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STATEMENT BY THE
HONORABLE FRANK G. ZARB, ADMINISTRATOR
BEFORE THE
SENATE INTERIOR & INSULAR AFFAIRS COMMITTEE
JANUARY 31, 1975

I appreciate the opportunity to appear before you today to discuss the Administration's proposals for dealing with the Nation's energy problems.

As Secretary Morton has indicated, the present energy situation is in many ways worse than that which confronted us a year ago during the embargo. The prospect we now face -- without broad, decisive and prompt government action -- can only be one of continuing deterioration: continuing erosion of our economic vitality and national security. In the case of energy, a bad situation can, and will get worse unless and until we rise to the challenge, find that unity as a people which has enabled us to survive and prosper for two centuries, and promptly formulate and implement a national energy policy that restores our independence.

The scope of the task suggests its wide-ranging and long-lasting significance -- and the very immediate need to begin our dialogue. It will not be easy: the situation is too serious, and the impact of our decisions will be great. The lives of the American people -- indeed, those of the people of much of the world -- will be most profoundly affected by what we do, or fail to do, in the weeks ahead. And they will not be affected not just for five years or for ten years, but for generations to come.

Some commentators and critics have complained of the complexity of the President's program. Of course it is complex -- complex because of the very nature of our energy dilemma. Simple programs might solve simple problems, but they will not solve our energy problems. There may be those who take aspirin when the doctor advises open heart surgery, but they will not be around for long.

The problem for our nation and the international economic system is that severe. This is reason enough for us to think, not emote, and act, not delay.

The President has faced up to the difficulties and has prescribed the proper treatment. If it is hard or tough that is only because it will take tough action to cure our energy ills.



I would like today to discuss the goals he has set for the Nation and the various elements of his program that will enable us to accomplish them and, thus, restore our nation's energy health and independence.

Goals

As you will recall from Secretary Morton's statement, the three, time-phased goals of the President's program are:

One: 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: Importation by 1985 of no more than 3-5 million barrels per day of our total petroleum consumption -- and the capability of immediately replacing that amount from storage and standby measures in the event of a supply disruption.

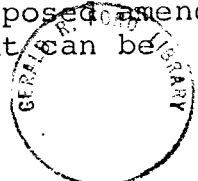
Three: Accelerated development of our new or exotic energy technology and resources so that the United States can meet a significant share of the energy needs of the Free World by the end of this century.

Actions to Meet the Short-Term Goal

In these crucial first 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. This increased production can amount to 160,000 barrels per day this year and 300,000 by the end of 1977.

As this Committee knows, 13 months ago the Senate voted to increase production from Elk Hills, but the House did not follow suit. We cannot wait any longer. This year, we trust, both Houses will act on the new legislation that will soon be submitted.

The Administration will also submit a set of comprehensive amendments to the Energy Supply and Environmental Coordination Act of 1974 to provide adequate authority for achieving the general goals of that law. The Administration's proposed amendments will greatly increase the number of plants 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. I am sure that most of us would like to feel that voluntary energy conservation would suffice -- after all, there are few Americans, indeed, who favor government intervention into their lives. But the facts are that voluntary conservation has not worked and that our national goals require considerably more. Some among us, faced with the imperative of government action, might favor the well-worn route of legislating a solution. To those who feel that a new law is always the answer, I would say that it is almost never the complete answer, that it has to be amended until, too often, it spawns new problems to replace those it has eliminated. The Administration's program, therefore has been structured in such a way that it combines voluntarism with legislation and involves in the effort a third, broad element -- maximum use of the workings of the free market.

Because we cannot wait months for the President's approach to energy conservation, legislative conservation measures must be administratively imposed. The first major action is an import fee of \$3 on all imported crude oil and petroleum products. This fee will be applied in three \$1 increments beginning in February and successive months.

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. As a matter of fact, although many in New England claim that their region would be hurt most by these actions, New England will actually experience a smaller price increase than almost any other area of the country. The increased import fees are only temporary and will be eliminated when Congress enacts more comprehensive tax legislation which includes an excise tax of \$2 per barrel on all crude oil and petroleum products.

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 new natural gas as previously proposed by the Administration, serve to prevent industry or utilities from 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 by April 1.

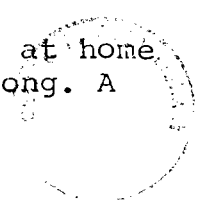
-- A program of income tax reductions and rebate measures to return to the economy the roughly \$30 billion estimated to be raised this year through these measures. Most of this money is to be restored directly to consumers, with special measures to provide funds for the poor.

The use of import fees and excise taxes to foster large-scale energy conservation has attracted the most attention and the most criticism.

I would like, therefore, to spend a few moments discussing alternatives. First, there is the alternative that no one advocates explicitly: the alternative of doing nothing. To those favoring this approach I would point out that we paid \$3 billion for imported oil in 1970, and \$24 billion in 1974. If we do nothing to reverse this trend, our bill will reach \$32 billion in 1977.

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 so 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, because 60 percent of the world's known oil reserves are there. Perhaps those who advocate delay or inaction expect the oil cartel to dissolve itself; perhaps they expect that those nations which combined to quadruple petroleum prices over the past year will voluntarily lower them to tolerable levels. Perhaps they believe that another dozen or so equally mythical events will transpire to relieve our dependence on unreliable sources of oil. Fortunately, there are others of us who are less sanguine about a future which does not include strong measures taken now. The plain facts are that while we have been talking ourselves into no action or rationalizing soft approaches to a hard problem, our vulnerability to political pressures from other nations has grown. The price of 40% 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 expensive, they should also reflect on the cost of the new embargoes within the next three years if we do nothing.

Some, however, feel that raising prices of energy at home will not help us cut back on consumption. They are wrong. A



comparison of our present consumption with that of last year shows that we are actually using slightly more now. But more importantly, we are using much less than we would have been if prices had not increased during the embargo. The result is that the cartel has cut back on production by several million barrels per day -- yet there is still a surplus of oil on the world market. There is evidence all around us that price is indeed effective in reducing demand.

There are others who question the costs of the Administration's program. Frankly, we have fully reviewed all of the analyses which have been in any form where they can be analyzed and they are wrong, either due to a misunderstanding of the President's Program or about the structure and economic behavior of the energy industries. No cost projection of such a complex subject is ever perfect, but our estimates are reasonable -- much more so than the others I have seen. More importantly perhaps for those who feel it is too expensive, the simple answer is -- it is too expensive not to act, and the President's Program, when all is said and done, will be the most effective one.

The other alternative to doing nothing is the greater use of government controls -- whether import quotas, allocation systems or rationing, or on a lower level, Sunday closings of gasoline stations, no-driving days, or other such so-called alternatives. We looked at all of those last year. We chose some and rejected others. And our reasoning was good at a time when we were managing a short-term crisis. We now face a longer-term one. And I doubt if any of us wants auto-less weekdays or gas-less Sundays for 10 years. That kind of alternative won't solve the problem; it would only launch an unending sequence of other new and annoying ones. In addition, each of these would involve some form of self-imposed shortages, built-in inefficiencies, burgeoning bureaucracies and regulatory proliferation, and demoralizing disruptions in the life of all American citizens. And most of them would also involve -- though their advocates often ignore or are ignorant of the fact -- higher costs to everyone. Gasoline taxes, for example, would have to be about 40¢ to 50¢ per gallon to save 1 million barrels of oil per day -- so those critics who complain of the higher prices implicit in the President's Program should not be heard taking the floor in favor of a straight gasoline tax. Nor is rationing a device that could provide adequate savings without higher prices. So, those critics who have just sat quietly through debate on a gas tax should be well prepared to exercise the same restraint when we get to rationing.

At present the average motorist in this country uses 50 gallons of gasoline per month, and pays \$27.50 per month for it.

Under the President's Program, if a driver still wanted to use 50 gallons, it would cost him a total of \$32.50 for the month.

Under the free-market rationing system developed last year, there would be only enough for the average driver to use 36 gallons per month. Beyond the first 36 gallons, each additional gallon would cost (including the purchased coupon) a total of \$1.75, so that 50 gallons would have a total cost of \$44.30.

Nor would those be the only costs. There would be a 15-20,000 man bureaucracy, the return of long lines at the gasoline pumps, and equally long lines at the coupon-distribution centers. Further, the income transfer effect would be very largely from the larger, rural states where people drive twice as many miles per capita, to the East Coast and other urban centers. And it would all last for ten years.

I think it's unnecessary for me to dwell on this at any greater length. Suffice it to say, many of the same faults lie with quotas or allocation schemes. Rather than continue the debate over preferences for the gasoline line or the coupon line, we must allow the free market to work to the maximum extent possible. This is what the energy conservation taxes and fees would do.

Mid-Range --1975-1985

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 supplies. In other words, by then our petroleum imports should amount to only about 3-5 million barrels per day of our consumption, and we should be able to implement standby measures and draw from storage enough to make up for any supply disruption. This is not much less than we import right now, but if we were to do nothing, we would be importing 12 or 13 million barrels per day by 1985'

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 national 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. And those decisions must begin now.

I have already mentioned the need for deregulation of new natural gas, which must be approved in this session of the Congress to reverse the trend of dwindling natural gas reserves, production and continued unemployment due to natural gas shortages.

The decline in domestic petroleum production can also be reversed, and higher prices will provide a strong incentive to produce more oil from known fields. But the largest part of increased production will have to come from wells drilled in major new frontier areas, including the Gulf of Alaska and the Atlantic.

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 15 to 20% earmarked for military needs and strategic storage. According to some 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 steps to take advantage of our most abundant energy resource, coal. The President vetoed the strip mining legislation passed by the last Congress, but it remains a valuable piece of work. With a minimum of changes to make the bill more precise, I am prepared to recommend that he sign a revised version into law. And I am prepared to work with the Congress so that those changes can be expedited and the law placed on the books as rapidly as possible.

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 also needs to 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 Secretary Morton and the Interior Department to adopt legal diligence requirements for existing Federal coal losses and to design a new program for accelerated leasing of Federal coal lands.

The first of the Secretary's meetings with the Governors to explore regional questions associated with new Federal coal leases has already taken place, so this program is underway.

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 as well. 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 delay and difficulties this industry is currently experiencing could well lead to higher oil import levels 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. In addition, the President will resubmit the Nuclear Facility Licensing Act for prompt Congressional action.

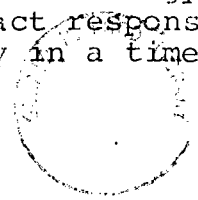
As we take these actions to increase our energy supplies, we must be aware of some potential problems. Before we achieve our goals of energy sufficiency, actions of oil producing nations, or economic conditions, could result in lower -- but unstable -- price levels that could weaken our continued commitment 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 with 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. 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. To do this, we must 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. To further insure stability as we move toward reduced vulnerability, we have requested legislation to authorize the use of tariffs, import quotas or other measures to maintain energy prices at levels that will protect domestic energy investment. 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 of 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 make available 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 prices uncertainty, raise capital and overcome unnecessary delays in bringing existing or nearly developed technologies into commercial use. The program will result in the demonstration of technologies of several types and the construction of major new plants, using both oil shale and coal resources.

Conclusion

A great deal has happened to change the energy outlook of this country since the first Energy Message to Congress in 1970. The changes have come more rapidly since the onset of the 1973 oil embargo. But now, since the President's State of the Union Message earlier this month, the time has come for all of us to stop for a moment and to put things into perspective. We can all agree on the goals that have been set forth -- and I believe the American people agree with them too. Starting from that agreement, we must get to work so that we move rapidly and wisely

toward the goals. Implementing this program will be hard -- but we all sit in these seats because we are supposed to be able to make hard decisions and carry through on them. The people of this country can accept difficulty and sacrifice if everyone shares the burden. And under this program, everyone will. Everyone will hurt a little, it is true; and various special interests will object to parts of the program that cause them distress. But if we listen to all of those special interests, if we think we can do away with the particular pains of every pressure group; then we will be left with no program, no improvement, and much greater pain for the country.

We cannot delay moving on the administrative and legislative parts of this comprehensive program. We can work together -- we must work together -- but on the whole program, and not on bits and pieces. Only a comprehensive program will meet the needs of the nation and the international community. We owe no less to those who are relying on us.

Thank you.

