. But had it not been for the drought in the mid-west and as a result, poorer agricultural exports than expected, we could well have had a balance of payments surplus despite the rapid escalation of foreign oil prices. My point is this—this economy is so large and our export potential is so great that higher oil prices are not going to bankrupt us. In fact, in one short year—a year when the price for foreign oil was tripled—we have already shown that we can offset these added costs through additional exports. Moreover, it seems clear that as the oil producing countries develop and maintain a high level of revenues from their oil sales in the future, there is created an exciting growth market for additional exports of American managerial, financial, technical, and manufacturing skills as well as a growing market for U.S. agricultural products. Another way to look at the transfer of $100-billion annually to OPEC countries which is occurring at the present time is to look at it as a growth opportunity for U.S. business and agriculture.

4. Another popular misconception relates to the world financial institutions' ability to manage the transfer of funds that are occurring and the oft-stated fears that "the Arabs" will take over the entire world economy. It is popular to note that at current stock market prices within a certain number of years the OPEC nations could buy out the whole New York Stock Exchange and own every major corporation in the United States. These simplistic and naive assertions are obviously designed to stir fear. But they are not valid.

In fact, the Administration itself has now recognized that the build-up of dollars and hard currencies in OPEC nations in the years ahead will be much lower than previously estimated. I attach a copy of an article from the New York Times of Friday, January 31, 1975 quoting Secretary of Treasury, William Simon's testimony in connection with a new and sophisticated economic analysis by the Treasury Department of the expected accrual or accumulation of funds in the OPEC countries. Mr. Simon stated that the producing countries might accumulate $200–250-billion by 1980, an amount which would level out and then decline after 1985. Mr. Simon concluded that ". . . there is not reason that the accumulation of substantial debt by oil importing nations to oil exporters need undermine either the solvency or the liquidity of oil importers as a group". Mr. Simon also stated that these new estimates ". . . support the view that the international financial aspects of the oil situation are manageable."

5. I would now like to comment on the Administration's twin objectives of insulating the U.S. from OPEC's prices and reducing and eventually eliminating the power of OPEC countries to cause significant economic damage.

I would say as a general comment, that these objectives cannot be achieved until or unless there is a Middle East peace settlement. The whole thrust of the Administration's policy, the achieving of "Project Independence", the emphasis on "national security" and the goal of becoming "invulnerable" by 1985 harks back in many ways to the economic isolation policies of the 1930's. It seems to me that its emphasis on reducing Arab oil imports was conceived in semi-panic and is dedicated to the proposition that we can turn back the clock. I don't deny that the Project Independence exercise may have developed some data that will be helpful in forming a cohesive national energy policy. But as for achieving the twin objective of "insulating" ourselves from OPEC or "eliminating the power of OPEC to cause significant economic damage"—that's just wishful thinking. In short, no matter how sophisticated the technical analysis, no matter how keenly we assess the computer runs, what faces us is essentially a political problem.

It is completely unrealistic for us to look at our exposure—our ability to be independent—in the context of how many barrels a day we can cut oil imports now brought from Arab countries. That is far too narrow a context. No matter what we do, Europe and Japan cannot escape overwhelming dependence on Arab oil to fuel their basic economies for the next decade. Of our total energy supply only 43% is represented by petroleum and only a little more than a third of that is imported. Thus, a maximum of only about 15% of our total energy supply would be directly affected by another oil embargo or other actions by OPEC countries to deny us oil supplies. Europe and Japan, on the other hand, depend on petroleum for 60 to 80% respectively of their total energy use. Moreover, almost all of their petroleum needs are covered by imports. They have long ago built strategic stock piles of oil through a "security" storage program. Thus, Europe, and to a lesser extent Japan, can weather short-term interruptions in oil supplies. But there is no way they can do without Arab oil for any period exceeding a few months short of virtually closing their economies down tight.

Given the interdependence of our economy with those of the European countries and Japan, their vulnerability is our vulnerability. There was a time just after World War II when the popular expression was if the United States catches a cold Europe catches pneumonia. That situation has changed. Now, if they catch pneumonia we do too.

It follows that we must move forward towards a Middle East peace settlement as a first priority. Only then can we hope to negotiate lower OPEC prices. Only then can we, as the world's most skilled, diverse and technically accomplished economy, expect to earn back more dollars than we spend for petroleum imports.

There must be some recognition that this is not 1967 or 1956. The world has changed. We do not have the unilateral options we had then. And we won't have them in this decade. The golden period of roughly 25 years after World War II when the United States could afford the luxury of doing about whatever it wished to do internationally is over.

In fact, looking realistically at the world and our position in it we must conclude that the United States is today living in an interdependent world economy. The Administration, however, seems to be approaching this truth in a compartmental way. It seems to be divided into two groups, one representing the energy and economics sector and a second dealing with political questions. Senator, I suggest that the politics and economics of the Middle East are about two facets of one problem and neither can be isolated or viewed in isolation. European countries and Japan recognize this, as do the oil producing countries themselves. For the United States to keep insisting that these are two separate problems is a head in the sand attitude. We must start dealing with the factual situation that exists and as a first priority we must get on with solving the basic political problems—achieving Middle East peace.

We cannot achieve security or independence by fiddling with the number of barrels per day of oil we import. No number of new FEA computer runs will change the situation one iota. By recognizing that fact one other fact also becomes clear—that is the foolishness of pursuing a course of "confrontation" with OPEC.

We, and other industrial countries need a certain volume of oil. The producing countries, for their part, want to diversify their economies and improve their standards of living. Between these two groups cooperation can yield a higher level of world trade and a growth in mutual interdependence. This is far the preferable course to confrontation.

One other disturbing thought is the suggestion by the Administration that we must move now—that every day we delay is a day that increases our vulnerability.

With all due regard to the need for action, what you are looking at in Congress is an energy plan that commits our country to a basic course of action for the next 10 to 20 years. You must resist rushing into such a long-term policy without full analysis and consideration. You must not buy the Administration's program just because it is the only one offered at this time. After all it was conceived in secrecy and is already being implemented without public hearings.

The Congress need not feel under any great pressure to move in one week or two weeks or even in one or two months. There is nothing in the Administration's program that protects us from an embargo over such a short time space. Moreover, even if an embargo were to be imposed during the next few months we are in far better shape today to cope with it than we were in October, 1973. Supplies of oil are ample both in the United States and around the world. There is a great deal of spare producing capacity in non-Arab countries. We have an established and operating mandatory allocation system which would avoid the regional spot shortages caused by the last embargo by spreading the available supply of oil equitably and evenly throughout the country. Finally our most vulnerable period—

the winter—is well along. It takes about two months for an embargo to bite and by that time we will be into milder weather, even in New England. Thus, while no one wants a new embargo it would hurt us less than the embargo of October 1973. The Congress does have time to analyze thoughtfully the Administration's energy policy and come up with its own alternative program.

As indicated at the beginning of this paper, there are a number of alternative actions which can, at very low cost, meet the President's basic objectives of achieving meaningful conservation and lessening oil imports. But we must use a surgical tool rather than a meat axe approach. The positive programs presented by the Independent Oil Men's Association and the New England Fuel Institute contain actions keyed to conserving the two fuels that are not being conserved currently—gasoline and natural gas.

Apart from these recommended steps Congress must recognize that our greatest vulnerability to foreign oil cutoffs at present is our high dependence (particularly on the East Coast) on imported residual fuel oil. We do need and must have additional fuel-oriented refining capacity in this country to lessen this vulnerability. However, the Administration's plan discriminates against U.S. refineries and would limit if not prevent the building of any new refineries here at home. This would occur, first of all, during the so-called transitional or tariff phase of the Administration's program since product tariffs are set lower than crude oil tariffs. This obviously leads to the favoring of construction of refining capacity abroad rather than here. Moreover, the long-term Administration program which equalizes tariffs between products and crude oil nevertheless puts overseas refineries in a preferred position. Under the Administration's program foreign refineries will have lower capital costs, lower working capital needs and lower freight costs than a new U.S. fuel refinery.

There must be positive incentives to build new independent refining capacity in this country and all of the independent marketing and refining groups will, I am sure, be happy to work with you and your staff and with other political leaders in Congress to help frame out the kind of incentive program that is vitally needed.

Senator Long, we are at a crossroads of such importance that it cannot be overstated at this point in our national economic life. We are going to opt either for a permanent high energy cost economy which will exacerbate our recession and our inflation, or we are going to embark on a conscious policy of more moderately priced energy designed to keep our economic structure competitive in the world market.

I would like to recommend that the Congress look at the establishment of a moderate energy cost program. The Administration wants to take the 85% of our energy that we produce domestically and hook it to the price of the 15% of our energy which we import—letting the tail wag the dog. This does not insulate us from OPEC. Rather it ties pricing for our whole energy structure directly to OPEC's prices—plus, of course, $2.00 per barrel. In a very real sense our entire energy production is put under the pricing control of the OPEC countries.

There are those in the oil and gas industry (and, indeed, within the Administration) who argue that price controls should be lifted on all domestic oil and gas so that they can rise the "free market" price. But there is no "free market" price in the world today. OPEC's prices are political, not economic. To illustrate: it costs 16¢ to produce one barrel of Saudi Arabia crude oil today; yet, today's selling price is $10.46 per barrel.

If we really wish to insulate our economy from OPEC pricing, the only logical way to do it is break away from their politically established prices by establishing prices of our own for the energy which we produce ourselves. We are uniquely able to do just that since we import only 15% of our energy needs.

I would recommend that the Congress take the two different prices which currently apply to domestic crude oil (the old crude oil price which is controlled at $5.25 per barrel and the new crude oil price which fluctuates at about the level of the landed cost of OPEC crude or, say, about $11.50 per barrel) and average these two prices thereby creating a new single price on all domestic oil. It could be set slightly lower than the weighted average of the two prices today. With a small roll back of domestic crude oil prices there would be a deflationary effect on the economy—rather than the wildly inflationary effect of the Administration's plan.

Such a weighted average price might be set at, say, $7.00 per barrel—a reduction of perhaps 20¢ to 35¢ per barrel from today's weighted average price. U.S. refineries under the Mandatory Allocation Act would continue to receive their pro-rata share of total domestic oil at the new fixed price. This would promote more refining capacity, including more independent defining capacity, since refiners would be able to count on lower weighted average crude oil costs than their foreign competitors.

Once the new lower domestic oil price has been established, new natural gas prices could then be deregulated without fear of a precipitous jump in natural gas prices, since only a small volume would qualify for deregulation in the first year and since a price ceiling would be set by the new lower domestic oil price. In short, new natural gas prices would only rise to the value of the alternative energy source, i.e. oil prices. The weighted average crude cost to U.S. refiners would be about $8.50 (70% at $7.00 and 30% at $12.00). Under the Administration's proposal, of course, deregulated natural gas prices would rise to the equivalent of $14.00 per barrel of crude oil. Similarly, the new lower domestic crude oil price would put a ceiling on price rises for coal. Yet, even with a moderate increase in natural gas prices resulting from this approach, conservation of natural gas would be increased just as conservation of heating oil during the past year has responded to higher heating oil prices.

Even at a new $7.00 price for all domestic crude oil there would still be adequate incentive to drill and develop additional oil supplies. And with new natural gas prices deregulated there would be an equal incentive, now missing, to drill for and develop additional natural gas supplies.

If an additional demand depressant is needed, and I am not sure it is, then plans such as those suggested by IOMA and NEFI could be put in place in order to moderately cut consumption of gasoline.

Such a low energy cost alternative to the Administration's plan would achieve the following:

Slightly reduce, rather than sharply raise, oil prices to consumers for all petroleum products except possibly gasoline.

Slightly raise gasoline prices, if other steps fail to curb gasoline use.

Go hand in hand with other long-term conservation measures, such as Federal taxes or high horsepower or heavy automobiles, new tougher insulation standards and tax incentives to insulate both commercial and residential building.

Provide sufficient incentive to continue drilling for new oil and increase incentive for drilling to discover and develop new natural gas supplies.

Increase incentives for the addition of new refining capacity, including new independent refining capacity, thereby reducing our dependency on foreign product imports.

Pinpoint conservation when it is likely to do the most good, i.e. natural gas and gasoline.

Continue the modest price reductions now flowing to the East Coast on imports of refined products by continuing the existing price equalization program.

Allow the tax rebate and tax reduction and reform measures to really do their job of stimulating the economy without an economic drag offsetting them from the energy sector.

Put a system into operation with the minimum of operational and administrative difficulty since allocation and price equalization regulations are already in place and functioning.

Eliminate the need for rationing, new tariffs or protective quotas.

Fit perfectly with an emergency strategic storage program designed to lessen our vulnerability to disruptions of foreign oil supplies.

Insulate our economy from OPEC price decisions whatever course they take.

Strengthen our competitive export position by providing lower energy costs to industry and agriculture than the energy costs now prevailing in other industrial countries.

Improve our balance of payments position as a result of our more competitive position in world markets.

In short, this alternative program is not inconsistent with the Administration's objectives. It does virtually everything the Administration wants to do. But it does so in a way that strengthens rather than weakens our economy in both the short and long term.

I would like to pause now at the conclusion of my remarks to try to gain perspective at this critical juncture by reflecting on a short poem by Robert Frost—a poet we like to call our own New England sage even though he was born in

California. Sometimes a poet like Frost can illustrate a truth in the language of nature in a way that makes us all understand the truth a little more fully.

"Two roads diverged in a yellow wood,
And sorry I could not travel both
And be one traveler, long I stood
And looked down one as far as I could
To where it bent in the undergrowth;

Then took the other, as just as fair,
And having perhaps the better claim,
Because it was grassy and wanted wear;
Though as for that, the passing there
Had worn them really about the same,

And both that morning equally lay
In leaves no step had trodden black.

Oh, I kept the first for another day!
Yet knowing how way leads on to way,
I doubted if I should ever come back.

I shall be telling this with a sigh
Somewhere ages and ages hence:
Two roads diverged in a wood, and I—
I took the one less traveled by,
And that has made all the difference."

Senator, as you may know the title of the poem is "The Road Not Taken". I would hope that when the Congress gets through fully analysing the President's energy program that it will become The Road Not Taken.

Appendix B

Economic Analysis of President Ford's Energy Program

(A staff analysis prepared at the request of Senator Henry M. Jackson, chairman, Committee on Interior and Insular Affairs, pursuant to Senate Resolution 45, the National Fuels and Energy Policy Study)

Economic Analysis of President Ford's Energy Program

Summary

The short-term impact on the economy of the President's energy proposals is tremendous. The cost of energy will rise in one year by over $40 billion, an amount greater than the steep increase initiated during the Arab embargo. The impact will be absorbed by an economy already facing recession and double digit inflation. Costs to low- and middle-income households will soak up 5 to 10 percent of before-tax income under either of the programs which the President has proposed: the one he can implement independent of Congress or the program which he has asked Congress to enact.

Both proposals have as their goal the reduction of energy consumption through a broad increase in energy prices which is being applied without regard for the degree of flexibility available to consumers to initiate conservation in the short run. The removal of energy prices from control insures that the price of all energy consumed in the United States will be affected directly by OPEC pricing policies.

Over the long run the impact of higher prices could be absorbed in normal economic growth and consumers would be able to adjust gradually to the signals which slowly rising prices would send by choosing not to consume energy and by increasing the efficiency of use for the energy which they do consume. The present administration proposal attempts to achieve long-term energy goals in the short run, and in doing so, threatens the quality of life of the large number of families for whom added energy costs and energy induced inflation mean substantially reduced purchasing power.

A number of economists feel that an increase in basic energy costs of $1.00 is transformed, as it "ripples" through the economy, into $1.50 to $2.00 in increased consumer costs. Thus, under this hypothesis, the ultimate cost of $30 billion annually which the administration itself ascribes to its program would be transformed into $45 to $60 billion by the time it reaches consumers. The analysis which follows does not include any estimate of ripple effects. Only a direct dollar-for-dollar passthrough of energy costs is assumed. The operation of a ripple effect would therefore increase each cost estimate which follows by at least 50 percent.

Program To Be Implemented by Executive Order

The energy pricing proposals announced in the State of the Union message which (1) can be implemented by the President without any additional grant of authority by the Congress and (2) do not require congressional approval, would cost the U.S. consumers an additional $33.5 billion on an annual basis. This cost includes (1) direct increases in the price of petroleum which result from Presidential action, and (2) induced increases in the prices of alternate fuels which compete, at the margin, with imported and uncontrolled oil.

This increase in the cost at the point of production or import of basic fossil energy is virtually equal to the increase in fossil energy costs experienced over the 1973–74 period. During that time, according to the Bureau of Mines, the cost of domestically produced fuels increased by $16.4 billion. According to the Department of Commerce the cost of imported fuels increased by $16.8 billion. The total of $33.2 billion amounted to an increase of 48 cents per million Btu on the average for all fossil energy consumed in the United States in 1974.

For the 3-month period beginning in February during which the program will be phased in, the cost of imported oil will increase by $844 million as shown in table I.

TABLE I.—3-MONTH PHASE-IN COST: IMPORTED OIL

[In millions of dollars]

Commodity	Cost: February	Cost: March	Cost: April	Grand total
Crude oil [1] (tariff)	109	242	351	702
Refined [2] (tariff)	73	161	234	468
Refined (rebate) [3]	(73)	(113)	(140)	(326)
Total	109	290	445	844

[1] Current import level of 3.9 mmbd assumed.
[2] Current import level of 2.6 mmbd assumed.
[3] Rebate is $1 per barrel in February, $1.40 per barrel in March and $1.80 per barrel in April.

The price of imported petroleum will increase under this proposal by 5.4 cents per gallon.

The costs calculated in table I apply only to imported oil. An import fee beginning at $1 per barrel on February 1 and rising to $3 per barrel on April 1 is assumed, along with partial rebates of fees on imported refined petroleum products such as fuel oil.

The President has announced that on April 1, he will act to decontrol the price of "old" oil, now selling for $5.25 per barrel. In calculating data for table II which follows, it is assumed that the program the President will place in effect on April 1 is permitted to go forward without alteration by Congressional action. The increases in the annual costs for imported oil, domestically produced oil, and competitive fossil fuels are summarized in table II.

TABLE II.—ANNUAL COST OF PRESIDENTIALLY IMPLEMENTED ENERGY PROGRAM

[Measures that do not require legislation]

	Annual cost (in billions)
Oil:	
Imported oil tariff ($3/bbl) 6.5 mmb/d × 365 × $3	$7.1
Rebate on imported refined products ($1.80/bbl) 2.6 mmb/d × 365 × $1.80	(1.7)
Increase in price of presently uncontrolled oil ($3/bbl) 3.0 mmb/d × 365 × $3	3.3
Increase in price of presently controlled oil ($5.25/bbl to $14.40/bbl) 5.7 mmb/d 365 × $9.15	19.0
Total oil costs	27.7
Natural Gas: Increase in the price of uncontrolled intrastate natural gas ($0.46/M ft^3) 10.4 tcf/y × 0.6 × $0.46	2.0
Coal: Increase in the price of coal ($10.71/ton) 0.540 bt/y × 0.5 × $10.71	2.9
Total all fuels	33.5

The calculations in table II utilize the levels of production and imports which prevailed in 1974 and assume that decontrolling oil prices will affect 5.7 million barrels per day, or 65 percent of current domestic production of crude oil and lease condensate. Imports of refined petroleum products in 1974 averaged 2.6 million barrels per day.

In the case of natural gas it is assumed that the commodity sold outside of FPC price controls—that is, intrastate natural gas—will respond in price on a Btu-equivalent basis to the net increase in price of imported and uncontrolled oil, which are the marginal competitors for uncontrolled natural gas. These categories of oil which are currently free from price controls encompass 9.5 million barrels per day (6.5 million barrels per day of imported oil and 3.0 million barrels per day of uncontrolled oil). The annual cost of this oil would increase by $8.7 billion (the sum of the first three entries in table II) under the President's program, or an average of $2.51 per barrel. This figure is lower than $3 per barrel because of the $1.80 per barrel rebate on refined product imports contained in the President's program. Crude oil at $1 per barrel is equivalent, on a Btu basis, to dry natural gas at 18.4 cents per thousand cubic feet, so that the price increase for uncontrolled and imported oil would induce a 46 cents per thousand cubic feet increase in uncontrolled natural gas prices.

Coal competes with oil and natural gas for electricity generation and is assumed to adjust to the price increase of the marginal oil supply—uncontrolled and imported oil. Crude oil at $1 per barrel is equivalent on a Btu basis to bituminous coal and lignite (a weighted average reflecting 1974 consumption) at $4.27 per ton. Thus the $2.51 per barrel net price increase for imported and uncontrolled oil would induce an increase in coal prices of $10.71 per ton.

The increases in the prices of alternate fossil fuels are contingent upon the expiration or renegotiability of existing contracts for these fuels so that higher prices can be implemented. Reliable data concerning these contracts are not available for the country as a whole, but rough estimates can be made. In computing coal and natural gas costs in table II it is assumed that 50 percent of coal and 60 percent of intrastate natural gas contracts will expire or be subject to renegotiation in 1975. It should be noted that these renegotiation rates are considerably higher than those used in administration projections of increases in coal and gas prices. The figure of 50 percent for coal was derived by dividing the 1973–74 increase in the average price per Btu of coal purchased by electric utilities by the increase in the average price of residual fuel oil.

The administration assumes that intrastate natural gas contracts will turn over at only 20 percent per year—a figure apparently derived from statistics of *interstate* pipelines. Our 60 percent figure reflects a typical intrastate contract term of 1–5 years in contrast to the 12–20 years required by the FPC in purchases by interstate pipelines, and the widespread existence in the former of "most favored nation" and other escsalation clauses of types disallowed by the FPC. The rates of production, 10.4 trillion cubic feet (tcf) per year for intrastate natural gas and 0.540 billion tons per year for bituminous coal and lignite reflect 1974 production levels. (Interstate natural gas production in 1974 is estimated at 11.5 tcf.)

The total cost of this Presidentially implemented program on an annual basis amounts to over $33 billion, nearly $160 for each man, woman and child in the United States, or over $630 for a family of four. Spread over approximately 70 million households (of which nearly 13 million are one-person households) the cost comes to $480 per household.

This proposal, should it remain in effect, will raise the price of all oil consumed in the United States—uncontrolled, formerly controlled and imported oil—by an average of $5 per barrel. This translates into a 12 cents per gallon on the average for all petroleum products, assuming a simple cost pass through. The economic impact will be as great as the impact of the price increases imposed for oil during the Arab embargo by the Organization of Petroleum Exporting Countries. These OPEC increases and domestic oil pricing decisions of the Nixon/Ford administration raised the price cost of all oil refined in the United States by just over $6 per barrel in a year, from $3.40 per barrel to $9.50 per barrel. During that period, gasoline and heating oil prices increased 15 cents per gallon and 18 cents per gallon respectively, reflecting more than a simple pass through of crude oil costs.

The cost of the approximately 69 quadrillion Btu of fossil energy which was consumed in the United States in 1974 would increase by nearly 50 cents per million Btu in 1975 under this program. The implied increase in average electricity rates amounts to 2.7 mills per kilowatt hour,[1] a 10-percent increase over the average cost of 27 mills per kilowatt hour for 1974.

One important effect of the President's proposal is to remove the insulation between the price policies of the OPEC cartel and a substantial portion of the fossil fuels which provide 95 percent of the energy consumed in the United States. Thus, if the President's proposal is implemented, the impact of a dollar increase in the price of oil on the world market would propagate rapidly throughout the U.S. energy supply system, affecting the prices of all domestic petroleum and substantial portions of domestic natural gas and coal. The impact would amount to $7.8 billion in added costs for each dollar per barrel increase in OPEC prices. The calculation is illustrated in table III.

TABLE III.—IMPACT OF $1 PER BARREL OPEC PRICE INCREASE

	Cost in billions
Oil: 15.2 Mmb/d × $1	$5.5
Natural gas: 10.4 fcf/y × 0.6 × $0.184	1.1
Coal: 0.540 bt/y × 0.5 × $4.27	1.2
Total	$7.8

PROGRAM PROPOSED BY THE PRESIDENT TO CONGRESS

The energy price and tax proposals which the President is submitting to the Congress differ in significant respects from the import fee/rebate and decontrol program which is being implemented without congressional approval by Executive order. The Congress is asked to replace the fees on imported petroleum which the President has set by a comprehensive price and tax program, including the following provisions affecting energy prices:

[1] On the average, electricity in the United States depends on energy sources as follows: Coal, 46 percent; oil, 16 percent; natural gas, 17 percent; hydroelectricity, 13 percent; and nuclear, 7 percent. The average heat rate of steam electric plants is 10,500 Btu/kWh. Average price increases for fossil energy implied in table II are 89 cents/MBtu for oil, 18 cents/MBtu for natural gas, and 22 cents/MBtu for coal or 26 cents/MBtu for the average fossil input to electricity generation.

(1) A tariff of $2 per barrel (without a rebate provision) on all imported petroleum;

(2) Excise taxes of $2 per barrel on all domestically produced crude oil, 37 cents per thousand cubic feet on natural gas, and $1.42 per barrel on natural gas liquids. These tariffs would increase the price of all domestically consumed petroleum liquids and natural gas by 36 cents per million Btu;

(3) A windfall profits tax on domestically produced crude oil would be imposed to capture rents earned through increases in the price paid to domestic producers;

(4) Deregulation of "new" natural gas, defined as gas produced from wells commencing operation in 1975 and gas covered by expired or expiring contracts. The deregulation of all domestically produced crude oil is also assumed; and

(5) Inclusion by electric utilities in the rate base for electricity prices of costs of construction and of the addition of pollution control equipment.

If the Congress accepts this program, the energy-related costs to U.S. consumers will increase by approximately $43 billion in 1975 and ultimately by over $50 billion annually as fuel supply contracts expire or are renegotiated to reflect higher prices. The impact of the program is summarized in table IV. In each case, the corporate revenues and Government tax collections are estimated.

TABLE IV.—ANNUAL COST OF PRESIDENTIALLY PROPOSED ENERGY PROGRAM

[Including measures requiring legislation]

Increased	Annual effect (billion dollars)		
	Consumer costs	Corporate revenues	Tax collections
Oil:			
Imported oil tariff ($2/b) 6.5 mmb/d×365×$2	$4.7		$4.7
Presently controlled oil:			
Decontrol (price increases from $5.25/b to $11.40/b) 5.7 mmb/d×365×$6.15	12.8	$12.8	
Excise tax ($2/b) 5.7×365×$2	4.2		4.2
Presently uncontrolled oil excise tax ($2/b) 3.0 mmb/d×365×$2	2.2		2.2
Windfall profits tax (interpolated from administration formula)		(15.3)	14.0
Total oil	23.9	(2.5)	25.1
Natural Gas Liquids: (excise tax $1.42/b) 1.7 mmb/d×365×$1.42	0.9		.9
Total natural gas liquids	0.9	0	.9
Natural gas:			
New interstate gas:			
Decontrol (price rises from $0.50/mcf to $2.00) 2.3 tcf/y×$1.50	3.5	3.5	
Excise tax ($0.37/mcf) 2.3 tcf/y×$0.37		(0.8)	.8
Intrastate gas:			
Influence of oil prices:			
(Price rises from $1.00 to $2.00 for 60 percent of contracts) 10.4 tcf/y×.6×$1.00	6.2	6.2	
Excise tax 10.4 tcf/y×$0.37		(3.9)	3.9
Controlled interstate gas:			
Excise tax ($0.37/mcf) 9.2 tcf/y×$0.37	$3.4		$3.4
Total natural gas	13.1	5.0	8.1
Coal: Influence of oil price (price rises for 50 percent of contracts) 0.540 bt/y×.5×$4.27×X (Total Coal)	2.3	2.3	0
Total all fuels	40.2	4.8	34.1
Electricity: Increase in electric utility rates from inclusion of construction and pollution equipment costs in rate base	3.0	3.0	0
Total costs	43.2	7.8	34.2

The calculations for table IV are in most cases similar to those employed in analyzing the Presidentially implemented program outlined in table II. The estimate of the capture of rents from the windfall profits tax on domestic oil is an interpolation which approximates result of the administration's more complex formula. Under that formula, revenues on a barrel of oil in excess of a base are taxed. The base escalates monthly from an initial level of $4.95 per barrel to $5.47 at the end of the first year. The effective tax rate for domestic oil during the first year would be $1.98 per barrel plus 90 percent of the difference between the excess over the base and $3. Initially, the windfall profits tax on a barrel of oil sold at $11.40 plus the excise tax would be $5.09; at the end of the year, the windfall tax would drop to $4.62. The annual revenues on 8.7 million barrels per day at these levels of tax are $16.1 billion and $14.6 billion respectively. In table IV, an interpolate between these values is used to estimate the first year's windfall profits tax at $15.3 billion.

The excise tax on natural gas liquids, which contributed 1.7 million barrels per day to the U.S. petroleum supply in 1974, is set at $1.42. On a Btu-basis, this tax is the equivalent of an increase of $2 per barrel in the price of crude oil. Natural gas liquids are currently under price controls, and no decontrol is assumed, although it seems likely that the competitive interaction of the same petroleum products derived on one hand from refinery operations and, on the other hand, from natural gas plants would lead to market distortions in the absence of this decontrol.

The decontrol of new natural gas is assumed to affect 2.3 trillion cubic feet of new gas and all gas under contracts which will have expired prior to the end of 1975. This includes contracts which expired in years previous to 1975, as well as those expected to expire in 1975. Some of this gas is now sold at $0.50 per thousand cubic feet; without the President's program it is assumed that it would all sell for $0.50 per thousand cubic feet during 1975. It is assumed that the price of this gas will rise to the current top price for intrastate uncontrolled gas of over $1.60 per thousand cubic feet plus the excise tax of $0.37 per thousand cubic feet, or, to a total of approximately $2 per thousand cubic feet. In the intrastate market the average price is now approximately $1 per thousand cubic feet. It is assumed that 60 percent of the contracts under which this gas is sold will expire or be subject to renegotiation in 1975, and that the new price will equal the price at which deregulated new gas sells—approximately $2 per thousand cubic feet. It should be recognized that under a climate of deregulation, a substantial reversal of the previous environment affecting gas prices can be expected. Currently interstate pipelines are forced to curtail interruptible customers. Under deregulation accelerated bidding for all gas can be expected as pipelines seek supplies to fill orders for previously threatened customers. This bidding will place considerably more pressure on all uncontrolled natural gas prices than would exist under the Presidentially implemented program which can by law contain no provision to deregulate interstate gas.

The program which the Congress has been asked to pass would raise the cost of energy consumed in the United States by over $43 billion, or $205 for each member of the resident population of approximately 210 million persons. Thus the bill for a family of four on the average will amount to over $800. These incremental energy costs will accumulate as they are passed through the economy to individual consumers in the form of increases in the prices of direct fuel purchases and as increases in the prices of all goods and services in proportion to the energy requirements of these goods and services. These added fuel costs represent an automatic 3 percent inflation in GNP before the impact of any dislocation costs which may be generated by higher fuel prices. According to the Bureau of Mines, U.S. energy costs increased by over $33 billion in 1974: $17 billion for imported oil, $11 billion for domestic oil, $1 billion for domestic natural gas, and $4 billion for domestic coal. These cost increases contributed to an inflation rate which is currently running at 12 percent per year.

During the 1973-74 period, fossil fuel prices for electricity generation increased as shown in table V. The last column shows the average increases in prices of individual fuels which the President's proposed program would produce.

TABLE V.—FOSSIL FUEL PRICES FOR ELECTRICITY GENERATION

[Cents per million British thermal units]

Fuel	September 1973	September 1974	Increase, 1973-74	Increase projected for Ford program
Oil	82	195	83	77
Natural gas	37	54	17	58
Coal	41	79	38	18

Source: FPC, data from table IV.

Based on the average fuel mix of U.S. steam electric generating plants, the price of a million Btu of fossil energy input will increase by 31 cents. This corresponds to an average increase in U.S. electricity prices of 3.3 mills per kilowatt hour, or 12 percent over 1974 average prices.

The automatic adjustment of electricity rates to pass through increases in fuel costs have caused electricity rates to rise much faster in many regions than this calculation of average figures would indicate. Thus in 1974 in many major Eastern metropolitan areas, the price of electricity has increased by 30 percent or more as increased fuel costs were transferred directly to consumers. These increases have just offset the utilities' fuel costs and have not resulted in increases in actual retained revenues. This failure to increase revenues occurs at a time when the utilities' nonfuel costs are also rising and the need to expand and improve capacity is widely recognized. High electricity prices, driven by fuel costs, have strongly stiffened consumer resistance to utility rate increases at a time when these rate increases are needed to fund utility construction programs. Further increases in fuel costs will only further solidify this resistance to the rate increases required to bring in the revenues which the financial viability and minimal growth of the industry requires.

A further increase in consumer costs for electricity which is unrelated to fuel has been proposed in an attempt to increase utility revenues. Part of the Presidential program to be submitted to Congress proposes that the State utility commissions, which regulate the major portion of retail electricity sales, permit the inclusion of construction costs for work in progress in the electricity rate base. This is not now common practice. Normally construction costs plus an allowance for interest on these costs may be passed on to customers only after the completion of work. This provision of the President's program, should it be enacted, could add $3 billion to the national electricity bill in 1975 depending on the construction undertaken and the amount of population control equipment installed. This would push the average increase in residential electricity prices to 20 percent—a jump equivalent to the national average for all 1974 increases. As in the case of the fuel cost adjustment effects, the impact of construction work on the rates individual consumers pay will vary widely with respect to local circumstances.

If $16 billion of construction work in progress were added to the utilities' rate base, and the State utility commissions allowed the utilities to earn 9 percent after taxes on their investments, after-tax income would be permitted to increase by $1.44 billion. Assuming a marginal Federal tax liability of 48 percent, the utilities would have to increase their revenues by $3 billion to retain $1.44 billion after taxes.

While this attempt to increase utility revenues increases consumer costs, it does produce needed revenues for utilities. Also, increases in electric rates generated by this provision now would be in part offset by lower rates later, because interest on construction costs would no longer be accumulated in the rate base. However, taken in the context of the entire Presidential program, which will substantially increase the rate of inflation, will substantially increase interest rates and will substantially increase consumer resistance to catch-up rate increases, the net effect on utilities may be negative in many regions of the country. In nearly all cases the net effect on utility customers will be increases in electricity prices comparable to the 1974 increases.

Because the program the President is sending to Congress would remove from price controls both new natural gas sales to pipelines and crude oil production, it would go further than the program implemented by executive order to link domestic energy prices to the prices set by the OPEC cartel. The effect of a $1-per-barrel increase in world oil prices on domestic energy costs will be larger than the estimate of table III because of the effect of decontrol of new natural gas. With this component of the U.S. energy supply also free to move with an OPEC price increase, the effect of a $1-per-barrel rise in the world oil price would cost consumers an additional $8.2 billion annually of which $2.4 billion would go to OPEC, $2.8 would be captured by the Federal Government in windfall profits taxes and $3 billion would accrue to energy producers.

Impact of Ford Energy Program on Consumers in Various Income Groups

Precise estimation of the detailed impact of the energy program proposed by the administration is complicated both by the absence of reliable data describing the consumption of energy at the household level in American society. Calculation using average figures for the country as a whole ignore significant regional differences in energy use, such as the relatively heavy dependence of New England on imported fuel oil for electricity generation and home heating, the widespread use of unregulated natural gas in gas-producing States and the importance of relatively cheap hydroelectric power in the Northwest. Thus, national averages often substantially obscure catastrophic regional impacts of specific events or policies affecting energy.

When the average impact of a policy nationally is a large as that of the administration's present energy pricing proposals, truly substantial regional dislocations and other cost impacts are bound to occur. Thus, the figures quoted below will often significanty underestimate impacts in places where dependence on oil and unregulated natural gas is heavy.

Any projection of additional costs to U.S. consumers from the administration program depends on a variety of assumptions including those regarding levels of production, pricing decisions by sellers of alternate fuels, and the flexibility of contracts between producers and consumers. Moreover, the added costs to be expected in 1975 are surely less than those which will be imposed in later years as the producers free themselves from long-term agreements negotiated at pre-1974 prices, and dislocation costs and markups in excess of dollar-for-dollar fuel cost passthrough are reflected in prices to consumers.

Estimates of the annual impact of acceptance of the administration's program range from $40 billion to over $60 billion as the ultimate cost. An administration spokesman's estimate of $55 billion was quoted by the UPI wire service on January 14, 1975.

None of these estimates include the effect of a further price increase by the OPEC cartel in the future in response to the U.S. import tariff. Each such dollar per barrel increase is estimated to add approximately $8 billion more to the annual energy bill for U.S. consumers.

These energy costs, whether they amount to $40 billion per year, $50 billion per year or, ultimately, much more represent nothing less than a major escalation in the basic cost of all fossil fuels consumed in the United States. This escalation, moreover, is entirely comparable to the shock received only a year ago from OPEC; the major difference is that this second major quantum jump in the cost of energy for consumers arrives at a time when the United States economy is in a deepening recession.

In 1974, according to preliminary figures from the Bureau of Mines, the United States consumed some 69 quadrillion British thermal units (Btu) of fossil fuels, a drop of 2.4 percent from 1973. The increase of $40 billion in fossil energy costs indicated in table IV would raise the price per unit of this basic fossil energy in the United States by nearly 60 cents per million Btu. An ultimate annual cost which reached $55 billion would amount to an increase of 80 cents per million Btu.

Under the assumptions associated with table IV, the price of the 15.2 million barrels per day of petroleum produced in the United States and imported would rise by approximately $24 billion. This is an average of 77 cents per million Btu: $4.30 per barrel, or 10 cents per gallon. The increase per gallon rises by 2.3 cents for each dollar per barrel of in future OPEC price increases; the effect of total decontrol is to cause any such increase to be passed through to all oil consumed in the United States. By comparison, the oil price of oil used in the United States increased by $6.10 per barrel from 1973 to 1974.

Under conservative assumptions, natural gas costs (excluding liquids) would rise by over $13 billion, equivalent to an average increase in natural gas prices of 60 cents per thousand cubic feet (58 cents per million Btu).

Finally, coal, which is a fuel which competes with oil and natural gas for electricity generation, would be pulled up in cost by at least $2.3 billion in total. This represents an average of 18 cents per million Btu or $4.27 per ton. By comparison, the increases in fuel prices which took place over the 1973–74 period are shown in table VI.

TABLE VI.—INCREASE IN FUEL PRICES, 1973-74

	Cents per million Btu
Oil:	
Domestic crude oil [1]	53
Imported crude oil [2]	160
Imported distillate fuel oil [2]	177
Imported residual fuel oil [2]	136
Natural gas:	
Interstate natural gas [3]	4
Instrastate natural gas [3]	14
Average for all natural gas [1]	8
Coal: Average for all coal [1]	27

[1] Bureau of Mines.
[2] Census Bureau.
[3] Inferred from Federal Power Commission and Bureau of Mines data.

These increases would impact the economy in a broadly based and fundamental manner. For example, nearly 80 percent of the electricity generated in the United States is derived from fossil energy sources. An average impact on electricity rates of approximately 3 mills per kilowatt-hour in fuel price increases and 2 mills per kilowatt-hour from inclusion of construction costs in the electricity rate base would amount to nearly a 20 percent total increase in the price of electricity. This would be identical to the experience of the United States on the average in 1974, when the Bureau of Labor Statistics index of retail electricity prices rose 20 percent over 1973. In areas where electric generation is dependent on expensive basic fuels—imported oil or intrastate natural gas—the cost of electricity is currently higher—over 40 mills per kilowatt-hour. In these areas, the price increase in electricity will correspond more closely to the oil and gas price increase, so that the cost of electricity may increase by 10 mills per kilowatt-hour, or nearly 25 percent.

Average costs represent the effect of direct household purchases of fuels and electricity plus the direct passthrough of energy costs in the prices of all other goods and services. These direct cost increases are relatively easy to estimate. In the case of home heating oil, the increase depends on the amount of the increased cost of crude oil allocated to heating oil. Under conservative assumptions, the impact of the direct cost associated with the administration program amounts to 10 cents per gallon. However, industry sources have indicated that the per gallon increase could be as high as 15 cents. Heating oil customers have less freedom to reduce consumption—especially since heating oil costs have already doubled during 1974. Thus, the added annual cost of 1,250 gallons of heating oil would be $125 to $185. A home heated with natural gas which used 150,000 cubic feet in 1975 would pay $90 more on the average.

The annual cost of 850 gallons of gasoline—16 gallons per week—could increase from $85 to $120. The price of 8,000 kilowatt-hours of electricity would increase by $40 on the average and as much as $80 in areas heavily dependent on oil and unregulated natural gas. These increases, contoured to the price of fuels and electricity purchased directly by households total to approximately $250 which administration representatives have indicated is the average cost of their program to American households. However, this estimate is a clear misrepresentation of the real impact of the program on the American household. Using the total number of households in the United States, approximately 70 million, the total cost of the program, derived from this administration estimate amounts to only $17.5 billion, much less than to other administration estimates of the total cost. Thus, $250 is only a third of the real cost of the program to an average American family. The difference is that this estimate includes only direct purchases of fuels and electricity by households. The additional impact of energy costs because of their passthrough in the price of all goods and services dependent on energy, is nearly three times as large as the direct purchases of fuels and electricity by households. These costs all reach the consumer; no one else pays them. Indirect energy costs arise from the increased prices for every item which must be transported before it is sold: food, clothing, construction materials, manufactured goods. Indirect energy costs arise from increases in the price of basic materials which are produced with a large energy input: glass, steel, cement, aluminum, petrochemicals.

Thus, the impact on the average American family of the administration energy pricing program is not $250 per year; it is at least three times that figure. This projection is an average for all families. Yet not all families consume the same amount of energy, nor do they possess similar abilities to pay for it. A study carried out by the Washington Center for Metropolitan studies for the Ford Foundation's energy policy project estimated direct and indirect energy use in families in different income categories for the year ending June 1975.[2] These results are presented in table VII.

TABLE VII.—ENERGY USE BY HOUSEHOLDS

Category	Number of households (million)	Average income (1972 dollars)	Million Btu/household: Direct purchase fuels and electricity	Indirect energy use	Total use[1]
Poor	11.8	2,500	207	353	560
Lower middle	27.6	8,000	294	549	843
Upper middle	12.6	14,000	403	843	1,246
Well off	13.4	24,500	478	1,095	1,573
Average			337	682	1,019

[1] Total energy use for this sample accounts for approximately 67 quadrillion Btu, compared to 68 quadrillion Btu based on fossil fuel consumed in 1972. Total fossil based energy consumption in 1974 was approximately 69 quadrillion Btu.

Source: Ford Foundation energy policy project.

[2] Ch. 5, "A Time to Choose," energy policy project of the Ford Foundation, Ballinger Publishing Co., 1974.

Table VIII shows the additional annual costs associated with an increase in the price of fossil-based energy of $0.60 per million Btu, assuming the consumption pattern of table VI. The income from which this energy must be purchased is expressed in 1975 dollars.

TABLE VIII.—INCREASED ENERGY COSTS FOR HOUSEHOLDS BY INCOME: DIRECT AND INDIRECT ENERGY PURCHASES

Category	Income [1] (1974 dollars)	Cost increase for direct energy purchases [2]	Cost increase for indirect energy purchases [3]	Total increase
Poor	$3,050	$124	$212	$336
Lower middle income	9,770	176	329	505
Upper middle income	17,000	242	506	748
Well off	29,900	287	657	944

[1] Income adjusted by the ratio of consumer price indexes: December, 1971/December, 1972=1.221.
[2] Purchases of fuels and electricity for households; energy costs assumed to increase by 60¢/MMBtu.
[3] Purchases of all products (food, automobiles, housing appliances, petrochemicals, services) dependent on energy; dollar-for-dollar passthrough of 60¢/MMBtu is assumed without any increase due to "ripple" effect.

Table VIII shows the significant effect of cost increases in the direct purchase of fuels and electricity and the even larger effect of indirect energy use on expenditures. Thus, for a poor family, approximately $125 in increased costs for direct energy purchases corresponds to nearly $340 in increased costs when purchases of nonfuel goods and services are accounted for. For middle-income families, $200 to $250 in increased costs for direct purchases of fuels and electricity become $500 to $700 in total cost increases per family when all purchases are considered. For well-off families the total cost will be in excess of the average cost.

This table also shows the disproportion between added energy costs and ability to pay. The poor must find extra cash to pay for a third as much energy as the well off, yet they must find this cash in an income which is on the average, only an 6th to a 10th as large. Thus, the basic requirements for food, shelter, heat, transportation, and essential clothing and manufactured goods place a floor on energy requirements which does not respect relative ability to pay. When basic energy prices increase, the burden falls much more heavily in proportion to ability to pay on the poor.

The table shows that added energy costs which the President's program would provide for will reduce the purchasing of the poor by over 11 percent while for the well off, only 3 percent of income will be affected.

Appendix C

Material Offered for the Record by Hon. Frank G. Zarb, Administrator, Federal Energy Administration (Referred to at page 127 of this volume)

Discussion Paper—Options for Reducing Petroleum Imports

There are three principal options for reducing petroleum imports in the short to mid-term. They include a tax on gasoline; the President's program of a petroleum tariff and decontrol of domestic oil prices; and a cap on imports with gasoline rationing and petroleum allocation. This paper briefly describes these options and discusses the impact of each on reducing imports, regional equity, inflationary impact, impact on the poor, administrative complexity and cost, and impact on the recession and employment.

Option A: Import Cap/Allocation/Rationing

A volumetric limit would be placed on imports equivalent to the reductions called for in the President's program.

The current system of price controls for petroleum would be strengthen, including control of new domestic crude; thus an artificial shortage would be created.

Since price is not used to determine distribution of petroleum products, the government would maintain its system of allocating to retailers, based essentially on historical use for products other than gasoline. The government would also control refinery yields.

To prevent long gas lines, coupon rationing would be introduced. Such a program would include as its basic features:

(1) Each licensed driver would receive an equal monthly coupon allotment; these coupons could be freely traded or sold. The coupon market (the "white market") permits those drivers with needs greater than those represented by the monthly allotment to purchase additional coupons from those who use less than their monthly amount. Thus the market, rather than the government, is responsible for assessing "need" for gasoline above the basic minimum ration.

(2) Commercial users, whether they buy in bulk or at the pump, would receive coupon allotments equivalent to a percentage of their consumption during the 1973 base period.

(3) For that limited class of users (migrants, handicapped, etc.) for whose special needs the coupon resale market is not a reasonable solution, a proportion of coupons would be set aside and distributed by the state. This distribution would be based primarily on emergency or hardship needs.

(4) Coupons would be picked up in person at Post Offices by each eligible individual. They will be invalidated at the pump at time of purchase, and deposited by retailers with banks in a special coupon account. Gasoline deliveries to suppliers will be made to retailers only for amounts equivalent to coupons collected.

Option B: Gasoline Tax With Rebate

The Federal Excise Tax would be raised by 30¢/gallon, and the fees collected in the distribution system using the current administrative mechanisms.

Commercial users would receive a rebate through adjustments in their tax rate.

Special provision would be made for certain groups (e.g., farmers) who do not now pay the current Federal excise tax to avoid the tax entirely.

The tax would be rebated to all adults over 18. About 120 million persons age 18 and over are currently including in the 80 million IRS filing units; they will collect their tax as a simple tax credit at the end of the year. The 20 million adults who do not now file are in about 12 million households; they will file a simple form immediately for a before-the-fact annual payment and then will file a simple 1040 form annually to reconcile. Those not now enumerated by Social Security will be required to obtain a Social Security Number before they file for the rebate.

There would be a low income provision to protect the indigent who are required to drive long distances to work, to buy food or medicine, or for other purposes.

Option C: President's Program of Tariff, Tax Decontrol and Rebate

After April 1975, this program would consist of an additional tariff on petroleum imports of $2 per barrel and an excise tax of $2 per barrel on all domestic petroleum.

Domestic oil prices will be decontrolled and a windfall profits tax implemented to ensure that the revenue generated will accrue to the government, not the oil companies. This will raise the overall price of petroleum by $2 a barrel. The tariff, taxes and decontrol, then, will add $4 to the price of a barrel of oil.

In addition, an exercise tax on natural gas equivalent to $2 a barrel would be adopted and new natural gas prices deregulated to equalize the impact on oil and natural gas consumers and decrease natural gas consumption.

$30 billion will be collected by the government from the tariff and taxes. These revenues will all be rebated to consumers and governments.

REGIONAL DISPARITIES

All three options have major regional impacts.

There are substantial regional variations in per capita gasoline use. Those in the Middle Atlantic states use less than two-thirds the gasoline of those in the Mountain States. Gasoline taxes or gasoline rationing, as the table below shows, weighs more heavily on residents of the mountain States, southwest, and mid-west than other citizens.

Per capita gasoline consumption (gallons/year)

New England:	
(Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, Connecticut)	421

Middle Atlantic:	
(New York, New Jersey, Pennsylvania)	368
East North Central:	
(Ohio, Indiana, Illinois, Michigan, Wisconsin)	459
West North Central:	
(Minnesota, Iowa, Missouri, N. Dakota, S. Dakota, Nebraska, Kansas)	531
South Atlantic:	
(Delaware, Maryland, District of Columbia, Virginia, W. Virginia, N. Carolina, S. Carolina, Georgia, Florida)	502
East South Central:	
(Kentucky, Tennessee, Alabama, Mississippi)	508
West South Central:	
(Arkansas, Louisiana Oklahoma, Texas)	556
Mountain:	
(Montana, Idaho, Wyoming, Colorado, New Mexico, Arizona, Utah, Nevada)	584
Pacific:	
(Washington, Oregon, California, Alaska, Hawaii)	482

Reliance on gasoline to bear the brunt petroleum cutbacks also discriminates against rural dwellers and in favor of those in cities. In the aggregate, rural dwellers use almost twice the gasoline/year of city residents.

The President's program, which includes both oil and natural gas, impacts most heavily on the Northeast and the Mid-West. The Northeast is the most heavily impacted area where fuel oil is the major factor in price increases. The Mid-West is also heavily affected due to reliance on natural gas.

PERCENTAGE INCREASE IN HOUSEHOLD FUEL COSTS RESULTING FROM PRESIDENT'S PROGRAM

	Percent increase	Percent above/below U.S. average increase
U.S. total	28.4	
New England	34.6	+16
Mid-Atlantic	32.3	+14
East North Central	29.8	+5
West North Central	27.7	−3
South Atlantic	26.0	−8
East South Central	19.7	−30
West South Central	25.9	−9
Mountain	27.0	−5

EFFECTIVENESS IN REDUCING IMPORTS IN SHORT AND LONG TERM

In the mid to long term the elasticity for gasoline is lower than that for other petroleum products. This is because there are fewer substitutes for gasoline than there are for other fuels. This means that an increase in the price of all petroleum products (President's program) will reduce imports more than an equal increase in the price (gasoline tax) of gasoline. In the short term this is not the case.

The reduction in imports from the President's program option is 900,000 barrels per day in 1975, 1.6 million in 1977 and 2.1 in 1985.

The gasoline tax would reduce imports by 250,000 barrels in 1975, 500,00 in 1977, and 1.3 million in 1985. Both this and the above estimate are not guaranteed savings, but are based on econometric studies.

The rationing/allocation option could obviously be adjusted to any level desired. The level considered in this paper is 1 million barrels per day in 1975 moving to 1.5 million in 1977.

Because of the complexity of the administration and the limited ability of a rationing program to adjust to changes in the economy (e.g., people moving, new businesses started) it is probably not a viable option for more than 1 or 2 years. Hence, it is not really a feasible part of a mild or long term program. Moreover, the longer the system lasts, the more exceptions are made, the more people learn how to evade the rules, and the greater are the opportunities for counterfeiting and abuse.

FEDERAL ENERGY ADMINISTRATION

Date: January 17, 1975.

Subject: Elasticity comparisons.
From: William W. Hogan.
To: Dennis Bakke.

At your request, I have prepared the following tables showing approximate time trends of elasticities used in the short term models and the Project Independence system. I caution you that the numbers have less meaning in the longer run because the assumption that other things remain equal (i.e. no substitution) is less tenable. I have attempted to estimate the effects of model interactions to show the approximate impact of price changes in petroleum alone.

ELASTICITIES RISES OVER TIME (ASSUMING PRICE INCREASES IN FIRST QUARTER 1975)

	1975	1976	1977	1980	1985
Gasoline (with respect to retail price ex-tax)	−.15	−.30	−.30	−.39	−.43
Aggregate petroleum	−.11				
(wholesale prices)	−.1	−.20	−.27	−.44	−.49

If we are to reduce significantly our vulnerability to imports in the mid and long term we must adopt an option to reduce consumption of petroleum that can be effective in 1980 and 1985.

IMPACT ON POOR

Gasoline rationing would have some beneficial impact as lower income people sold their excess coupons to those with higher incomes who in general use more gasoline. This effect would be somewhat limited by the plan to distribute coupons only to licensed drivers. The actual income transfer effects depend on the size of the shortage and the marginal price of the coupons and have not been calculated.

The gasoline tax and rebate system would transfer about $2.5 billion from those with incomes above $10,000 to those with smaller incomes.

	Income (thousand dollars)					
	0 to 3	3 to 5	5 to 6.5	6.5 to 8.7	8.7 to 10.8	10.8 plus
Net income transfer (million dollars)	253.1	262.4	163.9	92.9	107.1	−953.6
Transfer/adult (dollars)	30.86	24.07	13.89	7.31	7.09	−11.72

The President's program would transfer roughly $3 billion from those with incomes above $16,000 to those earning less than $5,000 per year, preliminary calculations indicate.

	Income (thousand dollars)			
	0 to 5	5 to 12	12 to 16	16-plus
Additional cost of energy (million dollars)	725	8,200	2,900	7,500
Rebated revenues (million dollars)	3,520	7,350	3,610	4,520
Net transfer	+2,795	−850	+710	−2,980

ADMINISTRATIVE COMPLEXITY AND COST

The gasoline tax and rebate would cost an estimated $50 million and between 400–500 additional people on the government payroll.

The cost and number of people required to implement the President's system of tariffs, taxes and rebates is about the same as that for the gasoline tax.

The complexity of administering gasoline rationing and allocation is considerably greater than the other two options, both because of the printing, distribution, collection and control of coupons and because of the exceptions process for the poor necessary in every state and local community. It will require an additional 17,000 government employees and approximately $2 billion per year to administer.

Rationing and allocation require government decisions on who gets less so that essential services may have all they need. Thus a government definition of essential vs. non-essential services must be made.

INFLATIONARY IMPACT

Imposition of a 30¢/gallon gasoline tax would raise the Consumer Price Index (CPI) by about 1½% in 1975. Through rebates to consumers, the overall level of disposable income would not change.

A $2/barrel import tariff plus excise taxes on domestic petroleum and natural gas would increase the Consumer Price Index by about 2½% in 1975. Again, these fees would be returned to consumers so that the overall level of disposable income would not be changed.

Under rationing, an equal number of coupons would be distributed initially to licensed drivers; such coupons would permit purchase of gasoline at a price above the controlled price. Those who desired to use more gasoline than their initial allotment would offer to purchase additional coupons through the "white market".

The cost of buying an additional coupon should stabilize at the market clearing level. Thus, there would be an "inflationary" impact similar to that created by a gasoline tax.

IMPACT ON THE RECESSION AND EMPLOYMENT

Using allocation and rationing to reduce imports by 1 million barrels per day would produce effects on the U.S. economy similar to an embargo: (1) it would create a drop of nearly $13 billion in GNP; (2) it would have an inflationary effect; (3) it would put several hundred thousand more workers on unemployment roles.

The petroleum tariff and tax plan (with rebate) would: (1) have a negligible effect on GNP; (2) increase prices on a largely one-shot basis by about 2½ percent; (3) not adversely affect employment.

A 30¢ gallon gasoline tax would: (1) reduce GNP by about 1½ billion; (2) increase overall inflation by about 1 percent; (3) have a slightly adverse effect on employment.