

States in such quantities as to threaten to impair the national security; that the President shall cause an immediate investigation to be made if he feels there is reason for such belief; and that the President, if he finds a threat to the national security exists, shall take whatever action is necessary to adjust imports to a level that will not threaten to impair the national security.

"The committee believes that this amendment will provide a means for assistance to the various national defense industries which would have been affected by the individual amendments presented.

"The White House issued on February 26, 1955, a report based on a study by the President's Advisory Committee On Energy Supplies and Resources Policy which indicates the importance of a strong domestic petroleum industry."

Congress had thus provided the necessary tools for the President to use in case the growing tide of petroleum imports did not subside.

Imports of petroleum continued to increase.

As a consequence of the increased level of imports and the projected increase in the level of imports scheduled for the last half of 1956, the Independent Petroleum Association of America (IPAA) filed a petition on August 7, 1956, requesting action under Sec. 7 of the Trade Agreements Extension Act of 1955 (National Security Amendment).

Pursuant thereto, the Director of Defense Mobilization held public hearings beginning on October 22, 1956.

Early in December 1956, due to the changed conditions growing out of the Suez crisis, the Director of Defense Mobilization suspended action on the case.

However, on April 23, 1957, upon further review of the oil import situation and projected increases in oil imports, the Director of ODM "advised the President pursuant to Sec. 7 of the Trade Agreements Extension Act of 1955, that he had reason to believe that crude oil is being imported into the United States in such quantities as to threaten to impair the national security."

The growing threat to the domestic petroleum industry as a result of Congressional, industrial, and administrative studies, and the ODM certification, led to the establishment by the President of the United States on June 26, 1957, of a Special Cabinet Committee to Investigate Crude Oil Imports. This committee was made up of: Sinclair Weeks, Secretary of Commerce, Chairman; John Foster Dulles, Secretary of State; Donald A. Quarles, for Secretary of Defense; George M. Humphrey, Secretary of the Treasury; Fred A. Seaton, Secretary of the Interior, and James Mitchell, Secretary of Labor.

The report of the Committee, among other things, stated:

"Your Committee's investigation of the oil import problem has been confined to the effect of the present trend of imports on national security.

"It is clear that there is a direct relationship between the nation's security and adequate and available sources of energy. Oil and gas account for two-thirds of all the energy that is consumed in this country. Furthermore, there is no adequate substitute in sight for the foreseeable future. Therefore, we must have available adequate supplies of oil.

"We have concluded, for reasons that are set forth later in this section of the report, that if we are to have enough oil to meet our national security needs, there must be a limitation on imports that will insure a proper balance between imports and domestic production.

"Before arriving at this conclusion, we considered and rejected, for the reasons noted below, the following three proposals that are based on a policy of permitting imports to follow whatever course they may take.

"1. *Import foreign crude oil and store it in this country within depleted fields or elsewhere.* The practical problems of cost and the physical problems connected with the storage of crude oil would make this solution impracticable from the standpoint of industry and government alike.

"2. *Enlarge government participation in exploring for oil reserves which, when discovered, would not be put into production.* Such a course would be costly to a already overburdened government and would be contrary to the principles of free enterprise which characterize American industry.

"3. *Encourage increased importations in order that our own natural resources might be conserved.* Your committee has concluded that for the following reasons: such a policy would be unsound.

"(a) It would result in a sharp decline in domestic exploration by private enterprise because the industry would have no assurance of an adequate market for domestic oil after discoveries had been made and, as a result, would reduce.

its exploratory operations. Barring government operations which would be undesirable, adequate exploration and the development of additional reserves can only be generated by a healthy domestic production industry.

* * * * *

"IV Effect on Consumers"

"Domestic consumers are utilizing an increasing amount of petroleum products for transportation, fuel, heating and many other aspect of consumer life. In the event of a national emergency, it is essential to these consumers that there be adequate supplies at reasonable cost, both now and in the future. The low cost of imported oil is attractive, but excessive reliance upon it in the short run may put the nation in a longterm vulnerable position. Imported supplies could be cut off in an emergency and might well be diminished by events beyond our control. This vulnerability could easily result in a much higher cost, or even in the unavailability, o foil to consumers. It is therefore believed that the best interests of domestic consumers, as well as of national security, will be served if a reasonable balance is maintained between domestic and foreign supplies.

* * * * *

"In summary, unless a reasonable limitation of petroleum imports is brought about, your committee believes that:

"(a) Oil imports will flow into this country in ever-mounting quantities, entirely disproportionate to the quantities needed to supplement domestic supply.

"(b) There will be a resultant discouragement of, and decrease in, domestic production.

"(c) There will be a marked decline in domestic exploration and development.

"(d) In the event of a serious emergency, this Nation will find itself years away from attaining the levels of petroleum production necessary to meet our national security needs.

* * * * *

"It is our conviction that as a Nation we must pursue a careful, considered course that will permit reasonable imports into our country and still stimulate a dynamic and vigorous exploratory and development effort in this country."

This high-level policy committee submitted its report to the President and on July 29, 1957, President Eisenhower, in a memorandum for the Secretary of the Interior and the Director of the Office of Defense Mobilization, declared:

"I have approved the recommendations of the 'Special Committee to Investigate Crude Oil Imports' as set forth in the attached report. I direct you to put these recommendations into effect as rapidly as possible."

Presidential approval of the Special Cabinet Committee's report thus established what was known as the "Voluntary Oil Import Program." This program was put into effect on July 1, 1957; but it did not work.

Meanwhile Congress continued to evaluate the matter of oil imports and the "National Security Amendment." In the House Ways and Means Committee Report No. 1761, 85th Congress, 2d Session, which accompanied the Trade Agreements Extension Act of 1958, the Committee declared:

"The National Security Amendment"

"Section 2 of the 1954 Extension Act provided that no trade agreement reduction in duty shall be made if it would threaten domestic production needed for projected national defense requirements. Section 7 of the Trade Agreements Extension Act of 1955 amended this section by adding a new subsection providing a procedure for investigation and action by the President if he agrees with the Director of the Office of Defense Mobilization that any article is being imported in such quantities as to threaten to impair the national security. The 1955 amendment provided that, if the President found such to be the case, he take such action as he deems necessary to adjust imports to a level that would not threaten to impair the national security.

"These provisions were the subject of voluminous testimony to the committee and of extended committee consideration. Most of the witnesses who addressed themselves to section 7 of the 1955 act were of the opinion that the provision should be amended in such a way as to speed up investigations and determinations under the section, and to clarify and make more specific the standards applicable to its administration. The committee has carefully considered the points of view expressed and has concluded that any question as to the adequacy of section 7 is resolved by the amendments to that section which the committee has made.

"Your committee was guided by the view that the national security amendment is not an alternative to the means afforded by the escape clause for providing industries which believe themselves injured a second court in which to seek relief. Its purpose is a different one—to provide those best able to judge national security needs, namely, the President and the Director of the Office of Defense Mobilization, acting with the advice of such Cabinet officers as the Secretaries of Defense, Commerce, and State, a way of taking whatever action is needed to avoid a threat to the national security through imports. Serious injury to a particular industry, which is the principal consideration in the escape-clause procedure, may also be a consideration bearing on the national security position in particular cases, but the avoidance or remedy of injury to industries is not the object per se. There are other differences between the two procedures, such as that the one here under consideration applies to all imports whether or not the subject of trade agreement concessions. Again, in the choice of remedies the President is not limited in national security cases to action which he might take under the authority delegated to him in the trade-agreements legislation. However, it should be pointed out that the actions he may take under the authority of the national security amendment are limited to actions to adjust imports. In emergencies and for such time as necessary, the President may also take any action available to him under any of his other powers. Your committee considered it paramount to emphasize, however, that any action, large or small, for a short or long time, can be taken only if warranted by national security considerations. The interest to be safeguarded is the security of the Nation, not the output or profitability of any plant or industry except as these may be essential to national security."

During the floor consideration on June 10, 1958, of this legislation, House Ways and Means Committee Chairman Wilbur Mills, and Ways and Means Committee member, Representative Ikard, took part in the following colloquy: "Mr. MILLS. Mr. Chairman, I yield 10 minutes to the gentleman from Texas (Mr. IKARD)."

"Mr. IKARD. Mr. Chairman, I would like to ask the distinguished chairman of the committee two or three questions."

"Is it a fact that the so-called national security section of the committee bill has as its purpose providing the executive department with a means of taking whatever action is necessary to avoid a threat to our national security through imports and to make sure that injury to a particular industry essential to the national security will be avoided?"

"Mr. MILLS. The answer is 'Yes.'"

"Mr. IKARD. Is it a fact that the national security amendment of the present law was amended by the committee as reflected in the committee bill for the purpose of improving and facilitating the operation of this provision by providing specific criteria and guidelines for use in its administration?"

"Mr. MILLS. The answer to that question is 'Yes.'"

"Mr. IKARD. The national security section of the committee bill specifies certain factors which would govern the Director of the Office of Defense Mobilization and the President in determining whether imports are a threat to national security. These are stated in the committee bill substantially as follows:

"The Director and the President shall . . . give consideration to domestic production needed for projected national defense requirements, the capacity of domestic industries to meet such requirements, existing and anticipated availability . . . products, raw materials, and other supplies and services essential to the national defense, the requirements of growth of such industries and such supplies and services including the investment, exploration, and development necessary to assure such growth, and the importation of goods in terms of their quantities, availabilities, character, and use as those affect such industries and the capacity of the United States to meet national security requirements."

"I am interested in knowing how these criteria would relate to the problem of excessive imports of petroleum and petroleum products. Is it intended that under this provision imports of petroleum and petroleum products be held at levels which would permit the domestic industry to engage in a vigorous program of exploration at a rate consistent with the demands of our economy?"

"Mr. MILLS. This provision is intended to hold imports at a level which will permit the United States to have sufficient oil, known, discovered, and developed as is required to meet our national security needs."

"Mr. IKARD. Does the committee amendment that will be offered to the national security section of the committee bill dealing with investment, exploration, and development necessary to assure the proper growth of an industry have any significance to the petroleum industry and other extractive industries?"

"Mr. MILLS. Yes. This amendment will be offered to the bill for the purpose of further clarifying the committee's intentions with respect to encouraging free enterprise, exploration for, and the development of our natural resources at a rate sufficient to meet the demands of our national security. If drilling and exploration activities do not reach a satisfactory level, then under this provision the President or his designate would have the responsibility of re-evaluating existing programs for the regulation and control of imports to see that they meet the requirements of the new standards in the committee bill."

This Voluntary Program continued in operation until March 10, 1959, at which time the President established the Mandatory Oil Import Program. In contrast to the Voluntary Program which covered only crude oil imports, the Mandatory Oil Import Program covered imports of crude oil and its products and derivatives.

The Mandatory Program was established after the Director of the Office of Civil and Defense Mobilization on February 27, 1959, "advised the President that imports of crude oil and its products and derivatives were threatening to impair the national security."

On February 27, 1959, the Director of OCDM, in his memorandum for the President, quoted the Secretary of Commerce as follows:

"It is my considered opinion that the present rate of imports of crude oil and its derivatives and products is a major contributing factor to the *decline in drilling operations* both for exploration and development in the search for new oil reserves . . . Continuation of this trend will inevitably result in a lowering of our *available reserves*." (Emphasis supplied)

In this same report, the Director said:

"The consequences would continue to upset a reasonable balance between imports and domestic *production*, with deleterious effect upon *adequate exploration* and the *development of additional reserves* which can only be generated by a healthy domestic *production* industry." (Emphasis added)

Thus the President issued Proclamation No. 3279, dated March 10, 1959, which placed in effect the Mandatory Oil Import Program to be administered by the Department of the Interior.

When he established the Mandatory Oil Import Program, the President issued the following statement:

"I have today issued a Proclamation adjusting and regulating imports of crude oil and its principal products into the United States.

* * * * *

"The new program is designed to insure a stable, healthy industry in the United States capable of exploring for and developing new hemisphere reserves to replace those being depleted. The basis of the new program, like that for the voluntary program, is the certified requirements of our national security which make it necessary that we preserve to the greatest extent possible a vigorous, healthy petroleum industry in the United States."

Presidential Proclamation 3279, as amended, remains today as the foundation of the Mandatory Oil Import Program.

APPENDIX B.—IMPORTANCE OF PETROLEUM TO NATIONAL SECURITY AND ECONOMIC GROWTH

Petroleum is vital to both the national security and the economic growth.

PETROLEUM AND NATIONAL SECURITY

Comprehensive studies by the Congress and the Executive Departments made during the past twenty years, and practical experience in times of emergencies, repeatedly have recognized and demonstrated the importance of petroleum to national security.

With a Federal budget including many billions of dollars for programs of defense against all types of aggression, it is apparent that our security requirements for petroleum are not limited to the needs of a nuclear war. Our mobilization base must match the needs of a nuclear war, large-scale conventional warfare, limited conflicts and a protracted cold war. We must also maintain a position

of strength to prevent and deter war. In this effort, experience has demonstrated that no munition is more important than oil.

When oil imports were cut off during World War II, six of the seven billion barrels needed to meet the requirements of the United States and our allies came from domestic sources. Oil constituted two-thirds of all materials shipped overseas during that war.

Later, the shut-down of Iranian oil in 1951 and the closing of the Suez Canal in 1956 and 1957 disrupted oil supplies for the free world. During this Suez crisis, Western Europe was faced with the prospect of industrial collapse. European troops were landed in Egypt and World War III threatened. The United States as in World Wars I and II was in a position to supply oil to Europe and it was U.S. oil that overcame shortages and averted war. Without alternate supply sources to replace Middle East oil, the European nations affected were faced with two choices (1) to pay the price demanded or (2) take the Canal by force.

More recently, the Middle East crisis last June resulted in closure of the Suez Canal again and it has remained closed ever since. The domestic industry supplied the energy demands on the U.S. East Coast, Eastern Canada and in Western Europe. U.S. production increased by more than a million barrels per day during this emergency. However, unless our exploration effort is increased markedly and soon, the next emergency might find the U.S. unable to make up for the interrupted imports.

Today, Russia is engaged in a positive and successful program of greatly expanded Soviet oil production to strengthen Russia internally and to increase oil exports as a prime weapon in the Russian economic and political offensive. It would be foolhardy in the extreme for the United States to pursue policies that would weaken our security position as to petroleum supplies while the Soviets exert their efforts to maximize their petroleum capabilities. We simply cannot afford the risks involved in becoming increasingly dependent on uncertain foreign sources of oil.

In short, national security and the peace of the free world require that U.S. oil imports be limited to the extent necessary to maintain a vigorous, expanding domestic petroleum industry.

PETROLEUM AND ECONOMIC GROWTH

In addition to its importance to national security, petroleum is vital to the economic growth of the United States and the Nation's standard of living.

Petroleum (oil and natural gas) supplies 74 percent of total U.S. energy needs and energy is the indispensable ingredient of higher standards of living. Through the increased use of energy, men produce more; work more efficiently; live in greater comfort; and travel farther and faster on land and sea, under the polar ice cap, through the air, and out into the far reaches of space. The well-being and material progress of mankind is directly related to energy consumption.

During the past three decades, national income in the United States has paralleled the growth in energy consumption. The relationship between U.S. energy consumption and national income also holds true in the case of other countries. When a total energy is expressed in terms of equivalent gallons of oil consumed per person per year, national income varies from country to country in the direct relationship of one dollar of national income per capita for each gallon of energy.

PER CAPITA NATIONAL INCOME COMPARED WITH PER CAPITA ENERGY CONSUMPTION

	Energy consumption (expressed in gallons of oil)	National income (U.S. dollars)
United States.....	2,165	2,909
Canada.....	1,801	1,841
United Kingdom.....	1,216	1,453
Australia.....	1,129	1,620
West Germany.....	996	1,450
Netherlands.....	767	1,277
France.....	695	1,447
Japan.....	420	694
Argentina.....	315	740
Brazil.....	83	217
India.....	41	86

Source: United Nations, 1965.

Petroleum producing activities provide the economic lifeblood for thousands of local areas and communities. The 1963 Census of Mineral Industries reported 14,378 establishments engaged in U.S. oil and gas field operations and over 93 percent falls in the category of small business with less than 20 employees.

The petroleum producing industry, employing 270,500 people in 1967, is an important segment of the Nation's economy. The direct effect of declining oil industry activity on employment in all business activities in the producing areas is far-reaching.

Petroleum is the principal mineral produced in the United States. The 1967 value of domestic oil and natural gas production was over \$12 billion and exceeded the combined value of all other mineral production including coal, iron ore, aluminum, uranium, gold, silver, etc. Oil or gas is being produced in 32 of our 50 states. In 12 states, petroleum is the principal mineral. The value of petroleum production in these states and the percentage of the value of total mineral production are shown in the following tabulation.

STATES IN WHICH PETROLEUM IS MOST VALUABLE MINERAL, 1966

State	Value of petroleum production	Petroleum as percent of total value of all minerals
Arkansas.....	\$83,657,000	46.9
California.....	1,090,699,000	63.9
Colorado.....	102,388,000	36.2
Kansas.....	452,373,000	79.8
Louisiana.....	3,194,341,000	94.1
Mississippi.....	174,513,000	86.1
Nebraska.....	40,834,000	58.1
New Mexico.....	520,934,000	63.7
North Dakota.....	81,052,000	81.7
Oklahoma.....	914,247,000	92.2
Texas.....	4,579,863,000	90.9
Wyoming.....	391,697,000	78.2

Over 336 million acres, about 15 percent, of the land area of the United States is under lease by the industry of which only 9 percent or 31.5 million acres has been proved productive. The rentals paid on oil and gas leases, and the royalty payments to farmers and land and royalty owners aggregate some \$2 billion annually, a substantial item in our economy.

It is apparent that a healthy domestic oil industry serves the interest of economic growth and increased employment.

APPENDIX C.—DETERIORATING CONDITIONS IN THE U.S. OIL PRODUCING INDUSTRY

The Department of the Interior in a comprehensive report published in January 1965 concluded that "what has been done since 1956 to find new supplies of oil, whether through new discoveries or through increasing recovery rates of oil deposits, has not been enough to provide a sound basis for future growth."

An examination of industry experience in recent years confirms this conclusion.

Despite steady historical growth in the U.S. demand for oil products and the expectation that it will continue to do so, the exploratory and development effort of the domestic industry, rather than increasing, has been declining for more than ten years. The unhealthy trends and depressed conditions in the industry may be summarized as follows:

<i>Decrease since base period 1957-59</i>		1967 (percent)
Geophysical activity	¹	-38.7
Active rotary rigs.....		-47.1
Exploratory wells		-35.1
Total wells		-35.8
Employment		-17.0
Crude oil price.....		-3.0

¹ 1966 latest available.

As could be expected, the amount of new oil reserves found and developed has not kept pace with increasing demand and production. The record of new reserves found, compared with production, for the past 12 years is as follows:

PROVED RESERVES PETROLEUM LIQUIDS

[In thousands of barrels]

	New oil found	Year-end reserves	Production	Ratio reserves/ production
1956.....	3,784,156	36,336,981	2,897,910	12.5
1957.....	2,562,192	35,987,765	2,911,408	12.4
1958.....	3,466,448	36,739,935	2,714,278	13.5
1959.....	4,370,189	38,241,655	2,868,469	13.3
1960.....	3,090,458	38,429,270	2,902,843	13.2
1961.....	3,352,253	38,807,601	2,973,922	13.0
1962.....	2,913,445	38,700,740	3,020,306	12.8
1963.....	3,052,230	38,643,968	3,109,002	12.4
1964.....	3,273,511	38,737,142	3,180,337	12.2
1965.....	3,880,391	39,375,925	3,241,608	12.1
1966.....	3,858,094	39,781,093	3,452,926	11.5
1967.....	3,891,880	39,990,901	3,682,072	10.9

Source: American Petroleum Institute and American Gas Association.

The ratio of total proved reserves of petroleum liquids to yearly production suffered a steady decline from 13.5 to 1 in 1958 to 10.9 to 1 in 1967. The volume of oil reserves found and developed during the past seven years has averaged only 3.5 billion barrels per year, in contrast to the average of 5.4 billion barrels estimated by the Interior Department as needed to meet future demands and maintain a stable reserves-production ratio. For crude oil alone, this ratio was 11.8 in 1957 increasing to 12.9 percent in 1958 and declining steadily thereafter to 10.3 in 1967.

The depressed conditions in the producing branch of the domestic industry can be further illustrated by the decline in the real price of crude oil, as measured in constant 1967 dollars. The real price of crude oil in 1967 was 57 cents per barrel below the 1956 price and 80 cents per barrel below the 1957 price. In contrast wholesale prices generally have increased 10 percent; the cost of oil-field labor 40 percent; cost of oil well casing 29 percent; oilfield machinery 18 percent.

The downward trends in U.S. exploration and development activities since the mid-1950's are analyzed in the January 1967 report of the National Petroleum Council, entitled "Factors Affecting U.S. Exploration, Development and Production, 1946-1965." That report concluded that incentives an dprospective profitability for new investments in U.S. exploration and development were reduced, "due in large part to the cumulative impact of sharply reduced rates of expansion in oil consumption, rising imports, increasing unused U.S. crude oil productive capacity, and a substantially lower growth in the market for domestic crude at less attractive prices". It is pointed out that the relative position of the smaller units, as a group, in U.S. exploration, development and production activities declined steadily since the mid-1950's. This group, consisting of independent producers and drilling contractors, historically has played an important role in the discovery of oil and gas, and the multiplicity of effort by these units has been reduced as the incentives and economic opportunities decreased.

These changes, in terms of index numbers with the Government base period of 1957-59 as equal to 100, may be summarized as follows:

	Percent increase of decrease in 1965 over base period 1957-59		
	Chase Bank group	All other	Total, United States
U.S. exploration and development expenditures.....	+15.9	-35.2	-7.6

The sharp drops in exploration and development expenditures and production experienced by independent producers have been offset by increases in other areas such as the Louisiana and Texas Gulf Coast, where the extremely high costs and large capital requirements restrict operations generally to the larger companies.

Total U.S. crude oil production increased by 750,000 barrels daily from 1959 to 1965. All of this increase was by the "Chase Bank Group" of larger companies whose total production increased by 890,000 barrels per day, or 20.3 percent. The combined production by the thousands of independents actually declined by 140,000 barrels or 5.2 percent from 1959 to 1965.

The independent's share of total U.S. production has dropped from about 38 percent when the oil import program was established, to 32.5 percent in 1965. Despite this trend, the degree of concentration in domestic oil and gas production is very low relative to most other basic industries. However, the deteriorating position of independent producers adversely affects their vital role in the search for, and the development of, the new reserves needed to meet expanding U.S. requirements for oil and gas.

To illustrate further, information on expenditures for exploration and development in the United States are available for the same Chase Bank Group of companies as compared with the expenditures by thousands of independents. Approximately the same total amount was spent by each group in 1952 (\$1.86 billion by the majors and \$1.77 billion by the independents). Both groups substantially increased these expenditures from 1952 to 1957. A drastic change, however, took place from 1957 to 1965. The majors increased exploration and development expenditures over the 1957 level. In contrast, the expenditures by the thousands of independent producers declined sharply by 44 percent from \$2.43 billion in 1957 to \$1.36 billion in 1965.

The facts show clearly that independent producers have not been sharing in the increased domestic oil production and income. Confronted by rising costs and price erosion, the funds and incentives have been progressively reduced for independent producers that have historically assumed the leading role in drilling exploratory wells and finding the new reserves needed for future expansion.

The foregoing analysis has been presented to establish that the entire domestic producing industry is far from healthy and vigorous. Over-all figures for the United States as a whole or for a selected group of larger companies obscure a dangerous and unhealthy situation existing within the industry. As a matter of fact, the reported earnings of all oil companies, large and small, do not reflect the high and increasing replacement costs of finding new petroleum reserves. The largest part of the domestic oil being produced today was found at a small fraction of present discovery costs. Even the Chase Bank Group of companies would appear far less "healthy and vigorous" if their earning statements were based on today's replacement costs.

It is a fact that the domestic producing industry remains in a seriously depressed economic state. While the industry has the technical capabilities to find, develop and produce adequate petroleum supplies to meet national requirements for the foreseeable future, today's economic conditions make it impossible to accomplish what is needed to assure the future growth in keeping with expanded requirements.

Certainly, there are many factors contributing to the economic difficulties that have plagued the industry during the past decade. The fact that imports are not the only factor exerting an adverse impact in no way denies that these imports are an important factor. The experience of the industry under the Mandatory Oil Import Program leaves little doubt that there is a need to do no less than maintain the basic structure of the program, and certainly not to weaken its effectiveness.

The petroleum producing industry by its very nature is a long-term undertaking. From the time exploratory efforts are first begun until reserves are developed, normally requires some three to five years, and very often a much longer period. It is obvious, therefore, that the first prerequisite of the import program, if it is to properly serve its national security objective, is to provide assurance to domestic producers that the program has long-range stability.

APPENDIX D.—ADVERSE ACTIONS TAKEN WITH RESPECT TO THE MANDATORY OIL IMPORT PROGRAM

As summarized below, there has been an increasing number of "special treatments," both within and outside the 12.2 percent limitation.

1. *Production Base for Import Quota:* Proclamation 3541 dated June 10, 1963, revoked the provision that required the maximum level of imports into District I-IV be based on *actual* production during a period, and provided, in lieu thereof, that imports be based on *estimated* future production. *Actual* production is

preferable because it is free of the uncertainty involved in estimating procedures and because imports would not increase until there was an actual increase in domestic production. The most disconcerting aspect of this change in the Proclamation was that the only apparent reason was to avoid a reduction in imports that otherwise would have been required.

2. *Foreign Trade Zones:* Applications by two major chemical companies for the establishment of foreign trade zones at Midland, Michigan and Taft, Louisiana have been approved by the Foreign Trade Zones Board. The President issued Proclamation 3693 on December 10, 1965, in which he delegated to the Secretary of the Interior authority over the movement of foreign oil into such foreign trade zones in the United States. To date no action has been taken on these two applications by the Secretary of the Interior. If the licenses were to be issued, such feedstocks would be used to manufacture chemicals or oil products which in turn could be shipped into the United States.

If the Secretary of the Interior should approve the now pending applications, this action would certainly invite more requests for similar treatment. Likewise, the precedents set by the Foreign Trade Zones Board could very well bring about additional applications.

During public hearings on the two applications approved by the Board, many companies engaged in the manufacture of petrochemicals testified that for competitive reasons they would be forced to seek similar treatment.

Foreign trade zones are authorized for the purpose of encouraging U.S. exports. They should not be used for purposes of circumventing the oil import program.

3. *Petrochemical Allocations:* Prior to 1966, allocations of crude oil and unfinished oils for further processing were made only to refiners who processed the imported oil or exchanged their allocation for domestic crude oil. Proclamation 3693, dated December 10, 1965, amended the program for the purpose of providing allocations of crude oil and unfinished oils to petrochemical plants including those operated by chemical companies which had not been eligible. Petrochemical plants do not use crude oil as feedstocks. This action, therefore, set the precedent of granting crude oil quotas to companies that do not use crude oil. But even more disturbing, the action taken to bring chemical companies into the program was based on economic considerations unrelated to the national security as to our oil supplies, the sole purpose of the program.

During the past three years, officials of the Department of Commerce have advocated that chemical companies be given increasing access to imported oil as feedstocks for petrochemical plants. These officials have been concerned with maintaining and expanding the chemical industry's exports in the interest of the balance of payments problem—a matter of proper interest to the Department.

Allocations to chemical plants were increased in 1967 and Secretary Trowbridge and Secretary Udall announced in December 1967 a further increase for chemical use for 1968. In addition, Secretaries Trowbridge and Udall announced decisions designed to enhance the competitive position of chemical producers both in the United States and foreign markets. The Secretarial decision included a key proposal of the chemical companies for an import-for-export program which would permit imports of crude and unfinished oils in relation to the exports of petrochemicals and selected petroleum products.

It is pertinent to note in regard to the export-for-import program that the allocations to chemical companies now being received already exceed the equivalent feedstocks (about 50,000 barrels daily) used for total petrochemical exports.

Furthermore, in addition to the import-for-export program, it was announced that two distinct sectors will be established—one for energy and one for petrochemicals in the implementation of the oil import program.

The special treatments for petrochemical plants and chemical companies constitute one example of the pressures that threaten the future stability of the oil import program.

4. *Imports of Unfinished Oils:* Proclamation 3693 dated December 10, 1965, revoked the requirement that imports of unfinished oils could not exceed 10 percent of total crude and unfinished oil imports. The proclamation delegated authority to the Secretary of Interior to determine the limit on unfinished oil imports. Subsequently, a general limit of 15 percent has been established; but, in the case of petrochemical plants, up to 100 percent may be allocated in the form of unfinished oils. There is no national security justification for unfinished oil imports that only came into being during the voluntary import program in 1957-58 as a circumvention of the restriction on crude oil imports.

5. *Shipments from Puerto Rico, the Virgin Islands and Guam:* Under the import program as established in 1959, shipments of petroleum from Puerto Rico to the United States were not *directly* controlled. They were *indirectly* controlled

by providing that imports into Puerto Rico could not be increased for the purpose of increasing shipments into the United States. Under this policy the then existing movement of about 35,000 barrels daily of light petroleum products from Puerto Rico to the United States was stabilized through 1965. This policy, however, was changed on December 10, 1965, by Proclamation 3693, which provided for the allocation of imports into Puerto Rico of feedstocks for facilities in Puerto Rico which will provide "... a substantial and much needed increase in opportunities for employment of its citizens..." Here a new criterion was interjected as a basis for action on oil imports for purposes extraneous to national security. Under this new provision, two facilities in Puerto Rico have been approved, involving the importation of 110,000 barrels daily of feedstocks into Puerto Rico and shipment of 54,300 barrels daily of gasoline, jet fuel, and other product components to the United States.

On November 4, 1967, Secretary Udall announced approval of a plan by the Virgin Island Government for establishing a petrochemical complex on the Island of St. Croix, in the Virgin Islands. Approval also was granted for shipment of 15,000 barrels daily of finished petroleum products for a 10-year period to the United States. The basis for this action was that a major petrochemical plant will upgrade the standard of living in the Islands.

On December 15, 1967, Secretary Udall granted Commonwealth Oil and Refining Company an allocation to ship an additional 10,000 barrels per day of gasoline from Puerto Rico to the East Coast of the United States. Commonwealth's present shipment of 10,000 barrels daily of gasoline to the West Coast of the United States will be terminated. Secretary Udall stated, "at the same time, this change will substantially expand employment opportunities in Puerto Rico through the further development of its petrochemical and satellite industries."

On the same date (December 15, 1967) Secretary Udall also announced that an amended application by Union Carbide for petrochemical feedstocks for its Puerto Rico plant would be approved. The amended application calls for the importation for ten years into Puerto Rico of between 39,500 barrels per day to 45,000 barrels per day, depending upon whether it is unfinished oil or crude oil respectively. Approval of the Union Carbide application involved no shipment of petroleum products to the United States. However, certain chemical intermediates produced at the plant are destined for shipment to the United States for further processing.

The application by Texaco for importation of feedstocks for a planned new refinery in Puerto Rico has not yet been acted upon.

These refineries and petrochemical plants have a preferred position in the domestic market over facilities located in the United States because of the fact that such refineries and plants have access to imports for 100 percent of their feedstock requirements whereas imports represent an average of only 13 percent of total feedstocks in the United States. It is obvious, therefore, that these changes in the Proclamation create, for purposes unrelated to national security, a strong incentive for locating petrochemical plants and refineries in Puerto Rico for shipment of products to the United States. This constitutes a serious threat to the stability of the oil import program.

6. *Imports from Canada and Mexico:* Overland imports from Canada and Mexico are included within the 12.2 percent limitation in Districts I-IV. Not being subject to formal quotas, the quantity of these imports is estimated by the Interior Department and deducted from the overall limitation to determine offshore imports. In District V, Canadian imports are also estimated for purposes of determining offshore imports subject to quotas. The following tabulation compares the estimates of imports from Canada with actual imports.

IMPORTS FROM CANADA

[Thousand barrels daily]

	Districts I-IV			District V			Total, United States		
	Estimate	Actual	Overage	Estimate	Actual	Overage	Estimate	Actual	Overage
1963.....	123	130	7	129	131	2	252	261	9
1964.....	139	150	11	143	147	4	282	297	15
1965.....	162	174	12	148	150	2	310	324	14
1966.....	180	212	32	155	172	17	335	384	49
1967.....	225	253	28	144	189	45	369	442	73
1968 (January and February).....	280	337	57	135	167	32	415	504	89

Canadian imports have consistently exceeded the estimates with the excess increasing to 49,000 barrels daily in 1966 and to 73,000 in 1967. The overage in 1968 is expected to be about 60,000 barrels daily in Districts I-IV.

Through agreement between the U.S. and Mexican governments, imports from Mexico have been stabilized at 30,000 barrels daily.

7. *Bonded Jet*: When the Mandatory Oil Import Program was established in 1959, there were no bonded imports of jet fuel. In 1968, such imports are expected to exceed 100,000 barrels per day. Such imports have never been within the Program and therefore are on top of the levels established in the interest of national security.

For several years, IPAA has recommended that all bonded jet imports be included within the total permissible import levels. These large volumes of jet fuel, outside of the import program, circumvent the intent and goals of this program.

In addition, there are several aspects of this matter that appear to violate the letter and intent of the law governing bonded imports. For example, Section 309 of the Tariff Act of 1930 (19 U.S.C.A. 1309) permits imported bonded jet fuel to be withdrawn free of the import tax for use on aircraft which is "actually engaged in foreign trade or trade between the United States and any of its possessions."

Under this authority, the Bureau of the Customs has permitted the use of bonded jet fuel by both domestic and foreign carriers on the domestic legs of foreign flights. This seems to be improper and in conflict with the law. For example, a flight originating in Paris destined for Los Angeles with a stop in New York is permitted to use bonded jet fuel on the New York to Los Angeles leg of the flight. The same aircraft then proceeds to Los Angeles with some or all of its Paris to Los Angeles passengers, together with passenger and cargo originating at New York. Passengers are permitted to enplane or deplane at these intermediate stops just as on purely domestic flights.

According to available information, more than 20 percent of the total bonded jet fuel used in the United States is consumed on domestic legs of such flights.

Another matter which appears to be in violation of applicable law is the policy of the Bureau of Customs in permitting the use of bonded jet fuel by aircraft engaged in flights between the United States and Puerto Rico.

It would seem that the exemption in Section 309(a) of the Tariff Act of 1930 would not apply to these flights since Puerto Rico is now a commonwealth and not a possession. Nevertheless, the Bureau of Customs has rules that such flights are exempt even though the exemption only applies to aircraft actually engaged in foreign trade or trade between the United States and any of its possessions.

8. *No. 4 Fuel Oil*: Proclamation 3794, dated July 17, 1967, changed the definition of "residual fuel oil" which had been in effect since 1959. The effect of the change was to define No. 4 fuel oil, which theretofore was a product included within the 12.2 percent quota, as residual and therefore outside the quota. Thus the 12.2 percent quota is thereby violated by an amount estimated to be in the order of 25,000 barrels daily. This action was taken without a hearing or request for comments from interested or affected parties.

9. *Low Sulphur Residual Fuel Oil*: Proclamation 3794 dated July 17, 1967, for the stated purpose of abating air pollution, delegated to the Secretary of the Interior authority to permit imports in excess of the established maximum national security levels to persons who manufacture low sulphur residual fuel oil. This action is for a commendable purpose but, again, the action is unrelated to the national security. Implementing this authority the Secretary on October 4, 1967, issued a regulation with grants bonus imports of crude oil to manufacturers of low sulphur residual fuel oil in District V (States west of Rockies). On May 24, 1968, proposed regulations to grant import allocations in Districts I-IV based on production of low sulphur residual fuel oil were issued. The imports would not be within the overall 12.2 percent limitation and Secretary Udall estimated such "bonus" imports would total 300,000 barrels per day within several years. So here again the industry is faced with actions unrelated to the national security which could have a far-reaching impact on the effectiveness of the program.

10. *Asphalt Imports*: Proclamation 3779, dated April 10, 1967, delegates to the Secretary of the Interior authority to permit asphalt to be imported in excess of the maximum import levels established in the interests of national security. On August 28, 1967, the Secretary of the Interior issued proposals to implement this proclamation. The purpose of this change in the Proclamation and the pending proposals of the Secretary are extraneous to the national security objectives as to oil supplies. In addition, this change in the import program is unnecessary because

there is no shortage of asphalt. This matter is still pending, and is another cause for apprehension as to the long-range stability of the Mandatory Oil Import Program.

This action marked the first time that a modification in the Presidential Proclamation was in advance of hearings or without solicitation of public comments from interested and affected parties. The Office of Emergency Planning was subsequently asked to conduct an immediate investigation of the national security implications of such asphalt imports. Although the OEP announced a "timely" inquiry would be made as to the national security implications of relaxing import restrictions in April 1967, to date no report has been issued by OEP.

11. Supply of No. 2 Fuel Oil: No. 2 fuel oil is used primarily for home heating purposes. Approximately 20 percent of total U.S. crude oil production is converted into No. 2 oil. It is the industry's second (gasoline is first) most important oil product. The basic purpose of the Mandatory Oil Import Program is to assure that the domestic industry is capable of supplying the demand for the principal petroleum products derived from domestic crude oil. The availability of crude oil, the magnitude of U.S. refinery capacity and the flexibility of refiners to adjust yields to maximize the output of No. 2 fuel oil leave no doubt that the supplies of this fuel will continue to be adequate.

Despite the adequacy of supply, on September 27, 1967, the Oil Import Appeals Board granted allocations to 3 petitions to import No. 2 fuel oil in the amount of some 3,000 barrels daily. The basis premise for this decision is the Board's finding that:

"The Board finds that the three subject petitioners for No. 2 oil allocations are suffering exceptional hardship attributable to oil import controls."

This finding is in conflict with the facts presented by the Director of the Interior Department's Office of Oil and Gas in a speech on October 3, 1967, as follows:

"If I were asked to summarize the outlook for distillate fuel oil this winter, I would describe it as good, but nevertheless, one to be watched closely. In its reaction to the vast dislocations of last summer, the petroleum industry has once again proved its flexibility and responsiveness. I see no reason why it should do less well in the present case."

In these "September" cases, the Appeals Board erroneously blamed the import program for some alleged isolated hardship claims which, even if justified, were due to the transportation problems created by the Middle East crisis and not to the Mandatory Oil Import Program.

In January 1968, some other No. 2 fuel oil dealers in the North East complained again of a threatened shortage of No. 2 fuel oil.

In spite of abundant evidence from governmental and industry sources that there was no real or prospected shortage of No. 2 fuel oil, the Import Appeals Board on February 28, 1968, granted to 12 fuel oil dealers import allocations of some 7,000 barrels per day for the balance of the year 1968. The Board made no real finding of a shortage for the early months of 1968 heating season. As a matter of fact, for the most part, the allocations which were granted for the entire year of 1968 were not even used during the first quarter winter heating season.

While the total volume of imports involved in these No. 2 fuel oil cases is not great, there is cause for concern. This action sets a precedent for opening up the import program to thousands of marketers of not only No. 2 fuel oil but also gasoline and other products. The purpose of the program is to assure adequate oil supplies for national security—not to solve the competitive problems of individual marketers.

12. Carry-over Unused 1967 Allocations: Because of the Suez crisis last year importers were unable to use their import allocations to the extent of about 143,000 barrels daily on the average for the year. On January 29, 1968, Secretary Udall, without have held a public hearing, announced that importers would be permitted to utilize these unused import allocations during 1968 and 1969. The Secretary further arbitrarily decided that one half of such imports would be included within the 12.2 percent ceiling and one half would be over and above said ceiling. As a result of this action, imports outside the 12.2 ceiling will be increased during 1968 and 1969 by approximately 36,000 barrels daily. These additional imports not only displace domestic production that would otherwise be produced but in addition will aggravate the balance of payments problem in the

order of \$36 million dollars annually. Also, this action rewards Middle East nations by restoring markets in the United States for oil denied to this country during the 1967 crisis.

APPENDIX E.—U.S. BALANCE OF PAYMENTS AND WORLD OIL TRADE

Oil is the largest item in world trade. Analysis of world oil trade reveals two significant facts: (1) that oil imports into U.S. constitute our largest trade deficit item; and (2) that the Mandatory Oil Import Program does not prevent a very healthy growth rate in the principal foreign oil producing countries.

OIL AND U.S. BALANCE OF PAYMENTS

Despite the Administration's program to improve the balance of payments, persistent deficits continue.

The deficit in U.S. petroleum trade is a significant item in our chronic balance of payments problem. Oil is now the Nation's No. 1 commodity import, dollar-wise. Petroleum imports last year were valued at \$2.1 billion according to the Department of Commerce. Even this reported total is understated since the values are based on the market value in the foreign country, or f.o.b. port of loading. The reported total does not include tanker freight payments to foreigners to haul the oil or U.S. military purchases abroad. If these payments are added the total outlays for foreign oil becomes \$2.6 billion in 1967.

A summary of the dollar value of U.S. petroleum imports and exports as reported by the Department of Commerce for the last ten years is as follows:

U.S. PETROLEUM TRADE BALANCE

[In millions of dollars]

	Exports, petroleum and products	Imports, petroleum and products	Petroleum trade balance
1956.....	762	1,286	-524
1957.....	992	1,548	-556
1958.....	557	1,615	-1,058
1959.....	480	1,529	-1,049
1960.....	479	1,534	-1,055
1961.....	445	1,637	-1,192
1962.....	443	1,729	-1,286
1963.....	446	1,782	-1,336
1964.....	419	1,873	-1,454
1965.....	418	2,052	-1,634
1966.....	436	2,104	-1,668
1967.....	539	2,089	-1,550

¹ Suez crisis caused a reduction in imports.

A stabilization in the volume of oil imported and the diversion of a portion of military purchases from foreign to domestic sources are two practical means of making a substantial contribution toward alleviating our balance of payments deficit. Equally important, such actions would serve the interest of national security by assisting in the restoration of vitality to the domestic petroleum industry so that adequate availability of oil and gas would be assured.

Unfortunately, rather than stabilizing imports, the Department of the Interior, through recent actions and inactions, has permitted imports over and above the 12.2 percent ceiling in the amount of about 240,000 barrels daily in 1968 with the result that the balance of payments has been adversely affected in the amount of about \$240 million annually.

OIL HAS CONTRIBUTED MORE THAN ITS FAIR SHARE

It is submitted that no one domestic industry should be called upon to contribute more than its fair share to the stimulation of foreign trade.

The history of oil imports shows that oil has made a disproportionate contribution.

The rapid growth in oil imports since World War II may be summarized as follows:

U.S. PETROLEUM IMPORTS

[Thousand barrels daily]

	U.S. crude oil production	Crude oil and products (except residual fuel)	Residual fuel oil	Total	Percent of U.S. production	
					Imports (except residual)	Total imports
1946.....	4,751	255	122	377	5.4	7.9
1956.....	7,151	991	445	1,436	13.9	20.1
1966.....	8,295	1,541	1,032	2,573	18.6	31.0
1968.....	8,950	1,692	1,150	2,842	18.9	31.8

This table shows that oil imports have not only grown rapidly quantitatively but that there has also been a spectacular growth in imports as related to domestic crude oil production, this ratio now being almost 32 percent.

Another indication of the substantial contribution oil has made is the fact that for many years, coffee was the principal import item. This was logical since we do not grow coffee here. In 1957, however, petroleum displaced coffee as our principal import item. This is an anomalous situation since about 18 percent of our producing capacity or 2,225,000 barrels per day, is shut-in and idle. It is like exporting coffee to Brazil or oil to Venezuela and the Middle East.

FOREIGN OIL PRODUCTION

The Mandatory Oil Import Program, in effect since 1959, has not prevented substantial growth in the principal foreign oil producing countries of the free world. The record of oil production in the Eastern Hemisphere, Venezuela and Canada has been as follows:

FREE FOREIGN OIL PRODUCTION

[Thousand barrels daily]

	Eastern Hemisphere	Venezuela	Canada
1959.....	5,420	2,771	521
1960.....	6,376	2,856	544
1961.....	6,977	2,919	643
1962.....	7,903	3,199	734
1963.....	8,881	3,248	786
1964.....	10,459	3,393	852
1965.....	11,571	3,473	922
1966.....	13,084	3,371	1,013
1967 (preliminary).....	14,260	3,537	1,115
Percent increase, 1967 versus 1959.....	+163	+28	+114

Eastern Hemisphere oil production has increased by more than 8,800,000 barrels daily since 1959. The increase in Eastern Hemisphere production would have been 177 percent without any shipments to the United States.

Venezuelan production shows an increase of 766,000 barrels daily or 28 percent from 1959 to 1967. During this period, shipments of Venezuelan oil to the U.S. market accounted for about one-third of the total increase in Venezuelan output with two-thirds of the increase going to foreign markets.

In the case of Canada, increased shipments to the U. S. market have been a more significant factor in the expansion of Canadian production. Canadian oil production rose by 114 percent from 1959 to 1967. Almost two-thirds of this increase in Canadian output was shipped to markets in the United States and one-third used in Canada.

These facts demonstrate that the Mandatory Oil Import Program has not prevented healthy increases in foreign production.

The principal markets for the foreign oil producing countries of the free world are markets other than the United States. The market pattern since 1959 has been as follows:

MARKETS FOR FOREIGN OIL, 1959-67

[Thousands of barrels daily]

	1959	1960	1961	1962	1963	1964	1965	1966	1967 ¹
Venezuela and NWI:									
To United States.....	1,106	1,159	1,151	1,240	1,232	1,311	1,360	1,404	1,377
To other markets.....	1,665	1,687	1,768	1,959	2,016	2,082	2,113	1,967	2,160
Total.....	2,771	2,846	2,919	3,199	3,248	3,393	3,473	3,371	3,537
Canada:									
To United States.....	95	117	188	248	265	300	326	387	454
To other markets.....	426	427	455	486	521	552	596	626	661
Total.....	521	544	643	734	786	852	922	1,013	1,115
Eastern Hemisphere:									
To United States.....	383	386	393	393	366	409	462	431	303
To other markets.....	5,037	5,990	6,584	7,510	8,515	10,050	11,109	12,653	13,957
Total.....	5,420	6,376	6,977	7,903	8,881	10,459	11,571	13,084	14,260
Total free world:									
To United States.....	1,780	1,815	1,917	2,082	2,123	2,258	2,468	2,573	2,536
To other markets.....	7,732	8,818	9,618	10,804	11,876	13,534	14,637	16,076	17,695
Total.....	9,512	10,633	11,535	12,886	13,999	15,792	17,105	18,649	20,231

¹ Preliminary

Source: U.S. Department of the Interior, Venezuelan Ministry of Mines and Hydrocarbons, and Oil and Gas Journal.

It is neither equitable nor in the interests of national security that the desire of foreign producing nations for ever-greater markets should take precedence over the need for increased exploration and development by the domestic industry in the public interest.

SOVIET OIL

The Soviet Union in 1960 displaced Venezuela and became the world's second largest crude oil producing country, second only to the United States. The following table compares the growth in oil production of the U.S. and the Soviet Union:

UNITED STATES AND U.S.S.R. CRUDE OIL PRODUCTION

[Thousand barrels daily]

	United States	U.S.S.R.
1955.....	6,807	1,397
1956.....	7,151	1,671
1957.....	7,170	1,967
1958.....	6,710	2,264
1959.....	7,054	2,591
1960.....	7,035	2,949
1961.....	7,183	3,321
1962.....	7,332	3,725
1963.....	7,542	4,121
1964.....	7,614	4,490
1965.....	7,804	4,893
1966.....	8,295	5,337
1967 ¹	8,812	5,797

	Increase	Volume	Percent	Volume	Percent
1955-60.....		228	3.3	1,552	111.1
1960-67.....		1,777	25.3	2,848	96.6
1955-67.....		2,005	29.5	4,400	315.0

¹ Preliminary.

Source: U.S. Bureau of Mines.

Russian production, which was only 20 percent of U.S. output in 1955, has increased steadily and in 1967 amounted to 66 percent of United States production. Exploration and development in Russia is expanding. There is a continuing decline in the United States.

Between 1955 and 1960, U.S. crude oil production increased 3 percent, total free world production rose 30 percent, but Soviet output more than doubled. During the interval 1960-1967, U.S. crude oil production increased by 1.8 million barrels per day, or 25 percent, while output in the U.S.S.R. rose by 2.8 million barrels per day, or almost double the U.S.S.R. production rate in 1960.

Soviet Bloc oil exports, excluding intra-Bloc trade, exceed one million barrels per day and constitute the largest trade item with free world nations. The Soviet Government arrangements for sale of petroleum to free world customers are usually made on a government-to-government basis. Terms are set to further the Soviet political and economic gains and effectively eliminate competition from other supply sources. The Soviet Union has used barter arrangements where oil is exchanged for a specified list of products. The value of oil in this arrangement varies according to the importance of the commodities received in exchange. Regular commercial sales are also made without exchange of goods with a Soviet discount sufficiently below established prices to close the deal. Petroleum exports are also arranged to satisfy trade deficits from previous imports. In addition, trade arrangements have been made wherein oil is shipped as part of a long term Soviet loan.

In view of Russia's increasing strength as to petroleum, the United States must have the assurance of adequate domestic oil supplies. This requires an effective program of limiting U.S. oil imports so that domestic production can expand in keeping with national requirements.

Mr. McCURE. I think we will proceed then with Mr. Clinton Engstrand, who represents the Kansas Independent Oil & Gas Association and the liaison committee. Clint.

STATEMENT OF CLINTON ENGSTRAND

Mr. ENGSTRAND. I am appearing in a dual role and I will cover the liaison committee first.

My name is Clinton Engstrand. I am appearing on behalf of R.A. Campbell, who is chairman of this committee, and I happen to be vice chairman.

The liaison committee is composed of representatives from 22 oil and gas associations spread throughout the United States, and I am merely going to make a short statement that we met in Biloxi, Miss., last month and voted to appear before this committee in full support of the testimony submitted by the Independent Petroleum Association of America.

The liaison committee endorses the need for congressional guidelines that will insure elimination of special treatment and volumetric loopholes in the mandatory oil imports program which now seriously threaten the program's integrity and effectiveness.

Mr. Chairman, the liaison committee strongly urges that Congress adopt legislation that would assure a sound import program free from administrative manipulation on behalf of the special interests and non-security objectives.

(The liaison committee's statement follows:)

STATEMENT OF POSITION ON THE MANDATORY OIL IMPORTS PROGRAM BY THE LIAISON COMMITTEE OF COOPERATING OIL AND GAS ASSOCIATIONS, R. A. CAMPBELL, CHAIRMAN

Mr. Chairman and members of the committee, my name is Clinton Engstrand of Wichita, Kansas. I appear before you on behalf of R. A. Campbell, Chairman of the Liaison Committee of Cooperating Oil and Gas Associations. I am Vice-

Chairman of this Committee. Mr. Campbell expresses his sincere regret for being unable to attend this hearing personally.

The Liaison Committee is composed of representatives from 22 oil and gas associations spread throughout the United States. The names of these associations are as follows:

- Alaska Independent Petroleum Association.
- American Association Oilwell Drilling Contractors.
- California Independent Producers and Royalty Owners Association.
- Cardinal Petroleum.
- Eastern Kansas Oil and Gas Association.
- Kansas Independent Oil and Gas Association.
- Kentucky Oil and Gas Association.
- Land and Royalty Owners of Louisiana.
- Michigan Oil and Gas Association.
- Mississippi-Louisiana Oil and Gas Association.
- National Stripper Well Association.
- North Dakota Independent Oil and Landowners Association.
- North Texas Oil and Gas Association.
- Ohio Oil and Gas Association.
- Oklahoma Independent Petroleum Association.
- Panhandle Producers and Royalty Owners Association.
- Permian Basin Petroleum Association.
- Southwest Kansas Royalty Owners Association.
- Southwest Pennsylvania Oil and Gas Association.
- Texas Independent Producers and Royalty Owners Association.
- Tri-State, Inc.
- West Central Texas Oil and Gas Association.

The Liaison Committee met in Biloxi, Mississippi last month and voted to appear before this Committee in full support of the testimony submitted by the Independent Petroleum Association of America. The Liaison Committee endorses the need for Congressional guidelines that will insure elimination of special treatment and volumetric loopholes in the Mandatory Oil Imports Program which now seriously threaten the program's integrity and effectiveness. Such legislation, in the opinion of the Liaison Committee, should, at the very least, secure a 12.2 ratio between non-residual fuel oil imports and domestic production in the United States east of the Rocky Mountains as an absolute maximum authorization for such imports. The Committee urges that this standard be placed in the law so that the nation's security will be preserved by according domestic oil producers the market stability required to reverse drastic downward trends in domestic oil exploration activities.

Domestic producers are drilling approximately 40 percent less wells today than they were drilling twelve years ago. As a result, domestic reserve productive capacity has fallen below the current oil imports level. Unless drilling is soon restored to more adequate levels, the United States will prove unable to provide necessary oil supply in the event oil imports should be drastically reduced in an emergency.

For these reasons, Mr. Chairman, the Liaison Committee strongly urges that Congress adopt legislation that would assure a sound import program free from administrative manipulation on behalf of special interests and non-security objectives.

I have a statement here from the Kansas Independent Oil & Gas Association, known as KIOGA, and I am appearing on behalf of Mr. Richard Hoover who is president. I happen to be a vice president, director, and a former president of KIOGA. I am just going to make a short statement.

The State of Kansas is historically and currently one of the leaders in production of both crude oil and natural gas. Activity in the State is carried on mostly by independent operators, especially in the field of exploration.

Now, in the State of Kansas we have experienced about the same decline in activity, production, and reserves as Mr. McClure stated in his testimony. From 1957 to 1967 our crude oil production dropped

from 125 million barrels a year to 98 million, a drop of 27 million, and our reserves dropped from 950 million barrels to 700 million barrels, and these figures came from the Kansas Corporation Commission and the API.

Our gas reserves dropped from 1959, at which time we estimated 20 trillion cubic feet, to currently 15 trillion cubic feet, a little bit over 15 trillion cubic feet.

In 1957 we were a net exporter of crude oil from the State of Kansas to other refineries outside the State and as of today we import approximately 70,000 barrels a day into the State.

Our well completions have dropped from 3,306 in 1960 to 2,572 in 1967. And our rotary activity is practically identical as one on the national scale. We dropped from 155 in 1957 to 41 in 1967 and currently it is estimated at 32 for 1968.

Mr. Chairman, I appreciate the opportunity to appear before this committee.

The CHAIRMAN. Without objection your entire statement will be made a part of the record.

Mr. ENGSTRAND. Thank you.

(Mr. Engstrand's prepared statement follows:)

STATEMENT OF CLINTON ENGSTRAND, VICE PRESIDENT AND DIRECTOR, KANSAS
INDEPENDENT OIL AND GAS ASSOCIATION

The State of Kansas historically and currently is one of the leaders in the production of both crude oil and natural gas in the United States. Activity in the state is carried on mostly by independent operators, especially in the field of exploration.

KANSAS IN DECLINE

Within the past decade the producing industry in Kansas has been devastated by powerful economic forces and government action. Its numbers have been drastically reduced, its productive capacity has dwindled, the search for vital energy reserves has declined alarmingly and daily production has diminished.

MANDATORY OIL IMPORT PROGRAM—ITS DEFECTS

This near depression and its acceleration have coincided almost precisely in point of time with the administration of the mandatory oil import program. In terms of its stated purpose of assuring a vigorous domestic petroleum industry for national security reasons, the program has failed miserably. Moreover, the program has come to be a principal factor in the frightening adverse balance of payments which now confronts the United States.

In the past year there have been mounting signs that the program is being totally dismantled. There are also unmistakable signs that this is the result of design rather than inadvertence.

Time here will not permit a delineation of all of the loopholes that have crept into the program. The record is replete on this point. As proceeding, the program can only lead to the use of autocratic power by the Secretary, unjust enrichment of international oil companies, ruination of the domestic independent operator and chaos in the producing areas of the United States.

What is needed is some stability in the program. Originally that was supposed to be one of its chief assets. It is now a factor least in evidence. Suffice it to say that the Secretary has ordered a bewildering array of exceptions to the program, none of which are grounded on national security. Most all have been totally unrelated to national security.

ENERGY BASE OF THE UNITED STATES THREATENED

The independent segment of the petroleum industry, which discovers most of the oil and gas reserves in the United States, is dismayed and discouraged by these developments. In numerous Department of the Interior hearings the administration has been warned that it was courting disaster by the manner in which it administered the program. It has ostensibly refused to acknowledge that today the United States cannot produce enough oil to meet domestic demand. During the Suez crisis and the dangerous summer of 1967, the domestic industry was able to adjust supply to meet demand. But that crisis only lasted a week. Even then discriminating observers were noting that production could not be sustained at so high a level for any extended period.

Even in that short period, the excess producing capacity of many fields was seriously impaired. Spokesmen for government and the international oil companies recklessly enunciated the position that the United States had much unused excess producing capacity. The facts do not support this assertion.

INTERIOR GUILTY OF MALADMINISTRATION

The Department of the Interior has gone the further step of putting a lid on oil prices. Adequate crude oil prices are the sine qua non of exploration. Without them the industry will not undertake a revitalized search for oil and gas reserves. A vexatious inflation has sharpened the difference between the price a producer receives for his oil and the price he pays for necessary goods and services. A scarcity of supply will guarantee increased consumer product prices. Energy demands in this country are increasing prodigiously. It is no secret to the distinguished members of this committee that so-called cheap foreign oil will be cheap only so long as we do not need it. It probably isn't very cheap today if we add to its current barrel cost the expense of maintaining the U.S. Sixth Fleet in the Eastern Mediterranean Sea so as to protect it.

INCREASED EXPLORATION NECESSARY

All reputable authorities assert that there are adequate undiscovered reserves of crude oil in this country, awaiting only the drillers bit. Success ratios of wildcat ventures in Kansas, despite a sharp decline in total effort, have held at about 16% for the past decade. This surely means that granted reasonable prices and stable markets, both of which are affected by the oil import program, we have the tools and know-how to discover needed supplies. We attribute the slight increase in wildcats drilled in 1966 to the optimism generated by a modest crude price restoration which occurred at that time.

SUMMARY

Productive capacity, production and exploration have declined alarmingly in Kansas in the past decade. The same trend has occurred in most of the other producing areas of the United States. Maladministration of the mandatory oil import program has been a principal contributing factor in this decline.

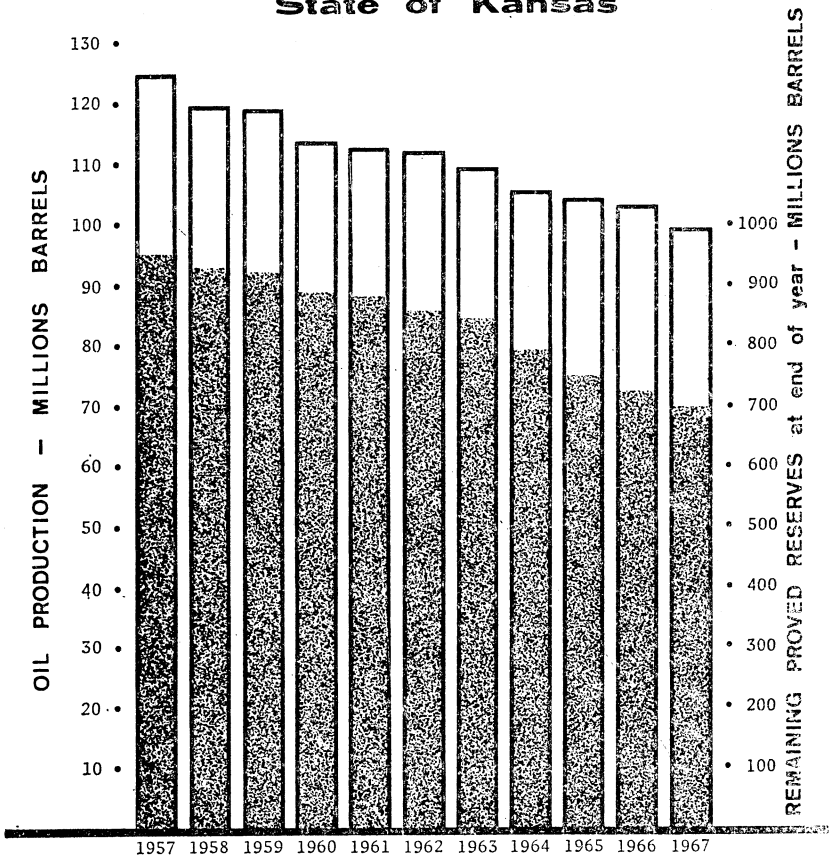
Powers of the administration and the Department of the Interior with respect to the program should be defined by statute. S. 2332 would effectuate this purpose.

Volumetric increases in oil imports are the largest single commodity factor in the imbalance of payments. These same imports threaten a great domestic industry.

Until stability is restored to the import program a renewed and revitalized search for oil and gas in the on-shore continental United States will not be undertaken.

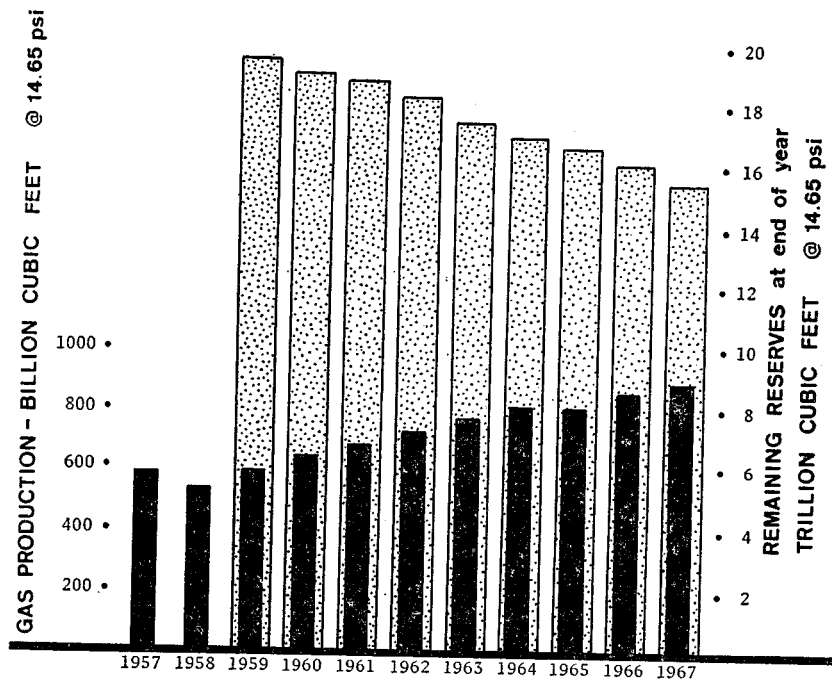
We congratulate and salute the chairman and this committee for conducting these important hearings and thank you for the opportunity to appear.

CRUDE OIL PRODUCTION **and** **REMAINING RESERVES** **State of Kansas**



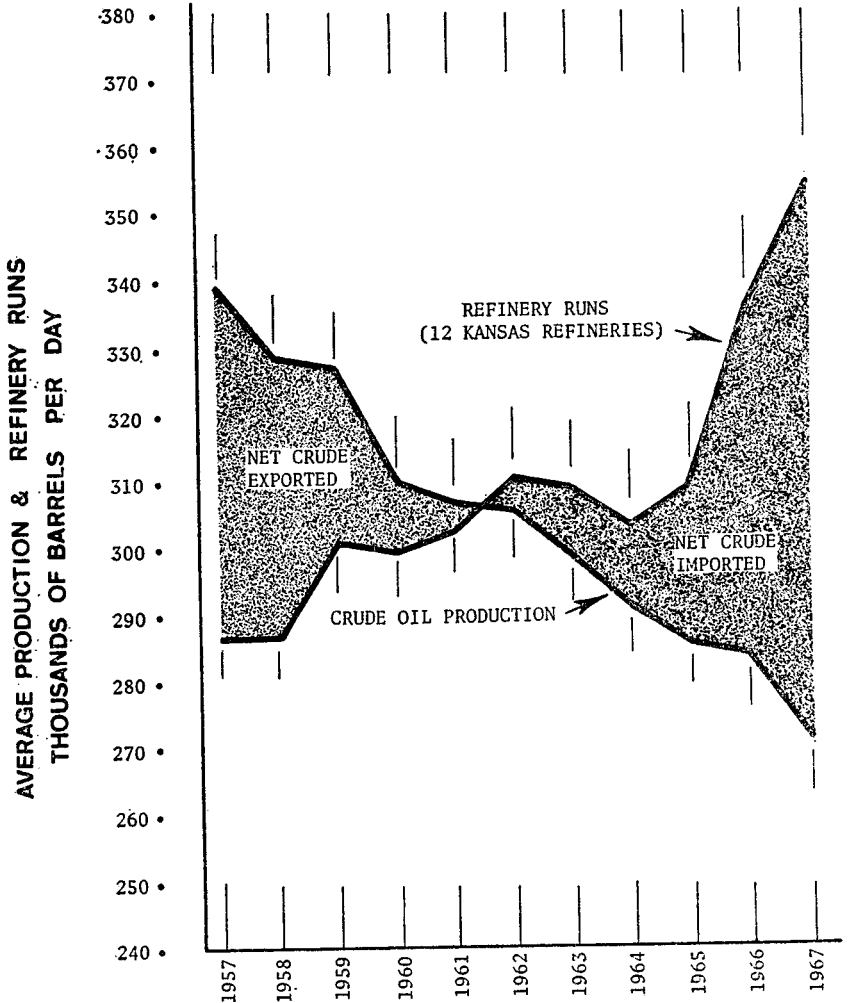
SOURCE: API and Kansas Corporation Commission

NATURAL GAS PRODUCTION and REMAINING RESERVES State of Kansas



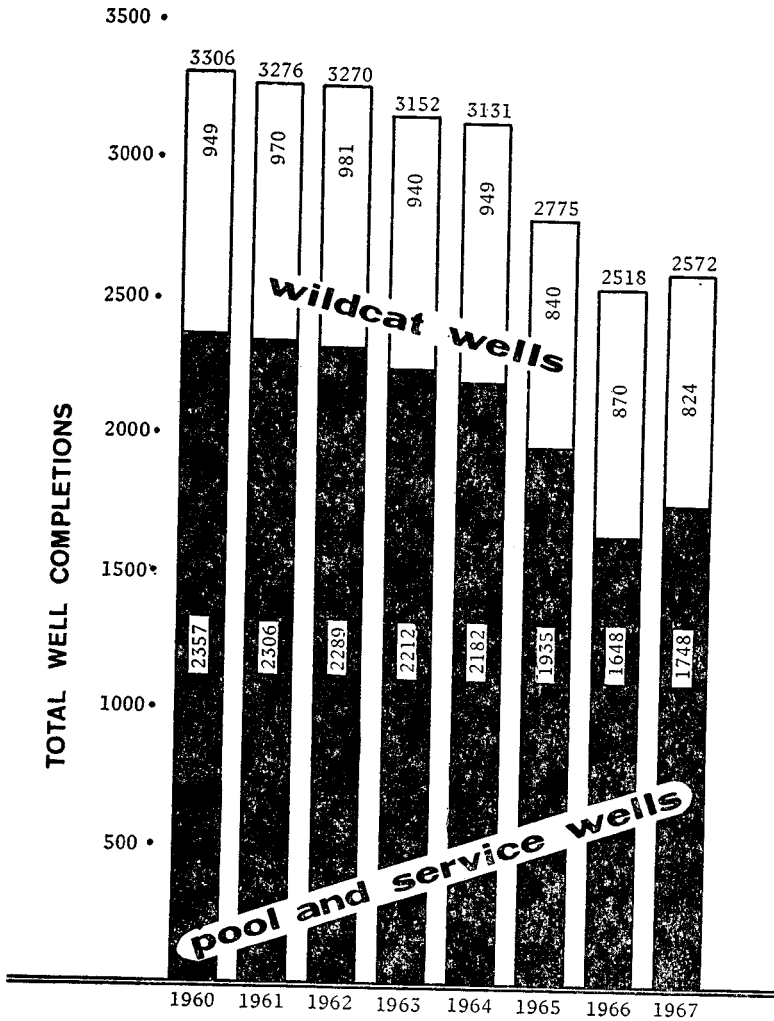
SOURCE: Kansas Corporation Commission

CRUDE OIL PRODUCTION and CRUDE OIL RUN TO KANSAS STILLS (REFINERIES)



SOURCE: STATE CORPORATION COMMISSION

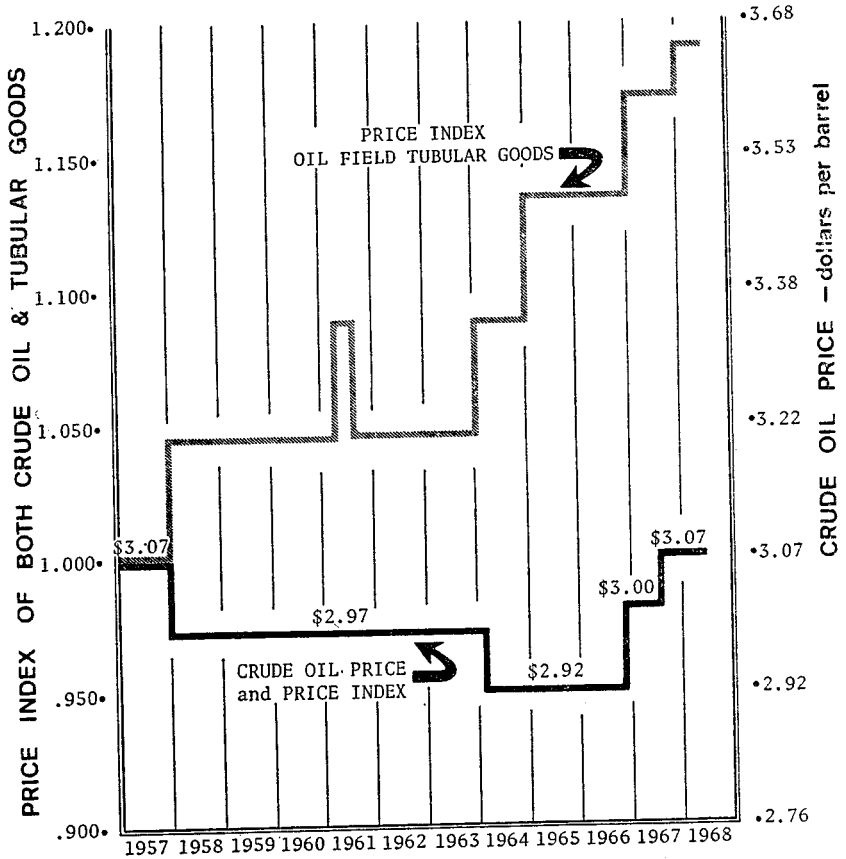
A COMPARISON OF WELL COMPLETIONS KANSAS* 1960-1967



*EXCLUDES TWENTY COUNTY AREA OF EASTERN KANSAS

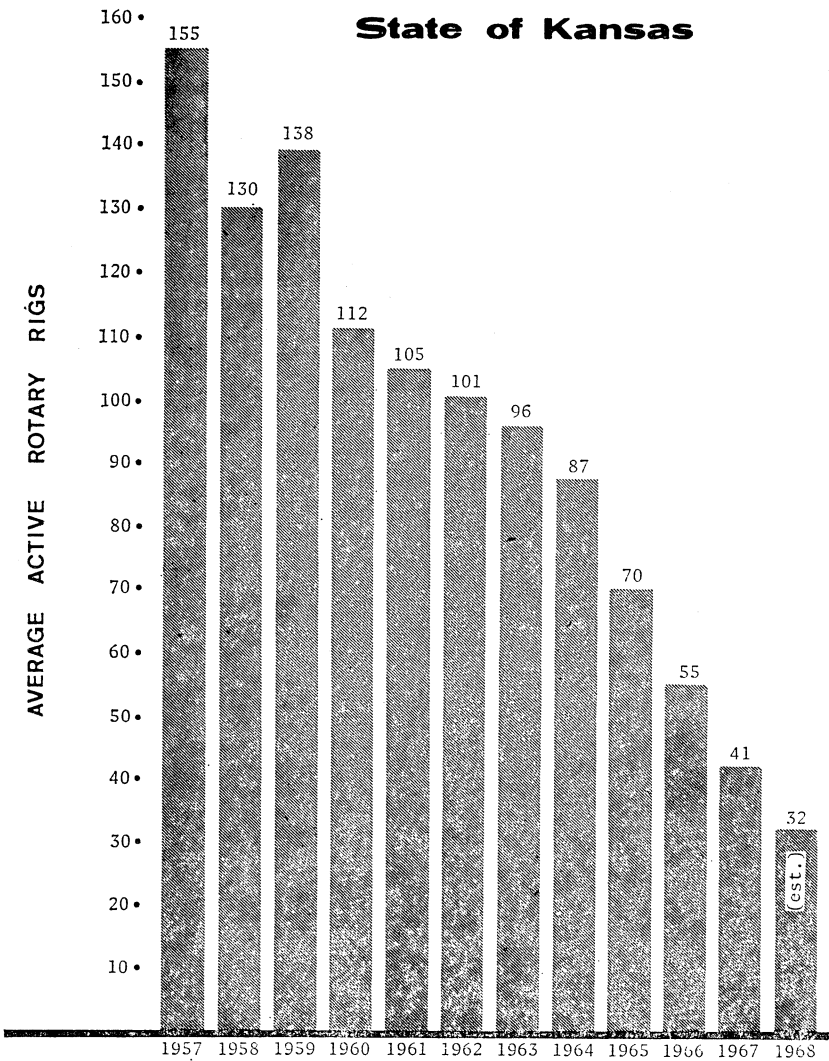
SOURCE: PETROLEUM INFORMATION

**POSTED PRICE FOR 36° API
KANSAS CRUDE OIL
&
PRICE INDEX FOR
OIL FIELD TUBULAR GOODS**



SOURCES: BOVAIRD SUPPLY COMPANY (tubular goods)
KIOGA files - - - - (crude prices)

ROTARY RIG ACTIVITY
State of Kansas



SOURCE: Oil and Gas Journal

The CHAIRMAN. Mr. McClure.

Mr. McCLURE. The next gentleman who will testify will be Don Watson, president of the Panhandle Producers & Royalty Owners Association.

The CHAIRMAN. Mr. Watson.

STATEMENT OF DON WATSON

Mr. WATSON. Mr. Chairman, members of the committee, I am Don Watson, of Amarillo, Tex., helium capitol of the world. As president of the Panhandle Producers & Royalty Owners Association, I represent 415 independent producers and royalty owners of the Texas Panhandle. Since oil was found in the panhandle in the early 1920's, independents have been the backbone of the industry in this locale.

I know that most of you are familiar with our geographic location, which comprises 26 counties in the panhandle. Seventeen of these have oil and/or gas production. In 1967, the Texas Panhandle alone produced over 1 trillion cubic feet of gas; and in area extent—the Panhandle-Hugoton gasfield is the largest gasfield in the world. Thirteen thousand-plus wells have accounted for cumulative production through 1967 of 1,199,666,000 barrels of oil. As you can well imagine, the economy of our area is most dependent on the petroleum industry. We have asked to present a brief report concerning the present condition of the petroleum industry in the Panhandle of Texas.

During the last 10-year period, our petroleum reserves have declined from 318 to 275 million barrels. Our production of crude oil is 6 million barrels a year less than it was 10 years ago. Last year we produced 33 million barrels of oil and discovered 17 million barrels of new reserves. This is a deficit of 16 million barrels.

Our drilling program over the same 10-year period follows the same negative pattern. In Texas Railroad Commission District 10, the Texas Panhandle, there were 1,307 field wells drilled in 1958. In succeeding years, 1,248; 1,043; 1,185; 1,030; 921; 887; 805; 590; and in the year 1967, 499. The year 1967 is down 62 percent from 1958. Wildcat wells, or those drilled outside any known field, were 118 in 1958, and 31 in 1967. Oil well completions were down from 725 in 1958, to 229 in 1967—or a decline of 69 percent. Gas well completions for the same period were 520 in 1958 and 126 in 1967—or a decline of 76 percent. The results of these figures I have just presented are as follows: The number of independent producers, who have in the past been primarily responsible for finding new oil and gas reserves in our district are rapidly declining drilling contractors, oil field service and supply companies and their related employees have also shown an alarming decline in numbers; many of the major companies have centralized their operations elsewhere; and many of our communities have suffered an economic recession.

The deterioration of the domestic petroleum industry in our region is certainly a contributing factor to the overall threat to our national security. In addition to the above, the rising cost of operations in relation to the near-static price imposed on our crude oil is forcing the independent out of business.

There still remain huge basins which are geologically favorable for exploration in our region. Unless adequate incentives exist for the independent producer, they will remain unexplored. If proven reserves can be discovered in this new area to reverse the trend of present declining reserves, we could again offer the Nation an ample supply of hydrocarbons during any national emergency.

Our association feels that the most effective act that can be initiated to check the general deterioration of the domestic petroleum industry in the Panhandle of Texas is for Congress to enact legislation limiting the flow of imported crude to 12.2 percent of our domestic production, as proposed in Senate bill 2332.

We feel that the present mandatory oil import program has failed to achieve its original objectives. The special exemptions and loopholes have damaged the domestic industry and are a threat to our national security. We urge that this program be returned to its original intent.

In closing, I would like to state that our association supports the testimony given to this committee by the Independent Petroleum Association of America, and the Texas Independent Producers & Royalty Owners Association.

Thank you, Mr. Chairman.

(The table referred to follows:)

TEXAS DISTRICT 10 STATISTICS FROM THE TEXAS RAILROAD COMMISSION'S ANNUAL REPORTS
(YEAR-END RESERVE FIGURE FROM AMERICAN PETROLEUM INSTITUTE)

	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967
Reserves ending (million barrels).....	318,359	316,275	300,624	283,496	264,100	244,255	228,426	313,453	291,568	275,470
New reserves (million barrels).....	---	37,086	22,445	20,691	17,453	16,659	20,225	120,281	12,307	16,856
Production (million barrels).....	38,322	39,170	38,096	37,819	36,849	36,504	36,054	35,254	34,192	32,956
Net change in reserves (million barrels).....	---	-2,084	-15,651	-17,128	-19,396	-19,845	-15,829	+85,027	-21,885	-16,098
Reserve reduction rate (percent).....	12.0	6.5	5.2	6.0	7.3	8.1	6.9	(+27.0)	7.5	5.8
Reserve withdrawal rate (production) (percent).....	12.0	12.0	12.5	13.3	13.9	14.9	15.5	11.2	11.7	11.9
Remaining productive years (static reserves).....	8.3	8.3	8.0	7.5	7.2	6.7	6.5	8.9	8.5	8.3
Remaining productive years (w/added reserves).....	---	153.0	19.2	16.6	13.7	12.3	14.5	(^c)	13.3	17.2
Field wells drilled.....	1,307	1,248	1,043	1,185	1,030	921	887	805	590	499
Oil completions.....	725	804	576	534	636	583	488	389	339	229
Gas completions.....	520	329	331	485	261	188	233	191	175	126
Dry holes drilled.....	207	205	185	216	181	186	163	200	166	90
Oil wells plugged.....	76	29	33	37	41	113	159	121	128	160
Gas wells plugged.....	22	33	53	46	64	57	64	75	47	39
Oil wildcats drilled.....	20	22	10	16	9	6	4	6	4	2
Gas wildcats drilled.....	4	3	5	42	26	16	28	3	8	1
Dry wildcats drilled.....	94	103	66	82	58	51	40	80	31	28

^c Inf.

The CHAIRMAN. Thank you, Mr. Watson. Mr. McClure.

Mr. McCLURE. The next witness will be J. Paul Jones, the president of the Bradford District Oil Producers Association, Bradford, Pa.

The CHAIRMAN. Mr. Jones.

STATEMENT OF J. PAUL JONES

Mr. JONES. My name is J. Paul Jones and I am president of the Pennsylvania Grade Crude Oil Association. Also, I am representing the Bradford Producers Association, and New York Producers Association.

Through these associations I represent all segments of the domestic oil industry; namely, producers, refiners, and marketers. It is, therefore, important that this testimony merits consideration because it comes from a cross section of the industry and not a particular segment.

AREA

The grade of oil produced, refined and marketed by the associations I represent occurs in what is commonly called the Pennsylvania grade region, stretching from southwestern New York State across western Pennsylvania into West Virginia and including production from southeastern Ohio. I might add, this region was formerly called the Appalachian region. It is right in the heart of the so-called Appalachia which we hear so much about. The industry has been contributing to the economic welfare of this region for over 100 years.

MARGINAL TYPE OF PRODUCTION

The Pennsylvania grade region is an area of historically declining production where all the producing wells are considered in the stripper well category. There are over 2,000 independent producers in the area, operating over 100,000 wells, with an average daily output of less than one-third barrel per day. The daily average production in 1967 was 34,700 barrels and the estimated recoverable reserves are in excess of 190 million barrels.

Pennsylvania crude has a paraffin base, is sulfur free and has a high yield of high quality lubricating oil. The refineries charging Pennsylvania grade crude oil have a very high relative finished lubricating oil capacity to crude oil capacity. Significant is the high viscosity index of Pennsylvania lubricating oil from a national security or defense viewpoint.

SMALL THROUGHPUT CAPACITY OF REFINERIES

The crude oil from this area is processed by 10 small refineries with throughput capacities ranging from 1,500 to 10,000 barrels per day. Some of these refiners are part owners of the pipelines and gathering systems transporting Pennsylvania grade crude oil, and their refineries are built to utilize only this special grade of crude. There are no other local markets for this type of crude, and, if there were, it would have to compete with other crudes selling at a much lower price.

EFFECT OF MANDATORY OIL IMPORT PROGRAM ON INDUSTRY

High quality lubricating oil is their bread and butter. However, three-quarters of each barrel refined consists of gasoline and distillate fuels which must compete with similar fuels refined and marketed on the east coast. Pennsylvania refiners are today marketing these products mostly at a loss. Profits from lubricants keep them in business. However, there is a limit to how much loss from gasoline and distillate fuels can be absorbed by lubricants. The import quota allocated to them is an important factor in keeping them alive. Without it they could very well cease to exist. Without the Pennsylvania grade refiner, the producer would lose his market and the Nation a valuable natural resource, impairing the national security. The primary purpose of the import program is to protect these natural resources and the Nation's defense capabilities, in fact the only legal basis for the entire program.

COMPETITION WITH EAST COAST REFINERS

A considered objective of the program is to maintain normal competitive relationships. In order to illustrate the competitive relationships in district I, you have only to look at a pipeline map showing the product lines from the east coast reaching into the marketing area of the Appalachian refiners. These lines deliver gasoline and distillate fuels into the region at a pipeline cost of less than 1 cent a gallon. Other competitive advantages such as higher throughput capacities with lower unit cost and the availability of low-cost foreign crude give the east coast refiner an economic advantage impossible for these small refiners to overcome.

In fact, most of the imported crude coming into district I to IV is landed on the east coast. The present policy of affording equal treatment to inland refiners along with coastal refiners through the ability to exchange import quotas is answering some of these economic problems and we urge most forcefully that in the interest of conservation and the protection of small inland refiners, it be continued.

The mandatory oil import program enables the Pennsylvania grade industry to compete with cheap foreign crude. It has special significance at this time in view of the administration's determination to improve the living standard in the area known as Appalachia. The Pennsylvania grade industry is located in the middle of it and has for over 100 years, contributed to its economic life.

OBJECTION TO GRANTING IMPORT QUOTAS OUTSIDE ORIGINAL INTENT

However, we are alarmed at what appears to be a definite trend in the direction of destroying the original basis, authority, and intent of the program. When the Interior Department began taking part of the allowable quota away from domestic refiners and using it for purposes never visualized or intended in the original construction of the program, our objections began to mount. I am referring, of course, to the granting of quotas for such purposes as fostering the economy of Puerto Rico, putting the domestic petrochemical industry in a position to compete with overseas plants, creating jobs in and beautification of the Virgin Islands, reduction of air pollution, conservation of recreational resources of territorial possessions, reducing the cost of

home heating oil to northeastern consumers, and perhaps other purposes which for the moment I do not think of.

There was even the threat at one time to use the quota as a means to prevent the domestic oil industry from passing along increased operating costs in the form of higher gasoline prices.

We are not saying that any of these purposes is not worthy of attention. What we are saying is that it was never the intent of the mandatory oil import program to spread a large part of the economic benefit from importing low cost crude oil to companies, territories, et cetera, outside the domestic oil industry. Rather, we think it was always the intent to preserve the viability of the domestic oil industry by allocating the economic benefit of importation among the members of the industry in an equitable manner.

The program itself is all right, but what has been done with it is wrong. Each new act of taking from the domestic oil industry for some outside purpose has created more complications, more demand by other special interest groups for the same consideration, more loopholes and more complexities from the standpoint of administration.

In summary, we like the program and think the way it was initially designed was of great benefit to the domestic oil industry. However, we think the program should be restored to its original basis.

I might conclude and say that these associations endorse the position of the Independent Petroleum Association and what they say to you in testimony.

The CHAIRMAN. Thank you, Mr. Jones. Mr. McClure.

Mr. JONES. I appreciate appearing before the committee. Thank you.

The CHAIRMAN. Thank you.

Mr. McCLURE. The next witness will be Netum Steed, the president of the Texas Independent Producers and Royalty Owners Association.

The CHAIRMAN. Mr. Steed.

STATEMENT OF NETUM A. STEED

Mr. STEED. Chairman Mills and gentlemen of the committee, we appear at this hearing to voice our concern over the lack of effectiveness of the mandatory oil import program which was administratively devised as the result of findings made under the National Security Section of the Trade Expansion Act.

This hearing, we trust, will afford an opportunity for appropriate consideration of this important matter and, in our judgment, will demonstrate the urgent need for new legislative guidelines limiting the level of oil imports.

Like representatives of the Independent Petroleum Association of America, and the more than 20 State and regional associations representing independent producers over this nation, we are concerned with total oil imports—but more particularly with nonresidential imports into petroleum districts I-IV (all U.S. area east of the Rockies), which is the portion supposedly limited to 12.2-percent ratio with domestic production.

Regulation of this security-sensitive portion of total oil imports into the United States has virtually ignored congressional intent clearly stated in the national security section of the Trade Act and now threatens to render the mandatory program virtually meaningless.

Gentlemen of the committee, we must respectfully take issue with representations made to you by Secretary of the Interior Stewart Udall as a leadoff witness for the administration.

We are grateful of course that this administration has seen fit to continue paying lipservice to the necessity of petroleum import limitations, but are distressed in the extreme that under Mr. Udall the import program has been manipulated into virtual ineffectiveness. It is all the more distressing that Secretary Udall would assure you that all is well in the oil import program and that, as a matter of fact, this program stands as shining evidence that Congress doesn't need to concern itself with steadily increasing imports—that the Johnson administration will do everything necessary to preserve a healthy home producing industry.

We charge that Secretary Udall is wrong when he told you that the oil import program has stabilized oil imports and preserved for the domestic producing industry all but a minor part of domestic market growth. Secretary Udall is wrong when he assured you that the 12.2-percent ratio limitation for nonresidual imports into Districts I-IV has been preserved. He is wrong when he implied that the national security purpose of the oil import program, which was clearly defined by legislative history, is being realized.

He is also wrong in assuring you that the manner in which the petroleum industry met the Mideast crisis of last summer established that no additional congressional directives are necessary to make the oil import program effective in terms of its national security purpose.

In arguing for what he terms "flexibility" of the program, Secretary Udall said: "Our oil industry was healthy and capable of meeting the increased demands placed on it, including assistance to Canada and Western Europe." The facts are that the domestic oil producing industry is not healthy, if measured in terms of drilling wells required to maintain defense-vital reserve productive capacity. Because of the drastic curtailment of exploration and drilling in this country, this Nation recently became an "oil-have-not-nation" with respect to petroleum—in the sense that we no longer are able to supply our own needs. We met the increased demand from the 6-day war in the Mideast, but only narrowly escaped some form of consumer rationing. And there is no evidence whatever that we can meet the next crisis, unless something is done to restore adequate drilling in this country. Although Mr. Udall has recognized the fact that drilling has dropped some 40 percent during the period of import restraints, and has expressed concern about it, he strangely implies before this committee that all is well. Said he:

We are convinced and emphasized, therefore, that imposition of rigid controls would not only result in serious repercussion in our foreign relations, but would adversely affect continued growth of our exports by inviting retaliatory action on the part of our major trading countries, adding:

We believe restrictive legislation would only make it more difficult to meet unexpected contingencies.

We submit, to the contrary, that moderate new legislative guidelines are absolutely necessary to accomplish the purpose of oil import controls. Under Mr. Udall, nothing effective is being done to arrest the deterioration in the domestic producing segment of the oil industry. Independent producers who historically account for some 85

percent of discoveries are simply unable to fulfill their obligation to this country under present import policies. We suggest to you that this administration is so anxious to retain total authority over oil import policy that it would misrepresent the situation faced by our Nation because of an ineffective oil import program. The national security objective of oil import curbs is not being realized, and there is no evidence it will be realized unless the Congress proves willing to penetrate these misleading assurances from Mr. Udall.

Gentlemen, I mentioned awhile ago that we were unable to take care of our own oil import situation, our own production, in this country now because we are importing $2\frac{1}{2}$ million barrels a day or more of oil and our reserve productive capacity's ability to produce more oil is only $2\frac{1}{4}$ million barrels.

Therefore, if our imports were cut off we would be short today some quarter of a million barrels of oil, and this situation is steadily growing worse as our oil imports increase, and as our demand increases, and as our productive capacity decreases, so I don't know that we would be able to meet another crisis, even a short one like we had last summer.

Our testimony is quite long and I will not read it all, Mr. Chairman. I would like to emphasize a few points and read the conclusions, if I may.

The CHAIRMAN. Your entire statement will be made a part of the record.

MR. STEED. Thank you, sir. The program has been continually liberalized and the points have been well brought out by the other witnesses here. There are a number of points which are above the 12.2, three of which I would like to mention that hurt us particularly.

The oil import from Canada is steadily increasing, is every year underestimated and is never made up. The excess oil that comes into this country from Canada is left outside the 12.2 and in effect it comes out of the domestic producers' hides, particularly Texas and Louisiana, who prorate to meet the market demand, so any excess oil that is brought in from Canada hurts us directly and this situation has kept growing and is not compensated for from year to year as these overages occur and it has always been an overage.

There is a proposal to give bonus quotas to low sulfur residual fuel oil processors. This could amount to 300,000 or 400,000 barrels a day in addition to what is now being brought in and this will all be outside of the 12.2 quota according to Secretary Udall's proposals.

We go into this in some detail in our statement and I commend it for your study, if you will.

A third point is the carryover of the unused 1967 import licenses. This is the oil from the Middle East that was not allowed to be brought in because the Arab countries would not permit it at the time and since then because of high tanker rates and other reasons it hasn't been brought in, but some 140 million barrels will be brought in before the end of this year according to the projections.

This is some 410,000 barrels a day which will be added on sometime during the balance of this year and this will mean a million dollars a day extra in the balance-of-payments situation, an increase in the deficit.

I will proceed to our conclusions on page 13, Mr. Chairman.

It is our belief that Secretary Udall, to whom authority over oil import policy has theoretically been delegated by the President, is unaware of or unwilling to confront the fact that excessive oil imports are the principal factor in our Nation's payments deficit.

We believe, as a matter of fact, that the Interior Department has yet to relate the payments crisis with its oil import policy. Yet, it is the petroleum trade deficit which is the biggest single element in our Nation's chronic payments deficit.

The Department itself recently supplied figures indicating that the petroleum trade deficit exceeds \$1.6 billion per year. Instead of moving to trim this deficit by a more effective oil import program, the Department is presently authorizing imports greatly in excess of the 12.2 ratio, which I just mentioned, including makeup imports for Mideast supplies which the Arabs denied us during 1967.

The result is that imports will soon increase by more than 400,000 barrels daily—at a time when the administration itself is declaring that the world money system may depend upon America's willingness to trim her payments gap.

We fail to comprehend how leading spokesmen for this administration can come before this very committee to urge drastic measures aimed at closing the payments gap, including a 10-percent surtax, on grounds that such measures are essential to free world economic order, and at the same time sanction Interior Department plans to increase oil imports substantially.

Even the most stringent measures to achieve payments equilibrium can be thwarted by an oil import policy which, under Mr. Udall, bears less and less relation to its national security purpose.

U.S. oil imports have not been effectively curtailed under the mandatory imports program. During the past 9 years, there has been a history of continuous liberalization in import flow. Recent administrative actions based on purposes other than national security threaten to ruin the program's effectiveness.

Consequently, U.S. oil policy is failing to cope with the problems of imports. All the criteria by which the success of the imports program was to be measured, as set forth in the security clause of the Trade Expansion Act, indicate its abject failure in terms of purpose.

There is mounting economic distress on the part of the domestic non-integrated independent oil producer segment of the U.S. oil industry, even while integrated companies are enjoying record earnings. There is, in consequence, a rapidly accelerating trend toward concentration in this industry.

Crude oil prices have deteriorated throughout most of the period of the program. This has led to a worsening depression of domestic exploration and drilling activity, which in turn is being reflected in lower crude oil reserves and defense-vital reserve-productive capacity.

In short, this administration has proved totally unwilling or incapable of resisting the pressures for ever-higher imports. Mr. Udall appears determined to consider the 12.2 ratio a floor rather than a limit, and we suggest to you that he has no intention, absent a congressional directive, to begin administering the oil import program in a manner consistent with its purpose.

In summary, therefore, we suggest there is urgent need to provide, first, a clear-cut quantitative limitation on imports, especially non-residual imports into district I-IV, as proposed by IPAA.

Additionally, we suggest the time is at hand to emphasize that the purpose of the import program was to insure adequate domestic oil supplies for national security purposes—and to that end the President was authorized to do “whatever necessary.”

Failure to exercise this authority, we submit, necessitates new congressional directives at this time.

Thank you, very much, Mr. Chairman.

(Mr. Steed's prepared statement follows:)

STATEMENT BY NETUM A. STEED, PRESIDENT, TEXAS INDEPENDENT PRODUCERS & ROYALTY OWNERS ASSOCIATION

Chairman Mills, gentlemen of the committee, I am N. A. Steed, president of the Texas Independent Producers and Royalty Owners Association. We appear at this hearing to voice our concern over the lack of effectiveness of the Mandatory Oil Import Program which was administratively devised as the result of findings made under the National Security Section of the Trade Expansion Act.

This hearing, we trust, will afford an opportunity for appropriate consideration of this important matter and, in our judgment, will demonstrate the urgent need for new legislative guidelines limiting the level of oil imports.

Like representatives of the Independent Petroleum Association of America, and the more than 20 state and regional associations representing independent producers over this nation, we're concerned with total oil imports—but more particularly with non-residual imports into Petroleum Districts I-IV (all U.S. area East of the Rockies), which is the portion supposedly limited to 12.2 percent ratio with domestic production.

Regulation of this security-sensitive portion of total oil imports into the United States has virtually ignored Congressional intent clearly stated in the National Security Section of the Trade Act and now threatens to render the Mandatory Program virtually meaningless.

Gentlemen of the Committee, we must respectfully take issue with representations made to you by Secretary of the Interior Stewart Udall as a lead off witness for the Administration.

We are grateful of course that this Administration has seen fit to continue paying lip service to the necessity of petroleum import limitations, but are distressed in the extreme that under Mr. Udall the import program has been manipulated into virtual ineffectiveness. It is all the more distressing that Secretary Udall would assure you that all is well in the Oil Import Program and that, as a matter of fact, this Program stands as shining evidence that Congress doesn't need to concern itself with steadily increasing imports—that the Johnson Administration will do everything necessary to preserve a healthy home producing industry.

We charge that Secretary Udall is wrong when he told you that the Oil Import Program has stabilized oil imports and preserved for the domestic producing industry all but a minor part of domestic market growth. Secretary Udall is wrong when he assured you that the 12.2 percent ratio limitation for non-residual imports into Districts I-IV has been preserved. He is wrong when he implied that the national security purpose of the Oil Import Program, which was clearly defined by legislative history, is being realized. He is wrong in assuring you that the manner in which the petroleum industry met the Mideast crisis of last summer established that no additional Congressional directives are necessary to make the Oil Import Program effective in terms of its national security purpose.

In arguing for what he terms “flexibility” of the program, Secretary Udall said: “Our oil industry was healthy and capable of meeting the increased demands placed on it, including assistance to Canada and Western Europe.” The facts are that the domestic oil producing industry is not healthy, if measured in terms of drilling wells required to maintain defense—vital reserve productive capacity. Because of the drastic curtailment of exploration and drilling in this country, this nation recently became an “oil-have-not nation” with respect to petroleum—in the sense that we no longer are able to supply our own needs.

We met the increased demand from the six-day war in the Mideast, but only narrowly escaped some form of consumer rationing. And there is no evidence whatever that we can meet the next crisis, unless something is done to restore adequate drilling in this country. Although Mr. Udall has recognized the fact that drilling has dropped some 40 percent during the period of import restraints, and has expressed concern about it, he strangely implies before this Committee that all is well. Said he:

"We are convinced and emphasized, therefore, that imposition of rigid controls would not only result in serious repercussion in our foreign relations, but would adversely affect continued growth of our exports by inviting retaliatory action on the part of our major trading countries," adding:

"We believe restrictive legislation would only make it more difficult to meet unexpected contingencies."

We submit, to the contrary, that moderate new legislative guidelines are absolutely necessary to accomplish the purpose of import controls. Under Mr. Udall, nothing effective is being done to arrest the deterioration in the domestic producing segment of the oil industry. Independent producers who historically account for some 85 percent of discoveries are simply unable to fulfill their obligation to this country under present import policies. We suggest to you that this Administration is so anxious to retain total authority over import policy that it would misrepresent the situation faced by our nation because of an ineffective oil import program. The national security objective of oil import curbs is not being realized, and there is no evidence it will be realized unless the Congress proves willing to penetrate these misleading assurances from Mr. Udall.

If, as Mr. Udall indicates, the 12.2 ratio is being maintained and shall be maintained without new directives, then he should have no objection to a Congressional mandate spelling out this limitation, with ample safeguards of course to prevent a possible domestic shortage of oil supplies. We say to you that only by manipulating figures and constantly redefining terms has Mr. Udall been able to pretend that the 12.2 ratio limit is being upheld. Had it not been for the fact that Arab nations refused to allow their oil to be marketed in this country for some period after the Mideast crisis, the surplus over the 12.2 ratio would have been much greater. Now that these Arab rulers have lifted the ban on oil exports to the U.S., and it has become profitable for importers to move that oil here, we are on the verge of witnessing an increase in oil imports so sharp as to thwart the most strenuous efforts of the Administration to move toward payments balance.

When the Program was set in motion in March 1959, its national security purposes was made clear. Oil imports were to be restricted so that the domestic oil producing industry could maintain sufficient health and vigor to explore for and develop adequate domestic reserves. The industry could thereby maintain the productive capacity needed to supply secure home oil whenever emergency conditions disrupt foreign supply.

Yet, during the decade of experience under import controls, the United States finds itself in the dangerous position of having become a "have-not" nation in terms of oil supply. Based on most recent industry studies of domestic oil productive capacity, domestic producers would now be unable to meet domestic oil demand fully if total oil imports were made unavailable. Reserve productive capacity is approximately 2.25 million barrels daily as compared with an average oil import flow exceeding 2.5 million barrels daily.

Projections indicate that in the absence of national oil policy change, this quarter of a million barrel per day deficit could increase to five million barrels per day by 1980. Should this projection prove accurate, one out of every three barrels of oil or gallons of gasoline used by American consumers—only twelve years from now—will come from abroad. Most of this supply will come from areas of the Free World which are considered relatively insecure.

In 1967, the latest Mideast crisis provided the United States with a clear warning of what disruption of foreign oil supply can mean, although the conflict lasted only six days. To meet emergency needs and to cover the loss of Mideast supply incurred by Europe, Canada, and the United States in June, domestic oil producers had to provide "extra" supply averaging some 330,000 barrels daily over the last half of the year. Much of this was required at twice that daily rate during the summer months.

American consumers were fortunate in that this clear warning or lesson was not costly to them. They did not have to experience rationing of supply or

crisis-related increases in price. But apparently because consumers experienced no adverse results, however, that warning was not as clear as it would otherwise have been. Because the industry gave the impression that it met the 1967 supply problem without undue strain, consumers and government officials have so far failed to recognize the proportions of the crisis which now hangs over our nation and her allies.

The next emergency will not likely be so short-lived or limited in its effect on Free World oil supply. Furthermore, the domestic producing industry is now in its twelfth year of decline in exploration and development activity. In Texas, for example, the industry drilled 56 percent fewer wells in 1967 than it did in 1956. Thus far in 1968, drilling rates are 9.9 percent below the depressed 1967 levels. Each additional year this severe decline in activity is experienced means less reserve capacity to cope with emergencies and steady increase in normal demand.

PROGRAM LIBERALIZATION

One of the main contributing factors to the 12-year decline in domestic oil producer activity has been the attitude of the Administration in administering the Mandatory Program. Throughout the life of the Program, there have been endless changes—beginning with the exemption of Canadian imports from regulation in June 1959 through the current proposal to provide large crude oil bonus quotas for clean fuel processors—virtually all of which have resulted in oil import increases in relation to domestic oil production.

Examples of such administrative change, in addition to the two cited above, include: decontrol of residual fuel; decontrol of asphalt products, creation of Foreign Free Trade zones, and new quotas for the petrochemical industry; provision for special product quotas granted to importing companies that help develop the Caribbean islands; assignment of quotas to those who export petrochemical products; liberalization of distillate fuel quota restrictions for East Coast marketers; and many other minor concessions to non-producing industry segments supposedly deserving subsidies by way of import quota privileges.

All such changes have had an adverse effect upon the non-participating domestic independent producer located in Districts I-IV, who must compete with others benefiting economically from oil imports. Not only is he denied the economic assistance import participation provides, but he also must lose some of his market for domestic crude each time the Program is weakened by change. Yet it is the independent producer who historically accounts for some 85 percent of the nation's oil exploration activity, and it was to protect this function that the import program was instituted in the first place.

There are currently three major changes, either contemplated or already in effect, relating to non-residual fuel imports into Districts I-IV which clearly illustrate the magnitude of this problem. Such imports are supposedly limited to 12.2 percent of domestic oil liquids production in these Districts by the Program. Contrary to what this Committee has been told by Secretary Udall, the 12.2 guideline has not been adhered to, and is not likely to be approached in the future in part because of the three adjustments outlined below.

1. *Canadian Oil Import Regulation.*—Oil imports from Canada are exempt from direct quota limitations on grounds that this oil is relatively more secure than the oil which has to move by ocean-going vessel. Yet these imports are supposedly kept within the 12.2 ratio, which means that at any time imports from Canada increase there has to be a corresponding reduction in imports from some other area. This is all right so long as the Canadian increase doesn't get out of bounds, in which case something has to give; either Venezuela or U.S. producers suffer.

The Department of Interior makes an "estimate" of how much oil they expect during the forthcoming quota period from Canada. Then the remaining portion of imports under the 12.2 ratio are allocated to other source areas. Since the Canadian imports always grow so much more than "estimated," that would mean pinching Venezuela and other source areas in the normal course of events. But to avoid this, Interior officials simply underestimate what the growth of Canadian imports will be each year, so that the effect is to make domestic production pay the price of Canadian excesses. Specific results of this change are as follows:

In 1963 the Interior Department "estimated" that imports from Canada would be 252,000 barrels per day. But Canadian imports exceeded that level by 13,000 barrels per day.

So in 1964 Interior raised its estimates of Canadian imports by a whopping 30,000 barrels a day. Even so, Canadian imports exceeded this by another 17,000 barrels per day.

In 1965, the Department jumped the "estimate" an additional 28,000 barrels daily. What happened? Canadian oil met the allowed increase and topped it by another 13,000 barrels per day.

In 1966 the "estimate" was again raised by 25,000 barrels per day for a total of 335,000 barrels daily. Once again Canadians revealed their disdain for this informal arrangement and exceeded the estimate by some 38,000 barrels per day.

In 1967, the "estimate" was raised to 370,000 barrels a day, and imports totaled 449,000 barrels a day—an average of almost 80,000 barrels daily at the expense of domestic producers.

The first four months of 1968 indicate this year will result in the most flagrant abuse of this Program deficiency yet experienced. The Interior estimate was raised again to 415,000 barrels daily, while during the first four months importers averaged 501,000 barrels daily for an excess at the expense of domestic producers of some 86,000 barrels per day.

All of these excesses permitted during the history of the Program are outside the 12.2 ratio. Yet the Secretary of Interior has repeatedly declared that this guideline will remain inviolate without new Congressional directives. In appearing before this Committee recently he based his assurances that no new legislation is required on the erroneous claim that he is honoring and will honor the 12.2 ratio limit. Because of this particular program loophole among others, the Secretary was not providing this Committee with an accurate picture—and hence his assurances that the Program is successful in terms of purpose, and that no new legislative mandates are necessary, should not be taken at face value.

2. Proposed Bonus Quotas for Low Sulphur Residual Fuel Processors in Districts I-IV.—The Department of Interior's current proposal to provide bonus oil import quotas for importing companies which manufacture or blend low sulphur residual fuel constitutes an even more serious threat to the Program's purpose and renders meaningless the supposed 12.2 ratio limit. By the Department's own estimate, this plan would lead to additional District I-IV crude oil import quotas outside of the 12.2 ratio provision equivalent to approximately one-third of the current authorized total. In its release announcing the proposal on May 24, 1968, the Department stated:

"Oil imported as credit (bonus oil) for the manufacture of low sulphur residual fuel oil would not be within the overall 12.2 percent limitation on imports into Districts I-IV. The volume of credit imports, within several years, is anticipated to be about 300,000 barrels daily, with a corresponding decline in other imports of residual fuel oil."

The most onerous feature of the proposal provides that participating importing companies are authorized bonus crude oil quotas in amounts and type varying according to what oil sources and processes are used for making low sulphur residual fuel. Essentially, bonus quotas are more generous for those companies using domestic or Western Hemisphere residual fuel. Ostensibly, this is to benefit the domestic producer and Venezuela, the more secure sources of oil supply for the U.S.

If this is the case, then there is no logic in providing restriction-free crude oil bonus quotas. Apparently, the participating importers can draw on financially desirable but insecure Eastern Hemisphere crude supply for his bonus oil. Thus, Mideast oil sources, along with the participating companies, will derive prime benefit from this crude oil bonus plan, while Western Hemisphere sources will enjoy increased markets for relatively low-profit residual fuel oil.

The crude oil bonus is further sweetened by relaxation of the long-standing Mandatory Program restriction on unfinished oil imports. Participating companies will be able to increase their unfinished oil allowance from 10 percent of the crude they import to 15 percent of the bonus quotas.

Reaction to this proposal on the part of responsible state conservation officials is perhaps best summed up in a letter from Texas Railroad Commission Chairman Jim C. Langdon to Secretary Udall. Said Judge Langdon in part:

"I am amazed that you would propose this scheme as a solution (to air pollution problems) as it will be detrimental to national security, independent producers, the oil industry, the nation's balance of payments position and, as a result, detrimental to the nation as a whole."

Langdon expressed confidence that the oil industry would be able to supply the needed low-sulphur fuel without such bonuses. He noted that some in the industry already are providing such fuel and questioned why they should be rewarded for doing something already found economically desirable to do.

The chairman also questioned the total volume of bonus oil the plan would create. He observed:

"While the immediate impact is calculated to be around 100,000 barrels daily, I visualize that it could grow to 400,000 or 500,000 barrels per day above the 12.2 formula within a few years."

Langdon also translated this into balance of payment dollars, putting the initial impact at \$73 million per year to be followed by a possible annual rate of a third billion dollars in later years.

The chairman urged that the plans rejection "for its adoption would be only one more step toward final destruction of the mandatory oil import program."

This proposal constitutes a classic example of Program manipulation by Executive Department officials for purposes wholly unrelated to the national security objective of that Program. In order to accommodate air pollution objectives which can be achieved through other means, the Secretary would sacrifice the national security value of the 12.2 ratio limitation, and at the same time largely abandon the avowed intention of relying on imported oil from the relatively secure sources. Moreover, by this measure he would be forsaking earlier plans to move toward elimination of imported unfinished oils in order to preserve domestic markets.

It is interesting, in this connection, to contrast Mr. Udall's words with his deeds. Just prior to his proposing this measure, he stated before the Senate Finance Committee that the oil import program was intended to serve only the national security interests. In this testimony, he stated in part: "I would like to state here, my firm view that in the present world petroleum situation, oil imports should be controlled in the interest of our national security. That is the paramount—the only—reason why such imports are controlled. In no sense does this position alter my views with respect to opposing trade barriers generally. But in the case of oil, our security would be jeopardized unless we have a strong, healthy, domestic oil industry, capable of meeting any demand. This we could not do if low cost oil from petroleum exporting countries were to flood this country, with consequent damage to our own energy producing industries."

3. *Carryover of Unused 1967 Import Licenses.*—The Middle-East war of last June disrupted the normal flow of oil to world markets and resulted in substantial decrease in the amount of licensed imports into Districts I-IV during the year 1967.

The resulting deficiency amounted to approximately 51.7 million barrels, or an average of 141,761 barrels daily for the full year.

In February of this year the Secretary of Interior announced that half of the unused licenses could be utilized in 1968 and the remaining half in 1969. He further stated that half of the unused licenses would be authorized above the 12.2 ratio. This amounts to 36,000 barrels per day for this year and next.

Domestic producers had no objection to allowing importers stuck with unused licenses to utilize them on a priority basis after the crisis—as long as licenses remained under the 12.2 ratio. The decision to break the 12.2 ratio with these quotas amounted to an insistence that the 12.2 ratio is a floor rather than a ceiling. It was in effect holding open the door to unreliable Mideast oil until the Arabs decide it can be dumped on us and until importers involved find that tanker rates have dropped sufficiently to make it profitable to supplant domestic production with the so-called cheap Mideast oil.

State conservation officials have urged Interior to reduce imports below the 12.2 ratio as necessary to keep states from having to do all the cutting back necessary to prevent another Mideast-aftermath oil glut. However, there was no serious consideration given by the Administration to the plea that imports share the cutback burden. The net result is that domestic producers are being penalized for meeting their obligation to the nation and the free world by making domestic oil available, at consirable expense, to fill the shortages resulting from the Mideast supply breakdown.

Unfortunately, the worst is yet to come. Importers, still waiting for reduction in tanker rates in the wake of the crisis and continued shutdown of the Suez Canal, have not only declined to bring in the 1967 unused quotas on schedule in 1968, but have also failed to fill their regular quotas. Consequently, the

nation is headed for a severe oil import glut beginning in August and lasting through the remainder of the year. The effect on our depressed domestic producing industry can be devastating.

During that period, license quota holders in Districts I-IV will have to import more than 410,000 barrels daily more than they have thus far in 1968 to complete their quotas. There is every expectation that they will do so, thereby causing sharp reductions in and long range damage to domestic crude oil production.

This drastic shift will occur at the very time the United States needs significant improvement in its balance of payments. The shift alone will cost the United States approximately one million dollars a day in its payments balance over a period of seven months.

CONCLUSION

It is our belief that Secretary Udall, to whom authority over oil import policy has theoretically been delegated by the President, is unaware of or unwilling to confront the fact that excessive oil imports are the principal factor in our nation's payments deficit. We believe, as a matter of fact, that the Interior Department has yet to relate the payments crisis with its oil import policy. Yet it is the petroleum trade deficit which is the biggest single element in our nation's chronic payments deficit. The Department itself recently supplied figures indicating that the petroleum trade deficit exceeds \$1.6 billion per year.

Instead of moving to trim this deficit by more effective oil import program, the Department is presently authorizing imports greatly in excess of the 12.2 ratio, including makeup imports for Mideast supplies which the Arabs denied us during 1967. The result is that imports will soon increase by more than 400,000 barrels daily—at a time when the Administration itself is declaring that the world money system may depend upon America's willingness to trim her payments gap.

We fail to comprehend how leading spokesmen for this Administration can come before this very Committee to urge drastic measures aimed at closing the payments gap, including a 10 percent surtax, on grounds that such measures are essential to free world economic order, and at the same time sanction Interior Department plans to increase oil imports substantially. Even the most stringent measures to achieve payments equilibrium can be thwarted by an oil import policy which, under Mr. Udall, bears less and less relation to its national security purpose.

U.S. oil imports have not been effectively curtailed under the Mandatory Imports Program. During the past nine years, there has been a history of continuous liberalization in import flow. Recent Administrative actions based on purposes other than national security threaten to ruin the Program's effectiveness.

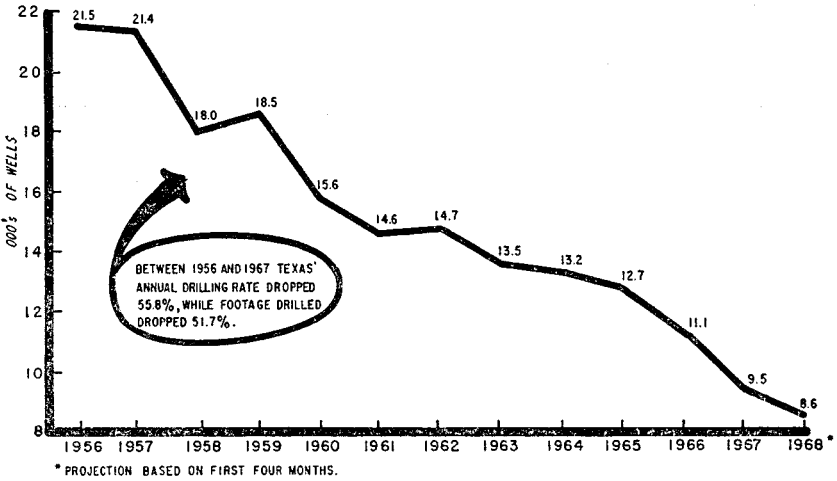
Consequently, U.S. oil policy is failing to cope with the problems of imports. All the criteria by which the success of the imports program was to be measured, as set forth in the security clause of the Trade Expansion Act, indicate its abject failure in terms of purpose. There is mounting economic distress on the part of the domestic non-integrated independent oil producer segment of the U.S. oil industry, even while integrated companies are enjoying record earnings. There is, in consequence, a rapidly-accelerating trend toward concentration in this industry.

Crude oil prices have deteriorated throughout most of the period of the program. This has led to a worsening depression of domestic exploration and drilling activity, which in turn is being reflected in lower crude oil reserves and defense-vital reserve-productive capacity.

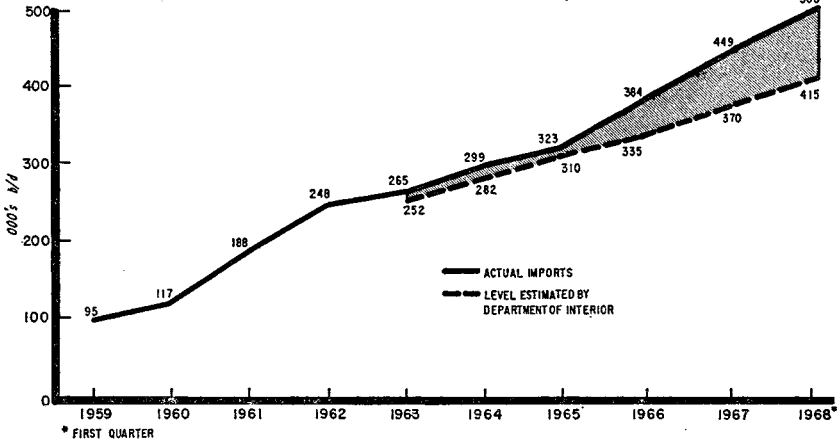
In short, this Administration has proved totally unwilling or incapable of resisting the pressures for ever-higher imports. Mr. Udall appears determined to consider the 12.2 ratio a ceiling rather than a limit, and we suggest to you that he has no intention, absent a Congressional directive, to begin administering the oil import program in a manner consistent with its purpose.

In summary, therefore, we suggest there is urgent need to provide, first, a clear-cut quantitative limitation on imports, especially non-residual imports into Districts I-IV, as proposed by IPAA. Additionally, we suggest the time is at hand to emphasize that the purpose of the import program was to ensure adequate domestic oil supplies for national security purposes—and to that end the President was authorized to do "whatever necessary." Failure to exercise this authority, we submit, necessitates new Congressional directives at this time.

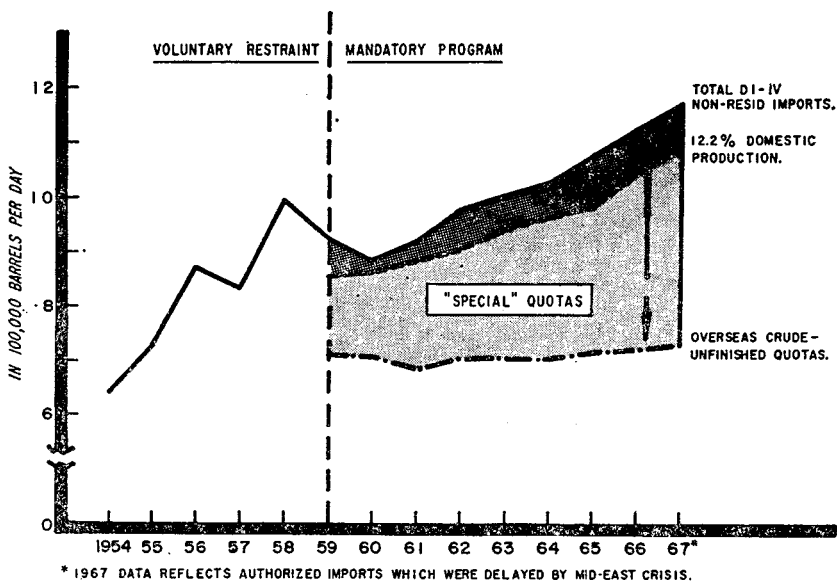
TREND IN TEXAS TOTAL ANNUAL WELL COMPLETIONS 1956-1968



CANADIAN CRUDE AND PRODUCT IMPORT GROWTH UNDER THE MANDATORY IMPORTS PROGRAM, 1959-68



**PRESENT OIL IMPORT ALLOCATION SYSTEM
CONSISTENTLY EXCEEDS 12.2 CEILING
AND ENCOURAGES "SPECIAL" QUOTAS IN DISTRICTS I - IV**



The CHAIRMAN. Mr. McClure, Senator Tower was to be with your group and I notice he is now in the room. Would you recognize him next?

Mr. McCLURE. Thank you.

The CHAIRMAN. Come on, Senator Tower.

We are pleased to have you with us this morning and you are recognized, sir.

**STATEMENT OF HON. JOHN G. TOWER, A U.S. SENATOR FROM THE
STATE OF TEXAS**

Senator TOWER. Thank you very much, Mr. Chairman. I appreciate the privilege of appearing before the most prestigious committee of the most prestigious legislative body in the world.

The CHAIRMAN. In view of that tell us very briefly just what you want.

Senator TOWER. Mr. Chairman, I don't know that I can add much to what Mr. Steed and other experts have said this morning but I would like to express my views on a continuing problem.

Our domestic proven crude oil reserves are dwindling at an alarming rate, while our domestic exploration has declined 40 percent in the last decade. Petroleum provided 74 percent of all U.S. energy requirements in 1967, and the U.S. demand for oil is steadily increasing.

Government estimates place national petroleum needs for the next 12 years at a level equal to total production over the last 100 years. It is important to note that 3 to 5 years must be allowed from the state of exploration to develop a proven field.

The gentlemen who will follow me are experts in petroleum exploration and production. They will discuss in detail the ills of this industry that provides the basic security and strength of our economy. However, I will take this opportunity to express my feelings and concern on three specific issues.

Our national security depends upon our maintaining a healthy and vigorous domestic petroleum industry. The past three administrations have recognized this fact, and have supported the mandatory oil import program. The Middle East crisis last year dramatically reminded us of the wisdom of this policy.

When that crisis disrupted the world flow of oil from the Middle East and Africa, our domestic producers applied the emergency demands of the U.S. east coast, eastern Canada and Western Europe. This was the most recent test of our domestic capabilities.

Fortunately for us, the crisis was short in duration. It emphasizes the urgency of recognizing our domestic oil shortage and Congress must take appropriate action that will insure us of an adequate domestic supply of oil.

The mandatory oil import program places a 12.2-percent ratio limitation on imports of foreign crude. The sole purpose of this program is our national security. Our security would be jeopardized unless we had a strong, healthy, domestic oil industry capable of meeting any demand.

This we could not do if low-cost oil from petroleum exporting countries were to flood this country, with consequent damage to our own energy producing industries.

The present administration has manipulated the program in such a manner that it is mandatory that Congress spell out its limitations. National security is being sacrificed for the benefit of special interest groups. The administration has proven they are incapable of resisting the pressures of these groups and appears determined to disregard the 12.2 ratio by making it a minimum rather than a limit.

I am informed that U.S. interests own 60 percent of all Mid-East oil production. These companies have made sizable investments across the sea and have discovered oil reserves of staggering magnitude.

However, it is not a dependable source of supply. This was dramatically proven last year in the Middle East crisis. We are not only at the mercy of the governments of these oil-rich countries, but also the shipping industry that must be depended upon to transport this oil.

If we are so blind that we cannot recognize these facts, and take the necessary steps to strengthen our domestic production, we could severely jeopardize our national strength.

The petrochemical industry and its products, although largely unrecognized by the layman, have become essential to our modern way of life. We have come to rely on these products as they play important roles in food production, clothing, household and industrial detergents, protective and decorative coatings, automobile tires, ubiquitous plastics, and scores of other applications.

The investment in domestic plants and factories by the petrochemical industry for bulk chemicals and plastics exceeds \$19 billion. Their employees number close to half a million. This industry must be recognized as a prime source of strength to the Nation in a time of emergency.

The raw materials that are the feed stock for this industry are crude oil derivatives and natural gas liquids, which are subject to control by the oil-import program. These oil and natural gas liquids are chemically converted by complicated, highly technical, and expensive operations into an enormous range and variety of synthetic organic chemicals and plastics. A \$4 barrel of oil can generate as much as \$40 in chemical sales.

At the present time, domestic feedstocks ethane, propane and butane, are priced essentially at parity with foreign feedstocks, such as naphtha or gas oil. If local demand for propane were to increase drastically for home and industrial uses, this competitive price advantage could disappear.

Now is the time to recognize this industry—its benefits to us, its needs, and the necessity of integrating it in a sound manner into the oil-import program.

I must stress that an honest evaluation of all the facts of our oil import must be accomplished to enable it to better serve the national welfare and interests of all those it affects.

The Oil Import Administration must be strengthened with the addition of specialists who have a keen knowledge and understanding of the industry which their decisions so vitally affect.

The oil-import program is of crucial importance to the petroleum and petrochemical industries. These future needs cannot be met by the policies of yesterday unless we wish to court disaster. Congressional action must be taken to spell out the limitations of this program.

Mr. Chairman, I thank you very much for allowing me this opportunity to appear.

The CHAIRMAN. Senator, we thank you, sir, for bringing your views to the committee. Mr. McClure.

STATEMENT OF HAROLD M. McCLURE, JR., ET AL.—Resumed

Mr. McCLURE. We have two additional witnesses and we will attempt to expedite the completion of this testimony. I would like to present to the committee Stark Fox, executive vice president of the Independent Oil & Gas Producers of California.

STATEMENT OF STARK FOX

Mr. Fox. Mr. Chairman and members of the committee, my name is Stark Fox. I am executive vice president of Independent Oil & Gas Producers of California, which is a consolidation of Oil Producers Agency of California and San Joaquin Valley Oil Producers Association. It is the only statewide organization of independent oil producers in California. I appear in support of pending legislation which would write the standard of the oil import program into law.

Mr. Chairman, I have a statement here which I am sure has been filed with the committee by Mr. Ralph W. Trueblood but I would like to make sure that is in the committee record.

The CHAIRMAN. Without objection it will be included in the committee record. (See p. 4269.)

Mr. Fox. We are pleased to be able to present our views as to the effectiveness of the mandatory oil-import program. I believe that I have appeared at every hearing, either by committees of Congress or by the Department of the Interior which has considered, or considered changes in, the program since its inception. In most cases, my testimony has been principally concerned with district V, the west coast, which I will now briefly discuss.

DISTRICT V PRODUCERS SUPPORT PROGRAM

The record of those hearings will show that the producers in district V have been consistent supporters of the program as it has been administered to date. We have suggested certain improvements, such as a certification procedure for exempt Canadian imports, for example. We will not burden the record here with further arguments for this proposal; we still urge its adoption, but for the sake of brevity in this statement, will rest upon the record we have made in previous appearances to support our case.

As I have heretofore indicated, we believe that in district V the oil import program has, in the main, accomplished its objectives. California reserves have increased. Production has recovered to a current 1,033,000 B/D from its postwar low of 809,000 in 1962 and is expected to continue its uptrend.

Alaskan production has risen from little or nothing just 5 years ago to 180,000 B/D today, and is also expected to increase—to at least 225,000 B/D by the end of the year.

DETERIORATION OF INDEPENDENT'S POSITION

This is the total picture. Within that picture, however, there is a disturbing element: The situation in which the independent producer finds himself. One statistic will suffice to illustrate the point. Since 1958, the independent's share of California production has declined from 45 percent of the State's total in that year to approximately 40 percent.

We think it no coincidence that during the same period, the average price of California crude dropped from \$3.05 per barrel to \$2.36—69 cents.

This price drop occurred during the period of mandatory import control over oil imports into District V, a control which pending legislation will continue without substantial change. The drop has caused near disaster for the independent producer, but it gives the lie to those who say that import controls result in higher prices.

If, in fact, this deterioration in the health of California independent producers has occurred during the effective period of the oil import program and if, in fact, proposed legislation will only preserve—not materially change—that program in District V, why do we support it?

EXCEPTIONS BREED EXCEPTIONS

Simply because we are convinced that exceptions and exemptions breed more exceptions and exemptions. We have seen the statement

of a group which desires to build a refinery in Guam. The statement was filed at the Interior Department's hearings of May 22-24, 1967, and put the Department on notice that the group wanted a quota to import 12,500 B/D of gasoline into District V. The proposed refinery is predicated on the securing of an import quota; without it, the refinery won't be built.

As we understand the purpose of the import program, it is to enhance the national security by maintaining an active, healthy, and vigorous domestic oil industry—not to provide an opportunity for someone to go into business. Make no mistake about our meaning: We have no objection to anyone's building a refinery anywhere in the world, including California, anywhere else in District V, or Guam, for that matter. We applaud his enterprise and wish him well, just so long as his project is based upon his estimate of its chances of economic success in the face of existing competitive conditions. When he says, however, that he is going into business because he expects to receive an import quota, and says that without it he would not proceed, we draw the line.

HAWAII'S MISCONCEPTION

We recently heard testimony presented by a Member of this House who has sought complete exemption of Hawaii from oil import controls, and has actually gone so far as to introduce a bill, now before this committee, to accomplish that objective. (Mr. Matsunaga; H.R. 12437.)

As we understand his argument, it is that Hawaii is some 2,400 miles from the west coast, hence tankers from that area are as vulnerable as tankers from any other oil source; and that, without controls, Hawaiian fuel supplies would be cheaper.

For the sake of discussion, we will stipulate that he may be correct in both cases. And then we will emphatically state that he shows complete ignorance of the fundamental purpose of the oil import program.

That purpose is to enhance national security—including all 50 States—by preserving a healthy, vigorous, and capable domestic petroleum industry. Had there not been such an industry in the 1940's Hawaii today might well be the easternmost outpost of the Japanese empire, instead of the youngest State in the Union.

OIL IMPORT CONTROL DIFFERENCES

We now turn to basic differences between legislative control over oil imports and similar control over any other commodity.

First, control over oil imports was instituted in 1958 and made mandatory in 1959 because the rate of imports was found, by the then Office of Civil and Defense Mobilization, to threaten to impair the national security. That office so certified to the President. Such a finding, to our knowledge has never been made as to any other industry.

Second, legislative standards for oil import control add nothing new in the field of foreign trade. As noted above, oil imports have been federally controlled for 10 years. What the proposed legislation would do is merely prevent future distortion of the national security purpose of the program by capricious administrative exceptions and exemptions wholly unrelated to that purpose.

Third, since oil import control legislation adds nothing new in the field of foreign trade, the argument that it would lead to counter-measures by other nations falls flat. Here again is a basic difference between oil and other commodities. Nations which might have been affronted by oil import controls have had a 10-year period in which to react; none of them has done so.

LEGISLATION ESSENTIAL

For the reasons stated herein, we urge the adoption of proposed legislation to spell out, by law, the intent of the Congress when it adopted the so-called Defense Amendment to the Trade Agreements Act. Recent events have convinced us that sight of the national security purpose of the program is being lost by the granting of special deals, and that legislation is essential if the program is to be returned to that purpose.

Thank you for this opportunity to present our views.

(Mr. Trueblood's statement referred to follows:)

STATEMENT R. W. TRUEBLOOD, PRESIDENT, BELRIDGE OIL COMPANY

The Belridge Oil Company is a typical non-integrated producer of crude oil in California. Because crude oil sales constitute our only source of operating income we are directly affected by changes in economic conditions which influence the marketability of crude oil. For this reason, we are qualified by experience to comment on the mandatory oil import program as it applies to Petroleum District V, the seven western states.

In our opinion, the domestic producing industry, particularly the independent producer, owes its continued existence to the adoption in 1959 of the mandatory oil import program. We believe that a continuation of this program is requisite to a viable domestic petroleum industry capable of meeting this country's needs. This does not mean to imply that we are completely satisfied with the present import program, nor that we feel that it cannot be strengthened and improved—quite the contrary. However, the incontrovertible fact remains that prior to the imposition of the mandatory oil import program in March 1959, excessive uncontrolled imports of foreign crude into District V had created such chaotic economic conditions that the welfare of not only the independent producer but also of the entire domestic industry was seriously threatened. The west coast area was being inundated by a flood of low priced foreign crude. The effect of the resultant oversupply was immediate and adverse. All phases of industry activity, including allied service industries, were curtailed with an accompanying reduction in employment and tax revenue which contributed to a marked deterioration in the general economy.

Subsequent to the adoption of the mandatory oil import program, gradual and steady improvement occurred in all generally recognized industry economic indices, except the price of crude which has never recovered and is currently severely depressed by any standard of measurement. Under the stabilizing influence of the import program it has been possible to maintain what may be termed minimal satisfactory conditions in District V. However, we are apprehensive that the recent spate of exceptions, exemptions and bonus quotas, granted to special interests in other areas by arbitrary executive order, will spread into District V, thereby seriously weakening the effectiveness of the import program here as it already has in the remainder of the country.

We believe that past history has unequivocally demonstrated the need for a continuation of the mandatory oil import program, essentially in its present form as applied to District V. Conditions in this area are particularly sensitive to an imbalance between supply and demand. Oversupply of crude is invariably accompanied by an immediate deterioration in the economic factors which affect the domestic petroleum industry and the general economy. There is an essential need for a program such as this which achieves an effective balance between domestic supply and total demand while still providing a means whereby increases in domestic production will find a ready market. Such a program is

necessary if employment levels are to be maintained and a strong and vigorous domestic producing industry is to be perpetuated in the interest of national security.

The record of this and other hearings held by Congress and the Department of Interior is replete with evidence in support of this premise. During the Eisenhower administration, a special cabinet committee found that foreign oil imports into the United States were excessive and constituted a threat to our national security. Accordingly, by executive order, the present mandatory oil import program was initiated.

The necessity for maintaining reasonable restrictions on foreign oil imports to encourage domestic petroleum self-sufficiency has been reaffirmed by both the Kennedy and Johnson administrations. The wisdom of this policy was graphically demonstrated during the recent Arab-Israeli conflict when Middle Eastern oil was curtailed. At that time our ability to provide sufficient petroleum to meet both our own needs and those of our allies prevented what otherwise would have been a major fuel crisis.

For these reasons we are greatly concerned over what we consider to be recent arbitrary bureaucratic manipulation of this essential program for purposes unrelated to its basic intent. The granting of exemptions, special import licenses and other dispensations by executive order has reached a point where the integrity of the entire program is in jeopardy.

In order to correct this situation it is strongly urged that the Congress of the United States officially recognize the fundamental need for controlling offshore foreign crude oil imports into this country and that concerted Congressional action be taken to legislate the present provisions of the mandatory oil import program into law. Such action is imperative if the demonstrated effectiveness of this program is to be preserved in the interest of national security.

The CHAIRMAN. We thank you, Mr. Fox.

Mr. McCLURE. Mr. Chairman, it will take us about 2 minutes to complete our formal statements. I would like to present to you Mr. Joseph C. Shell, executive director of the California Independent Producers & Royalty Owners Association.

The CHAIRMAN. Mr. Shell. Mr. Shell, before you begin, I want to recognize Mr. Utt.

Mr. UTT. Mr. Chairman, I just want to welcome Mr. Shell to this committee. He is a former minority leader of the State Assembly of California, an outstanding citizen of our State, and I welcome him here to the committee.

The CHAIRMAN. Thank you, Mr. Utt.

STATEMENT OF JOSEPH C. SHELL

Mr. SHELL. Congressman Utt, thank you very, very much for your complimentary remarks.

Mr. Chairman and members of the committee, my name is Joseph C. Shell. I am executive director of California Independent Producers & Royalty Owners Association. I have been a small oil producer in the State of California for 25 years and a member of the California Legislature from 1953 to 1963.

It is true that the overall picture of balance of payments as related to imports of oil is a large problem with many facets. To those of us who are small independent operators in the State of California however, the continuation of imports at their present rate into California has us hanging on the ropes. We are doubly susceptible to this import pressure because the price structure of crude oil in California has remained the same for the last decade while operating costs have accelerated sharply. There are thousands of wells in California which

will have to be abandoned if the existing relationship between production and imports is continued. The loss of these reserves could be a stringent blow in our national defense planning.

In California there are a total of 41,348 wells of which 27,195 are in the stripper well category (less than 15 barrels per day) which means that 65 percent of the wells in California are marginal in nature with another 7 percent approaching the marginal condition.

According to an interstate oil compact survey made in January 1967 there were 455,561,000 barrels of oil considered as primary reserves while secondary reserves were calculated at 710,962,000 making a total in both primary and secondary reserves of the marginal wells in California 1,166,523,000 barrels. The country and the State can ill afford to lose these reserves. Reductions in imports into California could keep these reserves active.

Having been an operator of such wells in the State for many years I know that each month that goes by under the existing price structure and import condition will see some of these wells abandoned and the reserves lost. The amount of cheap foreign crude that is brought into California under the current quota system certainly has a depressing effect on the price of crude oil.

It is the old story of the charges for wages and materials in this country being fixed on a plateau which makes competition with cheap foreign labor almost an impossibility unless our Government recognizes these facts and drastically reduces the import quotas into California.

It is not a matter of inefficient operation but a matter of a standard of living which has been established in this country by Government edict as to minimum wages and other such artificial factors. If these artificial factors are to be maintained there certainly should be consideration given in balancing them with more stringent protection against the influx of foreign production which is developed under conditions over which we do not have this same restrictive control.

The large integrated companies can continue to exist and prosper under this quota system but the small independent producer is being put out of business by this price squeeze which is related directly to imports.

In California we are moving rapidly toward a time when the only production and exploration for oil possible will be that done by the major companies. The small independent operator is a vanishing breed being killed by the pestilence of low-cost imports.

By reducing imports into California you gentlemen not only would be making a change in the balance of payments favorable to this country but would be pumping lifeblood back into the small independent who is being artificially destroyed.

The small independent operator in California is being artificially destroyed—not by a competitive system, but by prices constricted by cheap foreign oil imports and levels of operating expense decreed by government. California is the most critical area in the Nation in this regard.

I agree with Mr. Stark Fox in almost all instances. We work together very carefully. I want to convey to you very briefly, if I may, in addition to my prepared statement the position of and the condition of the small independent operators in California.

We are gradually going out of business in California as oil operators primarily because of the pressures that have been exerted on us. As Mr. Fox indicated, we have not only not had any price increases for 10 years, but we have lost money off the price of the crude oil that we are selling.

Anything that tends to depress that price certainly is tending to put the small oil operator out of business in the State of California. And the imports as they are coming in certainly are much cheaper to bring in.

I don't know at what point, and I don't believe anybody can tell us at what point, the independent oil industry, and especially the small operators, will be permitted to stay in business. I had a couple of leases up in the San Joaquin Valley that were extraordinarily fine leases. We run into this situation: That our wells are becoming so small in California that 65 percent of them are now in the stripper well category, as I said, and with this in mind if there is to be a small independent operation in California, not having all of the production being in the hands of the major oil companies, many things will have to change and I think one of those changes has to be in the import system.

I would prefer to see the imports much less into California. We are faced with another problem there. That is the problem of the Alaskan crude and that crude is growing very rapidly. It is going to continue to grow. We are going to get a major impact from that in the State of California, so those of us who are small operators in California are really hanging on the ropes and I would hope in this committee's deliberations that the committee will consider this, and I am not looking at it strictly as a matter of national defense, gentlemen.

Certainly I am looking at it as an operator who would like to stay in business, would like to see my fellows stay in business in that State of California, and under the existing circumstances we can't do it. We absolutely can't do it, so it would be my estimate that within the next 5 years we would probably lose 10,000 or 11,000 of these wells and if there is any impact on reserves for national defense, and certainly there would be, the impact on the individual operator who is going to go out of business would be much greater.

So this is my statement here this morning, gentlemen, primarily on the position of the small operator, being one of them and being in desperate circumstances in that State.

Mr. Chairman, I certainly appreciate the chance of being back here and seeing you gentlemen and certainly my old friend Jim Utt.

Thank you very much for your time.

The CHAIRMAN. Thank you, Mr. Shell.

Mr. McClure, does that complete your presentation?

Mr. MCCLURE. Mr. Chairman, that completes our formal statements.

The CHAIRMAN. We appreciate the statements of all of you gentlemen. Are there any questions? Mr. Burke.

Mr. BURKE. Mr. McClure, I notice that you mention the problem of No. 2 oil in the northeast section of the country. I happen to come from Massachusetts and last year we had many, many complaints from dealers up there that there was a shortage of No. 2 fuel.

In fact I think in April of this year the price of No. 2 fuel was increased, something that was unprecedented in the oil market, because

this is usually the end of the cold season and when sales drop usually the prices drop, and instead of the prices dropping at this time the price went up.

Why do you think that they are complaining up there if there is no problem?

Mr. McCLURE. Congressman Burke, in answer to your question, first, in a very exhaustive check of the supply problem there was no shortage of No. 2 fuel in the New England States. I would like to say from my own personal standpoint and from the standpoint of the industry that I have had the privilege of serving, that this industry has a very great concern for its stewardship; to see that the American public has the petroleum commodities needed. So to answer your question on the first count there was no shortage.

It was an artificially designed statement for other reasons.

In answer to your second question on the case of the price increase, I think that you have to go back and look at the record of price increase, price decrease, and there have consistently, as you pointed out, been fluctuations in the price of the commodity, fuel oil, but fuel oil delivered in New England today has not followed the commodity index.

It is lower in New England than the commodity index of all other prices.

Mr. BURKE. The retail price of No. 2.

Mr. McCLURE. Yes, the retail price of No. 2 is below the average of all of the commodity index in New England.

Mr. BURKE. What is the price for No. 2 fuel oil, say, in the northwest part of the country?

Mr. McCLURE. Where, sir?

Mr. BURKE. The northwest, the retail price?

Mr. McCLURE. If you are speaking about the northwest and you are speaking about Oregon and Washington, in this particular area—

Mr. BURKE. Yes, up in that area.

Mr. McCLURE (continuing). It will be comparable. It will be comparable to the commodity in the New England States. It will be within a percentile of the cents per gallon. I will be happy to supply exact figures and a complete study that we have done on this if you care to have us do so, sir.

Mr. BURKE. Well, I want to get back to this statement by you that there was no shortage there. I think in April of this year over 100 dealers, oil dealers, from Massachusetts came down here to Washington and met with the entire Massachusetts delegation and they seemed to be quite upset.

They said that their own supplies were depleted and if the climatic conditions continued, the cold weather continued, they felt that they would be without a supply of oil for that next month.

What would prompt them to do that?

Mr. McCLURE. They were prompted on the basis of an economic justification, sir. To prove the point that there was no shortage, a study was made by the Chase Manhattan Bank of this particular problem and an extensive report was done on it, but secondly, as requests came for emergency supplies by the oil import appeals board these requests came for an allocation for this key period.

It subsequently was granted but no part of that grant of import quotas of No. 2 fuel oil was utilized in the heating season just passed. In addition to the appeals board giving them what they had requested for this past heating season, they extended that into the 1968-69 heating season which means that all of the import quotas that they were granted under the emergency provision of the act will be utilized in the 1968-69 season. None of the import quotas which they were asking for were in any way utilized in the past heating season.

Mr. BURKE. Not in defense of the Secretary of the Interior, but I want to point out that you people are being critical of him because he has raised these quotas slightly and up in our area we are very critical of him because he hasn't raised them enough, so, you see, the Secretary of the Interior is a devil if he does and a devil if he doesn't.

I think he has tried to work in a very fair way with both your industry and with the problems in the Northeast. We would like to see the quotas up in our area raised a lot more so we could plan a lot better for our heating problems up there.

I would just like to ask this question. There seems to be a question here about the imports and I notice that according to the tariff figures here that the average imports under the ratio of imports to production for the years of 1961 to 1966 were 15.22 percent and in 1967 they dropped to 12.80 percent.

In other words, you have about a two and a half percent drop in the ratio of imports to production, so it looks like your position here is improving and ours is not improving up in the Northeast.

Mr. McCLURE. Congressman Burke, I think to answer your question in regard to 1967 we will have to cross the Atlantic to Cairo and ask Mr. Nasser why this occurred. Mr. Nasser said, "We are not going to let you have oil in 1967" and this was the reason for the reduction in imports in 1967.

Mr. BURKE. The problem in the Middle East.

Mr. McCLURE. That is correct, yes, sir.

Mr. BURKE. Irrespective of what caused it, nevertheless there was a drop and that certainly should be beneficial to your industry.

Mr. McCLURE. Really this is the whole point of our testimony; that when you depend on petroleum resources from outside the North American province you are depending on resources which you cannot control and then you are at the will and whim of such men as Nasser and others of his particular thinking and they say, "No, it shall not pass." Then where do you get it? I think this is really the reason for the whole import program, the ability to reach back in the certificates of deposit and be able to pull out on a given day, that rainy day, or that rainy day oil, that we need, and we were able to do it in 1967, sir.

Mr. BURKE. So I imagine that you can sympathize with the feelings of the people in the Northeast when they kind of object to getting caught in this terrific squeeze which is raising the prices of the domestic heating oil and also placing them in jeopardy of having quite a few cold days.

Mr. McCLURE. We are deeply concerned about that.

Mr. BURKE. The temperature up there, usually during the winter months of January and February, might drop down as low as zero and then you are right close to zero where it is very damp and penetrating, particularly in a lot of these homes in tenement districts where people buy oil day to day.

If there is ever a shortage created up there it would create a great deal of hardship so I think that we are justified up in our area for asking the Secretary of the Interior to raise the quotas slightly.

Mr. McCURE. If there was a shortage I concur and I will have to answer you this way. My home is in Michigan. I had told some of my friends I would come to the Montana-Wyoming area in February and they said, "Don't come. A Michiganiite can't stand the weather there."

So I do know what you are talking about as far as the weather is concerned and the fuel oil situation. We just object to using excuses and presenting them as reasons.

Mr. BURKE. Thank you very much.

Mr. McCURE. Yes, sir.

The CHAIRMAN. Any further questions? Mr. Schneebeli.

Mr. SCHNEEBELI. Mr. McCURE, you state that the oil trade deficit is about a billion and a half dollars annually. Mr. Steed I think mentioned \$1.6 billion. I am looking for some information. Is most of the oil brought into the United States brought in by U.S.-owned companies?

Mr. McCURE. The answer is yes, this is true.

Mr. SCHNEEBELI. Then the salaries paid to United States citizens who work for oil companies, the profits that are returned by these U.S. oil companies to the United States and the supplies brought into the United States, are they set up as compensating factors against this deficit? Do you give credit for these items? Is this a gross or a net figure?

Mr. McCURE. To answer your question, sir, the \$1.5 billion that the United States has to pay out in exchange for oil that is brought in from outside the United States is a gross figure.

There is no question that you can justifiably say that these companies do have earnings and there are salaries and profits that are earned outside the United States.

However, with the great demand in Europe, with the tremendous demand for energy resources across Asia, across Africa, and the rest of the world, those companies are going to produce and they are going to earn irrespective of whether those commodities, petroleum, are brought into the United States.

In other words, the argument is made that it is a compensating factor, but in reality we do not look upon it as such because we say they were earned, and produced, and drilled, and explored outside the United States.

Mr. SCHNEEBELI. But actually in the balance of trade you have to give credit for the dividends returned to the United States in compensation for this deficit.

As a matter of fact, as you know, the dividends being returned to the United States are greater than our new capital outlays at the present time. So I would be interested in what your net figure is.

Mr. McCURE. We can give you that figure.

Mr. SCHNEEBELI. If you would, supply that for the record. I think it is quite important.

Mr. McCURE. We will be happy to supply that for the record, Mr. Chairman. Again my only point is that those dividends would be returned to the United States by those companies regardless of whether there were imports into the United States or not.

Mr. SCHNEEBELI. That is right but I think for the record we would like to have the figure that you have.

(The following letter was received by the committee:)

INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA,
Washington, D.C., July 3, 1968.

HON. WILBUR MILLS,
Chairman, Committee on Ways and Means,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: On June 27, 1968, Mr. Harold M. McClure, Jr., President of the Independent Petroleum Association of America testified before the Committee on Ways and Means.

Congressman Schneebeli (transcript page 2879) requested that Mr. McClure supply certain information for the record relative to compensating factors against the U.S. deficit in petroleum trade (imports less exports) including the flow of funds related to petroleum operations abroad.

The information requested is as follows:

SELECTED DATA ON OILS' BALANCE OF PAYMENTS

[In millions of dollars]

	Petroleum trade deficit	Net capital outflow	Income returned to United States	Net balance
1960.....	-1,055	-452	+1,150	-357
1961.....	-1,192	-793	+1,336	-649
1962.....	-1,286	-606	+1,565	-327
1963.....	-1,336	-828	+1,715	-449
1964.....	-1,454	-760	+1,856	-358
1965.....	-1,634	-977	+1,799	-812
1966.....	-1,668	-876	+1,778	-76

Source: Department of Commerce.

It should be recognized that there are items additional to those listed above which enter into the overall balance of payments for petroleum. For example, purchases of oil abroad by the U.S. military, tanker freight and insurance payments, royalty fees etc., for which official Government statistics are frequently not available.

In evaluating this matter, it is important to keep in mind that the net capital outflow and the income returned to the U.S. from petroleum operations abroad would not be materially affected by adjustments in the Mandatory Oil Import Program. This is due to the fact that more than 85 percent of the production from these operations is marketed in foreign markets, with less than 15 percent being imported into the U.S.

Sincerely,

L. DAN JONES, *General Counsel.*

The CHAIRMAN. Any further questions? Mr. Collier.

Mr. COLLIER. Just to get your colloquy with our colleague from Massachusetts in some perspective, Mr. McClure, is there any need in the light of domestic production for there to be a fuel shortage in New England or any other section of the country?

Mr. McCLURE. In light of our present situation?

Mr. COLLIER. Yes, sir.

Mr. McCLURE. Is there any need to have a shortage?

Mr. COLLIER. Yes, sir.

Mr. McCLURE. The answer to your question is there is not. There is an imminent potential danger if this industry does not go back to work and start drilling the exploratory wells, the wildcat wells, necessary to keep this Nation strong. I can say there is a long-range potential problem if we don't face up to some of our immediate problems.

Mr. COLLIER. The immediate problem that could develop? Why would not the domestic industry be able to supply to prevent or avoid a fuel shortage in any section, or can they presently do it?

Mr. McCLURE. Presently it can be done. It has been done. It will be done.

Mr. COLLIER. What would be the advantage then for the New Englanders to have an increase in the quota? Because of the price?

Mr. McCLURE. That was the only justification; yes, sir.

Mr. COLLIER. This is quite interesting because those from New England in the course of these hearings, particularly my good friend from Massachusetts—and I am sorry he is not here—have suggested protection for the shoe industry. And while I am most sympathetic; because here is a case where they are not able to produce shoes in this country and sell them at the price they are produced by the foreign manufacturers.

It just points up one of the inconsistencies in dealing with this problem. Where the issue involved here is strictly a case of price, then we would have to apply the same rule of thumb in dealing with the shoe problem.

The fact that protection is sought there by the New Englanders on the basis that notwithstanding the fact that people in this country might be able to buy shoes, for example, at a little lower price, it seems to me that if they want some degree of protection for the shoe industry in New England they should be willing to accept a little higher price for domestic produced fuel oil as part of the package.

That is all I have.

The CHAIRMAN. Mr. Battin.

Mr. BATTIN. Thank you, Mr. Chairman. I think it would help the record if you haven't already put it in, to have the projected need for new discoveries of oil, new reserves in this country, based upon population growth and new uses of this particular form of energy. The figures that were given to me recently indicated that, unless we did go ahead and make some very substantial new finds as far as reserves are concerned, this country in as short a period of time as 10 or 15 years can be in a real deficit situation as far as meeting our own needs and our ability to produce and take care of the users in this country.

Do you have any figures on that?

Mr. McCLURE. Congressman Battin, I will respond in this way. First, as to the demand, it has been presented to us by the Interior Department, by the Secretary of the Interior himself, as we move into the 1975-80 period that we are going to experience tremendous additional demands for liquid petroleum products in the United States, even on a magnitude through 1980 anticipating requirements, of some 18 million barrels daily.

Our present figure is in the range of 12 to 13 million barrels of demand daily.

Now, if you do your arithmetic on this we are producing in this country something approximating 10 million barrels daily. Our ability to produce as we have done the work within the productive capacity committee of IPAA indicates we could produce over a sustained 6 month period about $2\frac{1}{4}$ million barrels in addition to our present production. This is what I called CD's in the bank or a rainy day production.

We need to maintain that. We also need to import. I feel strongly on that. But it needs to be in the balance as spelled out by the mandatory oil-import program.

Now, where do we need to go as far as looking is concerned? Here we have in the past 12 years or in the past decade moved up in consumption in the magnitude of 50 percent. The searching for petroleum, the wildcat wells, have declined and I have just done an intensive study on this.

In 1956 we drilled 8,700 wildcat wells, new field wildcats. In 1968, just 12 years later, that has been reduced to 5,200, or a reduction of 40 percent, at the same time this tremendous demand increase has been going up. I maintain that it is absolutely vital that we double the wildcat exploratory effort in the United States and this can only be done under the circumstances of a stable import program together with the economy of the oil business moving with the general economy.

We do not seek nor would we recommend that this Nation move its petroleum economy over and beyond the economy which exists, but we do think it has, a right and a responsibility to move within the economy that exists. Those two things we feel will find the reserves that are here to be found.

Mr. BATTIN. We hear a lot of discussion of new methods in finding oil. I wonder if you have a figure on the percentage on the average, drilling a hole wildcat, how many dry ones are there compared to producers?

Mr. McCLURE. These present some very interesting figures. For every 100 wildcat wells drilled, you will be able to complete approximately 10 of those and call them a discovery but then you have to look behind the scene and see what is a discovery; in other words, is that a discovery that will pay back the cost of drilling and so forth.

There are only three out of that 100 that will ever be economic ventures and turn out to be something that we would call an important discovery so that, to answer your question, it is three out of 100 wildcats that will turn out to be successful, important discoveries.

Mr. BATTIN. Hasn't that been pretty much the rule through many years of exploratory work?

Mr. McCLURE. The 10 discoveries method out of every 100 wells has been a historic pattern for the least two or three decades. It has been very consistent.

Where the consistency breaks down is that in any given year or any given 5 years you can't tell whether your discovery of gas is going to be greater than your discovery of oil or whether in that given interval you will have as great a number as in the prior year.

In our own particular business we have a 5-year cycle. In our small company we figure if we have 1 good year out of 5 we are doing well.

Mr. BATTIN. You keep looking in the vast State of Montana?

Mr. McCLURE. They are there to be found, Congressman.

Mr. BATTIN. Thank you.

The CHAIRMAN. Mr. Bush.

Mr. BUSH. Mr. Chairman, I see the distinguished Chairman of the Appropriations Committee here so that I will try to be very brief and save some of these questions I have for the substantive witnesses.

The CHAIRMAN. He does have a legislative program beginning at 12, do you not, Mr. Mahon.

Mr. BUSH. I have just one or two quick questions to ask.

Are there any other independent producers testifying later because I don't want to take the time.

The CHAIRMAN. If you have a number of questions, Mr. Bush, we could ask these gentlemen to return after we hear our two colleagues, Mr. Mahon and Mr. Matsunaga.

Mr. BUSH. I would just like to ask Mr. McClure some questions for the record later and that would suit me.

The CHAIRMAN. Would you gentlemen remain in the room and let us hear from our colleagues.

Mr. Mahon.

Mr. Matsunaga, we will hear you right after Mr. Mahon.

We are pleased to have with us today our very distinguished colleague from the State of Texas, the Chairman of the Appropriations Committee of the House, one of the great leaders of the House of Representatives.

You are recognized.

STATEMENT OF HON. GEORGE H. MAHON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. MAHON. Thank you, Mr. Chairman.

I come before you with a very special interest. I represent the largest oil producing congressional district in the United States and by far the heaviest oil producing area of Texas.

Naturally I am concerned about preserving a healthy and stable oil industry. I am concerned about it for reasons of my own constituency. I am concerned about it for reasons of national defense because the sinews of war are involved here. About 70 percent of all shipments to Vietnam is oil in one form or another. Like you who are members of the Ways and Means Committee, I am concerned about it from the standpoint of the balance of payments.

Oil importation, of course, is necessary but the more we import the more it tends to contribute to the unfavorable balance.

Following my remarks, Mr. Chairman, I would like to file a statement for the record from the president and the executive vice president of the Permian Basin Petroleum Association located at Midland, Tex., a former home of Mr. George Bush of your committee.

The CHAIRMAN. Without objection, the statement will appear in the record following Mr. Mahon's remarks.

Mr. MAHON. Mr. Chairman, I am confident that this committee need not be reminded that there is no commodity more vital to this Nation's security than petroleum. Repeatedly since World War II, this Nation's petroleum industry has been called upon to meet emergency needs as well as the requirements of friendly nations in times of crisis. The most recent event is the continuing crisis in the Middle East. Fortunately, during this crisis the U.S. industry has been able to increase its production by 1 million barrels daily to help fill the supply gap in Europe, Canada, and our own east coast.

Mr. Chairman, your committee has been or will be furnished by other witnesses extensive facts and statistics concerning the serious declines that have been taking place in this most essential industry over the last decade. Therefore, I will not address myself to these alarming

trends except to say that my district, as well as the entire State of Texas, is experiencing similar downward adverse trends in exploratory drilling, employment, and the addition of new reserves of oil.

The Department of the Interior over 2 years ago issued a report concluding that in the years ahead we must increase our discovery of new reserves by 50 percent over recent experience.

In contrast with the declining trends in the U.S. industry, I am advised that the industry in the Soviet Union is undergoing rapid growth, their production having quadrupled since 1955. Oil has become a principal weapon in their worldwide economic and political expansion.

These adverse trends in our domestic industry must be reversed if we are to regain a strong and viable petroleum-producing industry capable of contributing to improvement in the overall economic posture in this Nation.

I would like to highlight two most important factors—national defense and this Nation's international trade deficits.

The President in 1959, in establishing the mandatory oil import program, cited as the one and only reason for the program: "The certified requirements of our national security which make it necessary that we preserve to the greatest extent possible a vigorous, healthy petroleum industry in the United States." This pronouncement came after a comprehensive study by a special Cabinet Committee which concluded:

"It is clear that there is a direct relationship between the Nation's security and adequate and available sources of energy. Oil and gas account for two-thirds of all the energy that is consumed in this country. Furthermore, there are no adequate substitutes in sight for the foreseeable future. Therefore, we must have available adequate supplies of oil."

The decision to establish as a national policy the maintenance of a vigorous and healthy petroleum-producing industry was reached only after careful study. Three presidents have recognized the need to limit oil imports into the United States.

In viewing the world as we find it today it has always been a source of comfort to know that this Nation has had adequate oil reserves whenever needed. However, I am now deeply concerned. If the deteriorating conditions that have persisted for 10 years are permitted to continue, this industry will not be able to meet future emergencies.

I have grave doubt under existing trends whether this Nation could meet the challenges as it did in World War II when more than half of all the tonnage shipped from the United States to our military forces consisted of petroleum products. During World War II, America was called upon to fuel not only its own fighting machine but also the forces of its allies.

Now in Vietnam, oil comprises in the order of 70 to 75 percent of the tonnage required to prosecute this conflict.

Mr. Chairman, during the past 2 years frequent changes have been made in the mandatory oil import program for reasons other than national security, such as the stimulation of employment and economic conditions in Puerto Rico and the Virgin Islands; to promote beautification and conservation; and to solve the air pollution problem. These are worthwhile objectives but the import program should not be used as a tool to solve them.

As a result of these actions the integrity and meaningfulness of the program are in grave doubt. The industry does not know what to expect next. It cannot with full confidence make plans for the future.

The industry needs to know whether or not our Government intends to remain self-sufficient as to oil or does it intend to become increasingly dependent on oil imports.

I urge this committee to provide a clear answer by writing into the law definite legislative standards which would please general limits on administrative discretion.

Mr. Chairman, I also wish to emphasize the tremendous impact oil imports have on the balance of payments.

Even with the mandatory oil import program, we import oil on a scale I doubt any other nation would permit in competition with its own essential industry. Total oil imports now amount to 30 percent of our crude oil production. It is my understanding that oil imports now generate about a \$2 billion annual dollar outflow.

As one heavily engaged in seeking ways and means to improve our critical fiscal situation, I feel that the Congress must reevaluate the impact of petroleum imports with regard to our balance-of-payments position and otherwise.

I recognize, Mr. Chairman, that this question of trade policy is filled with complexity. It is my conviction, however, that we must put priority on our national self-interest, from both a defense and an economic standpoint.

In this question of oil imports and the deteriorating effect on the domestic industry, both our defense posture and our economic strength are vitally affected. I urge that this committee give this matter its most earnest consideration and take action that will rectify what appears to me to be a dangerous situation involving our future oil supply position.

(The statement of Permian Basin Petroleum Association, referred to, follows:)

STATEMENT OF ROBERT M. ORR, PRESIDENT, AND ED THOMPSON, EXECUTIVE VICE-PRESIDENT, PERMIAN BASIN PETROLEUM ASSOCIATION

This statement is presented specifically for the more than 3,000 members of the Permian Basin Petroleum Association and generally for all those involved in the Independent Domestic Oil Industry in the Permian Basin, either directly or indirectly. In other words, for those responsible for some 85% of the economy of the area.

First let me define the Permian Basin. It is an area covering over 100,000 square miles in 57 counties in West Texas and 4 counties of Southeastern New Mexico. This is the nations largest single petroleum producing area, with more than 92,000 oil wells producing one and three quarter million barrels of oil per day and some 10,000 gas wells producing about four billion cubic feet of gas per day. You can easily see why some 85% of the economy is derived from the petroleum industry, with the other 15% making their living in related industries.

For some time now, our people have been losing faith in the Mandatory Oil Imports Program, although, at its inception, they gave it full support, recognizing the need for some foreign imports of both oil and gas. The PBPA has appeared before Interior hearings, to point up the need for incentives for domestic exploration and point out the dangers of the developing loopholes in the program, to no avail.

Interior Secretary Udall and Assistant Secretary Moore have failed to answer questions as to the validity of various new gimmicks with the stated purpose of the Presidential Proclamation . . . insuring our national security by safeguarding a vigorous and healthy domestic petroleum industry. In fact, their answer

has been "We do have a vigorous and healthy domestic petroleum industry. Look at the profits as reported by Chase-Manhattan Bank, and see how well we did during the 1967 Mid-East crisis".

The first of these criteria covers only the giants of the industry, and they are not the ones who have customarily found 85% of all domestic production. That has been the responsibility of the Independent segment of the industry. And, while drilling has been drastically reduced, the latest available figures (1966) show that the independent operator was still responsible for finding 74% of domestic production. A simple check of a few West Texas-Southeastern New Mexico telephone directories will soon reveal how many of those independents, some 40%, are no longer in business. The second criteria—how well we met the demands of the 1967 Mid-East crisis, was in no way a result of Interior Department planning, but the wisdom of the states in producing according to demand and having reserve production available in time of need.

The reserve productive capacity was limited even then. Oklahoma and Kansas were unable to increase production beyond a certain point and only certain fields in Texas could meet increased allowables with equal increases in production. With each increase the gap between under-production and allowables widened in most fields throughout the United States. We did meet the short term demand, but there were definite signs that on a long term basis we could well be depleting our reserves to a point of dependency on foreign oil during a possible future emergency. But, what was the reaction to an industry effort to see that no American went without oil, that no American fighting man ran short in fuel, and that European losses were minimal? Instead of praise and appreciation, the industry is threatened with not just a make-up of the Imports lost, but actually stepped up imports as well.

The Mandatory Imports Program was set up to see that this very thing could not happen. Although the oil industry is considered to be in its old age, given proper incentives, such as an assured level of imports and a one cent per gallon crude price increase, we believe the independent can, and will, find the necessary reserves to meet the demand, at least until some of the other energy sources can be developed to fill the gap.

Some, no doubt will say that we have cried for the poor independent operator, but have made no case. Our case is not for these individuals alone, but for everyone in these United States. The automotive industry, airlines, trains and trucks, large and small manufacturers, in fact all segments of our economy, plus the military, agree—that without oil our nation cannot function. And, we do have some facts and figures to point up our concern. (See attached charts)

For over ten years there has been a continuing decrease in all phases of the search for domestic hydrocarbons. At the same time, there has been a continually increasing demand for both oil and gas. Already we are using more crude oil than we are finding and predictions are that by the mid-1970's this same condition will exist for natural gas. In both instances, today there is a much smaller ratio of reserves to producibility than ten years ago. Without faith in the Mandatory Imports Program and proper incentives to seek additional reserves, these conditions will continue to deteriorate.

Yes, the independent operator is being, and will continue to be, hurt. But the real loser will be the consuming public, and our nation. We will be forced to a dependency on foreign oil and the whims of unstable, even unfriendly, governments. Look at the nations of Europe. Here is a perfect example of what really happens at the gasoline pumps in countries where all their crude oil is cheap foreign imports and there is no depletion provision. Gasoline is priced anywhere from 55 to 85 cents per gallon, the quality is inferior to ours, and service is practically non-existent. While in our country, product quality has continued to improve but the price, except for increased taxes, has remained noticeably unchanged. More frightening is the fact that supplies can be cut off at a moments notice and, while most of these nation's are not yet as highly industrialized as our own, they would be almost at the mercy of their suppliers.

We are not asking for any special privileges for the independent operator. Only that all be treated equally under the Mandatory Oil Imports Program, without loopholes or handouts, and that the independent operator be allowed to participate in our growing economy by getting current prices for his product in the market place, just as he has to pay current prices for what he buys in the market

place. For both the national economy and our national security, we urge that this program be returned to its original intent.

First: By investigating all areas of administration of the Imports Program to see why the original intent is not being achieved, and

Second: By setting guidelines within whose framework there can be restored confidence in the Program and its Administration.

SUMMARY

A description of the Permian Basin and the impact of the Petroleum Industry on our economy, pointing up that with the continuing downgrading of the domestic industry through favoritism, handouts and loopholes, that not only the operators but the consumer and economy are all being put in jeopardy by such thoughtless acts.

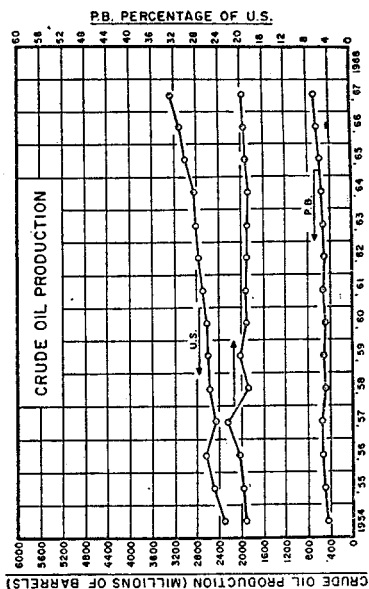
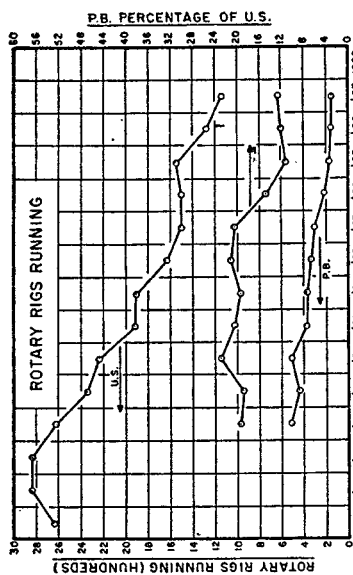
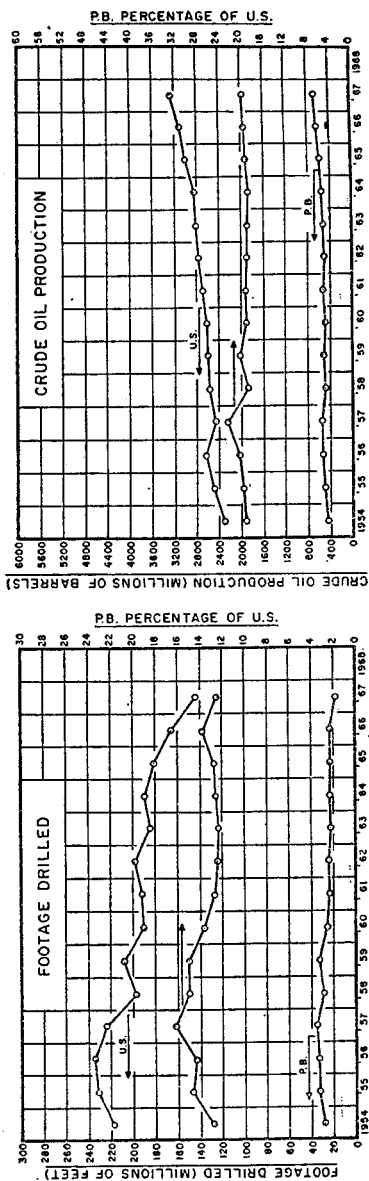
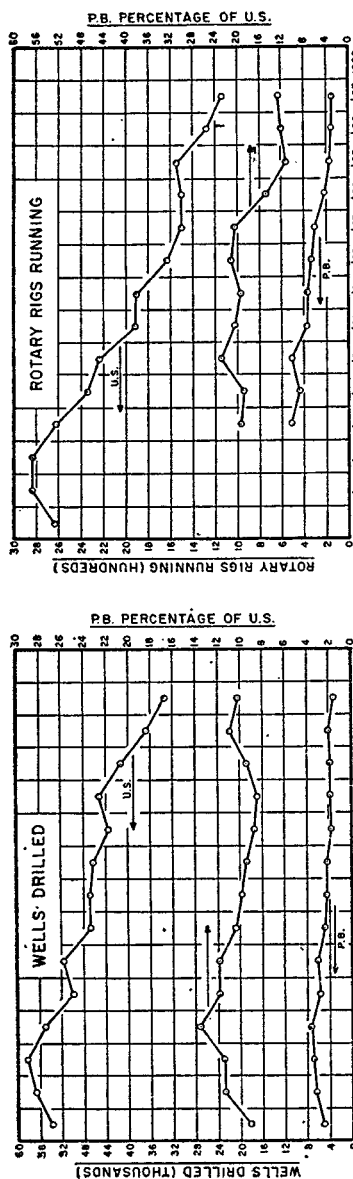
We are asking for a one cent per gallon crude oil price increase; fair treatment for all under the Mandatory Import Program with a chance to sell, as well as buy, at today's prices; an investigation of the Administrative process to see why the Import Program has failed to achieve the original intent; and the setting of guidelines within whose framework there can be restored confidence in the program and its administration.

Year	Wells drilled					Rotary rigs running				
	West Texas District 7C-8-8A	SE New Mexico	Total, Permian basin	Total, United States	Permian basin, percent of United States	Permian basin	Texas-New Mexico	Total, United States	Permian basin, percent of United States	
1954-----	4, 177	785	4, 962	53, 930	9.1	(1)	812	2, 654	(1)	
1955-----	5, 340	1, 114	6, 454	56, 682	11.4	(1)	1, 004	2, 856	(1)	
1956-----	5, 592	1, 103	6, 695	58, 160	11.5	(1)	1, 112	2, 843	(1)	
1957-----	6, 202	1, 304	7, 506	55, 024	13.6	515	1, 095	2, 624	19.6	
1958-----	4, 960	969	5, 929	50, 039	11.8	443	828	2, 356	18.8	
1959-----	5, 194	1, 015	6, 209	51, 764	11.9	512	863	2, 245	22.8	
1960-----	3, 771	1, 199	4, 970	46, 751	10.4	388	710	1, 915	19.3	
1961-----	3, 551	1, 075	4, 626	46, 962	9.8	370	730	1, 911	20.4	
1962-----	3, 453	980	4, 433	46, 179	9.5	347	664	1, 636	21.2	
1963-----	3, 058	806	3, 864	43, 653	8.7	307	584	1, 501	20.5	
1964-----	3, 034	904	3, 938	45, 236	8.6	224	554	1, 502	14.9	
1965-----	3, 126	798	3, 984	41, 423	9.4	172	480	1, 552	11.1	
1966-----	3, 188	836	4, 024	36, 626	11.0	162	447	1, 273	12.0	
1967-----	2, 652	770	3, 422	33, 588	10.2	142	396	1, 134	12.4	

1 Not available.

Year	Crude oil production			Footage drilled				
	Permian basin (millions)	United States (millions)	Permian basin, percent of United States	West Texas District, 7-c, 8-8-a (thousands)	SE. New Mexico (thousands)	Permian basin total (thousands)	U.S. total (thousands)	Permian basin, percent of United States
1954-----	446	2, 314	19.3	23, 670	4, 540	28, 211	218, 986	12.8
1955-----	490	2, 484	19.7	28, 388	4, 965	33, 354	226, 270	14.7
1956-----	535	2, 617	20.5	28, 071	5, 292	33, 363	233, 902	14.4
1957-----	551	2, 448	22.5	29, 549	6, 598	36, 147	223, 087	16.2
1958-----	488	2, 574	18.9	24, 979	4, 835	29, 814	198, 224	15.0
1959-----	522	2, 575	20.2	27, 138	4, 684	31, 822	209, 231	15.0
1960-----	505	2, 621	19.2	19, 949	6, 082	26, 031	190, 703	13.6
1961-----	517	2, 676	19.3	18, 672	5, 763	24, 435	192, 116	12.7
1962-----	516	2, 756	19.1	19, 386	5, 319	24, 705	198, 559	12.4
1963-----	531	2, 804	18.9	18, 033	4, 787	22, 820	184, 357	12.3
1964-----	540	2, 850	18.9	18, 576	5, 466	24, 042	189, 922	12.6
1965-----	570	3, 000	19.0	18, 864	4, 909	23, 773	181, 427	12.7
1966-----	607	3, 100	19.5	17, 913	4, 704	22, 627	166, 025	13.9
1967-----	640	3, 250	19.6	13, 563	4, 486	18, 049	144, 234	12.5

A COMPARISON BETWEEN THE
PERMIAN BASIN
AND THE
UNITED STATES



Mr. Chairman, I would now like to present to you the chairman of the Texas Railroad Commission, Jim Calhoun Langdon, who is very rightly concerned and interested officially in this question which is before you.

I would like permission for Chairman Langdon to file a statement following the statement which I have submitted.

The CHAIRMAN. Without objection, the statement will appear in the record.

STATEMENT OF JIM C. LANGDON, CHAIRMAN, RAILROAD COMMISSION OF TEXAS

Mr. LANGDON. Thank you very kindly, Congressman Mahon.

I simply wanted to appear here to express the concern of the State of Texas and my personal concern as chairman of the Texas Railroad Commission, which is charged with the responsibility of regulating the oil and gas production of that State, with the matters that this very important committee does have under consideration.

I am sorry that Congressman Burke, of Massachusetts, who was questioning Mr. McClure, is not here at the present time simply because I would also like to have had an opportunity to answer his question about why the No. 2 heating oil might have cost a little bit more in Massachusetts as a result of the Middle East crisis.

Unfortunately this is one of the prices I think that this Nation must pay for national defense. It is not a very large price. I don't think it was a high price to pay even in Massachusetts.

In any event, gentlemen, I will file the statement. I want to thank you for inviting me here and I especially want to thank my good friend George Mahon for introducing me to this committee.

The CHAIRMAN. Mr. Bush.

Mr. BUSH. I would like to emphasize the importance of the work that the Texas Railroad Commission does in conservation of oil and the importance it has as the top regulatory body in Texas, to say that Mr. Langdon is one of our outstanding experts in the field of oil conservation and really because of the nature and importance of the role of Texas in this whole country. In this field the Texas Railroad Commission has such a predominant influence on what goes on in the production business and I want to say that in my personal knowledge I say that everybody in Texas knowledgeable in the oil business has a high regard for the chairman of the commission.

It is one commission, though political by definition, that has stayed way, way above partisan politics and has done a tremendous job in terrifically difficult circumstances such as the Suez crises.

I used to be in the oil business. When I was assigned to this prestigious committee I divested myself of such holdings but I dealt in it for 20 years and I think it is important that this committee realize the prestige and importance of the Texas Railroad Commission and I am just glad that you had the chairman of that body here today.

Mr. LANGDON. Thank you.

(Mr. Langdon's prepared statement follows:)

STATEMENT OF JIM C. LANGDON, CHAIRMAN, RAILROAD COMMISSION OF TEXAS,
AUSTIN, TEX.

Mr. Chairman and Members of the Committee: the time has come to back off and take a good, hard look at our Oil Import Program—its purpose and necessity, its history, its bright moments, its dark moments, where it is now—and, most important—where it is going.

I. PURPOSE AND NECESSITY

The single essential purpose of the Import Program always has been crystal clear. The Mandatory Oil Import Program was established by the President under authority of the "National Security" clause of the Trade Agreements Extension Act following a report of the Special Committee to Investigate Crude Oil Imports, in which the Committee found, among other things: "That imports of crude oil and the principal crude oil derivatives and products threaten to impair the national security."

The realism and good sense of the concept was dramatically demonstrated by last year's Middle East crisis. In a compelling way, the crisis underscored the necessity for a strong, viable domestic oil industry with adequate reserve producing capacity to meet the nation's needs in normal and emergency periods.

But the industry's seeming ease in dealing with sudden and exceptional demands last year should give us no cause for complacency. A single dramatic success should not blind us to the fact that next time we may not be so well prepared. And, if we fail to cope with a future crisis, it will be because we have not kept the overriding objective—a vigorous domestic petroleum industry—firmly in our minds.

II. ITS BRIGHT AND DARK MOMENTS

The Program, while far from perfect, was well conceived and, taken as a whole, served the nation well until 1965. The national security was protected, and the distribution of quotas was systematic and reasonably sensible and equitable.

Starting in 1965, and proceeding thereafter at an accelerating pace, the Program has undergone almost continuous change for the worse. The crazy-quilt patchwork of regulations has yielded to the pressures of special interest groups, and concessions have been granted that are in no way related to the original purpose. For the past three years, the Program has been plagued with "loop-hole-itis"—a disease which could be fatal to the Program, and thus to our national security.

The special grants of quotas to individual firms for operations on the island territories have produced a virtual land rush of applications for similar concessions. One concession stimulates new pressures for many others because of competitive necessity. On April 19 of this year, another special deal for Puerto Rico was approved by Secretary Udall, and others are still pending.

While various excuses may have been given for these special grants, it is irresponsible to jeopardize national security to accomplish minor economic benefits to the Caribbean Islands. This trend must be stopped or a large segment of new U.S. petroleum and chemical facilities will be located in the Caribbean Islands—not for sound logistic or economic reasons, but based on loophole economics created to favor special interests. This mislocation will cause the U.S. consumer to eventually pay more for his products. Moreover, it can hardly be in the interest of national security to have these facilities located across a large body of water on an island territory that does not need and cannot consume the volume of products produced.

As a result of political pressure, resellers of No. 2 Fuel Oil on the East Coast were given import tickets this past winter when supplies were tight. While spot prices were probably higher. It should be pointed out that No. 2 Fuel Oil was available in the industry to all customers on the East Coast throughout an extremely cold winter. Such grants, while wholly unjustified, should have been limited to that particular heating season ending in April, 1968. However, they are valid for the remainder of 1968, and for the most part, will be used next fall. Can this be anything but an outright subsidy?

In recent months, as reported prominently in the press, criticism of the program has taken on massive proportions. Criticism of the program has reached the Congress and cause it to become increasingly interested in the program and particularly the manner in which it is being administered.

On May 13th and 14th the Interior Committee of the House of Representatives held public hearings to review the Oil Import Program "as it relates to the domestic oil industry." The hearing was timely and focused attention on the strengths as well as the weaknesses of the program.

It is obvious today that the administration of the program has wandered far afield. Exceptions to its basic rules have been piled on exceptions. Such exceptions, granted by administrative fiat without regard to the explicit authority and intent of the program, are numerous. I will mention some of the main ones only briefly:

1. *Asphalt*

On April 10, 1967 Presidential Proclamation No. 3279 was amended to permit the Secretary of the Interior to allow the importation of foreign asphalt into the United States, "on top of" the historic 12.2% ceiling.

2. *Low sulphur residual fuel oil*

On July 17, 1967 the Presidential Proclamation was amended again to permit the Secretary of the Interior to grant import quotas to manufacturers of low sulphur residual fuel oil. The Secretary has exercised this authority in District V. On May 24, 1968 he proposed granting such quotas in Districts I-IV which would be "on top" of the 12.2% ceiling and which, he estimated, would increase to 300,000 barrels daily within several years.

3. *Foreign trade zones in the United States*

The Foreign Trade Zones Board has approved applications by two major chemical companies for the designation of foreign trade zones at Midland, Michigan and Taft, Louisiana. Applications for import licenses have been filed with the Department of the Interior, however no trade zone quotas have yet been issued by Interior. Under the foreign trade zone laws the operator of the zone may import foreign feedstock into the zone, manufacture chemicals and in turn ship chemicals into the United States. For chemicals shipped into the United States he has a choice of either, (1) paying the regular import duty on the particular chemical or, (2) paying whatever duty the feedstock would have required had the feedstock been imported. Since most feedstocks are light petroleum hydrocarbons the duty is 10.5c per barrel, therefore chemicals from a foreign trade zone pay an import duty negligible in comparison to the duty imposed upon foreign chemicals coming into the United States. The Foreign Trade Zone is clearly a device for evading practically all chemical import duty.

For the independent producer, a foreign trade zone can be looked upon as a device for permitting foreign oil to come into the United States in the form of chemicals. Foreign trade zone allocations will undoubtedly be on top of the 12.2% ceiling.

4. *Puerto Rico and the Virgin Islands*

On April 20, 1967 a public hearing was held by the Department of the Interior to receive comments relative to applications filed with Interior involving special oil import allocations for existing or planned refineries and petrochemical plants in Puerto Rico and the Virgin Islands.

In late 1967 Secretary Udall granted special allocations to Hess Oil & Chemical Company, Commonwealth and Union Carbide Corporation. Approval of the Hess and Commonwealth applications will result in 25,000 barrels per day of petroleum products moving from the islands into the East Coast of the United States effective at the start of this year. The approval of these two applications was announced as being quantities of finished products that would be within the 12.2% ceiling.

Under its approved application, Union Carbide Corporation will not be permitted to import any petroleum products into the United States, however it will be permitted to consume approximately 50,000 barrels per day of naphtha, produce chemical intermediates and ship the chemical intermediates into the United States. For the oil and gas producer the approval of the Carbide application means that 50,000 barrels per day of foreign oil will come into the United States in the form of chemical intermediates which will be on top of the 12.2% ceiling.

On April 19, 1968 the Department of the Interior announced that crude oil allocations for a Puerto Rico core facility had been granted to Sun Oil Company. By this authority Sun Oil Company will be permitted to import 60,000 barrels per day of crude oil into Puerto Rico, manufacture certain petrochemicals, finished and unfinished petroleum products and ship 29,500 barrels per day of jet fuel components, No. 2 fuel oil, and lubricating oils into the United States.

Still pending is an application by Texaco involving facilities that Texaco proposes to construct in Puerto Rico.

5. *Canada*

In recent years the quantity of exempt overland oil moving from Canada into the United States has increased dramatically.

In 1966 exempt overland Canadian oil imports into Districts I-IV were estimated by the Interior Department at 180,000 barrels per day. Actual imports exceeded 210,000 barrels daily during that year. In 1967 the estimate was increased to 225,000 barrels per day but imports actually jumped to over 250,000 barrels per day. For the first half of 1968 Interior estimated that the overland movements of crude oil from Canada into the United States would total 280,000 barrels per day, but imports have been exceeding this estimate by about 60,000 barrels daily. These overages effectively displace substantial quantities of oil that could be produced from reserves in the southwest. Future growth in Canadian shipments of oil into the United States should level off to some reasonable amount.

6. *Carryover of unused 1967 licenses*

The Middle East War of last June disrupted the normal flow of oil to world markets and resulted in a substantial decrease in the amount of licensed imports experienced during the year 1967.

The deficiency of imports into Districts I through IV during the year totaled 51,700,000 barrels or about 141,761 barrels per day for the full year.

In mid-February the Secretary of the Interior announced that half of the unused 1967 import licenses would be valid for the year 1968 and the remaining half would be valid in the year 1969. Interior further announced that one-half of the unused licenses would be within the 12.2% ceiling. This decision will result in about 36,000 barrels per day of oil being imported "above the 12.2% ceiling" for the next two years.

7. *The "import-for-export" plan*

During mid-1967 a group of nine large international chemical companies known as the "Chemco" group pushed for government approval of a plan publicized as the "Chemco" Plan that would permit unlimited shipments of foreign petroleum products (primarily naphtha) into the United States.

In addition to unrestricted access to foreign feedstocks the Chemco Plan contained a separate provision that would permit imports of foreign petrochemical feedstocks equivalent to the quantities of feedstock consumed to manufacture products that are exported.

At a press conference on December 28, Secretaries Udall and Trowbridge jointly announced that the "unlimited access" feature of the "Chemco Plan" has been rejected.

During the same press conference the two Secretaries announced their desire to adopt a new "import-for-export" plan for both the petrochemical and petroleum industries. Quotas to be assigned as a result of this plan were designated "bonus" quotas. The status of the "import-for-export" plan is still pending. Also unanswered is whether the quotas granted under such a plan would be within or on top of the 12.2% ceiling.

In my judgment, the largest single exception threatening the program is the proposal to "exempt" quotas to the petrochemical industry from the Mandatory Oil Import Program. This industry has claimed a need for access to foreign feedstocks both as a matter of competitive capability and as a matter of equity.

Neither of these claims has any basis in fact. An authoritative study by Stanford Research Institute last year indicated that adequate supplies of domestic petrochemical feedstocks are and will continue to be available in the United States at internationally competitive prices. The net petrochemical export position of the United States, the study showed, will improve—irrespective of the level of feedstock imports—from about \$1.3 billion to \$2.3 billion by 1975. Thirdly, the study indicated, changes in import quotas for petrochemical feedstocks will not measurably affect the positive trade balance for the industry.

The offshore territories provision, that allows increases in imports of crude and unfinished oils into Puerto Rico to promote expansion of employment and conservation, is likewise a major loophole in the program. Under the provision, petrochemicals made from crude and unfinished oils imported into Puerto Rico can enter the United States without restriction. Hence, the right to import petro-

chemical feedstocks into Puerto Rico is equivalent to allowing them to be imported to the United States mainland.

Concessions made in relation to these projects also allow light products to be shipped to the mainland in growing quantities. They now total 80,000 barrels daily including the special allocation given to the Virgin Islands Project. Even when they remain inside the formula ceilings, they reduce domestic refinery runs and reduce the refiner's ability to support the producing industry. In addition to the volume, new and dangerous features in the form of price and marketing restrictions have crept into these special allocations.

Foreign trade zones, for which allocations are left to administrative decision, can be used for circumventing the program and creating inequities both in the oil and petrochemical industries. There are no clearly defined rules which assure equal opportunity to everyone under their jurisdiction. These rules—if, indeed, the provision is retained at all—should be made to achieve the purpose for which foreign trade zones were intended—that of promoting foreign trade. They should not be used as a back-door way of giving preferential treatment for petroleum and petrochemical products made from imported feedstocks.

The Appeals Board actions in the case of No. 2 fuel oil are other cases in point. While the volume of imports is not great, it is cause for concern both because it is one more step away from the overriding original objective of the program and because it is unnecessary. The original controls on the import of this fuel neither created a physical shortage of heating oil nor caused unusual financial hardship. The industry can meet all the demands without relaxation of controls, as was clearly demonstrated in the last heating season.

These are some of the major exceptions granted with a profligate hand in recent years. But I want to stress that it is not only the volume of such exceptions that gives rise to concern. The flimsy base on which they have been granted, with no reference to the paramount objective of national security, is cause for even greater concern.

Nor can we derive comfort from the reflection that these exceptions are all for causes that may be worthy in themselves. The dispensers of these favors may have been well intentioned. But I would say to you, gentlemen, that the overall effect of this patchwork of exceptions is a program that rides off in all directions at once, instead of focusing on the single objective for which it is intended.

One of the most disturbing practices of Interior is its proclivity to act without notice and hearings, which are basic to our American way of Government. While it shocks me as a lawyer and a former judge, it is even more shocking to businessmen desperately trying to follow ever changing course and direction of this hodgepodge Program.

Only time prevents discussion of further aspects of the "loop-hole-itis" plaguing the administration of the Program.

III. WHERE PROGRAM IS TODAY

Where is this Program today? It's in one heck of a mess! State conservation agencies and the industry don't know from one moment to the next when a new exception or special favor will be handed out—with or without benefit of notice and hearing. State agencies and the industry need stability to maintain a viable, expanding program for developing and conserving the nation's oil and gas resources.

Severe competitive inequities have been created, and our economy operates on fair competition for all. Such inequities will destroy the Program just as would excessively increasing the overall level of imports.

All this has been brought about for the simple reason that the administrators lost sight of the purpose of the Program.

And now the Program is tottering!

IV. WHERE PROGRAM IS HEADED

So where do we go from here? Something has to give. The Program cannot continue on this trend.

The first thing that should be done is to call a moratorium. No new quotas or exceptions should be handed out. Those recently granted should be cancelled, or systematically rolled back and phased out to approximate the conditions of the program as they existed in 1965. This would have an immediately favorable effect by restoring industry confidence in the integrity and direction of the program.

The industry can, then, devote its energies to consider ways and means of strengthening the program instead of expending its efforts in combatting its deterioration.

Secondly and finally, if our industry is to remain free and healthy, it must operate within the limits of a program that provides constructive guidelines and incentives. Placing the program under statutory regulation is a solution, but I have not advocated legislation because it could introduce an undesirable degree of rigidity. In my judgment the best solution is a return to and a reinforcement of the program's original objectives and principles. This must be accomplished. If it will not or cannot be done by administrative actions, further legislative action is the only alternative.

SUMMARY

One thing is absolutely certain—the nation must have an effective oil import control program. Its purpose—national security—is as clear today as it was in the beginning. In a large way we find ourselves back at the same point in history that the nation faced in 1959. The program needs to be restored and “nailed down,” with a firm commitment to the sole purpose of the Program—national security. We have the nails, the shoes, the horses and if we work together this nation will not be lost for want of a horse.

The CHAIRMAN. Thank you.

Mr. Matsunaga, we appreciate having you with us and we are sorry to have held you so long.

You are recognized.

STATEMENT OF HON. SPARK M. MATSUNAGA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF HAWAII

Mr. MATSUNAGA. Thank you, Mr. Chairman.

I appreciate this opportunity to appear before your committee. Mr. Chairman and members of the committee, I appear before you to express myself with respect to a bill which I have introduced and which has been referred to this committee, H.R. 12437, to exempt the State of Hawaii from the mandatory oil import program.

Mr. Stark Fox stated a few minutes ago that the program was designed for the security of all 50 States. We agree that it was so intended. It was for this reason that Hawaii raised no objections when the program was first instituted. However, the experience of the past 9 years has proven that Hawaii ought to be exempted—that it was a mistake to include Hawaii in the program, in the first place.

Congress has in many instances recognized the unique situation of Hawaii. Only recently, Mr. Chairman and members of the committee, you will recall that the House passed a bill exempting Hawaii from the strict requirements of the Farmers Home Administration Act, which restricted loans to owners or prospective owners of land, and allowed loans to leasehold owners of land in Hawaii only.

There are many other instances where Hawaii, because of its insularity, its uniqueness in its geography, and its uniqueness in its heritage, has been recognized by the Congress to be deserving of exemption from general laws otherwise applicable to all 50 States.

I was somewhat amazed by the statement of Mr. Fox that had it not been for this program, Hawaii would not be the westernmost bastion of the United States but the easternmost bastion of Japan.

I will remind the gentleman that the mandatory oil import program came into existence with the issuance of Presidential Proclamation No. 3279 on March 10, 1959, long after the end of the war with Japan.

Hawaii, then a territory, was classified, for the purposes of the proclamation, in district V, along with the States of Arizona, Nevada, California, Oregon, Washington, and Alaska.

The proclamation disclosed the underlying effort to foster overland sources of oil supply in order to promote our national security. Indeed, within the limits of the continental United States, national security would definitely be strengthened by users purchasing domestic oil.

However, our national security is recognized as a much broader concept than simple self-sufficiency, and the present administration has stated that "to an important degree it is identified with a strong, prosperous, free world economy which is in turn dependent upon a large and expanding trade."

Assistant Interior Secretary J. Cordell Moore, in testifying earlier this year on this subject before the Subcommittee on Mines and Mining of the House Committee on Interior and Insular Affairs, went on to say, and I quote:

Our oil import policy has therefore evolved as a balance between the need for security of our oil supply and the need to accommodate other Free World nations who value our trade and who in turn are our good customers as well * * * The result is that the largest part of our domestic petroleum market is reserved for domestic producers and refiners, but a substantial trade is permitted with friendly nations who have oil to sell.

With Presidential Proclamation 3279 based on such worthy aims, Hawaii, separated from the west coast by some 2,300 miles of international waters, has posed something of a dilemma.

It is clear that even in our present day of technological advancement we cannot have oil delivered to Hawaii from the west coast by pipeline. It is equally clear that because Hawaii is absolutely without any indigenous sources of fuel, the program's objective of having users rely on domestic oil is virtually meaningless.

Hawaii must import all of its fuel requirements. In the event of any national emergency, tankers approaching Hawaii from the east with oil from the mainland United States would be equally vulnerable to enemy submarine attack as tankers approaching from the west carrying foreign oil.

Under these circumstances, the conclusion is inescapable that Hawaii was assigned to district V in the mandatory oil import program without a careful study of its unique insularity and without regard for its incongruity in district V.

It appears that somebody felt that Hawaii ought to be placed in one of the five established districts and just stuck the Islands into district V, regardless of consequences.

This conclusion is strengthened by a review of the sources which supply Hawaii's crude oil requirements under the mandatory oil import program. In 1967, a total of 12.5 million barrels of crude oil was shipped into the State, and 97 percent of the crude oil which was refined in the sole refinery in Hawaii was shipped in directly from Saudi Arabia, Iran, and Indonesia. Only 3 percent came from domestic sources.

Hawaii is situated between these foreign sources of crude oil and the west coast of the continental United States. Theoretically, therefore, Hawaii ought to enjoy a price advantage over the west coast. Actually, however, Hawaii pays higher prices.

How is this inconsistency explained by the oil-importing interests? A vice president of the west coast oil company which owns the Hawaiian refinery, in testifying on this subject before the Fourth Legislature of the State of Hawaii on March 25, 1968, explained as follows, and I quote:

Foreign crude * * * oil can be imported only by the use of quota generated * * * elsewhere in District V or by the use of quota acquired * * * from other refiners in the District. A premium must be paid to acquire this quota. When this premium is taken into account, the total cost of such foreign crude brought into Hawaii is equivalent to the cost of domestic oil. In short, 96% of the crude oil we refine in Hawaii costs us the equivalent of California crude, even though it is of foreign origin.

The witness left unanswered the crucial question: Why, if the cost to his company of foreign crude oil is "the equivalent of California," is the 96 percent foreign crude oil refined in Hawaii not being replaced by domestic crude to further the aims of the mandatory oil import program?

The answer is readily apparent from a comparison of so-called poster prices for crude oil which are available at the Department of the Interior. For example, 34 gravity crude oil at Signal Hill, Calif., recently showed a posted price of \$3.17 per barrel, as compared with the posted price of \$1.80 at an Arabian Gulf source.

The price differential between foreign and domestic crude oil is widened by such factors as the lower rates charged by foreign tankers carrying foreign oil and the extensive practice of discounting followed by foreign oil producers and foreign shipowners which inures to the benefit of purchasers of foreign crude oil.

Under the actual operation of oil import controls, therefore, virtually all crude and unfinished oil consumed in Hawaii is imported from foreign sources in any event, and the oil import controls have not encouraged the suppliers of Hawaii's fuel requirements to use U.S.-produced oil, as it had been hoped under the 1959 Presidential proclamation.

Moreover, the controls have merely tended to raise the cost of energy on the local market to excessively high levels so that Hawaii's energy costs to the consumer are among the highest in the Nation.

Hawaii offers no opposition to the oil import program as such. It only seeks to be relieved of an unintended inequity imposed upon it by natural circumstances beyond its control. It seeks equity within the stated purpose of the oil import program to insure a healthy domestic oil industry for reasons of national security.

If Hawaii is to play a vital part in the program, because of its unique geographic position it ought to be considered for a special role. In the future, as this Nation continues and deepens its involvement in the Pacific, and as the need for petroleum, fertilizers, plastics, and the host of other oil derivatives needed by developing countries grows, it will be increasingly beneficial to this Nation, both logistically and for our balance of payments, to develop an international oil center in the Island State.

But this manifestly is not possible so long as Hawaii continues to be restricted by district V quotas. As my bill provides, the exemption of Hawaii from these crippling and inequitable restrictions is a necessary first step.

This committee is in a position to provide valuable assistance in enabling Hawaii to take that necessary first step successfully.

I earnestly urge that H.R. 12437 be given favorable consideration by this committee.

Thank you very much.

The CHAIRMAN. Mr. Matsunaga, we thank you, sir, for bringing to the committee your statement. You have well represented your own State as usual.

Are there any questions?

Thank you, sir.

We will ask Mr. McClure and your group to return to the witness stand.

STATEMENT OF HAROLD M. MCCLURE, JR., ET AL.—Resumed

The CHAIRMAN. All right, Mr. Bush.

Mr. BUSH. While Mr. Matsunaga is here I was going to ask a question of the IPAA.

On the problem of Hawaii, isn't it the position of the witnesses at the table that Hawaii is part of the United States. That this national program is one that encompasses all the States, and that it is done because it is readily apparent, to me at least, that in the light of the last two Suez crises that no State within the 50 United States can have its cake and eat it, too?

It is part of an overall national policy which says that we must have these restrictions if we are going to keep a strong domestic industry, not to protect an inefficient industry. But do protect our defense capabilities.

I would like Mr. McClure to confirm or deny that the problem that Hawaii has, though unique, is somewhat similar to the problem of fuel oil in New England—in that this is a national policy and there could be some price differentials. There could be some inequities if you had totally free trade. But that the history of this country has demonstrated rather clearly that we can't in the sensitive area of basic minerals have free trade. The mechanics of the oil industry are such that you just can't turn that valve and hope to produce and hope to develop the reserves necessary.

So, isn't the problem Hawaii faces one of saying, "Look, you do have a price problem and, sure, you could get it from the tankers of Arabian Oil, the Japanese company producing in the Middle East." But aren't they being asked, through this program, to make some sacrifice because of the benefits they get in protection that comes from a strong domestic industry?

Is that a fair appraisal, Mr. McClure, of the Hawaiian situation?

Mr. MCCLURE. Congressman Bush, in that connection we are 50 States and 50 great States. There is a responsibility of the total United States to see that each and every segment thereof is properly and adequately protected.

I think that the Congressman from Hawaii made a very excellent presentation of their case, but there are several things that I don't believe he has taken into consideration.

The reason that he can reach out and make a statement that petroleum is available to them at a somewhat lesser figure, and we will dis-

agree on the spread which he gave to you, but that is irrelevant, the reason is that there is a secondary source which can supply Hawaii in a time of an emergency.

I think he should look to the concern, the deep concern that the Japanese are experiencing today on what might happen to them if their sources are cut off in the Middle East and they are looking to North American reserves, produced in Canada and Alaska, to protect them from this very problem.

It is something to be concerned about. The problem is one that totally you need to take the whole United States into consideration.

This is just as true in the area of Puerto Rico, the possessions. Our responsibility as a nation is to protect, and that is the reason for this problem.

Mr. BUSH. Mr. Chairman, if it is appropriate, I would certainly like Mr. Matsunaga to respond. I would identify myself with the remarks of the chairman, that he had an excellent statement and certainly one that, if it could, in the national interest, be effected, would undoubtedly be beneficial to this constituency, and this I certainly respect. I only ask the gentleman that he put this in the context of the whole national defense policy. If he would like to respond, sir, I think it would be appropriate to have it on the record.

The CHAIRMAN. All right, Mr. Matsunaga.

Mr. MATSUNAGA. Mr. Chairman, if I may reply to the gentleman, we have no intention in any way to subvert any program which is for the national security and which would serve the national interest over and above the interest of my constituents, but what we are trying to point out here, Mr. Chairman and members of the committee, is that the program has not served its purpose where Hawaii is concerned.

Ever since its institution in 1959 the record shows that no less than 90 percent of all the oil imported into Hawaii came from foreign sources and not from domestic sources, and that whether it be from foreign sources, whether it be from domestic sources, all oil imported into Hawaii must be shipped out there by surface vessels, and if the oil companies had used the application of the law to Hawaii as an instance to develop the domestic industry, well and good; but this is not so.

It has not served to enhance the purpose of the oil import program one iota, and we have suffered under it for 9 years now by paying higher prices, and we are not so much complaining about higher prices. We would be willing to pay the higher prices if by paying the higher prices we will be serving the national interest, but we are not. This is what we are trying to say.

And we will be made to suffer, as a sister State of the 49 other States, an inequity wholly unintended by the program. In a democracy such as ours, I am sure we don't intend to say that, because Hawaii is a State within the Union of States, it must suffer even though the 49 other States do not suffer under a given law.

We in Hawaii suffer in other ways, but we don't complain. For example, in World War II and the Korean war and in Vietnam, Hawaii has suffered the greatest rate of casualties of all States in the Union. We have not complained, and I believe I can safely state that at least 80 percent of the people of Hawaii still support our efforts in Vietnam.

We are seeking equity, equity in the form of relief from the burdens of a program which as made applicable to Hawaii serves neither the national interest nor the security of our country. So I ask that you consider the matter from the point of fairness, of plain justice.

We have been to the administration on this, and have met with frustrating procrastination. I was asked to withhold the introduction of my bill, because something would be done. This was 3 years ago. Last year the Department of the Interior indicated something would be done. This year again they said they would do something by March of this year. It has never been done.

So I come to you, my colleagues, to do something to eliminate an injustice which is being imposed upon one of our 50 States.

The CHAIRMAN. Mr. Bush, would you yield to me?

Mr. BUSH. Yes.

The CHAIRMAN. Mr. Matsunaga, I followed your statement with a great deal of interest. What is the reason for the differential in price in your country since you do have more than 90 percent of your oil coming from sources outside the United States?

Perhaps a tanker leaves oil in your State on its way to the mainland, to California.

Mr. MATSUNAGA. That is correct.

The CHAIRMAN. Why is it so much more to the consumer in your State than it would be in the State of California, for example?

Mr. MATSUNAGA. Because of this arbitrary mandatory oil import program and we are placed within district V.

The CHAIRMAN. What part of it is what I am getting at. Why does it operate that way?

Mr. MATSUNAGA. Well, we are required under this program to purchase from domestic producers.

The CHAIRMAN. Who are importing from foreign sources?

Mr. MATSUNAGA. That is correct.

The CHAIRMAN. And those from whom you purchase it do not have the quota themselves. Do they have to go out and buy it from someone else?

Mr. MATSUNAGA. This is the claim they make. They go to foreign sources. They go to Indonesia, for example, and bring the crude oil in tankers and drop it off in Hawaii for Hawaii's consumption, and yet we are charged the freight from the west coast to Hawaii.

The CHAIRMAN. You operate within a total quota for all the 50 States. I am trying to ascertain whether there is a reason which could be corrected within the quota system, that causes you now to have to pay more for your fuel than is the case in the State of California, and I only use that as an example.

Mr. MATSUNAGA. Well, so long as we are within district V of the quota system, it appears that we will continue to pay the domestic prices as posted in California, the west coast.

The CHAIRMAN. That would be the same price, would it not, as that which is paid by the user in California? I understood you to say that you pay more as users in Hawaii.

Mr. MATSUNAGA. Yes, we do, because of the transportation and other costs which are tacked on to the California price.

The CHAIRMAN. But if 90 percent or more of your oil is coming from foreign sources, it must be brought past your State apparently to get

to the mainland or am I wrong? Is it brought to California from some other way and then out 2,300 miles to Hawaii?

Mr. MATSUNAGA. This is the thing that puzzles us, Mr. Chairman, that they bring in the oil from the East directly to us in Hawaii, without first taking it to the mainland.

The CHAIRMAN. Right by you?

Mr. MATSUNAGA. Yes, right by us, drop off the oil and yet charge us more for the oil.

The CHAIRMAN. There is no justification for that because it is 2,300 miles nearer to you than it is to the mainland.

Mr. MATSUNAGA. That is it exactly. Frankly speaking, Mr. Chairman, somebody is making a lot of money at the expense of the people of Hawaii.

Mr. BUSH. Mr. Chairman.

What is the price for a gallon of gasoline on the average?

Mr. MATSUNAGA. About 10 cents per gallon higher in Hawaii than the west coast.

Mr. BATTIN. What is it?

Mr. MATSUNAGA. About 48 cents per gallon.

The CHAIRMAN. Pardon me just a second.

Do I understand that most of the fuel that you use either in the form of gasoline or otherwise in Hawaii is refined within Hawaii?

Mr. MATSUNAGA. Yes, right now, at this one oil refinery that was established several years ago.

The CHAIRMAN. And this refinery contends that it does not have a quota to bring oil into the United States and therefore must buy it from somebody else, is that the point?

Mr. MATSUNAGA. That is the statement which I read from the vice president of the oil company.

The CHAIRMAN. What is the company's name?

Mr. MATSUNAGA. The Standard Oil Co. that Mr. Fox represents.

Mr. Fox. I beg your pardon. I would like to correct that for the record. I have no connection whatever with the Standard Oil Co.

Mr. MATSUNAGA. I am sorry.

The CHAIRMAN. Who does?

Mr. MATSUNAGA. It is the Standard Oil Co. of California, Mr. Chairman. I thought Mr. Fox did. I am sorry.

The CHAIRMAN. What I am getting at is whether or not you would have any better price under the existing circumstances if you were out from under the quota?

Mr. MATSUNAGA. If we were exempted from the quota? Yes.

The CHAIRMAN. How were you going to get your oil then?

Mr. MATSUNAGA. Then we could import the oil directly from foreign sources, free of this quota system.

The CHAIRMAN. You can import it now from anybody who has a quota to ship to the United States.

Mr. MATSUNAGA. But the importers are also the domestic oil producers.

The CHAIRMAN. I understand, but you are only dealing with one of them.

Mr. MATSUNAGA. They have a monopoly because they run the only refinery there.

The CHAIRMAN. Why is that the case? Have you given them a monopoly under any State law or provision of law?

Mr. MATSUNAGA. It is merely by the law of economics, Mr. Chairman, because Hawaii, after all, is a State of only 785,000 people.

The CHAIRMAN. And the Governor and the rest of you need to stir up a little competition, it sounds to me, because if you are going to have a monopoly, even if you were outside the quota, I don't know whether your price would be different.

Mr. MATSUNAGA. Whether Hawaii can sustain more than one oil refinery is the question.

The CHAIRMAN. That doesn't make a difference to the oil companies. I have seen them put filling stations on all four sides where the streets cross, when the man who went there said he was barely making a living to begin with. I don't think that would stop the oil companies. They like competition.

Mr. MATSUNAGA. We would like to see competition, Mr. Chairman, and have been inviting companies to come in to provide that competition.

The CHAIRMAN. I think that is your real answer.

Mr. MATSUNAGA. That is true, but you know what is happening, Mr. Chairman, is that the competing oil stations with different labels buy from the same refinery.

Mr. UTT. They do that in California.

The CHAIRMAN. You get you another refinery in Hawaii, and I think you will improve your situation.

Mr. MATSUNAGA. I think if you remove us from the quota, this will be the fastest way.

The CHAIRMAN. You were not able to get one from the United States. Are you going to get a foreign producer to come in with a refinery?

Mr. MATSUNAGA. If we are exempted from the quota system, even the present domestic producers could bring the oil in outside of the quota, without having to pay any premium.

The CHAIRMAN. You get ahold of Texaco or Shell or Gulf or some of these companies.

Mr. MATSUNAGA. Mr. Chairman, taking Hawaii out of district V would be the fastest way. This is why I am appealing to your committee, Mr. Chairman. We have studied this for years, Mr. Chairman, and I ask that you give serious consideration to this request.

The CHAIRMAN. I will try to be helpful to you because I think there is a way to do it without taking a step of exempting one State out of the 50 from a national quota. Now, if there are going to be quotas, it has always been my thought that they have to be uniformly applied to all 50 States. That is just a thought I have had. Maybe I am wrong.

Mr. MATSUNAGA. Mr. Chairman, there is only one State 2,300 miles in the middle of the Pacific Ocean. This uniqueness, this insularity must be taken into consideration, Mr. Chairman. This is what we are trying to say. I wish that the committee will not blind itself as the Department of the Interior has to this fact.

The CHAIRMAN. The U.S. quota, at least the quota for the other 49 States, would have to be reduced by the amount of the total quota

that is utilized by Hawaii or else that which you have now in your quota would just be added to the quota of the other 49 States.

Mr. MATSUNAGA. Hawaii has less than 2 percent of the whole quota.

The CHAIRMAN. It wouldn't make a lot of difference, but I would think that, if we did what you are suggesting, then the total of the quota would have to be reduced or else the net effect would merely be to increase the quota for the other 49 States.

I am hopeful that there is some way that we could work with you because we are interested in all of our States, in the progress of all of our States, and the peoples of all of them. I wish there were some way to work with you to correct the apparent monopoly.

Mr. MATSUNAGA. Mr. Chairman, I would say that if any of the other States would suffer as a consequence, that is a matter to consider, but I don't think any of the other States will suffer because of the minuteness of the quota assigned to Hawaii.

The CHAIRMAN. My concern is primarily based, of course, upon whether or not we have the constitutional authority to really exempt a State from a rule that is conceived to apply nationwide.

I am not a constitutional lawyer but uniformity was one of the things that I always learned was necessary with respect to the Constitution.

Mr. MATSUNAGA. Well, Mr. Chairman, as I said earlier, we have studied this question for many years very seriously and the question of constitutionality—

The CHAIRMAN. Was never raised.

Mr. MATSUNAGA. Was not raised.

The CHAIRMAN. It may not be a point. My questions are not to be argumentative, but merely to get information because I would like to be helpful to my colleague. I want to again thank you for what I think was a very impressive statement of your views, very well delivered.

Mr. MATSUNAGA. Thank you.

The CHAIRMAN. I say again that you always have done a good job in representing the viewpoint of your constituency as some of us know so well.

Mr. Bush.

Mr. BUSH. Mr. Chairman, that is all I have. I would certainly agree and I would think there would be some way to do it.

In conclusion of this colloquy I would like to say that I don't think it is fair that Hawaii be exempted so that they could reap the benefits in time of distress from the national defense posture but then be exempt so that they could enjoy the fruits of the low-priced Middle East crude. I couldn't sit here for a minute and defend on a free-trade basis the pure economics because I know what the size of the reserves are and what the production costs are. That is the only point I would like to make.

Mr. MATSUNAGA. I would like to point out to the gentleman that the quota system was not in effect during the emergency.

Mr. BUSH. In which emergency?

Mr. MATSUNAGA. World War II when Hawaii was hit.

Mr. BUSH. I am talking about the two Suez crises when not only our country had to respond to an increase in demand; but I was over in Scotland when this first Suez crisis hit, and all of our strongest allies

were giving us tremendous criticism because the Texas Railroad Commission wouldn't open the valve and wouldn't flood the country with domestic production in order to save their hides. So I would simply urge on the gentleman the concern that some of us have about the national defense posture in it.

I am sympathetic to the pure economic problem which you have, and I would like to help supply an answer to it.

Mr. MATSUNAGA. I assure the gentleman that we have no intentions of subverting the national defense posture, and we are saying that this in no way will detract from our defense program.

Mr. BUSH. I would like to visit with the gentleman privately and maybe we can come up with something.

Mr. MATSUNAGA. Thank you very much, I would be happy to.

Mr. BUSH. Mr. Chairman, I have one or two other questions.

The CHAIRMAN. Mr. Bush.

Mr. BUSH. Mr. McClure, as I understand the main thrust of your testimony, is it correct that your main concern with the program is the exemptions recently entered into by the Secretary on this low-sulphur residual? Is that the main worry that you have at this minute?

Mr. McCLURE. Exception is the key word in our testimony. In other words, we have said and sincerely believe that the mandatory oil import program as it was conceived and implemented is a fine program, it serves the Nation well. We have raised considerable question about the exemptions, Congressman Bush, and one of the exemptions you just mentioned has not been implemented by the Secretary, but let me just speak to that point.

The Secretary has in mind the granting of import tickets to import crude oil into the United States over and above the 12.2 ratio, saying that by granting these tickets he will cause low-sulphur residual fuel oil to be burned in such areas as Boston, New York, and the east coast for the specific purpose of reducing air pollution.

We fervently aspire and adhere to the philosophy that we as a nation must improve our quality of air, and we as an industry will and should do everything within our power to see that this takes place.

But when laws exist on the books of the city of New York, Boston, other places in New Jersey, that require that sulphur fuel of a particular percentage of sulphur be burned, there is no rhyme or reason, in our judgment, for awarding a bonus to a company for adhering to that law.

It would be just as much of a rationale to expect that in Illinois, in Chicago, the constituents of Congressman Collier would be reimbursed \$50 for not speeding on the freeway, you see.

So this is what we are objecting to, the excuses that are being given for these exemptions when there is no validity in them and this low-sulphur fuel which is under consideration by the Secretary is just one of a multitude.

Another exception that has been granted is the Puerto Rican situation. This is a highly critical exemption process and certainly should not have been allowed by the Secretary.

In other words, put it this way, administrative rules and regulations and the law should be administered without fear or favor, but we do have these exceptions coming in and experiencing this type of favor

on either a company aggrandizement basis or a local area aggrandizement basis.

Mr. BUSH. One of the references in one of the papers was to—I believe the word was—threats. I recall a couple of years ago I think it was where the Secretary, at least it was my impression, used the concept of increasing oil imports under his voluntary program in order to do something about domestic pricing.

Is that a realistic recollection on my part and, if so, has it happened again?

Mr. McCCLURE. Congressman, you do recollect correctly. There have been definite instances, and one was a case in point where gasoline was moved from Puerto Rico to the west coast in the amount of 10,000 barrels a day and it was granted primarily on the basis of the Secretary using this to hopefully influence prices on the west coast.

Mr. BUSH. That hasn't happened again, has it?

Mr. McCCLURE. They withdrew the 10,000 barrels from the west coast upon substantial complaints and then took the same 10,000 barrels a day and brought it into the east coast. It is this type of thing that is very distressing.

Mr. BUSH. I have two very brief questions.

You had a graph showing the decline in the number of rotary drilling rigs. This would mainly be small business, would it not, in terms of the way we think of large business?

Aren't mainly the rotary drilling rigs owned by independent operators so that we are talking about a loss of small business in this country?

Mr. McCCLURE. The answer is yes to your question. Most of the contractors who operate rigs of this nature operate one, two, three, a maximum of five or six. There are several what we might call contractorwise slightly larger companies, but they are all in the small business category within the United States.

Mr. BUSH. I have one last question and that is related to the production in Pennsylvania.

One of the arguments you hear by people in the Congress is what we ought to do is shut in our existing production, use foreign crude; then if we get into a bind we can open the tap on our domestic production. We have saved all the reserves therefore and we have availed ourselves of lower prices because of the foreign crude.

Now, as a dramatic way of refuting this, is it appropriate to suggest that, if you shut in those wells in Pennsylvania, you just wouldn't get them back on except for tremendous expense and work or whatever is required to go back in those retired wells and get them producing again? Isn't that a fallacious argument?

Mr. McCCLURE. Congressman Bush, I have been on a lot of those type of wells that you speak of. Mr. Jones is our expert from Pennsylvania who will respond to it. It isn't a case of going back and opening them up again. These wells, once they are shut down, are abandoned and forgotten. I had occasion to be in Pennsylvania recently. Some new techniques presently being applied to the Pennsylvania production indicate they may have a possibility of recovering as much as an additional 25 percent of the reservoir reserves that are in this Pennsylvania area.

Had these wells been abandoned, or where leases have been prematurely abandoned, the expense of going back and redrilling and placing these on production is sufficiently onerous that the job isn't done and the oil is permanently left there.

I was raised under a stewardship concept that these resources are great God-given resources and that we do have responsibility to steward them, and to leave any amount of this reserve in the ground wantonly is just as bad as wasting it on the surface.

So that these wells don't remain in existence. It is almost like taking an ice cream cone on a hot summer day and walking 2 miles in the sunshine. When you get home, the ice cream is gone. It has melted in your hand if you haven't eaten it on the way home. This is what happened to the oil. It will be a rare occasion that they will go back in and redrill these reservoirs at excessive cost to get the oil.

Those who espouse it are the theoretical economists, and we don't think their concept is valid.

Mr. BUSH. Do you witnesses at the table all take the position on the exemption of this in-and-out oil from down in Brownsville, Tex.—this stuff where you can put it in bond, run it across the bridge, and bring it in? Are you unified in your position on that?

Mr. McCLURE. We have taken a position on that, and it is an exception, and we don't feel that those types of gimmicks that are developed for the specific purpose of evasion or avoidance of the mandatory import quota are in the best interests of the Nation, and our only purpose in testifying here today is not a question of whether our company or any company continues to exist, but whether this Nation has a strong base of petroleum resources.

Mr. BUSH. Thank you, Mr. Chairman.

Mr. WATTS (presiding). Are there any further questions?

I want to ask one. I got here a little bit late. I am assuming you are not appearing here to do away with the import quota. You like that, but you don't like the exemptions to it.

Mr. McCLURE. As it is administered. This is our problem; yes, sir.

Mr. WATTS. But it would take legislation then to prescribe certain conditions under which exemptions could be granted. It is wide open now, isn't it? It must be, if your testimony is that they make exceptions every now and then.

Mr. McCLURE. The proclamations that have been signed by the President have given the Secretary of the Interior very, very broad powers under the mandatory oil import program, and we feel that the Secretary has not used good discretion in administering those proclamations which have been handed to him or in searching out some of those proclamations from the President.

Mr. WATTS. There is no way that this committee or Congress can deal with demand for discretion except eliminate it.

Mr. McCLURE. That is correct. We feel that we would like to receive from the Congress of the United States some direction in this regard.

Mr. WATTS. Have you proposed any directions?

Mr. McCLURE. We have indeed, sir. There are 46 bills now before the Congress that cover this particular item. There is also a Senate bill which we feel will give the kind of direction that is necessary for the industry to go ahead and do its job in the next decade.

Mr. WATTS. Does that go in the direction of directing the Secretary under what conditions he can grant exemptions, or does it do away with exemptions entirely?

Mr. McCLURE. It pretty well pins where this thing needs to be, sir.

Mr. WATTS. What?

Mr. McCLURE. It puts the 12.2-percent limitation on imports from outside the United States in context.

Mr. WATTS. Without any exemptions?

Mr. McCLURE. Within the 12.2 he would still have some very great latitude and discretion. Also within the provisions of that legislation is that anytime this Nation is in peril or in a defense posture the President of the United States retains the ability to do whatever this Nation has to do to keep itself up.

Mr. WATTS. Are they now importing 12.2 or more?

Mr. McCLURE. They are importing an amount greater than 12.2, and today it exceeds that figure by over a quarter of a million barrels a day.

Mr. WATTS. That is due to the exemptions?

Mr. McCLURE. That is correct, and the exemptions are fast eroding all of the basics underneath it. In other words, you can see here by the chart, the oil imports in districts I through IV, the lower portion, the dark portion indicates that amount which is allocable under the normal import program.

The red indicates the exceptions under the program and, as you can see, the growth of these exceptions is not only going above the 12.2 No. 1, but, No. 2, projected to 1972 the program, will be nothing but exceptions.

Mr. WATTS. In other words, to use an old country phrase, the tail has got to wagging the dog?

Mr. McCLURE. It is about this. When Uncle John runs the candy store and tells Jimmy to come by after school and he can have a candy bar, he doesn't understand why 20 kids are standing outside the door next afternoon, but Jimmy told them.

Mr. WATTS. Thank you.

Are there any further questions?

If not, the committee will adjourn until 2 o'clock this afternoon.

Mr. McCLURE. Thank you so much, Mr. Chairman.

(Whereupon, at 12:25 p.m., the committee recessed, to reconvene at 2 p.m., the same day.)

AFTER RECESS

(The committee reconvened at 2 p.m., Hon. Al Ullman, presiding.)

Mr. ULLMAN. The committee will come to order.

Mr. De Blois, we are happy to have you before the committee. Please identify yourself for the record and proceed as you see fit.

STATEMENT OF ROBERT De BLOIS, NEW ENGLAND FUEL INSTITUTE

Mr. DE BLOIS. Mr. Chairman and gentlemen, I am Robert De Blois, an independent businessman from the State of Rhode Island, today representing the New England Fuel Institute. The New England

Fuel Institute is a nonprofit corporation incorporated under the laws of the State of Massachusetts, is an association with 1,143 retail fuel oil distributors as members.

The institute's members distribute at retail 72 percent of the No. 2 fuel oil in New England. No. 2 fuel oil is the prime source of heating energy in the six-State region. Over 8¼ million people of New England's approximately 10 million population are heated throughout the cold rigorous winters, by No. 2 fuel oil. Eighty percent of New England's homes utilize this fuel for central heating.

Over 4 billion gallons of No. 2 fuel oil are consumed annually. Thus a 1-cent-a-gallon price increase represents an additional \$40 million in cost to the consumers of the region.

An adequate supply of reasonably priced No. 2 fuel oil is therefore vital to the health and comfort of more than 8 million consumers. Nothing demonstrates with more emphasis the need for an ample and consistent supply than these figures.

Unfortunately, an ample supply has not been the case. During the past two winters, deepwater terminal operators, both independent and major oil company operated, have been without No. 2 fuel oil on numerous occasions. Recently the Oil Import Appeals Board, in an unprecedented action, acknowledged the severity of the supply crises by granting 12 emergency interim import allocations for No. 2 fuel oil.

The escalation of No. 2 fuel oil prices during the past 4 years is further eloquent testimony to the unsatisfactory price-supply situation which has developed for this essential product. For example, wholesale prices have over the past 4 years increased 28.5 percent. The retail price over the same period increased only 12.5 percent. Thus during this period, New England's retail fuel oil distributors, pressed by competitive fuel energies and competing freely with each other passed on less than one-half of the percentage cost increase for their product to the consuming public. However, this unhealthy situation and trend for retail fuel oil distributors must not be allowed to continue.

The oil import control program, as presently constituted, aggravates this economically unhealthy situation by artificially creating higher prices for domestic crude oil. In addition, domestic refiners now have new refinery techniques which enable them to extract higher percentage yields of higher-priced products, such as jet fuel and gasoline. This further contributes to the short supply of No. 2 fuel oil.

The New England Fuel Institute is definitely opposed to any proposals seeking to legislate or otherwise permanently restrict the liberalization of the oil imports program and feels strongly that any such action would introduce an extremely undesirable element of rigidity into a program that must be more, rather than less, flexible. Such flexibility is required to serve the Nation's constantly growing and changing energy needs. In fact, any such legislation would place the Nation in an energy straitjacket which would result in higher petroleum product prices for the consumer.

Therefore, in face of the recurring supply crises and a rising No. 2 fuel oil price, the New England Fuel Institute through unanimous vote of its board of directors wishes to go on record as follows:

In order to protect the New England consumer from dislocations of distillate supply, as happened with other fuels in New England during the winter of 1967-68:

And to provide for the interests of national security;

And to further provide the consumer on the east coast with a continuing ample supply of low cost distillate fuel oil, the New England Fuel Institute strongly recommends positive action as follows:

1. Import quotas on distillate No. 2 fuel oil to be relaxed immediately so that allocations of more distillate oil can be made available to all independent terminal operators on the east coast, such allocations to be based equitably on the historical terminal input of calendar year 1967.

2. If necessary or required, a supplemental allocation of crude oil be made available through a similar relaxation of import quotas.

Mr. Chairman, and gentlemen, thank you very much for listening to me. If you have any questions I will be more than glad to try to answer them.

Mr. ULLMAN. Are there any questions of Mr. De Blois? Mr. Burke.

Mr. BURKE. Mr. De Blois, I wish to commend you for your statement. You very clearly outlined the problem which faces us in New England.

Mr. DE BLOIS. That is correct.

Mr. BURKE. And this morning one of the witnesses testified that oil prices have risen much less than overall prices in the past few years. Would you care to comment on this insofar as it relates to New England?

Mr. DE BLOIS. I actually would not be in a position, Congressman, to determine how much other prices have risen. I do know that the competitive situation in the New England market has definitely been one of the factors in a least maintaining a reasonable ceiling on retail fuel oil prices.

The situation, however, as can be seen from the figures that were quoted, a raise of 28.5 percent since May 1 of 1964 in wholesale prices, and a much smaller, approximately 12 to 13 percent raise, in retail prices, puts the retail distributor in a very unhealthy situation at a time when all other costs are rising.

In addition to this, the retail price cannot help, if this situation continues, but continue to escalate at a much faster pace. We are basically now being put into a squeeze. Labor prices, truck prices, everything else is in the process of rising quite rapidly.

Our wholesale costs, on the other hand, are rising and the consumer from this point forward is going to have to take the brunt of this.

Mr. BURKE. I know the dealers have found a great deal of increases being passed on to them by the wholesalers. We met with the people back in April who were discussing the problems that they were facing.

Do you know the relationship between imports of a No. 2 oil and domestic output? What has been the trend in these stocks?

Mr. DE BLOIS. I don't know what the particular trend has been. I do know that they are infinitesimally small insofar as the overall picture is concerned. Emergency allocations were obtained last, well, winter

actually to meet a crisis that was going to occur in March had these not been granted and even with these you have to realize that from the time they were granted until the time oil can be found and transported there is a timelag.

As a consequence, even with these, several terminals this past winter ran out of No. 2 fuel oil at a time that was most inopportune from the standpoint of the dealers. You have to remember, Congressman, that 50 percent of the product that we sell during a calendar year is sold or delivered to our customers in a 3-month period, basically, December, January, and February.

As a consequence to talk about stocks at this particular time of the year is almost inconsequential. We would expect that there would be a sufficient amount of product at this particular time. A reserve, however, does have to be built up to carry us through those periods of extremely cold weather that I am sure you are cognizant we get in Massachusetts, Rhode Island and the other New England States so that we can work against this reserve.

We saw in the natural gas shortage this past winter what happens in New England if a product runs out for just a short period of time. They became chaotic in the Portland, Maine, area, and the northern New Hampshire area and you have to remember that if this ever happened with No. 2 fuel oil it would be not dealing with perhaps 2 or 3 percent of the population such as natural gas services in that particular area; it would be dealing with roughly 80 to 85 percent of the population and it would be frankly chaotic.

Mr. BURKE. Thank you. In your opinion what do you think would happen to the prices of oil if the imports were reduced?

Mr. DE BLOIS. If the imports were reduced I would say the same basic thing that has happened already when supply has become tight, exceedingly tight as it is now.

It cannot help. We operate basically on a supply-demand situation. The price would invariably go up, Congressman.

Mr. BURKE. Thank you very much. That is all, Mr. Chairman.

Mr. ULLMAN. Mr. Schneebeli.

Mr. SCHNEEBELI. Mr. De Blois, I am sympathetic to your problem. I have been a petroleum distributor for 30 years. I would observe that the retail price increase that you note here, which is considerably less than the wholesale price increase, is inevitable because if you pass on let's say a 2-cent-per-gallon price increase from 10 to 12 cents wholesale that is a 20-percent increase, but if you increase the retail price from 14 to 16 cents it is only a 14 percent increase, so you are dealing from different levels.

Your lesser price percentage increase at retail is due to your higher level, so I want to straighten this out, that passing on this price increase which normally distributors do, and I would observe in my own case that I think my margins are as great as they were. As a matter of fact, from the point of view of dollars and cents I think my margin is a little bit better than it was 10 or 15 years ago.

Mr. DE BLOIS. Ten or 15 years ago you are correct.

Mr. SCHNEEBELI. Or even in the last 2 or 3 years it has remained rather constant. I think perhaps my margin has been a little better

than it was 2 or 3 years ago and I am in north central Pennsylvania and I am dealing with a major company.

Mr. DE BLOIS. I cannot answer from the standpoint of Pennsylvania. I do know in the Rhode Island market as concerns our own company, and here again I have to take myself out of the classification of talking now for the fuel oil institute and talking as to what I know exactly is the case, our margin has been reduced considerably, I would say to the tune of about three-quarters of a cent a gallon over the past year, year and a half.

I would say half to three-quarters of a cent a gallon.

Mr. SCHNEEBELI. I haven't had that experience.

Mr. DE BLOIS. This has been our experience and these can be verified if you would care to.

Mr. SCHNEEBELI. I have two very good friends in the oil distributing business up there, Rolly Booma and Les Godwin.

Mr. DE BLOIS. I know Rolly pretty well.

Mr. SCHNEEBELI. Give him my regards.

Mr. DE BLOIS. I sure will do that.

Mr. SCHNEEBELI. Thank you very much.

Mr. ULLMAN. Mr. Bush.

Mr. BUSH. Sir, on the top of page 2 in your testimony you talk about these increases which certainly are very real. I wonder if you could enlighten the committee on where these increases come from. The price of crude oil hasn't gone up appreciably, has it? Do you have figures on that?

Mr. DE BLOIS. I don't have any figures on the price of crude.

Mr. BUSH. In the last 5 or 10 years I believe you will find that the price of crude oil in this country has gone down. Certainly it has where I used to live so I wonder what is your feeling here in this price thing? Who is getting it?

Mr. DE BLOIS. That is a very good question, Mr. Bush, and I wish I could give you a positive answer. I would probably be a lot smarter than I really am. I really honestly don't know. I know basically that we are not getting a percentage of it.

Mr. SCHNEEBELI. May I interrupt here?

Mr. BUSH. Yes.

Mr. SCHNEEBELI. I think a lot of it is the increased cost of transportation.

Mr. DE BLOIS. This was the case. Transportation costs during the height of the Suez crisis, there is no question, took a considerably steep climb; but these have since come back down. At least I am led to believe it.

Mr. SCHNEEBELI. These are internal transportation costs within the country which are considerably higher, pipelines, trucks, and railroads.

Mr. DE BLOIS. For example, Mr. Bush, there was a price increase, I am going to say the beginning of May—it may have been June 1—of approximately a half a cent a gallon on the wholesale price. As near as I can determine there was no economic justification for this.

You get all different kinds of answers from all different kinds of people. They mention, possibly, wage-price, for instance, as being one of the things in the country. They claim that this is just a correction that should have taken place a long time ago.

The fact of the matter remains that this particular increase will cost the New England consumer approximately \$20 million if it stays status quo. The thing that we are concerned about is, whenever there is an apparent short supply, the price invariably tends to go up. It has always been this way, basically.

We operate under a free enterprise system.

Mr. BUSH. My question really is kind of a two-part question. I just asked the first part. The second part is in paragraph 3, on page 2, you say that "any such legislation would place the Nation in an energy straitjacket which would result in higher petroleum product prices."

We are dealing here primarily with crude oil and I didn't know whether you meant crude oil prices having gone up in this country. From an economic standpoint I think maybe it would be difficult to justify that broad claim. I don't mean to be unsympathetic to the consumer, wherever he is, with increased prices; but we are dealing here essentially with crude oil imports, the magnitude of this problem; and, if domestic crude has not risen and if the legislation in some field would help the problem in terms of our whole import program, would hold at existing levels, how can you conclude from that that the price would go up?

Mr. DE BLOIS. Basically, this: I think that on the present import restrictions which are now administered through the Department of the Interior, the Department of the Interior does have some flexibility in its administration of these particular things.

We, of course, in New England, feel that they have not been free enough. We heard testimony this morning just exactly the opposite. We feel they have been too firm.

However, to legislate this particular thing would take it out of the realm of flexibility and make it basically—well, legislation which would make it the policy of the country that you would be breaking the law to do otherwise, you see.

This would make it inflexible. We feel that with the way it is at the present time there is a flexibility that can be used and has been used, we think wisely, by the Department of the Interior in meeting crises as they come up; for example, this past winter, granting these 12 emergency allocations.

We for sure, Congressman, are for a strong domestic industry. There is no question about that.

Mr. BUSH. You have to be.

Mr. DE BLOIS. We have to be, I agree with you. The domestic industry has shown a certain flexibility in increasing their quotas. However, we do feel that this should be left where it is, with the Department of the Interior, which is in a position to meet the varying crises from different sections of the country better than it would be, say, to have to come in and try to obtain emergency legislation or something like that.

Mr. BUSH. I think the only thing I quarrel with is, you know, a literal interpretation of that comment that "any such legislation would place the Nation in an energy straitjacket which would result in higher petroleum product prices."

Because if you freeze it at existing levels I don't see how that is going to make increased prices. This is getting a little technical but I just don't see your rationale there.

Mr. DE BLOIS. Basically the rationale I believe is that energy consumption in the United States is increasing at a very rapid rate. For example, jet fuel is being used much, much faster today. Gasoline is going up at a higher rate, fuel oil to a lesser degree, but it is still climbing at approximately a 2- or 3-percent rate.

Mr. BUSH. Are you suggesting then the domestic industry wouldn't be able to meet the needs? I think if you are talking something like that, that throws the whole economic factor into the equation; but what I think the industry is suggesting, and those of us who feel we need a little more formalization in this program, is that given the existing ability to meet the needs I just don't see how the price structure is going to change if the formula stays the same.

If you change the formula I can see a change in the price structure; but I don't want to belabor this point, Mr. Chairman. Those are all the questions I have, sir.

Mr. ULLMAN. Thank you, Mr. De Blois, for bringing your views to the committee.

Mr. DE BLOIS. Thank you.

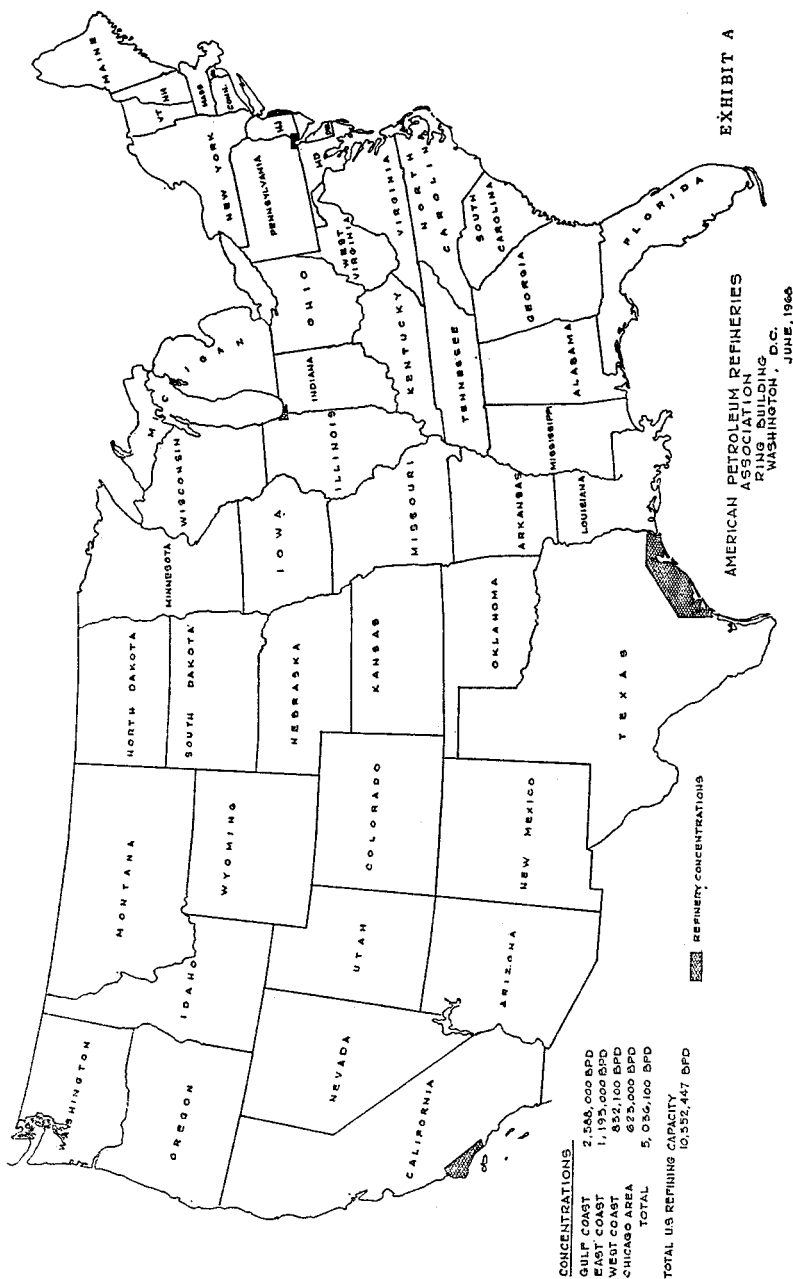
Mr. ULLMAN. The next witness is Mr. Famariss. We are happy to have you before the committee, Mr. Famariss. Would you please identify yourself for the record and proceed as you see fit.

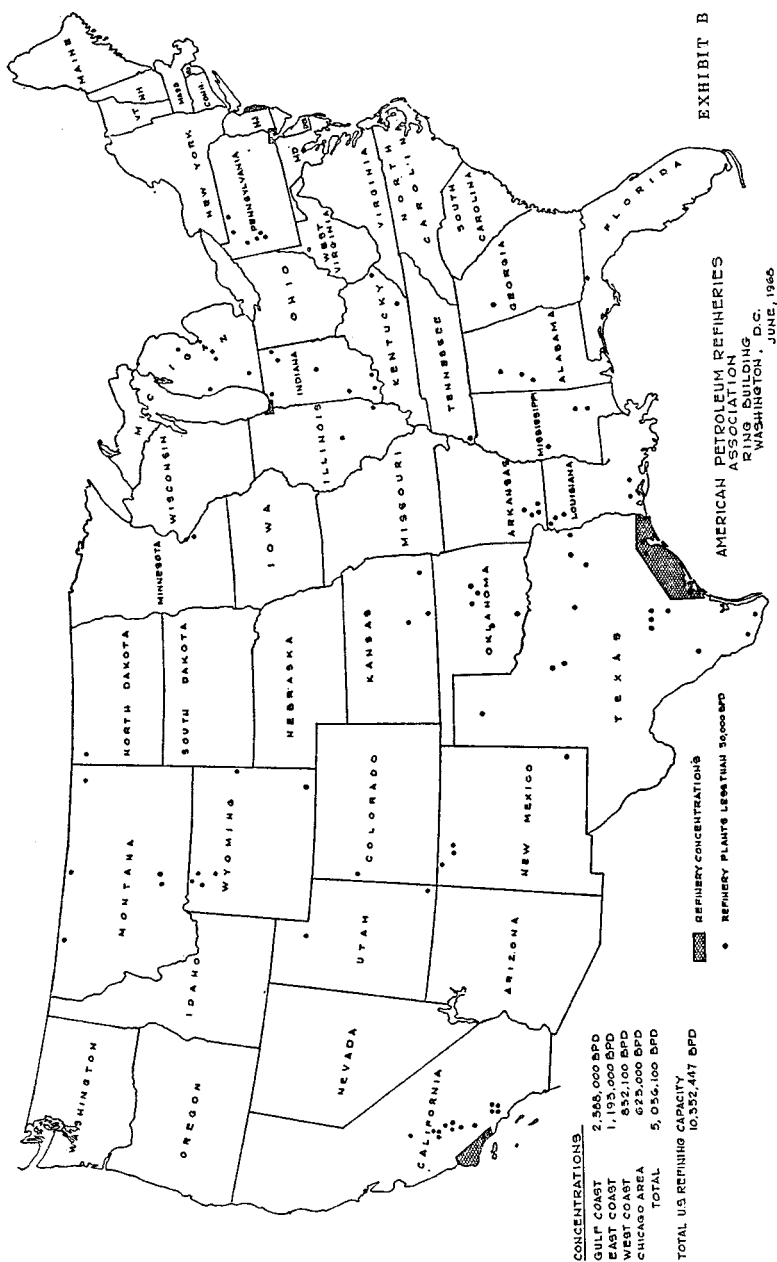
STATEMENT OF WALTER FAMARISS, JR., PRESIDENT, AMERICAN PETROLEUM REFINERS ASSOCIATION

Mr. FAMARISS. Thank you, sir. Mr. Chairman and members of the committee, my name is Walter Famariss, Jr. I am president of the American Petroleum Refiners Association, the membership of which is limited to "small oil refiners" as defined by the Small Business Administration. I am also president of Famariss Oil & Refining Co., located at Hobbs, N. Mex.

My appearance here today is to emphasize the critical importance that any import legislation recommended by your committee and enacted by Congress is to the small oil refiners throughout the country. Certain types of import limitations could prove disastrous to them unless proper safeguards are provided. Their continuation in the domestic economy is imperative, not only for their potential and considerable contribution to any national defense efforts, but also from the viewpoint of providing a necessary competitive element in the economy of the petroleum industry.

Mr. Chairman, 50 percent of the refining capacity of the United States, 5,036,000 barrels per day, most of which is owned by major oil companies, is concentrated in three coastal areas and near Chicago, Ill. What a crippling blow it would be should these complexes be destroyed. They are graphically shown on exhibit A attached. In contrast, the national security aspect of small oil refiners is quite apparent from the fact that their refining facilities are located in inland locations widely dispersed all across the Nation as shown on exhibit B attached. Numbering 105 plants, these geographically protected facilities control approximately 750,000 barrels per day of refining capacity and because of the simplicity of their technology, these plants could conceivably be converted quickly to the production of military jet fuel.





Secretary of the Interior Stewart L. Udall recognized the indispensable nature of small refiners in contributing to national defense in the following statement:

Small independent refineries represent a dispersed and decentralized refining capacity of critical importance to national defense and such refineries are in less vulnerable target areas than large concentrations of refining operations, particularly those located in coastal areas and in large industrial complexes. The small decentralized refinery locations are accessible to sources of domestic crude oil supply and the products are accessible to military installations which require their products. (Affidavit of Secretary Udall of February 15, 1962 set forth at page 28, Defendant's Motion for Summary Judgment, *Standard Oil Co. v. Stewart Udall* 2496-61, U.S. District Court for the District of Columbia.)

As the Secretary pointed out, many small oil refiners are located in the vicinity of crude oil producing fields, thus if railroads or pipeline transportation systems were destroyed, crude oil could be trucked to their refineries for processing. Furthermore, even though the facilities of small refiners might be damaged or sabotaged, they are of a type which could be repaired and put back on stream within a relatively short time.

Aside from the clear logistic value of small oil refiners located near outlying military installations, these refiners have a vital role in preserving a healthy competitive condition in the domestic petroleum economy. Anticompetitive forces in this industry and a rapid trend toward heavy concentration of refining capacity in a relatively few major oil companies has long been of much concern to both Congress and the administration.

It can be demonstrated that small refiners furnish the real competition in the petroleum refining industry. They provide the principal means of keeping prices of petroleum products at reasonable levels, thus protecting the interests of the consumers in the marketplace. Proof of these statements lies in the clearly demonstrable fact that in Alaska and Hawaii, where small refiners have no operations, retail prices of petroleum products are considerably in excess of those in other States where they supply necessary competitive forces to keep prices down. In late June of 1967 the Federal Trade Commission released their report on anticompetitive practices in the marketing of gasoline. In this report they unequivocally document the competitive importance of the small refiner by the following statement:

The record is clear that independent refiners and marketers exert a beneficial influence upon competition that is disproportionate to their actual representation within the petroleum industry: they have long been innovators of marketing methods and have been the primary agents in translating efficiencies at the production and distribution levels into lower prices at the retail level. They play a part in the industrial pattern that is "entirely disproportionate" to their size "in keeping markets competitive, flexible and dynamic and in preventing a recognition of interdependence and the possible bureaucratic conservatism that go with size and quasipermanent life from stultifying competition." (De Chazeau and Kahn, *Integration and Competition in the Petroleum Industry*, 383, Yale Univ. Press 1959.)

In the final analysis the continued health of the petroleum industry as well as their customers depends upon the small refiner continuing as a vital factor in the domestic petroleum economy.

It has been noted that your committee has now heard testimony on across-the-board quotas for imports and is presently hearing witnesses on establishing quotas for specific commodities and industries. It has been indicated that tariffs on petroleum imports might be increased or limited to a percentage of an antecedent or estimated base. We are opposed to limiting petroleum imports by way of tariff regulations. In our opinion such action would serve only to raise prices of petroleum products to consumers as well as increase the crude oil costs for small oil refiners.

As you know the existing mandatory oil import program is predicated upon national security objectives under the provisions of the Trade Expansion Act of 1962. It is our recommendation that the basis for this program be continued.

In event your committee decides to report out legislation with respect to the import control program imposing certain policy guidelines, we respectfully suggest that such an act encompass the following items:

1. No rigid or fixed percentage limitation related to an antecedent or estimated base be placed in such act. It is felt that any legislated percentage, as previously stated, would eventually result in increased consumer prices. It is imperative, if fixed limits are set by laws, that the act contain authority for the President to adjust such fixed percentage within definitive limits based upon his review and study of domestic economic and industry conditions.

2. Clear guidelines requiring that allocations of permissible imports be distributed on a graduated, sliding scale based upon the size of individual companies. Such graduated allocations do not, as is sometimes alleged, amount to a windfall or a special deal for small refiners, as each refiner, including all majors and regardless of size, gets exactly the same benefits for any given bracket. The graduated scale serves to distribute the benefits attached to crude oil imports equitably among all refiners. This equalization is necessary since it is recognized that tremendously large integrated enterprises actually wield a disproportionate amount of economic power. These giant international oil companies have tremendous amounts of domestic crude oil production. The price they realize for these domestic crude oils has increased because of import limitations on crude oils. They also receive additional benefits from foreign tax credits and from depletion allowances based upon higher domestic crude oil prices. Such benefits are available mostly to the large integrated refiners.

3. In order to prevent small oil refiners from having their benefits under the graduated scale curtailed or eliminated, the act should provide for a separate set-aside for refiners who process less than 30,000 barrels a day in their facilities. Similar preference for small businesses of all types is a well established policy under several Federal statutes. The amount of imports required to provide this economic assistance would be a very small percentage of any total permissible imports.

We believe, insofar as legally possible, using the oil import program for special treatments to assist social and environmental purposes, should be eliminated, thus assuring permanence and stability in the

program and returning it to the original intent of Presidential Proclamation 3279. In support of this proposal, we cite the testimony presented by the Independent Petroleum Association of America before the House Interior Subcommittee through which was stated that 145,000 barrels per day of product imports are entering the United States over and above the limitations set by the program. Special privileges within the program have granted 50,000 barrels per day of product imports for Caribbean refineries. Importation of any petroleum products into the United States denies American labor and the American economy the economic benefits which would accrue were these products manufactured in the continental United States.

The American Petroleum Institute in its publication, Petroleum Facts and Figures, for the year 1967 reveals that the economic value of refining a barrel of oil in wages, taxes, and similar is \$1.29. The circumvention of the program through imports outside of the program and special privileges granted a few companies inside the program actually has weakened the industry, whereas the purpose for promulgating the program in the first place was to maintain a strong and healthy domestic industry with apparently no intentions of benefiting those with refineries beyond the continental United States who would be valueless to us in case of war. The Honorable J. Cordell Moore, Assistant Secretary of the Interior for Mineral Resources, analyzed the situation clearly when he told the National Oil Jobbers Council in Washington, D.C., on May 21, 1968, that he is opposed to opening the gates for imported petroleum products where there are adequate supplies in the United States because this would lead to exporting our refining capacity.

Sample data we have received from a random group of small oil refining companies show the following consolidated figures:

Total number of employees.....	1,216
Total annual payrolls.....	\$6,750,000
Total annual gross sales.....	\$88,480,000
Ratio of net profit to gross sales (percent).....	3.2
Ratio of value of import allocations to net profit.....	100.7

Taking this sample as a basis and projecting these figures, the 87 small refining companies operating 105 refineries as shown on exhibit B would result in the following:

Total number of employees.....	8,787
Total annual payrolls.....	\$58,937,500
Total annual gross sales.....	\$641,479,971

Please note that the sample survey of the actual operating statistics of small refiners discloses that the ratio of value of import allocation to net profit is 100.7 percent. A 3.2-percent net profit on gross sales is an irreducible minimum situation to say the least. Should the import program be revised in any manner resulting in any lesser benefits from cheap foreign crude oil, small refiners would find their position untenable and most would be forced to go out of business.

It has also been ascertained that since January 1, 1965, the posted price of domestic crude oil purchased by small oil refiners has increased on the average 16 cents per barrel. This increased cost has absorbed

over 60 percent of the effective value of exchanges of foreign oil import allocations. A further similar increase would wipe out the entire effective value of such exchanges with the result that small oil refiners would be lost to the competitive economy and the defense effort.

On behalf of our members, I thank you for the opportunity to appear before your committee and bring to your attention the urgent requirement to protect the interests of small oil refiners in any legislation your committee may report to the House. Without preserving their competitive position in the domestic petroleum economy, they will not be able to survive. This is clearly demonstrated by the statistics heretofore noted.

I would apologize for going over my allotted time.

Mr. ULLMAN. Are there questions?

Thank you very much, Mr. Famariss, for bringing your views before the committee.

Mr. FARMARISS. Thank you, sir.

Mr. ULLMAN. Mr. Buschman, we are glad to have you before the committee. Will you please identify yourself for the record and with the understanding your full statement will be in the record proceed as you see fit.

STATEMENT OF ROBERT A. BUSCHMAN, PRESIDENT, AMERICAN ASSOCIATION OF OILWELL DRILLING CONTRACTORS

Mr. BUSCHMAN. Thank you. My name is Robert A. Buschman. I am vice president and general manager of Field Drilling Co. of San Antonio, Tex. I appear at these hearings as president of the American Association of Oilwell Drilling Contractors, a national trade association whose primary membership consists of firms engaged in the business of drilling wells for oil and gas producers.

A study by the U.S. Department of Interior has forecast that the U.S. annual consumption of oil by 1980 will be 2 billion barrels more than in 1967, an increase of 50 percent.

Such prospective immediate growth rates raise question concerning the industry's ability to find sufficient new supplies of oil and gas to fulfill the needs of the Nation. Not since the great oil shortage scare of the early 1920's which led to the enactment by Congress of the oil and gas depletion tax provisions as a drilling incentive for producers has there been such widespread doubt concerning the ability of the United States to maintain its oil producing capacity at levels adequate to satisfy future consumption requirements.

Concern about adequate future supplies is spawned by a sizable recent decline in oil discovery rates. For the first time since enactment of the oil and gas depletion provision the United States is failing to discover enough new oil to keep known reserves abreast of rising production.

During the last decade, 1958 to 1967, nearly 4 billion barrels less oil was discovered than in the preceding decade, while production was advancing by 4 billion barrels. Discovery volume exceeded production by 8.8 billion barrels in the decade which ended in 1957 but in the last decade discoveries exceeded production by only 1.1 billion barrels.

Over the past 5 years production actually has exceeded the amount discovered by 12.5 million barrels. With production exceeding discoveries of new oil supplies in recent years there has been a drastic decrease in the ratio of crude unproduced reserves to production.

At the end of 1958 crude unproduced reserves were 12.9 times greater than the current annual production in that year. A steady decline in ratio of reserves to production has occurred since 1958. At the end of 1967 the ratio had fallen to 10.3 barrels in reserve for each barrel produced during the year. This is the smallest ratio of reserves to production since 1924.

Unless future discovery rates are vastly larger than in recent years this country is on the threshold of a shortage in domestic oil supplies.

The stakes are high. National security is dependent upon an abundant supply of cheap oil. Operation of the Nation's industrial plants is dependent upon an abundant supply of cheap oil. All forms of transportation are dependent upon oil. Oil and gas are prime ingredients in today's modern petrochemical world.

The sudden and drastic changes in the Nation's outlook for an abundance of future crude oil focuses attention on why less oil is being found and how discovery may be stimulated. Despite the popular notion that oil has become too difficult to find in the United States, figures prove this to be a false premise.

It is extremely important to realize that the amount of oil discovered has remained remarkably consistent with the amount of effort made to discover new oil supplies. Practically the same amount of oil in ratio to the number of wells drilled is being found today as in past years.

The ratio of volumes discovered to exploratory wells drilled also has maintained a remarkable similarity over the years. In the 1948 to 1957 period new reserves found amounted to 64,000 barrels for every well drilled, contrasted with nearly 63,000 barrels in the latest decade. These figures are in my statement in much more detail.

In terms of barrels found per exploratory well drilled, only 3,000 less barrels were found in the latest decade than in the preceding 10 years. Since 1956 drilling activity has undergone continual, substantial reduction falling to just 36,883 wells in 1966 and then dipping to only 32,473 wells in 1967.

The 1967 drilling rate represented a decline of 44 percent from the alltime peak of 1956. Meanwhile crude oil production rose 22 percent between 1956 and 1967 and U.S. consumption of petroleum advanced 62 percent.

A continuation of these widely contrasting trends will undermine the industrial, social, and military strength of the United States. In a published study entitled "An Appraisal of the Petroleum Industry of the United States" the Department of the Interior concluded that efforts to find new supplies of oil since 1956 have not been enough to provide a sound basis for future growth.

In addition, the Department of the Interior declared discovery rates must be increased to 6 billion barrels annually. Doubling of recent annual discovery rate levels will be a most difficult task. Drilling is the only way oil can be found and be recovered from the depths of the earth.

The economic health of the domestic producing industry must be restored to a level where financial incentives will encourage producers to expand oil discovery efforts by drilling more wells. Many factors have contributed to the economic deterioration of the producing segment of the U.S. oil industry during the last decade.

Large scale imports of foreign oil have been an especially important factor. Total controlled and noncontrolled imports of crude oil and refined products advanced from an annual total of 188 million barrels in 1948 to 575 million barrels in 1957 and to 650 million barrels in 1959 when mandatory import quotas were established, then to over 900 million barrels by 1965.

Large increases in imports of foreign oil have occurred at a time when domestic producers needed expanded markets to sell excess producing capacity.

The combination of these circumstances caused crude oil prices to be depressed below 1957 levels. Recent small advances have not restored these price reductions. Unfortunately, depressed crude oil prices have come at a time when inflation, the additional expense of deeper drilling, and the high cost of offshore drilling have combined to boost the cost of drilling wells.

Expenditures for drilling advanced from an average of \$46,500 per well in 1955 to \$60,648 per well in 1965, an increase of 30.6 percent. With drilling costs up and crude oil prices received down, there has been less incentive for producers to drill.

The mandatory oil import program was established in 1959 for the purpose of preserving to the greatest extent possible a vigorous, healthy petroleum industry in the United States. Deep concern has been created by recent issuance of special import grants and exceptions.

These open the door for more and more requests for the same treatment. Unless corrective action is taken the effectiveness of the import program will be destroyed.

Therefore, it is recommended that Congress enact a law which will, (1) limit imports to a fixed ratio with actual instead of estimated domestic oil production, and, (2) clearly define what types of oil imports are exempt from the import limitations.

Thank you.

(Mr. Buschman's prepared statement follows:)

STATEMENT OF ROBERT A. BUSCHMAN, PRESIDENT, AMERICAN ASSOCIATION OF OILWELL DRILLING CONTRACTORS

My name is Robert A. Buschman. I am Vice President and General Manager of Field Drilling Company, of San Antonio, Texas. This statement on United States imports of Foreign oil is presented in my capacity as President of the American Association of Oilwell Drilling Contractors, a national trade association whose primary membership consists of firms engaged in the business of drilling wells for oil and gas producers. The Association's contractor member firms operate over 1,400 drilling and well servicing rigs. Member-owned rigs are located in every oil-producing state of the nation and in all territorial waters undergoing any oil activity. In addition, the Association's membership includes firms engaged either in the manufacture or distribution of oil field drilling equipment, firms which furnish a variety of services to drilling rigs, and a small number of oil producing companies and individuals.

The United States consumes far larger quantities of petroleum today than it did a very few years ago. The nation's use of petroleum is expected to continue growing at an unabated pace in coming years. U.S. consumption of oil rose to the colossal sum of $4\frac{1}{2}$ billion barrels annually during 1967. At this level, the U.S. consumed 50 percent or $1\frac{1}{2}$ billion barrels more oil than in 1954, a scant 13 years ago.

The next 13 years are expected to see the nation's ravenous oil appetite rise another 2 billion barrels to an annual total of $6\frac{1}{2}$ billion barrels by 1980, according to the U.S. Department of Interior in a study entitled "An Appraisal of the Petroleum Industry of the United States", published in January, 1965.

This forecast means that by 1980 consumption of oil will be nearly 50 percent higher than 1967 rates. It means the U.S. will consume almost as much oil during the next 13 years as in all previous history.

QUESTION OF ADEQUATE FUTURE SUPPLIES

Forthcoming gigantic increases in consuming rates force attention upon the enormity of future oil requirements of this country. Future oil discovery rates must be much larger than in recent years, if this country is to continue to enjoy the advantages of an abundant and readily available domestic oil supply and avoid dependence on foreign sources which can be cut off over night. This can be achieved only by a complete reversal of the 10-year downward trend in efforts to find new supplies of oil within the Continental Limits of the U.S.

Not since the great oil shortage scare of the early 1920's (which led to enactment by Congress of the oil and gas depletion tax provision as a drilling incentive for producers) has there been such widespread doubt concerning the ability of the U.S. to maintain its oil and gas producing ability at levels which will satisfy future consumption requirements. Widespread deep concern regarding the possibility of inadequate future supplies has been spawned by a sizeable decline in oil discovery rates at a time when crude oil discovery rates should be advancing to keep abreast of rising production.

DISCOVERY RATES DECLINE

Nearly 4 billion barrels less new oil were discovered in the latest decade (1958-1967) than in the preceding decade (1948-1957), while on the other hand almost 4 billion barrels more oil were produced in the last decade (Table 1, Page 4). With less oil found and more oil produced, the volume of crude oil discovered exceeded production by less than 1.1 billion barrels during the last 10 years. In contrast, discoveries in the preceding decade (1948-1957) surpassed the amount produced by 8.8 billion barrels.

The ratio of discoveries to production has deteriorated to an even greater extent during the last five years (1963-1967). More oil was produced than discovered in these years. Although slightly more oil was found the last five years than in the preceding five years, rising production exceeded the amount discovered by 12.5 million barrels. These figures get down to the basic crux of the problem—a need to discover more oil as production grows.

Whereas proved unproduced reserves remaining in the ground for future use rose 7.0 billion barrels in the decade which ended with 1957, there has been only minor growth in reserves during the latest decade. Proved unproduced crude oil reserves in the U.S. at the end of 1967 totaled 31.4 billion barrels, only a little higher than the 30.0 billion barrels in existence back in 1955, and in contrast with a peak of 31.7 billion barrels in 1961.

With production exceeding discoveries of new oil supplies in recent years, the ratio of proved reserves to current production has undergone drastic reduction since 1958. Whereas, proved unproduced crude oil reserves at the end of 1958 were 12.9 times greater than the amount produced in that year, this ratio fell to only 10.3 barrels in reserves for each barrel produced during 1967. This is the smallest ratio of reserves to production since 1924.

TABLE 1.—U.S. OIL DISCOVERY RATES FAIL TO KEEP ABREAST OF RISING CRUDE OIL PRODUCTION

[Figures in thousands of barrels annually]

End of year	New supply discovered	Annual production	Discovered versus production	Proved unproduced reserves	Ratio of reserves to production
1948	3,795,207	2,002,448	+1,792,759	23,280,444	11.6
1949	3,187,845	1,818,800	+1,369,045	24,649,489	13.6
1950	2,562,685	1,943,776	+618,909	25,268,398	13.0
1951	4,413,954	2,214,321	+2,199,633	27,468,031	12.4
1952	2,749,288	2,256,765	+492,523	27,960,554	12.4
1953	3,296,130	2,311,856	+984,274	28,944,828	12.5
1954	2,873,037	2,257,119	+615,918	29,560,746	13.1
1955	2,870,724	2,419,300	+451,424	30,012,170	12.4
1956	2,974,336	2,551,857	+422,479	30,434,649	11.9
1957	2,424,800	2,559,044	-134,244	30,300,405	11.8
1958	2,608,242	2,372,730	+235,512	30,535,917	12.9
1959	3,666,745	2,483,315	+1,183,430	31,719,347	12.8
1960	2,865,328	2,471,464	-106,136	31,613,211	12.8
1961	2,657,567	2,512,273	+145,294	31,758,505	12.6
1962	2,180,896	2,550,178	-369,282	31,389,223	12.3
1963	2,174,110	2,593,343	-419,233	30,969,990	11.9
1964	2,664,767	2,644,247	+20,520	30,990,510	11.7
1965	3,048,079	2,686,198	+361,881	31,352,291	11.7
1966	2,963,978	2,864,242	+99,736	31,452,127	11.1
1967	2,962,122	3,037,579	-75,457	31,376,670	10.3
5-year summaries:					
1948-57	16,708,979	10,236,110	+6,472,869	-----	-----
1953-57	14,439,027	12,099,176	+2,339,851	-----	-----
1958-62	13,478,778	12,389,960	+1,088,818	-----	-----
1963-67	13,813,056	13,825,609	-12,553	-----	-----
10-year summaries:					
1948-57	31,148,006	22,335,286	+8,812,720	-----	-----
1958-67	27,291,834	26,215,569	+1,076,265	-----	-----
Difference	-3,856,172	3,880,283	-7,736,455	-----	-----

Source: American Petroleum Institute annual reports.

Note: Ratio of reserves to production calculated by dividing proved unproduced reserves end of each year by annual production during that year.

SHORTAGE WOULD ENDANGER SECURITY

Obviously the U.S. is in very serious trouble if crude oil discovery rates continue to decline at a time when consumption is going to rise so rapidly. Unless future discovery rates are vastly larger than in recent years, this country is headed toward a shortage in domestic oil supplies.

The stakes are high. National security is involved. Without oil: planes cannot fly, ships cannot sail, armored vehicles become immobile, and guns cannot fire. The nation's economic health also is involved. Oil fuels and lubricates our plants. Oil powers our planes, automobiles, trucks and tractors. Oil is one of the prime sources of heat for our homes, schools, plants and offices. Together with gas, oil is a primary source of the petrochemicals which play so important a role in today's modern world. The remarkable dependence of the U.S. on an adequate supply of petroleum has been recounted too many times to need repeating here.

The sudden and drastic changes taking place in this nation's outlook for an abundance of future crude oil focuses attention on the question of why less oil is being found than in the past. It is commonplace to hear someone express the thought that it has become too difficult to find oil in the U.S. However, an analysis shows this is a false premise not supported by fact.

LESS DRILLING CAUSES DISCOVERY DECLINE

The truth is that the relationship between the amount of oil discovered in the U.S. and the amount of effort expended to discover new oil supplies has remained remarkably consistent over the years (Table 2, Page 6). In the 1948-1957 decade, the finding of 31.1 billion barrels of new crude oil reserves was equivalent to 64,394 barrels for each of the 483,710 wells drilled in those years. In the decade between 1958 and 1967 discovery of 27.3 billion barrels of new crude supplies represented 62,775 barrels for each of the 434,757 wells drilled.

TABLE 2.—U.S. DISCOVERY EFFORTS DROP DESPITE RISING CRUDE OIL PRODUCTION

	Number of wells drilled annually		Wells drilled per million barrels of crude oil produced		Barrels of crude oil discovered per well drilled	
	All wells	Exploratory	All wells	Exploratory	All wells	Exploratory
1948-----	39,477	8,013	18.5	3.9	96,137	473,631
1949-----	38,682	9,058	20.5	4.9	82,412	351,936
1950-----	43,307	10,306	21.4	5.2	59,175	248,660
1951-----	45,996	11,756	19.8	5.2	95,964	375,464
1952-----	46,509	12,425	19.8	5.4	59,113	221,271
1953-----	49,480	13,313	20.5	5.7	68,325	247,587
1954-----	52,179	13,100	22.2	5.7	55,875	219,316
1955-----	55,879	14,942	22.5	6.0	51,999	192,124
1956-----	58,418	16,207	22.3	6.2	51,827	183,522
1957-----	53,783	14,714	20.6	5.6	46,283	164,795
1958-----	49,101	13,199	19.9	5.3	53,120	197,693
1959-----	50,179	13,191	19.2	5.1	73,073	277,979
1960-----	46,831	11,704	18.2	4.5	50,508	202,096
1961-----	45,644	10,992	17.4	4.2	58,224	241,764
1962-----	45,997	10,785	17.2	4.0	47,414	202,216
1963-----	43,126	10,664	15.7	3.9	50,413	203,874
1964-----	44,149	10,747	15.8	3.8	60,358	247,954
1965-----	40,374	9,466	14.2	3.3	75,496	322,003
1966-----	36,883	10,313	12.1	3.4	80,352	287,402
1967-----	32,473	8,878	10.1	2.9	91,218	333,647
5-year summaries:						
1948-52-----	213,971	51,558	20.9	5.0	78,090	324,081
1953-57-----	269,739	72,276	21.8	6.0	53,530	199,776
1958-62-----	237,752	59,871	19.2	4.8	56,692	180,870
1963-67-----	197,005	50,068	13.5	3.5	70,115	275,886
10-year summaries:						
1948-57-----	483,710	123,834	21.7	5.5	64,394	251,530
1958-67-----	434,757	109,939	16.6	4.2	62,775	248,245

Source: All wells drilled from "World Oil" annual review-forecast issues. Exploratory tests drilled from American Association of Petroleum Geologists annual drilling reports.

Another statistical measurement of discovery efficiency is the amount of oil found in relationship to the number of exploratory wells drilled. Exploratory wells are those tests drilled outside of known producing limits of a field for the purpose of finding new producing fields or of extending the producing area of previously found fields. Here again, there exists a remarkable similarity between the last two decades. The volume of new reserves found between 1948-1957 was equivalent to 251,530 barrels for each of the 123,834 exploratory wells drilled, while discoveries in the 1958-1967 period amounted to 248,245 barrels for each exploratory well drilled.

This comparison of discovery volumes and discovery efforts shows a 12 percent reduction in number of exploratory tests drilled resulting in the discovery of 12 percent less oil in the last 10-year period. Therefore, we can conclude that lower oil discovery rates in the U.S. are the result of a drastic reduction in drilling activity. To increase the volume of oil discovered, we must increase the amount of drilling in the U.S. Drilling is the only way oil can be found and can be made recoverable from the earth.

DRASTIC DROP IN DRILLING

Contrary to the need to increase drilling, there has been a drastic reduction in U.S. drilling activity during the past decade. In the years between 1948 and 1956, the volume of total wells drilled annually advanced sharply, rising from 39,477 wells in 1948 to an all-time peak of 58,418 wells in 1956. During these years drilling activity grew at a somewhat greater rate than crude production, the number of wells drilled per million barrels of production advancing from 18.5 in 1948 to better than 22 wells per million barrels of crude oil production during the years 1954, 1955, and 1956. With drilling at high levels, new oil found exceeded production by comfortable margins.

This upward trend came to a sudden end in 1957, when drilling activity turned sharply downward. By 1961 U.S. drilling rates had dropped to 45,000 wells annually. Drilling continued to undergo steady substantial reduction, failing to just 36,883 wells in 1966, then to only 32,473 wells in 1967. Only 10.1 wells were drilled per million barrels of crude oil production in 1967, contrasted with the drilling of 20 to 22 wells for each million barrels of production during the years 1953 through 1957.

The 1967 well completion rate was the lowest since 1946, and was less than the prewar peak of 35,213 wells drilled in 1937. The 1967 completion rate was 25,945 wells or 44 percent less than the all-time peak of 58,415 wells drilled in 1956. Meanwhile, crude oil production rose 22 percent between 1956 and 1967, and U.S. consumption of petroleum advanced 62 percent.

A decrease in drilling efforts to make more oil available at a time when U.S. consumption and production is undergoing rapid growth is a path wrought with many far-reaching perils. A continuation along this course will undermine the industrial and military strength of the U.S. in the most distant future.

INTERIOR SAYS NOT ENOUGH DRILLING

The Department of Interior in its previously mentioned "Appraisal of the Petroleum Industry of the United States" concluded that efforts to find new supplies of oil since 1956 have "not been enough to provide a sound basis for future growth." We concur with this conclusion by the Department of Interior. Unless frightening downward trends in discovery rates are reversed within a relatively few years, the U.S. will lack the readily available and abundant supply of oil and gas upon which it has built its industrial, social and military health and strength.

In its appraisal of the industry, the Department of Interior declared discovery rates must be increased to 6 billion barrels annually. This means oil discovery rates must be doubled. This will be a difficult task. It cannot be achieved unless the economic health of the producing segment offers sufficient incentive to domestic producers.

Many factors have contributed to the economic deterioration of the producing segment of the U.S. oil industry during the last decade. Large scale imports of foreign oil have been an especially important factor. Total imports of crude oil and refined products advanced from an annual total of 188 million barrels in 1948 to 575 million barrels in 1957, to 650 million in 1959, then to over 900 million barrels per year by 1965.

CRUDE PRICES DECLINE—COSTS RISE

These large increases in imports of foreign oil have occurred at a time when domestic oil producers were in need of expanded markets in which to sell excess producing capacity. The combination of these circumstances caused crude oil prices to be depressed below 1957 levels, and small advances during the past 18 or more months have not yet restored these price reductions. U.S. crude oil prices averaged \$2.93 per barrel in March, 1968, compared with \$3.17 per barrel in early 1957.

Unfortunately, depressed crude oil prices have come at a time when inflation, the additional expense of deeper drilling, and the high cost of offshore drilling have combined to boost the cost of drilling wells. According to annual studies known as the "Joint Association Survey of Industry Drilling Costs", expenditures for drilling advanced from an average of \$46,500.00 per well in 1955 to \$60,648.00 per well in 1965, an increase of 30.6 percent. Drilling costs rose from an average of \$11.55 per foot drilled in 1955 to \$13.44 per foot in 1965. These are the latest available drilling cost figures. When data for 1966 and 1967 becomes available, these surveys are likely to reflect additional advances in drilling costs.

With costs up and prices received down, there has been less incentive for U.S. producers to drill. The result: less drilling and less oil discovered, as already related.

In the final analysis, all the factors influencing the willingness of producers to invest in drilling ventures boil down to the simple equation of profit probabilities. Producers will expand their oil discovery efforts by drilling more wells whenever economic conditions provide sufficient financial incentives.

The rapid rise of oil imports into the U.S. following World War II aroused sufficient concern to attract the attention of the Federal Government as early as 1955. At that time, the President's Committee on Energy Supplies and Resources stated further significant increases in oil imports would damage the domestic oil industry to such an extent as to jeopardize national security. Congress responded by early enactment of a law empowering the President to limit imports of commodities whenever they threatened to impair national security. President Eisenhower initiated a voluntary oil import program in 1957. Total

imports of oil continued to rise, leading to the establishment of the present mandatory oil import program in 1959. In initiating the latter program, the President of the United States declared it is "necessary that we preserve to the greatest extent possible a vigorous, healthy petroleum industry in the U.S."

After nine years it is obvious that the mandatory program has failed to provide enough assistance to create healthy economic conditions for domestic oil producers. Therefore, it is time to re-evaluate the program.

TOO MANY CHANGES AND EXEMPTIONS

The program has been subject to frequent change, especially in recent years. Less than half of the total amount imported is subject to import control. Recent months have seen the establishment of exempt foreign trade zones, especial allocations to petrochemical plants, a 5 percent increase granted on imports of unfinished oils, permitting larger shipments from plants in Puerto Rico and the Virgin Islands, failure to include nearly 60,000 barrels per day of jet fuel under the program, the placing of No. 4 fuel oil imports outside the 12.2 percent import quota, and have seen Canadian imports consistently exceed estimated import volumes.

The foregoing rash of special grants, exemptions, etc., threaten to destroy the effectiveness of the program. The door has been opened for more and more companies to request the same treatment. Unless corrective action is taken immediately, further import growth is probable.

It is essential for immediate steps to be taken which will stabilize import policies. Only by firmly established policies can the mandatory oil import program be restored to a long-range staple basis. Otherwise, the U.S. oil import program faces severe deterioration. This would bring further hardship to domestic oil producers. Fewer wells would be drilled and less oil would be discovered. National security would be impaired by forcing this country to become dependent upon the uncertain availability of a plentiful supply of foreign oil at reasonable prices.

NEED LAW TO STABILIZE CONDITIONS

Therefore, it is recommended that Congress enact a law which will: (1) limit oil imports to a fixed ratio with domestic oil production, and (2) clearly define what types of oil imports are exempt from this limitation, such as residual fuels into Districts I-IV. Otherwise there will be irresistible pressures to place increasing amounts of imports outside and fixed basic limit.

Mr. HERLONG (presiding). Thank you very much, Mr. Buschman, for your contribution. Are there any questions?

Mr. BYRNES. Mr. Chairman.

Mr. HERLONG. Mr. Byrnes.

Mr. BYRNES. In the last 15 to 20 years have there been any scientific developments to help in this discovery process, or are we still limited to the same kind of scientific information we had at that time?

Mr. BUSCHMAN. Is this concerning the drilling of wells?

Mr. BYRNES. Well, the discovery. You were talking about discovery, where oil is.

Mr. BUSCHMAN. Of course, certainly I am primarily qualified to comment on drilling, but as far as the techniques—

Mr. BYRNES. But you were talking in your testimony about the need for discovery.

Mr. BUSCHMAN. Yes, sir.

Mr. BYRNES. And I was just wondering to what degree there have been scientific advances in the area of discovery.

Mr. BUSCHMAN. There certainly has been meaningful new methods of seismographic work and things of that nature that the industry has developed that are more helpful now.

Mr. BYRNES. And yet the rate of discovery is declining.

Mr. BUSCHMAN. Yes, oil discovery has gone down, but not per well drilled. It is remarkably consistent and the charts I have in this testimony show that over a 20-year period the amount of proven reserves found per well drilled is almost the same as it was 20 years ago.

We are not drilling enough wells. If we drill more wells we will find more reserves.

Mr. BYRNES. Thank you.

Mr. HERLONG. Any further questions?

Mr. BUSH. I would just like to commend the gentleman, Mr. Chairman, on his statement, and having been in that business before, certainly I know you are faced with a terrible plight. It is a business made up predominantly of small operators, small individuals, and I for one think that the testimony given with that particularly in mind makes a great deal of sense.

I thank the gentleman for his statement.

Mr. HERLONG. Thank you so much for your appearance before the committee.

Mr. BUSCHMAN. Yes, sir.

Mr. HERLONG. Mr. Herman Intemann. Mr. Intemann, we are happy to have you before the committee and if you will identify yourself for the record and proceed in your own way we will appreciate it.

STATEMENT OF HERMAN K. INTEMAN, VICE PRESIDENT, UNION CARBIDE CORP.; ACCOMPANIED BY GEORGE C. WELLS, VICE PRESIDENT

Mr. INTEMAN. Thank you, Mr. Chairman. My name is Herman K. Intemann and I am accompanied here today by George C. Wells and we are vice presidents of Union Carbide Corp.

Union Carbide is a major chemical and petrochemical producer involved extensively in both export and import trade as well as in overseas producing. We have submitted a longer and more detailed statement to the committee which I hope will be made a part of the record in full.

Mr. HERLONG. Without objection it will appear at length in the record following your oral statement.

Mr. INTEMAN. Thank you, sir.

I will summarize it briefly with emphasis today on what we believe to be the impact of the oil import control program on the domestic petrochemical industry. Late last year the management of Union Carbide decided its own detailed study and analysis product by product was needed to evaluate the effect on our corporation of the Kennedy round and related developments such as changes in the European tax system.

Our analysis now nearly complete shows that the Kennedy round tariff changes in combination with EEC border taxes and export tax exemption granted to EEC companies will have a net adverse affect on Union Carbide's profits by 1972 when the full extent of the changes have become effective.

The order of magnitude of this unfavorable effect as determined by our detailed study totals many millions of dollars. Despite this Union Carbide does not require nor does it expect to receive through legis-

lation or other political means any artificial or special advantage over its foreign competitors, assuming that the economic factors beyond our control such as raw material prices, labor rates, taxes, and non-tariff barriers, are or can be made relatively equal.

We ask only for equality of competitive opportunity; in other words, to be subjected to the handicaps or the restrictions or to enjoy the advantages no greater or no less than those affecting the foreign chemical producers.

Unfortunately, such equality does not yet exist as far as the petrochemical industry is concerned. The price trend of raw material feedstocks from petroleum and natural gas in the United States as compared with foreign prices is such that by 1970 to 1972 our foreign competitors will have a decided advantage in terms of raw material cost because of the fact that under the oil import control program the domestic petrochemical industry has only limited access to foreign feedstocks.

This would be a source of concern in any event to a chemical company like Union Carbide which is so dependent upon economical raw materials for profitable operation.

However, it is rendered more than ever serious when superimposed upon the anticipated adverse effect on Union Carbide of the Kennedy round and European tax disadvantage.

The oil import control program restricts the imports of foreign oil. For areas east of the Rocky Mountains imports are restricted to 12.2 percent of production and the bulk of our consumption must be supplied by domestic sources.

The program produces and protects a difference between the U.S. price of crude oil and world market price. As a result oil averages \$1.25 per barrel higher in price in this area of the United States than elsewhere in the world. This is a price differential of 3 cents a gallon or 60 percent above world price.

The forced usage of domestic crude oil at its higher price does not work a hardship on companies in the U.S. energy market. Energy products such as gasoline and heating oil, while more costly in bulk than foreign products, are sold only in the United States and are protected against imports by the same quota program.

But the program poses a clear and present danger for the U.S. petrochemical industry. Petrochemicals are made from oil and natural gasolines. These raw materials are subject to the oil import control program and their cost to the chemical industry inevitably reflects the higher domestic price of petroleum. The quota protected price differential for oil, 60 percent higher at home, would be critical if not fatal in petrochemical production where in many cases raw material costs account for more than 50 percent of the cost of the basic price.

Furthermore, U.S. petrochemical products have only a slinking level of tariff protection in the domestic market. Foreign petrochemicals, on the other hand, need no import quotas for their shipments to the U.S. market and are not restricted in their access to low cost oil from the Middle East or South America.

For this reason adequate access to foreign feedstocks is fundamental to the health and growth of the domestic petrochemical industry.

A great deal is at stake. First, the continued growth of U.S. exports of petrochemical products. Petrochemicals currently contribute more

than \$1.1 billion a year to the natural balance of trade. These exports will inevitably go the way of the steel industry's exports but for different reasons if the burden of higher raw material costs are added to the adverse effect of the Kennedy round tariff changes and the border tax.

Second, the potential loss of a significant part of the domestic market for petrochemicals, a market whose size by 1972, 1975, will double and reach an estimated \$35 billion. Lower raw material cost combined with lower U.S. tariffs, foreign export tax rebating, will give overseas products a running start on sales in the U.S. market.

Third, the possible outflow of large numbers of jobs and large sums of capital. If the petrochemical industry is unable to remain competitive for plants in the United States it can only retain its market share by investing in foreign plants. This would hurt the very domestic petroleum industry which the oil import program is designed to protect because overseas plants will not use domestic petroleum either as feedstocks or as fuel.

These are the clearly foreseeable consequences unless the domestic petroleum industry is allowed the access to low-cost raw materials which its foreign competitors enjoy. The question is, How can the oil import program be modified to provide the petrochemical industry with the access to foreign raw materials it must have to remain competitive in domestic and foreign markets?

We believe that this can and must be accomplished without impairing the national security objective of the oil import program and without damage to the domestic petroleum producer.

We recognize the vital importance of the U.S. oil industry and are keenly aware that the petrochemical producers cannot hope to solve their critical problems by ignoring the welfare of the domestic oil and gas producer.

The interests of petrochemical producers and petroleum producers are not irreconcilably in conflict. Despite its size as the Nation's third largest manufacturing industry in terms of investment the petrochemical industry's demand for petroleum raw materials is small in comparison to the quantity of oil going into the fuel and energy markets.

Chemical requirements today take less than 5 percent of the total domestic oil and natural gas production.

Furthermore, even if it were physically and economically practical to have a total shift to import raw materials by the petrochemical industry it would not significantly reduce the continued growth of the oil and gas production in the United States.

In fact the petrochemical industry will require a new increasing quantity of domestic materials even if it has greater access to foreign feedstocks. Obviously there are a number of ways in which the oil import program can be changed to meet the critical needs of the petrochemical industry.

Along with other companies Union Carbide has made suggestions and is ready to offer others and to work with all concerned to develop the urgently needed long-term program. While a long-term program is being developed we believe it is imperative that an import-for-export plan be promptly put into effect.

The concept of the import-for-export program is that U.S. exports of petrochemical products shall not be handicapped by noncompetitive raw material costs. The act of exporting petrochemicals would establish the right to import additional oil on an equivalent wait basis. This program has been recommended by the Secretary of the Interior and the Secretary of Commerce.

It was approved by the President on January 29 of this year, but it has not been put into effect because necessary regulations have not been written and issued.

Implementation of the import-for-export plan will strengthen the export capability of the domestic petrochemical industry in a key way and help to assure a continuation of its essential contribution to our balance of trade. A drop of less than 1.5 percent in the petrochemical exports of \$1.5 billion will cost the balance of payments more than the cost of oil imports involved in this program.

An increase in petrochemical exports can repay the balance-of-trade account several times over. A dollar's worth of oil imports can generate as much as \$20 worth of petrochemical export sales.

We hope the committee will recognize the problems of the chemical industry in whatever recommendations on trade policy it may make to the House. Our detailed statement outlines in rather specific terms the impact on a major American chemical firm of decisions and problems like the Kennedy round negotiations, European tax change, and the oil import program in an effort to be helpful to the committee and without making detailed legislative recommendations.

We are, however, strongly opposed to the enactment of H.R. 10178 and H.R. 10686 and related oil import bills. In their present form these bills would tighten the noose of higher raw material costs firmly around the neck of the domestic petrochemical industry.

A healthy, vigorous chemical industry is essential to our national security. A competitive chemical industry is essential to a favorable balance of trade. Access to foreign petroleum raw materials is essential in both cases.

Thank you very much.

Mr. HERLONG. Thank you, Mr. Intemann. Do you want this entire appendix made a part of the record?

Mr. INTEMAN. I would appreciate that, sir.

(Mr. Intemann's statement and appendixes referred to follow:)

STATEMENT OF HERMAN K. INTEMAN, VICE PRESIDENT, UNION CARBIDE CORP.

I. Introduction and Summary

Union Carbide Corporation is a major international producer involved extensively in both export and import trade, as well as overseas manufacturing. Although we are widely diversified from a product standpoint, chemicals and plastics represent approximately 40 percent of our total business. We, therefore, have a considerable interest in the foreign trade policy of the United States as it may affect the chemical industry. Because the subject is broad and complex, this statement is confined to the chemical (including plastics) segment of our business.

First, it might be pertinent to outline briefly the scope of our operations. In 1967, the total worldwide sales of Union Carbide amounted to \$2.5 billion, of which chemicals accounted for \$1.1 billion. We are owned by 185,000 stockholders and have 74,000 employees in the United States. In addition, our affiliated overseas companies employ 40,000. In the United States, there are 415 locations where Union Carbide has business establishments, including 225 manufacturing plants, many of which are capital intensive. Outside the United States, there are

175 plants in 30 countries around the world, operated by affiliated companies in which or ownership ranges from 50 percent to 100 percent.

The implications of the Kennedy Round negotiations, as well as other economic changes such as revisions in European tax systems, will have a profound effect on the nation and on individual companies such as our own. In fact, a company like Union Carbide cannot effectively plan its long-term business strategy and capital investment policy without evaluating as best it can the probable impact of these far-reaching developments upon its own operations.

Therefore, the management of Union Carbide undertook such a detailed study and analysis, product by product, to guide its own decisions. This study, which has required many months, is sufficiently near completion to warrant certain preliminary observations. We therefore felt that it might be useful to share with the Committee and the Congress some of the findings of this detail study. It should be emphasized, however, that the viewpoints and information set forth relate primarily to Union Carbide. Although to some extent they may apply to the chemical industry as a whole, or to other companies within it, our statement is not intended in any way to speak for or represent the chemical industry.

Speaking generally as a corporation with major global interests, Union Carbide is convinced that liberalization of trade barriers over the long term is essential to the growth of world trade. Further, we believe it would be adverse to the growth and development of the U.S. economy if the trend in this direction were now to be unnecessarily impeded or reversed. More specifically we realize that the final results of the Kennedy Round may have a favorable long-term effect on the total economy. However, we recognize that in reducing such barriers, it is obviously difficult to negotiate concessions which are reasonably reciprocal and equitable as far as an individual industry or company is concerned.

Our findings and conclusions may be summarized as follows:

(a) Although the Kennedy Round may well have a long-term beneficial effect on the overall economy, our analysis shows that the tariff changes which it will bring, in combination with EEC Border Tax changes and the export tax exemption granted to EEC competitors, will have a net adverse effect on Union Carbide's profits by 1972 when the full extent of the changes has become effective. The order of magnitude of this unfavorable effect, as determined by our detailed study, totals many millions of dollars. However, for competitive reasons, some of the specific data cannot be incorporated in public testimony.

Of course, it has to be recognized that under the Kennedy Round approach, where the objective was to reduce existing tariffs on both sides by an equal percentage, the result would likely be unfavorable for corporations in industries having higher average American tariff levels, particularly for a corporation such as Union Carbide where domestic business is about ten times its exports. Furthermore, the likelihood that our estimates are realistic or even understated is increased in view of the severe overcapacity which will exist in the petrochemical industry in 1972, in Europe and in the United States.

Despite the anticipated adverse impact, we hope that between now and 1972 there will be offsetting factors, such as continued growth in petrochemical consumption and further improvements in methods, cost control, and operating efficiency. However, these favorable influences could be expected to develop anyway.

(b) Assuming that economic factors beyond our control such as raw material prices, labor rates, taxes, and nontariff barriers are or can be made relatively equal, Union Carbide does not require nor does it expect to receive through legislation or other political means any artificial or special advantage over its international competitors. All we ask is to have equality of competitive opportunity—in other words, to be subjected to handicaps or restrictions, or to enjoy advantages, no greater or no less than those affecting the foreign chemical producers.

Unfortunately, such equality does not yet exist as far as the petrochemical industry is concerned. The price trend of raw material feedstocks from petroleum and natural gas in the United States as compared with foreign prices is such that by 1970-72 our foreign competitors will have a decided advantage in terms of raw material cost because of the fact that under the Oil Import Control Program the U.S. petrochemical industry has only limited access to foreign feedstocks.

This would be a source of concern in any event to a chemical company like Union Carbide which is so dependent upon economical raw material costs for profitable operation. However, it is rendered even more serious when superimposed upon the anticipated adverse effect of the Kennedy Round and European tax changes.

The difference between foreign and domestic raw material costs can range up to 60 percent. This is especially critical because in the case of many petrochemical products, raw material costs account for more than 50 percent of total production cost. Under such circumstances, the entire profit potential can be eliminated for many major products. Therefore, unless the oil import quota system can be liberalized to give petrochemical producers access to feedstocks at competitive world prices, serious consideration must be given to placing a larger proportion of our production capacity overseas.

(c) Our analysis shows that our export business, and probably that of most American exporters, will be disadvantaged by the relative increase in EEC border taxes as compared with the accompanying increase in indirect taxes borne by our EEC competitors. We also anticipate that our exports to third countries will be unfavorably affected by the exemption of competitive EEC production for export from the new TVA tax. Accordingly, we believe that, in equity, EEC products which now pay no border tax coming into the United States should be subject to the same indirect tax burden as a domestic product. Because EEC production for export is exempt from TVA, the U.S. exporter must also be exempt from any indirect U.S. tax to which it is now subject if he is to be competitive. There may be some risk of retaliation if a border tax—export rebate is instituted by the United States. If the Committee feels that this might be of controlling importance, we think that serious consideration should be given to the alternative of imposing an import surcharge to apply at least as long as the balance-of-payments problem exists.

(d) Clearly, the results of our study, detailed as it is, are only estimates and projections of what may happen several years ahead. Unforeseen changes in products, technology, and economic conditions would conceivably produce quite different results. But there seems to be no doubt that the Kennedy Round will have a major impact, both favorable and unfavorable, on companies such as Union Carbide. For this reason, we hope that there will be a "breathing spell" for a reasonable period of time, and that the U.S. will make no further concessions in tariffs or related subjects until sufficient time has passed to enable a complete evaluation in actual practice of the full effect of the Kennedy Round and the other economic changes taking place in world trade.

II. Balance of Trade Considerations

The chemical industry has developed consistently favorable U.S. trade balances over the years. During the period 1951-1966 inclusive, the chemical trade balance cumulative surplus was \$16.4 billion or almost 20 percent of the total U.S. trading surplus of \$83.8 billion. During the same period, the reported U.S. net deficit on balance-of-payments was \$30.9 billion. For the year 1966, the chemical trade balance was \$1.7 billion and in 1967 rose to \$1.8 billion.

It would indeed be shortsighted to assume that favorable chemical trade balances will always be generated. Any change in trading conditions or lack of equivalence of competitive opportunity which affects a U.S. chemical manufacturer adversely in comparison with overseas competition will manifest itself not only by impairing the employment, investment and profit position of the U.S. company, but also by affecting adversely the U.S. balance of trade.

The history of the iron and steel industry demonstrates how quickly a major industry with substantial exports can find itself in a hard struggle to maintain even its domestic competitive capability. In 1950, with a positive trade balance of \$281.3 million, the exports of iron and steel continued to increase to a record positive balance of \$855.5 million in 1957. Then the reversal occurred. By 1959, only two years later, the industry had a trading deficit of \$155.7 million which rose rapidly to \$747.5 million by 1966. The lesson to be learned from iron and steel is that the favorable trade balance of a major industrial sector like chemicals must not be taken for granted.

The following data from the Department of Commerce and O.E.C.D. highlight the importance of chemicals in the U.S. international trade picture, in contrast to the changing pattern of the iron and steel trade.

[In millions of dollars]

Year	(1) Trade balances, iron and steel, SITC-67	(2) Trade balance, chemicals, SITC-5	(3) Total U.S. export-import trade balances	(4) Net U.S. balance of payments (liquidity basis)
1950.....	281	(1)	1,423	-3,580
1951.....	188	646	4,065	-305
1952.....	430	497	4,483	-1,406
1953.....	237	457	4,900	-2,152
1954.....	386	718	4,818	-1,550
1955.....	541	774	4,059	-1,145
1956.....	595	899	6,322	-935
1957.....	856	1,029	7,608	-520
1958.....	410	1,012	4,660	-3,529
1959.....	-156	1,069	2,005	-3,743
1960.....	174	1,270	5,540	-3,881
1961.....	97	1,317	6,249	-2,370
1962.....	-42	1,353	5,283	-2,203
1963.....	-135	1,376	6,208	-2,670
1964.....	-109	1,668	7,758	-2,798
1965.....	-606	1,633	6,113	-1,335
1966.....	-748	1,719	4,777	-1,357
1967.....	-812	1,839	4,718	-3,575

¹ Not available.

Sources: Cols 1 and 2—1965-67, Census Bureau of Department of Commerce. Census Bureau has not published redefined figures for prior years. Earlier data from OECD, as most nearly comparable; cols. 3 and 4—Department of Commerce.

It should be noted that the rate of growth in the chemicals balance of trade indicated above has slowed down considerably in recent years. From 1951 through 1960, and from 1961 through 1967, the growth rate of exports was 6 to 7 percent. However, the growth rate of imports speeded up from 3 percent in the first of these periods to more than 10 percent in the last seven years.

It may be appropriate at this point to examine some of the major reasons for this historical favorable balance of trade generated by chemicals and also to evaluate the future environment.

III. Competitive Developments in the European Chemical Industry

Based on announced or completed expansions of petrochemical facilities in Europe, we anticipate that the production will far exceed demand for basic petrochemicals by the early 1970's. This will also be the situation in the U.S. The following table showing projected capacities and estimated consumption in 1970, based on studies conducted by Marketing Research groups,¹ highlights the magnitude of these important changes:

[Billions of pounds]

	Consumption	Capacity
Ethylene:		
Western Europe.....	11.4	20.1
United States.....	15.3	20.2
Low-density polyethylene:		
Western Europe.....	3.3	6.6
United States.....	3.6	4.5
Ethylene oxide:		
Western Europe.....	1.2	2.2
United States.....	3.2	3.4
Benzene:		
Western Europe.....	6.4	8.5
United States.....	7.7	11.9

As a result of this coming major shift in the European supply-demand relationship, aggravated by excess capacity in the U.S., competition in the chemical markets of the worlds must inevitably become more and more intense. We anticipate pressure not only in our domestic markets but in third countries as well, and it will be on a "cut-throat" price-cutting basis because of this extreme excess of capacity. As a result, European producers will be forced to virtually disregard

¹ Both our own as well as outside firms.

normal price-cost-profit relationships in their search for export possibilities. A capital-intensive industry, such as the chemical industry, tends toward capacity operation at almost any cost, justified by incremental pricing philosophy (i.e., pricing to dispose of excess production, usually in export markets, at a level sufficient to cover only direct cost). Our experience has been that this philosophy is most prevalent with our European and Japanese competitors, particularly in the case of state dominated or subsidized operations. American business principles and philosophies are generally sounder from the economic standpoint and are oriented more toward earning a reasonable profit on the overall investment under our private enterprise system.

From the foregoing, it is evident for the chemical industry that a major change will take place in the world competitive situation and in the trading environment of the future. Europe, which not many years ago represented a major market for our exports, must now seek export markets for their basic chemical products which will be more and more in excess supply.

In view of these developments, the economic advantage of scale will no longer be a factor on our side; for example, the May 10, 1968 issue of *European Chemical News* highlights the start-up of a 770 million pound per year ethylene plant by Rheinische Olefinwerke (ROW), a joint venture of Badische and Shell Oil. There has been, and continues to be a significant overall change generally in petrochemical production scale in Europe during the 1960's. Typical capacity of the latest individual ethylene producing units in millions of pounds as compared with the past is as follows:

[In millions of pounds]

	1965	1970
Monteshell.....	220	550
Houllierias de Lorraine.....	26	440
Petrochim.....	18	440
ROW.....	220	770
Imperial Chemical Industries.....	308	990

Nor will we any longer have an advantage in technology. Our foreign competitors, although late entrants, have applied the latest knowledge and have installed technologically sophisticated facilities. As a result, our European competitors will be as efficient as we are. They will also have the added advantage of lower costs not only in labor, but in raw material as well, unless the U.S. oil import restrictions are relaxed for petrochemical production.

IV. Changes in Tariffs and European Taxes

In the chemical industry, partly because of its capital intensive nature, long "lead-time" is required from the design of a plant to its actually coming "on stream". This requires that our strategic planning take into consideration the overall competitive environment which we anticipate will exist at the time that the new investment becomes operational. In addition to the problems of excess capacity and unfavorable price trends outlined in the foregoing, we have to consider the probable effect of the Kennedy Round tariff reductions on both our domestic and export business, as well as the potential effect of the EEC tax system changes on an American exporter to those countries.

Our understanding is that it was not the intent of the Kennedy Round to equalize tariff levels, but only to reduce existing tariffs proportionately. Chemical tariffs in this country were significantly higher on average than those of our European trading partners. As a result, the economic effect of the agreed upon reduction in tariffs, even with the repeal of ASP, will benefit our European competitors to a greater extent in terms of potential price reduction than would be the case with respect to an American chemical producer such as Union Carbide.

For example, pre-Kennedy Round U.S. duties on chemicals in general averaged in the range of 25 to 30 percent, whereas those of the EEC countries were around 17 percent. Therefore, the 50 percent reduction in our tariff levels called for by the Kennedy Round gives foreign producers the potential to reduce prices of products exported to the U.S. market up to 15 percent without reducing profit. Unfortunately, this potential price reduction is more than the U.S. profit margin on many of the bulk, commodity-type chemical products which contribute most to our balance of trade. Conversely, assuming the repeal of ASP, a 50 percent

reduction in the EEC average tariff provides only about half this price reduction potential as a means of expanding export volume from the United States into the EEC.

Over and above the difference in potential price reductions stemming from the differences in tariff reduction, there is an important difference in size of market to which these reductions apply. The U.S. domestic petrochemical market is larger than the European market. Therefore, with a larger potential reduction in price applicable to this larger market, the European competitive producer has improved his export position vis-a-vis the United States to a greater extent than a U.S. company in the reverse direction. Of course, this result could be influenced in a major way to the extent that U.S. tariff levels remaining after the 50 percent reduction provide a sufficiently high barrier to prevent the entry of competitive European products.

Although not a part of the Kennedy Round itself, another economic change in Europe will have a significant influence on the competitive position of American exporters attempting to compete in EEC countries. This is the EEC tax harmonization program involving the switch from the so-called "cascaded" turnover tax to the value-added system known as TVA.

Under the old turnover tax system in these EEC countries, there was a border tax imposed on imports which, in general, amounted to the same turnover tax percentage rate imposed on one transaction of a domestic producer. Since even the most integrated domestic producer was involved in more than one transaction, the average "cascaded" turnover tax which he paid was higher than the border tax.

With the change to TVA, most indirect taxes, including border taxes, will arrive at one uniform percentage of approximately 15 percent. This means that the impact of the tax harmonization program will place U.S. producers exporting to the EEC at a clear disadvantage over their European competitors. The effect ranges from a maximum of about 5.6 percent on selling price in the case of Belgium down to an actual gain of about one percent in the case of Italy, the one country where the border tax was higher than the "cascaded" turnover tax on the domestic producer.

There are many misconceptions about the effect of the change in EEC tax systems upon the importer, and for that reason we made a thorough investigation in Europe of their implications for Union Carbide exports into the EEC. Attached as Appendix No. 1 is a detailed description of the changes in European tax systems, together with our findings as to the probable effect on our competitive position as an exporter into the EEC.

V. The UCC Study

Although we believe that the developments and conditions outlined previously in this statement would qualitatively have an adverse effect on the operations of UCC over the next several years, we considered it important to attempt to quantify these effects financially. Therefore, we undertook a detailed study of all of these influences, both positive and negative, which appeared to impinge upon our situation. Because our chemicals business involves more than 400 individual products, a really definitive quantitative analysis, covering both the effect on our domestic business as well as our overseas activities, represents a massive undertaking, even with the benefit of computerization which we are utilizing extensively. Appendix No. 2 discusses in detail the principles and assumptions which we used and provides a breakdown of the quantitative findings of the effect in Europe and other major export markets. Major elements or aspects of the study were:

1. Potential effect of Kennedy Round tariff reductions and the improved EEC export rebate with respect to our domestic business in the environment of substantial excess capacity on the part of our European competitors. This involved a full consideration, by the "business teams" responsible, of the market position of our major chemical products under the changed economic environment. (As explained previously, specific dollar findings have been omitted here.)

2. Potential effect of tariff reductions by other countries on our export business.

3. Potential effect of the change in border tax on exports into EEC countries resulting from the change from the "cascade" turnover system to the TVA method.

4. The effect of increased export tax rebate on exports from the EEC to third countries.

5. Changes in pricing, particularly in Germany, the first country to switch from the "cascade" turnover tax to the TVA method.

Each of these elements was evaluated and the potential consequences measured on a basis which included and excluded the retention of the American Selling Price (ASP) method of valuation for duty calculation, as well as the other elements of the "Separate ASP Package." The following tabulation summarizes the effect of these changes on UCC's export business (only) as detailed in Appendix 2.

ESTIMATED REDUCTION IN UCC EXPORT PROFIT (BEFORE TAX) ON CHEMICALS RESULTING FROM KENNEDY ROUND AND EUROPEAN TAX SYSTEM CHANGES, 1972

	Without ASP	Retain ASP
g. Change in netback on UCC chemical exports to EEC countries:		
Gain from duty reductions.....	+\$1,665,000	+\$639,000
Loss from border tax change.....	-580,000	-580,000
Net gain to UCC.....	+1,085,000	+59,000
h. Change in netback on UCC chemical exports to third countries:		
To EFTA countries:		
Gain from duty reduction ¹	+197,000	+82,000
Loss from tax system changes (export rebate only).....	-132,000	-132,000
Net gain to UCC.....	+65,000	-50,000
To other third countries:		
(a) Loss from tax system changes (export rebate only) in all countries except Japan and Canada.....	-588,000	-588,000
(b) Effect of volume loss.....	-88,000	-88,000
(c) Change in netback on exports to Japan and Canada from all factors.....	+486,000	+486,000
Net loss to UCC.....	-190,000	-190,000

¹ Including effect of increase in volume to United Kingdom.

From the foregoing summary tabulation of the effect of the Kennedy Round and European tax changes on our export business, it can be seen that the overall net advantage we expect to realize is only \$960,000, assuming repeal of ASP. If ASP is retained, the net effect is slightly negative, the tax changes offsetting duty reduction. As indicated earlier the anticipated profit reduction on our domestic business as the result of reduced barriers to competition and European export tax exemption is many times greater than this minor potential improvement in export.

Other points which might be of interest in this summary are as follows:

1. The estimated gain to UCC (before tax) from duty reduction under the Kennedy Round agreement in other countries amounts to \$1.2 million if ASP is retained. Should ASP be repealed, this gain in netback would increase to \$2.3 million.

2. The anticipated loss from border tax increase under the change in EEC tax method is estimated at \$580,000 annually.

3. As far as the question of ASP is concerned, the figures indicate there is only minor direct financial effect on UCC whether this system of valuation is retained or repealed. This is not surprising because the proportion of our total sales represented by benzenoid products is relatively small. Also, American Selling Prices have deteriorated substantially for many chemical products relative to European prices since the converted tariff percentages were calculated in 1964.

Furthermore, these quantitative findings do not measure the full impact on Union Carbide of the proposed change in ASP. This is because our business depends in a major way upon sales of intermediates to benzenoid converters whose business could conceivably suffer by the elimination of the ASP system and thus reduce their purchases from us. On the other hand, there could be some offsetting effect from price decreases on their purchases stimulated by U.S. Kennedy Round duty reductions. Accordingly, the adverse implications to us of the effect on such customers is impossible to quantify.

We believe it is impossible to generalize on the question of ASP. Each individual company in the chemical industry will be affected differently, depending upon the size of its benzenoid business, its product mix, and the impact on its products of the relative change in American Selling Price versus European prices since 1964.

VI. Equivalent Competitive Opportunity

At this point, we would like to re-emphasize that as a matter of fundamental principle Union Carbide does not require, neither does it expect to gain, any special advantage through legislation or other political means over its foreign international competitors. This is provided, of course, that, in the future, economic factors beyond our control such as raw material costs, differences in tax impact, and labor rates are taken into consideration in negotiating what are intended to be reciprocal reductions in tariff and other barriers to international trade. Actually, we feel it is only reasonable for American chemical companies to have equality of competitive opportunity with respect to our international competition. In other words, assuming that economic factors beyond our control are reasonably comparable, we should neither be handicapped or advantaged vis-a-vis our foreign competitors as far as trade barriers are concerned.

Since we believe in liberal trade policies provided there is equality of competitive opportunity, it would be our preference to operate internationally in the environment just described. However, from the practical standpoint, we realize that it is hardly feasible under today's conditions to have no trade barriers at all. Nevertheless, competitive opportunity as between international chemical producers could still be reasonably equivalent if all nontariff barriers were eliminated and tariff levels were set solely to compensate for differences in labor and tax rates, always providing that all producers were allowed equal access to the same low-cost raw materials.

What is the situation in which the American chemical industry actually finds itself today as far as equality of opportunity to compete is concerned? Unfortunately, at least as far as UCC is concerned, we find ourselves in a somewhat non-reciprocal position at both ends of the equation as compared with our foreign competitors.

When a company like Union Carbide and an entire industry, like petrochemicals, are adversely affected to the extent indicated by our study of the Kennedy Round and the European tax changes, then it is all the more important that we move toward equality of opportunity in other areas. In this respect, the problem of access to petrochemical raw material feedstocks at world prices becomes more and more important.

Because the petrochemical industry is not well understood or widely known, it may be useful to briefly describe the industry and its products.

Largely unrecognized by the layman, petrochemicals have become essential to the modern way of living. Petrochemical products play important roles in the production of food and clothing, in household and industrial detergents, protective and decorative coatings, automobile tires, and the ubiquitous plastics.

Products of the petrochemical industry are essential to national defense in scores of applications. As a recent study by the National Academy of Sciences pointed out, "the petrochemical industry would be a prime source of strength to the nation in a time of emergency. It is contributing to every facet of the economy and is uniquely suited to supply the imagination and broad perspective for quickly finding alternate sources of supply and substitute materials during an emergency in the critical areas of food and agriculture, clothing, shelter, transportation, communications, and medical supplies."

The basic petrochemical and plastic products of the industry, more than \$18 billion worth last year, are produced by more than 320,000 employees at 2,500 plants and factories in the United States. These plants and factories involve investments of more than \$19 billion. In addition, hundreds of thousands of employees in thousands of other plants process these chemicals and plastics into finished products. They are the molders, extruders, and formulators who make the toothbrushes and dish pans, and those who apply the dyes, coatings, adhesives, and chemicals in the course of their own production operations.

The Oil Import Control Program was established by a Presidential Proclamation in 1959, pursuant to the provisions of the National Security Amendment to the Trade Agreement Extension Act of 1958, and was designed to protect the domestic oil industry. If crude oil from South America or the Near East were given free access to this country, the production of more expensive oil and the exploration for additional reserves in the U.S. would be sharply curtailed. The Office of Emergency Planning and the President have determined that our national security requires protection for this segment of the oil industry since world developments could make the nation completely dependent on domestic wells. Union Carbide has no quarrel with the program's objective.

Basically, the Oil Import Control Program restricts the import of foreign oil into areas east of the Rocky Mountains to 12.2 percent of the consumption, with the remaining 87.8 percent to be supplied by domestic sources.

The program produces, and protects, a difference between the price of U.S. crude oil and the world market price. As a result, oil averages \$1.25 per barrel higher in price in the United States than elsewhere in the world. This is a price differential of 3 cents a gallon, or 60 percent above the world price.

The forced usage of domestic crude oil, at its higher price, does not work a hardship on companies in the U.S. energy market. Energy products, such as gasoline and heating oils, while more costly in bulk than foreign products, are sold only in the U.S. and are protected against imports by this same quota program.

But the program poses a clear and present danger for the U.S. petrochemical industry. Petrochemicals are made from oil and natural gas liquids. These raw materials are subject to the Oil Import Control Program and their cost to the chemical industry will inevitably reflect the higher domestic price of petroleum.

The quota-protected price differential for oil—60 percent higher at home—would be critical, if not fatal, in petrochemical production, where in many cases, raw material costs account for more than 50 percent of the cost of the basic products. Furthermore, U.S. petrochemical products have only a shrinking level of tariff protection in the domestic market. Foreign petrochemicals, on the other hand, need no import quotas for their shipments to the U.S. market and are not restricted in their access to the low-cost oil of the Middle East, Africa, and South America.

For these reasons, adequate access to foreign feedstocks is fundamental to the health and growth of the domestic petrochemical industry. This was highlighted by the results of a 1967 Department of Commerce survey of petrochemical producers—involving projections of their operations to 1970.

A great deal is at stake:

1. The continued growth of U.S. exports of petrochemical products. Petrochemical exports currently contribute more than \$1.1 billion a year to the nation's balance of trade. These exports will inevitably go the way of the steel industry's exports, but for other reasons, if the burdens of higher raw material costs are added to the adverse effects of the eventual tariff and tax changes.

2. The potential loss of a significant part of the domestic market for petrochemicals—a market whose size by 1972–1975 is estimated at \$35 billion. Lower raw material costs combined with lower tariffs will give overseas producers a running start on sales in the U.S. market.

3. The possible outflow of large numbers of jobs and large sums of capital. If the petrochemical industry is unable to remain competitive from plants in the United States, it can only retain its markets by investing in foreign plants. Among many others, this would hurt the very domestic petroleum industry which the Oil Import Program is designed to protect, because overseas plants will not use domestic petroleum, either as a feedstock or as fuel. This possibility is neither remote, nor far-fetched. Since the investment risk in European plants is similar to that in the United States, and since tax rebates on exports are available in Europe, producers there will attract the marginal productive capacity for petrochemicals if competitively priced raw materials are not available in the United States. This additional capacity, along with the excess capacity already forecast for Europe, will be available for sales to third country markets—countries where there is no domestic petrochemical industry. These third country markets are today the fastest growing. They offer the greatest possibility for increased exports from the U.S., if we can compete on equal terms with European and Japanese firms. We cannot compete if domestic raw material prices are 60 percent higher.

These are the clearly foreseeable consequences unless the domestic petrochemical industry is allowed the access to low-cost raw materials which its foreign competitors enjoy.

The question is how can the Oil Import Program be modified to provide the petrochemical industry with the access to foreign raw materials it must have to remain competitive in domestic and foreign markets.

We believe this can, and must, be accomplished without impairing the national security objectives of the Oil Import Program and without damage to the domestic petroleum industry. We recognize the vital importance of the U.S. oil industry and are keenly aware that petrochemical producers cannot hope to solve their critical problem by ignoring the welfare of domestic oil and gas producers.

The interests of petrochemical producers and petroleum producers are not in irreconcilable conflict. Despite its size as the nation's third largest manufacturing industry in terms of investment, the petrochemical industry's demand for petroleum raw materials is small in comparison to the quantity of oil going into the fuel and energy markets. Chemical requirements, today, take less than 5 percent of the total domestic oil consumption.

Even if a total shift to imported raw materials by the petrochemical industry were practicable, it would not significantly reduce the continued growth of oil and gas production in the United States. In fact, the petrochemical industry will require, and use, increasing quantities of domestic raw materials, even if it has greater access to foreign feedstocks.

Some of the reasons that lead us to this conclusion should be mentioned. Petrochemical plants in existence today, built to use the customary domestic raw materials, cannot use imported raw materials without being substantially rebuilt at a cost which would average many million dollars each and take more than a year. For this reason, plants using domestic raw materials today will continue to use them. If foreign feedstocks are adequately available, we believe that at least half of the new petrochemical capacity to be built in the U.S. in the next ten years will also use domestic feedstocks. Only half of the new capacity would use foreign feedstocks.

Furthermore, access-as-needed to foreign raw materials would substantially increase the growth rate of the domestic petrochemical production over what will otherwise be the case. This will result in increased demand for domestic feedstocks and fuels. On the other hand, the loss of export and domestic markets would significantly cut the petrochemical industry's growth and curtail its need for the products of the domestic oil and gas industry and depress the growth rate of that industry.

Obviously, there are a number of ways in which the Oil Import Program can be changed to meet the critical needs of the petrochemical industry. Union Carbide, along with a number of other petrochemical companies, submitted a specific and detailed plan to the Administration a year ago. But there is no need to recount the details of this, or any other proposal or to argue their merits. They are complex and technical, necessarily so because that is the nature of the Oil Import Program itself. The Executive Branch of the government already has the authority to make the necessary changes. We are ready to offer additional suggestions and to work with all concerned to develop the urgently needed long-term program.

While a long-term program is being developed, we believe it is imperative that an import-for-export plan be promptly put into effect. The concept of the import-for-export program is that U.S. exports of petrochemical products shall not have the added handicap of non-competitive raw materials costs. The act of exporting petrochemicals would establish the right to import additional oil, on an equivalent weight basis. This program has been recommended by the Secretary of the Interior and the Secretary of Commerce. It was approved by the President through a Proclamation issued on January 29, 1968. But it has not been put into effect because the necessary regulations have not been written and issued. Every week of delay increases the difficulties U.S. producers face in marketing our exports, for reasons outlined earlier. Markets once lost are not easily regained.

Implementation of the import-for-export plan will strengthen the export capability of the domestic petrochemical industry in a key way and help to assure a continuation of its essential contribution to the balance of trade. A drop of less than 1.5 percent in the petrochemical exports of \$1.5 billion will cost the balance of payments more than the cost of oil imports involved in this program. An increase in petrochemical exports can repay the balance of trade accounts several times over. A dollar's worth of oil imports can generate as much as \$20 worth of petrochemical export sales.

Conclusions

We hope the Committee will recognize the problems of the chemical industry in whatever recommendations on Trade Policy it may make to the House. We have tried to outline in rather specific terms the impact on a major American chemical firm of decisions and problems like the Kennedy Round negotiations, the European tax change and the Oil Import Control Program in an effort to be helpful to the Committee and without making detailed legislative recommendations.

We are, however, strongly opposed to the enactment of H.R. 10178, H.R. 10686 and related oil import quota bills. In their present form, these bills would tighten the noose of higher raw material costs firmly around the neck of the domestic petrochemical industry.

A healthy, vigorous chemical industry is essential to our national security.

A competitive chemical industry is essential to a favorable balance of trade.

Access to foreign petroleum raw materials is essential in both cases.

APPENDIX No. 1

EFFECT OF EUROPEAN TAX HARMONIZATION

1. Under the so-called turnover or "cascade" tax system effective through 1967 in all of the EEC countries except France, from a given total invoice price to the ultimate buyer the domestic producers and suppliers who contributed directly or indirectly to manufacture of the product were required in effect to pay to their government the sum total of all the turnover taxes levied upon each exchange of goods and services required for its production, and pyramided upon each other including the 4% tax on the ultimate sale. Under these conditions total accruing tax burden carried by a product through final sale ranged upward from a theoretical minimum of 4% (for a product produced by a completely integrated industry requiring no outside purchases and only one final sales transaction), up to 20% or more for products involving several purchase and sale transactions prior to final sale.

2. In the case of Germany the government has estimated that for industry as a whole the accrual or "cascade" effect produced an average total tax burden of 12% of value of final product. (See Surrey speech before NICB 2/15/68.) However, because the petrochemical industry is relatively highly integrated, the total turnover tax on such products was considerably less than the industrial average.

With regard to Germany we were advised through the German government that this average was only 7.2% of final sales value, which under the accounting methods used included the "cascaded" value of all turnover taxes paid. As a percentage of *sales value net of tax*, this 7.2% becomes 7.8%.

3. With the change to the so-called value-added tax system (TVA) there is to be a harmonization for the entire EEC which will result by 1972 in a uniform single tax of approximately 15% on *sales value net of tax* paid by the ultimate buyer and in theory shifted entirely to him. It should be recognized that philosophically the German government evidently looks upon the previous "cascaded" turnover tax as having in effect been passed on to the ultimate consumer in the selling price, even though from the accounting standpoint it actually went into the operating cost of the producer. Therefore, it is not expected that producers will profit significantly long term by the change in system but will follow a pricing policy which eventually will result in only the *increase* in overall tax burden being shifted to the consumer under the new TVA approach. Another way of saying this is that the netback to the producer after TVA has been paid by the ultimate buyer should be no more than the producer's netback after the turnover taxes which he previously paid. This in turn requires under TVA that selling price to which TVA is added must be lower by 7.2% than selling price under the old system which included tax.

4. In the case of the German petrochemical industry the average increase in total tax burden on domestically produced product under the first stage of TVA now in effect would theoretically be 2.2 percentage points—the difference between the 10% added to selling price (before tax) and the 7.8% average formerly paid (on selling price net of tax). Price trends in the industry beginning immediately after January 1, 1968, actually show that the net selling price to which TVA is now added averages only about 5% below the former selling price including tax, which means that the netback has been temporarily increased in the order of 2%. Since prices are still deteriorating, we expect that when the second TVA change to 11% takes place they will be down by about the full 7.2% to the level where the netback position of the producer after all indirect taxes have been paid *would be the same* as under the previous system. Thereafter, even when the final increase in TVA to 15% is made in 1972, it is not

believed that the German petrochemical industry will make further reductions in price before TVA for tax reasons, but will allow the full incidence of the additional 5% TVA to fall upon the ultimate buyer.

In other words, the producer will try to maintain his netback at the same level in order to maintain his Return on Invested Capital in the neighborhood of 6% which appears to be accepted as reasonable by the leading German producers. This does not preclude the possibility of price revisions for reasons of other than tax system change, such as changes in supply-demand and other market factors. Barring such fluctuations, however, by 1972 total cost including TVA to the ultimate buyer should have risen by 7.2 percentage points, the difference between 15% and the average 7.8% turnover tax (on selling price net of tax) prior to 1968.

5. As far as imported product was concerned, under the "cascade" turnover tax system there was a so-called "border tax" of 4% of total selling price (including duty and this tax), equivalent to the final 4% turnover tax on domestic production. As a percentage of selling price net of tax, this 4% becomes 4.3%. This was intended to be (and was sometimes referred to as) a Turnover Equalization Tax so that domestic product paying local indirect taxes would not be at a significant disadvantage with respect to imported product.

During the "cascade" turnover tax period this border tax was allowed to be lower than average "cascaded" taxes on domestic product perhaps in recognition of the fact that imported product was subject to other costs such as indirect taxes in its home country which were not always fully rebated. Hence, from the same total invoice price charged on domestic product, the importer had only to turn back to the government this 4.3% border tax, as compared with 7.8% (on selling price net of tax) paid by the domestic petrochemical industry.

This in effect permitted the importer to netback, after sales taxes, more of the sales price at the border than the domestic producer at his plant, to the extent of the "cascaded" taxes on the domestic producer's transactions preceding the final 4%—that is, 7.8% less 4.3%, or 3.5% more than the domestic producer's netback.

This higher netback at the border helped to offset not only indirect taxes paid in the U. S. by the exporter, but also the heavy other costs and taxes involved in importation, such as duty, ocean freight, etc., to which the domestic producer is not subject. Such higher netback at the border is necessary to enable imported product to be anywhere near competitive, since it obviously cannot stand the same total sales tax burden as domestic product and compete after being penalized also by the payment of duty as well as indirect taxes in the country of origin, freight, etc.

6. With the change to TVA the border tax has become equal to the TVA percentage, which means that by 1972 border tax will have become 15%, an increase of 10.7 percentage points over the 4.3% formerly paid on imported selling price (before border tax). Therefore, if the importer is not to suffer loss of netback as a result of the change in system, he would have to be able to raise selling price (before border tax) by this increase of 10.7 percentage points. Since obviously the ultimate buyer will not submit to a total cost including tax of more than he is required to pay for domestic product, the importer will be able to increase selling price (before TVA) by only the 7.2 percentage points (on price before TVA) expected as price rise on domestic product between December, 1967 and 1972 (See 4 above).

This means that in contrast to the domestic producer who maintains the same netback as under the old turnover system, the importer will suffer a reduction in netback amounting to 3.5% of the new selling price before TVA—that is, the 10.7 percentage points increase in border tax less the 7.2 percentage points increase in selling price to which he is limited by the anticipated maximum invoice cost of domestic product. Depending upon the price which one wishes to use, this 3.5% is equivalent to 3.3% on the previous netback, and 3.2% of the previous gross selling price including tax.

7. An example of the comparative effect of the change in system on domestic and imported product is shown for the following hypothetical transaction:

[In cents per pound]

	Domestic product	Imported product
Under cascade turnover system:		
Selling Price to Customer (Total Invoice Cost).....	100.0	100.0
Less: Tax paid by seller.....	¹ 17.2	⁴ 4.0
Netback after indirect taxes.....	92.8	96.0
Under TVA:		
Selling price (netback).....	92.8	92.8
Plus: Tax paid by buyer.....	² 13.9	² 13.9
Total invoice cost to buyer.....	³ 106.7	106.7
Loss in netback.....		⁵ 3.2

¹ 17.8 percent of 92.8.² 15 percent of 92.8.³ 6.7 percent higher than previous selling price (or 7.2 percent of TVA selling price).⁴ 4.3 of 92.8.⁵ 3.5 percent of 92.8.⁶ 3.33 percent of 96.0.

As shown in the foregoing table, the importer must by 1972 reduce his selling price at the border (before tax) by about 3.3%, and a reduction of this order of magnitude will indeed be significant. Because of the many additional costs inherent in export business, profit margins are low. In fact, a 3.3% reduction in net price can mean 50%-70% reduction in profit. This is more than enough to seriously impair effective marketing export programs and the ability to be competitive. In the case of some products it can mean the difference between profit and loss, and depending upon tariff level, it can more than offset the potential benefit from the 20% tariff reductions called for by the KR negotiations.

8. As far as UCC is concerned, the disadvantaging effect of the change to TVA can be approximately quantified overall in terms of dollar loss on exports to EEC countries by determining for each country the approximate percentage reduction in netback, and then applying this percentage to total export value at the border of each country. In our study, because our sales figures at the border include tax, we have used the lower percentages, such as 3.2% in the case of Germany, which apply to the gross sales value. In total, it is estimated that the harmonization of EEC tax systems into a uniform TVA system of 15% will produce by 1972 an adverse effect on UCC export profit amounting to approximately \$580,000 annually.

Another important feature of the change in EEC tax systems which can have a significant effect competitively on American exporters in third countries, and into the United States as well, is the fact that under TVA the EEC competitive producer can export completely free of indirect taxes. Under the previous cascaded turnover tax system, it was the intention to exempt exports from indirect taxes as well. It was, therefore, the procedure to forgive the final turnover tax on the last transaction—that is, 4% in the case of Germany, but the remainder of the cascaded effect had to be estimated.

In the case of Germany the government estimated that this remainder would amount to an average of 2% for the chemical industry which of course was an underestimation of 1.2% because the total tax burden on the German producer was 7.2%. In other words, the German producer actually paid 1.2% indirect tax on his exports—namely, 7.2% minus 4% minus the 2% balancing rebate allowed by the government.

Therefore, when the domestic producer became completely free of tax on exports with the change to TVA, his netback on exports was improved by this 1.2%. This of course can be used, in whole or in part, to cut prices either in export or domestic in order to gain competitive advantage without overall loss of profit.

Hence, the new TVA system can provide incentive to the domestic producer with a proportionately large export business even to reduce his domestic profit through price cutting without necessarily reducing his overall global profit.

Since the EEC competitive producers have as much as 3 or 4 times the export business outside of the EEC as do American producers outside of the United States, this increased export tax rebate is an important consideration in international competition, not only from the standpoint of exports into the United States from the EEC but also into third countries.

9. It seems evident that increasing EEC border taxes from 4% to the same relatively high level of 15% eventually applicable to domestic production under TVA is inequitable and in effect discriminates against imported product from countries where no border tax is applied to imports and indirect taxes exist but are not applicable to imports. In other words, German product comes into the United States free of U.S. sales and other indirect taxes, whereas U.S. product going into Germany must pay an indirect tax eventually increased from 4% to 15%.

APPENDIX No. 2

This Appendix presents a detailed analysis of the potential gains and losses to Union Carbide from KR duty changes and revisions of the EEC tax systems in the environment of European petrochemical overcapacity. The basic principles and assumptions used were as follows:

1. 91 products were analyzed individually for the potential import effect into the U.S. of KR duty reductions and export rebate advantage to foreign competition. The domestic sales of UCC for these products in 1967 were \$579,000,000, or 62.5% of the total UCC chemical sales of \$926,000,000. For various business reasons such as price level, capacity, service requirements, etc., it was felt it would not be possible for foreign competition to reduce prices into the U.S. by the full amount of the KR duty reductions. Accordingly, each of the 91 products covered in the study was carefully considered individually from the standpoint of all pertinent marketing and competitive considerations. This resulted in assumed price reductions on the part of importing competitors, all met by UCC, varying from zero (48 products) to 100% of the full theoretical advantage from KR duty reduction plus improved export tax exemption effect (22 products). In addition, we assumed a further loss of profit which would result owing to some inevitable loss of business—taken at 5% of domestic sales. The total estimated loss of profit for these 91 products was then extrapolated to be applicable to total sales. (As mentioned in the main body of the report, the specific result for our domestic business is not disclosed here because of its confidential nature.)

2. Approximately 25 products representing about 70% of total UCC chemical product exports into the EEC countries were analyzed individually and by countries for probable effect on UCC of KR duty reductions and disadvantaging from change in tax systems. In all EEC cases it was assumed that 100% of the duty cuts would accrue to UCC in terms of increased netback because margins on these products are so relatively low and the percentage reductions so comparatively small as to render price reductions unsound from the marketing standpoint for the purpose of attempting to increase volume. Furthermore, detailed individual consideration of all products not now being exported to EEC owing to insufficient netback in the U.S., did not reveal any significant new export opportunities resulting from duty reduction.

After obtaining netback changes in this manner on 23 products, these were then extrapolated to reflect the probable effect on total UCC export sales volume to the EEC. Examples of the method in which these netback changes were developed, both on exports into EEC and imports into the U.S., are set forth in detail on computer models for six major products as attached hereto on Schedules 1-6.

3. As explained in Appendix No. 1, the total turnover tax burden was 7.2% on the selling price (including tax) for an integrated German chemical producer. Using this figure for the domestic German producer and 4% for the Border Tax paid by the importer, the comparative potential change in netback after tax for each was calculated for Germany as illustrated in the appended examples, Schedules 1-6. Similarly, by adjusting the various turnover tax rates for the other countries to put them into the same integrated relationships as the German 4.0% compared with 7.2%, estimated tax relationships on a comparative basis were arrived at for other EEC countries as set forth in the following tabulation (percentages being based on selling price including tax).

[In percent]

Country	Basic turnover tax rate	Cascaded turnover tax on domestic producer	Border tax	Relative loss in netback to importer under TVA ¹
Germany.....	4.0	7.2	4.0	-3.2
France ²				0
Italy.....	4.0	7.2	8.2	+1.0
Belgium.....	7.0	12.6	7.0	-5.6
Holland.....	6.4	11.5	6.4	-5.1
Luxembourg.....	3.0	5.4	3.0	-2.4

¹ See app. 1 on tax harmonization for method of determination.

² Since France was already using the TVA system, no additional relative disadvantage was assumed for the importer.

These relative loss-in-netback percentages were then applied to total export sales value (including tax) into each EEC country individually in order to quantify the disadvantaging caused to UCC by the change in tax system.

Conversely, with respect to exports to third countries made by competitive producers of chemical-type products in countries formerly utilizing the cascaded turnover system of taxes, the change to the TVA system will in effect result in an improvement to their netback on exports from increased rebate, to the extent of about 1.2% as explained in Appendix #1 on European Tax Harmonization. This increase of 1.2% can and probably will be utilized to some degree as a competitive advantage in third countries by enabling competitive producers to translate it either partially or wholly into export price reductions.

5. (a) Although there are indications that the EFTA countries will also undertake indirect tax harmonization along the same lines as the EEC, only Denmark has so far switched to TVA, and here the export sales of UCC are not large enough to expose UCC to significant disadvantaging from change in tax system in comparison with domestic producers. Having insufficient information with respect to other countries, we are not in a position to attempt to quantify, but it seems likely that tax disadvantaging similar to that being experienced in the EEC will eventually take place.

(b) Since the EFTA countries are in effect "Third Countries" as far as the large EEC and U.S. chemical producers are concerned, and because of the 1.2% rebate advantage on exports that the EEC producers will obtain from the change to TVA, it cannot be assumed that the KR duty reductions will translate 100% into increased netback to UCC. Particularly in view of the large excess capacity building up in the EEC, it must be conservatively assumed that under these conditions the EEC competitors will take advantage of the EFTA duty reductions in terms of price cutting, at least to the extent of half the duty reduction, plus utilization of the 1.2% rebate improvement, in an attempt to expand export volume thereto.

(c) As far as new volume opportunities from KR duty reductions are concerned, we believe that this would be significant in terms of additional UCC exports only in the case of the UK, where the reductions in tariff barriers are relatively large. After detailed individual consideration of all major UCC products, and taking into account our UK producing facilities, an increase of 10% in export sales volume to the UK is the most that could be expected with 50% duty reduction assuming ASP repealed. Otherwise, the increase is estimated at 5%.

(d) Applying the above criteria individually to products again representing about 70% of total UCC exports to the EFTA countries, the results with respect to improvement in netback to UCC thereby obtained were extrapolated to the total sales volume to EFTA.

6. Criteria used in arriving at effect on UCC export business to all countries other than EEC and EFTA (30% were accounted for by sales to Canada and Japan) were as follows:

(a) In all of these countries an American producer such as UCC could be subject to adverse competitive effect through price cutting resulting from the 1.2% rebate advantage of the EEC producers. Also, it has been assumed that additionally this adverse effect will result in an estimated 3% loss of export volume in all countries except Canada and Japan.

(b) On the other hand, there will be potential gain in netback for UCC on exports to Japan, accruing from substantial reductions in duty as well as probable increase in export volume resulting therefrom. Here, probable change in marketing conditions such as beneficial effect of tariff changes including stimulus to export volume, reduced by probable price cutting by foreign competitors, has been carefully considered and evaluated for each major UCC product individually in order to arrive at the potential net change in profit on UCC exports to Japan.

(c) This will not be the case into Canada, where KR duty changes either were negligible or actually turned out to be increases. Furthermore, since UCC sales to Canada are largely to an affiliated company, it is not felt that the 1.2% rebate effect will actually apply significantly.

(d) As far as the remaining countries are concerned, these constitute largely the less-developed countries for which tariffs were not affected by the KR reductions, but within which UCC will be subject to the adverse 1.2% and 3% effects cited in (a) above.

Based on the foregoing criteria and assumptions, the quantitative effect on UCC export operations is estimated in detail as follows:

		Estimated increase in netback (before tax) 1972	
		ASP ¹ repealed	ASP ² retained
I. UCC chemical exports to EEC:			
(a) From KR duty change (100 percent of reduction):			
Germany.....	+449,000	+148,000	
France.....	+646,000	+323,000	
Italy.....	+175,000	+52,000	
Belgium.....	+283,000	+83,000	
Holland.....	+95,000	+28,000	
Luxembourg.....	+17,000	+5,000	
Total.....	+1,665,000	+639,000	
(b) Disadvantage from border tax change (see table on p. 3):			
Germany.....	-262,000	-262,000	
France.....	0	0	
Italy.....	+29,000	+29,000	
Belgium.....	-262,000	-262,000	
Holland.....	-80,000	-80,000	
Luxembourg.....	-7,000	-7,000	
Total.....	-580,000	-580,000	
II. UCC chemical exports to EFTA:			
(a) From KR duty change (50 percent of reduction):			
United Kingdom.....	+102,500	+41,000	
Sweden.....	+22,000	+9,000	
Norway.....	27,000	+11,000	
Denmark.....	21,000	+8,500	
Finland.....	0	0	
Switzerland.....	+6,500	+3,000	
Austria.....	0	0	
Total.....	+179,000	+72,500	
(b) Disadvantage from additional price cutting expected from export tax rebate effect.....			
	-132,000	-132,000	
(c) Profit on expected increase in UCC export volume to United Kingdom.....			
	+18,000	+9,000	
III. UCC chemical exports to third countries other than EFTA:			
(a) Disadvantage from pricecutting expected from export tax rebate effect, all countries except Japan and Canada.....			
	-588,000	-588,000	
(b) Loss in profit from estimated 3-percent reduction in export volume resulting from (a).....			
	-88,000	-88,000	
(c) Net change in netback on exports to Japan resulting from all marketing factors evaluated upon an individual product basis.....			
	+486,000	+486,000	
(d) Canada, no change ³			
	0	0	

¹ Assumes Kennedy Round duty cuts of 50 percent, and includes all other features of "ASP separate package."

² Duty cuts stay at 20 percent.

³ Canadian Kennedy Round duty changes are not yet definitely announced, but we understand that for UCC major products some tariffs may increase and others decrease. We can only assume here that possible advantaging from net duty reduction (if any) will offset loss from price reduction by EEC competitors expected from export tax exemption effect.

PRODUCT A—NONBENZENOID
[Comparative netback (in cents per pound)]

	December 1967 ¹	January 1968 ²	July 1968 ³	1972, no ASP ³	1972, ASP ³
A. Into German market:					
1. American Exporter:					
Total invoice price including border tax ⁴	10.77	11.22	11.10	11.50	11.50
Less border tax.....	.42	1.02	1.10	1.50	1.50
Net selling price.....	10.35	10.20	10.00	10.00	10.00
Less German duty.....	1.27	1.25	1.01	.65	1.01
Netback at border.....	9.08	8.95	8.99	9.35	8.99
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	10.77	11.22	11.10	11.50	11.50
Less turnover or TVA.....	.77	1.02	1.10	1.50	1.50
Netback (net selling price).....	10.00	10.20	10.00	10.00	10.00
3. Potential net advantaging, American Exporter (1-2).....	—	.33	—	+.27	—
B. Into American market:					
1. German exporter:					
Total invoice price.....	10.00	10.00	10.00	10.00	10.00
Less U.S. duty.....	2.50	2.16	2.16	1.20	1.20
Subtotal.....	7.50	7.84	7.84	8.80	8.80
Less German turnover tax not rebated.....	.13				
Netback at border.....	7.37	7.84	7.84	8.80	8.80
2. Local American producer:					
Total invoice price.....	10.00	10.00	10.00	10.00	10.00
Netback.....	10.00	10.00	10.00	10.00	10.00
Potential net advantaging, German exporter (1-2).....		+.47	+.47	+1.43	+1.43
C. Relative potential gain—German producer (B-A).....		+.80	+.56	+1.16	+1.52

PRODUCT B—NONBENZENOID

A. Into German market:					
1. American exporter:					
Total invoice price including border tax ⁴	14.91	15.62	15.36	15.92	15.92
Less border tax.....	.57	1.42	1.52	2.08	2.08
Net selling price.....	14.34	14.20	13.84	13.84	13.84
Less German duty.....	1.63	1.61	1.54	1.03	1.54
Netback at border.....	12.71	12.59	12.30	12.81	12.30
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	14.91	15.62	15.36	15.92	15.92
Less turnover or TVA.....	1.07	14.2	1.52	2.08	2.08
Netback (net selling price).....	13.84	14.20	13.84	13.84	13.84
3. Potential net advantaging, American exporter (1-2).....	—	—	—	+.10	—
B. Into American market:					
1. German exporter:					
Total invoice price.....	14.28	14.28	14.28	14.28	14.28
Less U.S. duty.....	4.20	3.83	3.83	2.24	2.24
Subtotal.....	10.08	10.45	10.45	12.04	12.04
Less German turnover tax not rebated.....	.18				
Netback at border.....	9.90	10.45	10.45	12.04	12.04
2. Local American producer:					
Total invoice price.....	14.28	14.28	14.28	14.28	14.28
Netback.....	14.28	14.28	14.28	14.28	14.28
Potential net advantaging, German exporter (1-2).....		+.55	+.55	+2.14	+2.14
C. Relative potential gain—German producer (B-A).....		+1.03	+.96	+2.04	+2.55

See footnotes at end of table.

PRODUCT C—NONBENZENOID

	December 1967 ¹	January 1968 ²	July 1968 ³	1972, no ASP ³	1972, ASP ³
A. Into German market:					
1. American exporter:					
Total invoice price including border tax ⁴	11.23	11.71	11.57	11.99	11.99
Less border tax.....	.43	1.06	1.15	1.57	1.57
Net selling price.....	10.80	10.65	10.42	10.42	10.42
Less German duty.....	1.72	1.70	1.04	.67	1.04
Netback at border.....	9.08	8.95	9.38	9.75	9.38
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	11.23	11.71	11.57	11.99	11.99
Less turnover or TVA.....	.81	1.06	1.15	1.57	1.57
Netback (net selling price).....	10.42	10.65	10.42	10.42	10.42
3. Potential net advantaging, American exporter (1-2).....		-.36	+.30	+.67	+.30
B. Into American market:					
1. German exporter:					
Total invoice price.....	13.10	13.10	13.10	13.10	13.10
Less U.S. duty.....	3.50	3.06	3.06	1.70	2.80
Subtotal.....	9.60	10.40	10.04	11.40	10.30
Less German turnover tax not rebated.....	.13				
Netback at border.....	9.47	10.04	10.04	11.40	10.30
2. Local American producer:					
Total invoice price.....	13.10	13.10	13.10	13.10	13.10
Netback.....	13.10	13.10	13.10	13.10	13.10
Potential net advantaging, German exporter (1-2).....		+.57	+.57	+1.93	+.56
C. Relative potential gain—German producer (B-A).....		+.93	+.27	+1.26	+.26

PRODUCT D—BENZENOID

A. Into German market:					
1. American exporter:					
Total invoice price including border tax ⁴	26.07	27.42	26.85	27.82	27.82
Less border tax.....	1.00	2.49	2.66	3.63	3.63
Net selling price.....	25.07	24.93	24.19	24.19	24.19
Less German duty.....	3.27	3.25	2.59	1.56	2.59
Netback at border.....	21.80	21.68	21.60	22.63	21.60
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	26.07	27.42	26.85	27.82	27.82
Less turnover or TVA.....	1.88	2.49	2.66	3.63	3.63
Netback (net selling price).....	24.19	24.93	24.19	24.19	24.19
3. Potential net advantaging, American exporter (1-2).....		-.86	-.20	+.83	-.20
B. Into American market:					
1. German exporter:					
Total invoice price.....	24.39	24.39	24.39	24.39	24.39
Less U.S. duty.....	9.60	10.60	10.60	4.82	4.75
Subtotal.....	14.79	13.79	13.79	19.57	19.64
Less German turnover tax not rebated.....	.31				
Netback at border.....	14.48	13.79	13.79	19.57	19.64
2. Local American producer:					
Total invoice price.....	24.39	24.39	24.39	24.39	24.39
Netback.....	24.39	24.39	24.39	24.39	24.39
Potential net advantaging, German exporter (1-2).....		-.69	-.69	+5.09	+5.16
C. Relative potential gain—German producer (B-A).....		+.17	+.49	+4.26	+5.36

See footnotes at end of table.

PRODUCT E—BENZENOID

	December 1967 ¹	January 1968 ²	July 1968 ³	1972, no ASP ³	1972, ASP ³
A. Into German market:					
1. American exporter:					
Total invoice price including border tax ⁴	15.47	16.20	15.94	16.51	16.51
Less border tax.....	.59	1.47	1.58	2.15	2.15
Net selling price.....	14.88	14.73	14.36	14.36	14.36
Less German duty.....	1.92	1.90	1.81	1.18	1.81
Netback at border.....	12.96	12.83	12.55	13.18	12.55
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	15.47	16.20	15.94	16.51	16.51
Less turnover or TVA.....	1.11	1.47	1.58	1.18	1.81
Netback (net selling price).....	14.36	14.73	14.36	14.36	14.36
3. Potential net advantaging, American exporter (1-2).....	—	—	—	—	—
B. Into American market:					
1. German exporter:					
Total invoice price.....	15.51	15.51	15.51	15.51	15.51
Less U. S. duty.....	7.38	6.89	6.89	3.26	3.64
Subtotal.....	8.13	8.62	8.62	12.25	11.87
Less German turnover tax not rebated.....	.19				
Netback at border.....	7.94	8.62	8.62	12.25	11.87
2. Local American producer:					
Total invoice price.....	15.51	15.51	15.51	15.51	15.51
Netback.....	15.51	15.51	15.51	15.51	15.51
Potential net advantaging, German exporter (1-2).....	—	—	—	—	—
C. Relative potential gain—German producer (B-A).....	—	+1.38	+1.09	+4.09	+4.34

PRODUCT F—BENZENOID

A. Into German market:					
1. American exporter:					
Total invoice price including border tax ⁴	42.89	44.88	44.18	45.77	45.77
Less border tax.....	1.65	4.08	4.38	5.97	5.97
Net selling price.....	41.24	40.80	39.80	39.80	39.80
Less German duty.....	5.38	5.32	4.25	2.80	4.25
Netback at border.....	35.86	35.48	35.55	37.00	35.55
2. Local German producer:					
Total invoice price including turnover or TVA tax.....	42.89	44.88	44.18	45.77	45.77
Less turnover or TVA.....	3.09	4.08	4.38	5.97	5.97
Netback (net selling price).....	39.80	40.80	39.80	39.80	39.80
3. Potential net advantaging, American exporter (1-2).....	—	—	—	—	—
B. Into American market:					
1. German exporter:					
Total invoice price.....	27.51	27.51	27.51	27.51	27.51
Less U. S. duty.....	7.75	7.65	7.65	3.62	3.88
Subtotal.....	19.76	19.86	19.86	23.89	23.63
Less German turnover tax not rebated.....	.51				
Netback at border.....	19.25	19.85	19.86	23.89	23.63
2. Local American producer:					
Total invoice price.....	27.51	27.51	27.51	27.51	27.51
Netback.....	27.51	27.51	27.51	27.51	27.51
Potential net advantaging, German exporter (1-2).....	—	—	—	—	—
C. Relative potential gain—German producer (B-A).....	—	+1.99	+1.92	+3.50	+4.65

¹ December market price.² January market price.³ German producer assumed to reduce total invoice price in July 1968 when TVA increases to 11 percent, but only to extent necessary to return netback to December 1967 level. The final increase to 15 percent in 1972 is assumed to be borne entirely by the customers.⁴ Assume U.S. exporter meets local producer price.

Mr. HERLONG. Any questions? Mr. Battin.

Mr. BATTIN. I am sorry that I didn't hear all of your statement. Did you have anything to say on the American selling price?

Mr. WELLS. Congressman, if I may attempt to speak to that, we do have in the detailed statement a reference to American selling price. In fact, in this specific quantitative study which we undertook in depth of the impact of the Kennedy round and related factors on Union Carbide, and I emphasize that only because we are speaking only for Union Carbide and not for the chemical industry as a whole as far as that aspect is concerned, we did make our calculations on the basis of retention of the American selling price valuation basis and on the assumption of its repeal.

I think it is important to emphasize that the question of impact of change in method of valuation can or must necessarily differ greatly between individual companies, depending upon a number of factors.

First, the proportion of your business which is in the benzenoid area is important. Secondly, the product mix within that classification of products is an essential factor or consideration.

Thirdly, and I think a point which is sometimes overlooked, is that at the time the converted tariff rates which were supposed to really equalize the overall total tariff receipts of the United States under the proposed new method of valuation, using European export price, with the tariff receipts under the American selling price, were based on conditions, prices, which existed in 1964. Necessarily the relationship between European prices of benzenoid chemicals and American selling prices were a key determinant of whether or not there would be the equality which was attempted and desired in the negotiations.

Now that relationship has changed and it has changed as far as its effect is concerned for each company in the industry. In our particular case, our figures have indicated that today, because of these changes, there really is little or no direct difference as to whether or not the American selling price method of valuation is changed.

It is relatively insignificant. There is an effect but it is minor, not within the realm of estimating capability. This is counter to what we found 2 years ago when we made some preliminary estimates based on the 1964 conditions. I think we should emphasize that the impact on a company like Union Carbide can only be quantified in some degree on the basis of our direct operations. But our benzenoid business is dependent in a major way upon sales to benzenoid product fabricators and converters whose situation may be completely different from ours as far as the impact of ASP is concerned. They can be adversely influenced, depending upon whether the new tariff rates on their products happen to be below or above the average of the new rates which have been established.

Also they can be affected in the other direction by any price reductions which may result from the changes brought on by the Kennedy round negotiations. Therefore, while we feel that we are going to be disadvantaged somewhat in our sales to benzenoid fabricating or converting customers who happen to be adversely affected, this is just impossible for us to quantify.

The point is that we don't feel that you can generalize about the impact of the possible change in ASP on the chemical industry as a whole. It has to be looked upon and considered on the basis of each individual company in the industry.

Mr. BATTIN. Thank you.

Mr. HERLONG. Any further questions? Mr. Bush.

Mr. BUSH. Knowing of Union Carbide's interest in and ability in the field of producing oil as well as related fields in which the company is much better known, you do have some oil production, don't you, Union Carbide?

Mr. INTEMAN. Yes, sir.

Mr. BUSH. The people I have been acquainted with in this company are real good oil people. Is it H.R. 10178 and 10686 that would put into law what is now—

Mr. INTEMAN. Yes, sir, 12.2 percent limit on imports.

Mr. BUSH. Why do you think those would have an adverse effect on price? This is one of the questions I asked an earlier witness. I am just not clear on the economics you are using in your statement.

Mr. INTEMAN. Well, always the law of supply and demand of course is going to govern what prices are despite most anything else. We feel very strongly that—

Mr. BUSH. I would understand that, if you would let me interrupt, if we are talking about changing the ratio but we are not. Those bills don't talk about changing the ratio. They talk about keeping it the same so I get lost on why people feel—

Mr. INTEMAN. So far to date, Congressman Bush, I think you are well aware of the problems that the petrochemical industry has had with the Department of the Interior in establishing with them the need for greater participation in feed stocks which are equivalent to what, as I have said in my statment, to foreign competitors.

Mr. BUSH. Yes.

Mr. INTEMAN. We don't object to the 12.2 percent part as much as we do that there is nothing in those bills that would recognize the problem of the petrochemical industry.

Mr. BUSH. Well, in other words, your objection is not the formalization through legislation of the 12.2, rather it is objection to 12.2, is that correct?

Mr. INTEMAN. That is part of it. We say as presently written. Other provisions in the bills would also trouble us. As you know, we did offer some amendments to those bills.

Mr. BUSH. Yes, I know you did.

Mr. INTEMAN. There was no action taken on any of them as of yet.

Mr. BUSH. That answers my question.

Mr. INTEMAN. We have not attacked the 12.2 percent, as such.

Mr. BUSH. But you are afraid if you formalize it it would be more difficult for you to get exceptions.

Mr. INTEMAN. We think now is the time to really put focus on problems in a very important industry to America, both from its prosperity standpoint as well as national security.

Now is the time to put the focus on and clear the matter up so we know where we stand.

Mr. BUSH. Would you agree with me that formalizing of the 12.2 relationship that now exists in the so-called voluntary or mandatory program would have no effect on the price at all except as to the——

Mr. INTEMANN. No; whether 12 under law of 12.2 or 15 under law or 8 under law or 8 would not change the price trends.

Mr. BUSH. That is the only thing I want to clear.

Mr. INTEMANN. There is no question about that.

Mr. BUSH. Thank you.

Mr. HERLONG. No further questions?

We thank both of you for your appearance before this committee.

Mr. INTEMANN. Thank you.

Mr. WELLS. Thank you, Mr. Chairman.

Mr. HERLONG. Mr. Robert Burch.

Mr. Burch, for the purpose of the record will you identify yourself and you may proceed in your own way.

STATEMENT OF ROBERT BURCH, ROCKY MOUNTAIN OIL & GAS ASSOCIATION

Mr. BURCH. Thank you, Mr. Chairman.

My name is Bob Burch. I live in Denver, Colo. I am an independent oilman and I am representing the Rocky Mountain Oil & Gas Association.

The Rocky Mountain Oil & Gas Association is an association of substantially all of those engaged in the discovery, development, production, transportation, and refining of oil and gas in the seven-State area comprising Colorado, Montana, Nebraska, Idaho, South Dakota, Utah, and Wyoming. Our membership includes major and independent companies and individuals.

The mandatory oil import program is based upon the congressional delegation of authority to the President set forth in the national security clause of the Trade Agreements Extension Act. This provision of law has but one purpose—the safeguarding of the national security. This authority was exercised to establish the oil import program for the express purpose of maintaining a healthy and vigorous domestic petroleum industry. The Middle East crisis of last summer serves dramatically to remind us of the wisdom of that policy.

The mandatory oil import program has been in effect since 1959. It is our firm conviction that the program has been vital to our national security. We, as an association, have strongly supported the program and have cooperated with the Government to improve its effectiveness.

The stated policy of our association adopted in 1959 and reaffirmed from time to time is to favor the limitation of imports of crude oil and petroleum products to the extent that such imports will not impair our national defense.

Despite the contribution that has been made by the mandatory oil import program, the health and vigor of the domestic petroleum industry has suffered a persistent deterioration since 1959.

Changes have been made in the import program, to serve objectives extraneous to the national security. As a result of the cumulative effect of these actions there is a widespread concern in our association that the program is losing the essential element of long range stability and

incentive for the discovery and development of domestic petroleum resources needed for national security.

This concern led to the adoption of the following resolution on May 18, 1967:

Whereas the mandatory oil import program provides long range assurance of stability and incentives for the discovery and development of U.S. petroleum resources needed for national security, the security of the free world.

Whereas, the Rocky Mountain Oil & Gas Association is opposed to any action which will weaken, undermine or circumvent the said program.

Whereas, applications now before the Oil Import Administration for import quotas to import foreign crude oil and unfinished oils into Puerto Rico, the Virgin Islands, and Guam and to ship unfinished products and unfinished oils therefrom to the U.S. mainland would, if granted, weaken, undermine and circumvent the program.

Whereas, the granting of such applications or similar applications for locations outside the 50 States for special import quotas would threaten the integrity and effectiveness of the whole oil import program.

Now, therefore, be it resolved: That this association stands opposed to the granting of any further applications for import quotas to import foreign crude oil and unfinished oils into territories and possessions, such as Puerto Rico, the Virgin Islands, and Guam, for the purpose of shipping finished products and unfinished oils to the continental United States from any such territories or possessions.

Since the adoption of this resolution many of the applications for special treatments then pending have been granted. Many additional applications for special treatments have been granted and many more are pending.

These special treatments have so circumvented the basic objective as to undermine the program and threaten its present and future effectiveness.

As further evidence of the deterioration of the program, the Department of the Interior recently announced that it had under consideration a proposed system for auctioning oil import licenses. The Rocky Mountain Oil & Gas Association is opposed to such a system.

The problems faced by the domestic segment of the petroleum industry are critical. It is faced with how to reverse the declining domestic exploration effort to provide adequate reserves of oil and gas for our country's needs. The domestic industry is confronted with a constant effort to circumvent the mandatory oil import program. The accumulation of pressures on the executive branch of the Government for greatly increased imports resulting from actions already taken and from applications and proposals for special treatment of individual companies and geographical areas now very seriously threatens the long range stability of the program.

The location where capital formation takes place is generally where the exploration takes place. Therefore, the increase in imported crude and petroleum products removes capital from the domestic exploration effort and lessens the domestic industry's ability to carry on the effort needed for this country to remain self-sufficient in discovered and developed petroleum resources.

Unless corrective action is taken, continued growth can be expected in imports, inconsistent with the national security objective of assuring adequate domestic oil supplies.

Incentives to discover and develop domestic petroleum reserves, including the realistic administration of the import program, are essential to the national interest and security.

If I may make two points that I did not have in my prepared testimony, it seems to me that running through all of these statements that the industry and other people have made they have used a reserve production ratio.

It seems to me that the American consumer, the American public, is more concerned with a ratio that I would call the reserve consumption ratio than they are with the reserve production ratio.

While they are quite concerned with that, the reserve consumption ratio would make our present reserves less than adequate based on the rule of thumb that I understand the Department of the Interior and some other people have used.

In other words, they are trying to use a ratio of something like 7 to 1 or 8 to 1. I think on a reserve consumption basis that we are actually already below that and I think that is what the American public is concerned with.

As you know, we have been called on to provide protection for the free world and I think when the situation is analyzed properly that we need additional reserves not only for our own use but also for the protection of the free world.

I want to thank you for the opportunity of appearing before you and I would be glad to answer any questions.

Mr. HERLONG. Thank you very much.

Are there any questions?

If not, we do appreciate your appearance before the committee, Mr. Burch. Thank you for your contribution.

Mr. BURCH. Thank you.

Mr. HERLONG. Mr. Sergio Camero. We are happy to have you before our committee, sir, and if you will identify yourself and those who are with you for the purpose of the record we will be happy to hear your statement.

**STATEMENT OF SERGIO CAMERO, ADMINISTRATOR, PUERTO RICO
ECONOMIC DEVELOPMENT ADMINISTRATION; ACCOMPANIED BY
ANTONIO COLORADO, EXECUTIVE ASSISTANT, AND JOHN RIGBY,
LEGAL COUNSEL**

Mr. CAMERO. Thank you, Mr. Chairman.

My name is Sergio Camero, I am administrator of the Economic Development Administration of the Commonwealth of Puerto Rico.

To my left is Mr. Antonio Colorado, who is my executive assistant, and to my right Mr. John Rigby, the legal counsel for the Commonwealth of Puerto Rico.

Mr. HERLONG. Thank you. You may proceed.

Mr. CAMERO. Thank you, sir.

Mr. Chairman, members of the committee, it is a privilege for me to be here today and I am here in opposition to pending legislation concerning the limitation of foreign oil imports. In essence, these bills—there are some 47 of them now before you—would contradict the historic “free trade” relationship prevailing between Puerto Rico and the United States since 1900 and reduce or eliminate entirely the necessary flow of petroleum products from insular refineries to the mainland.

Resident Commissioner Santiago Polanco-Abreu will appear here next week to discuss in greater detail the implications of these bills for the political relationship between the Commonwealth of Puerto Rico and the United States. Therefore I will confine myself to the economic consequences, not because I believe politics and economics are mutually exclusive, but because it is my agency's task to develop Puerto Rico's economy.

To propose the reduction or elimination of petroleum product shipments at this stage in Puerto Rico's development is, in a very real sense, to accept responsibility for the survival of a critical segment of the island's industrial economy, and it is to accept responsibility for the jobs and future well-being of tens of thousands of U.S. citizens.

Puerto Rico's refinery and petrochemical industry is neither old nor large by mainland standards. But the availability of a wide range of petroleum products represents the best—perhaps the only immediately feasible—way for Puerto Rico to build a modern industrial economy capable of supplying employment requirements for the next decade.

Investment in insular petrochemical and chemical facilities today totals upward of \$400 million. And here, I want to stress that this is not proposed investment represented by applications for import quotas awaiting approval by the Interior Secretary. This is \$400 million in operating facilities already employing 4,000 persons. In addition, in excess of \$230 million is now committed to new and expanded refinery and petrochemical projects under quota awards granted within the last few months. We hope that within the next 10 years total investment will grow to \$1.5 billion and employment to 60,000 in this sector of the insular economy.

Yet these figures present only a quantitative picture of Puerto Rico's petrochemical industry. They say nothing about the important qualitative factors.

Puerto Rico has struggled for more than 20 years to raise its living standards by building an industrial base for its economy. Until the coming of the petrochemical era in the Mid-1950's, this struggle was waged in the face of the pessimistic prospect that the best the island could hope for was to exist as an appendage of the mainland U.S. industrial system, a sunny Caribbean subassembly plant, modestly prosperous perhaps, but without true industrial potential. Why? Simply because Puerto Rico is an island virtually without natural resources. Without such resources, it is almost impossible to construct a heavy industrial base or to integrate the diverse light industrial sectors through a common denominator of products or services.

Petrochemicals today are Puerto Rico's "substitute natural resources." A single "core" refinery supplying a range of building block chemicals will service a host of satellite plants. Fertilizers, plastics, industrial gasses, fabrics, yarns, shoe materials—these are just a few of the industries now drawing upon local petrochemical sources.

The ability to start with a locally available basic raw material and process it through successive stages to the consumer goods level also multiplies potential job opportunities. A single "core" refinery, though its operation requires only a few hundred skilled technicians, can be responsible for creating thousands of jobs in dependent and related industries. And, of course, the jobs created in the petroleum and petrochemical industry are generally those permitting higher wages and thus upgrade the overall labor force in Puerto Rico.

A modern petrochemical complex in Puerto Rico looks exactly like its mainland counterpart. But there the resemblance ends. Since the oil import program was modified by Presidential order in 1965 to permit additional Puerto Rican refineries, new projects have been tailored to fit increasingly sophisticated and imaginative economic development criteria. The specific terms of the agreements reached between companies and the Commonwealth government vary. But for the companies' part they have included guaranteed investment levels, profit reinvestment, maximum local utilization of outputs, participation by local capital, secondary support facility investment and even contributions to a conservation fund that we have.

Two illustrations of how individual projects represent the sum of many interrelated parts are those of the Phillips Petroleum Co. and Sun Oil Co. in addition to building a \$45 million refinery, Phillips agreed to reinvest all of its profits from the operation over a 10 year period in Puerto Rico. Phillips has already invested \$100 million including construction of a nylon 66 plant as a joint venture with Rhone-Poulenc of France. The first stage of this satellite already employs 1,500 workers with a direct employment potential of 4,500 by 1970. The recently approved Sun project is no less impressive. Sun guarantees to invest \$125 million in facilities. The company will also construct a \$12 million deepwater port near its Yabucoa Valley refinery site on the island's southeast coast. This will give Puerto Rico a fourth major ocean port. Sun will also make available at favorable prices a part of its refinery output so that the Puerto Rico Water Resources Authority can generate low-cost electric power. The port plus the power will hopefully enable the investment of \$150 million in bauxite processing facilities by other companies, thus adding another element to the island's heavy industry.

The Yabucoa Valley, where the Sun project will locate, is a depressed sugar growing area of 40,000 population with an unemployment rate of 30 percent. Thus, it is easy to see why the Sun project will have considerable impact. But the need for more jobs and better paying jobs is chronic throughout Puerto Rico, not just in the Yabucoa Valley. By 1975 we must generate more than 200,000 new jobs if Puerto Rico's unemployment rate is to fall below 10 percent. The rate is now around 12 percent, or about three times the mainland U.S. rate.

The Commonwealth government feels that it is up to Congress and the Interior Department to decide whether the 12.2 percent formula should be enacted into law. The petrochemical projects sought by the Commonwealth, and approved by the Department of the Interior, have been accommodated within the 12.2 percent formula. However, the 12.2 formula can be written into law without raising artificial barriers to "free trade" or damaging Puerto Rico's economy. Amendments proposing such a change—that is, incorporating the 12.2 formula but without destroying Puerto Rico's petrochemical industry—are already pending before the Senate Finance Committee and I hope this committee will give similar language serious consideration in the event it acts on the measures before it.

Successive Congresses under both Democratic and Republican administrations have encouraged economic progress in Puerto Rico be-

cause a prosperous Puerto Rico is an asset to this Nation. It would be self-defeating and contrary to this Nation's best interests to cripple Puerto Rico's capacity to achieve its economic and social goals.

Thank you.

Mr. HERLONG. Thank you, Mr. Camero.

Mr. CAMERO. Mr. Chairman, with your permission I would like to offer for the record an analysis of the petrochemical industry in the overall development of Puerto Rico.

It points out in detail why we have to restructure the island's economy and how we are trying to do it.

Mr. HERLONG. It will be included at this point in the record.

(The analysis referred to follows:)

PUERTO RICO AND ITS ECONOMIC DEVELOPMENT—"OPERATION BOOTSTRAP"—THE
ROLE OF THE PETROCHEMICAL INDUSTRY

Puerto Rico's future economic development for the near and long-range future hinges, to a decisive degree, upon the petroleum and petrochemical industry. Puerto Rico's basic goal is the development on the island of an integrated chemical industry, providing the base for scores of thousands of employment opportunities.

I. PUERTO RICO'S ECONOMIC PROGRESS—AND PROBLEMS

A. A decade and a half of progress (1950-65)

Before reviewing the economic development of the past decade and a half, it is well to note that at mid-century (after 50 years of U.S. sovereignty over the island) "poverty, disease, hunger and insecurity were still the lot of the average Puerto Rican." It is against this reality that the progress made to date must be reviewed.

During the past 15 years our industrialization and tourism promotion programs for which the Economic Development Administration is responsible have been the primary factors underlying the island's effort to reduce unemployment. Population pressures and the paucity of natural resources dictated that these two areas would have to be the keystones of Puerto Rico's effort to raise its standard of living. What we have been able to accomplish to date has been effected by enlisting the technical and financial resources of private enterprise. The limited availability of both of these resources on the island made it necessary that we try to attract them from the Mainland. Economies of scale and the small local market meant that, for the most part, the manufacturer in Puerto Rico would have to channel his output into the Mainland market.

Our first stage of development can be said to have been completed in 1955 when net income originating from manufacturing equaled that generated in agriculture. Most of the new plants attracted during this stage fell into the category of light industry, notably wearing apparel. The next stage was attended by considerable diversification into such industries as metalworking and the production of electrical goods and light chemicals. The apparel industry continued to grow and achieve a degree of integration. Some heavy industries also located on the island in this period (1955-65)—these represented very large investments but did not contribute correspondingly to the opening up of employment opportunities. Nevertheless, so many new plants were establishing that by the end of 1965 employment in manufacturing exceeded employment in agriculture. This can be said to mark the end of our second stage of development and the entry of Puerto Rico into the category of a truly industrialized area.

Since 1956 manufacturing net income has exceeded that generated in agriculture and this "gap" has been widened in each succeeding year. We view this ever-widening gap with mixed emotions because, in addition to measuring industrial progress, it also reflects, unfortunately, severe limitations on the capacity for growth of agriculture. The human dimension of this ever-widening gap between manufacturing and agriculture is appalling—a steady decline in employment opportunities in agriculture which, in turn, requires an intensification of our effort to industrialize.

The gross product of the island rose from an estimated $\frac{3}{4}$ billion dollars in 1950 to over \$2.7 billion in fiscal 1965, an increase of some 260%. Annual per capita net income rose from \$279 in 1950 to \$900 in fiscal 1965, an increase of 225%.

Physical indicators are probably more meaningful measures of economic changes than general economic indicators of growth. Some of the physical changes that have taken place on the island are impressive.

Motor vehicle registrations in Puerto Rico in 1950 were about 60,000; 15 years later the figure was approximately 319,000; a fivefold increase.

In 1950 installed electrical generating capacity in Puerto Rico totaled 140,560 KW; 15 years later the capacity was 743,920 KW.

There were 32,000 telephones in service in Puerto Rico in 1950; in 1965, the number was some 182,000.

Another relevant statistic refers to the island's external trade. In 1950, external trade amounted to less than \$600 million; in fiscal 1965, two-way trade reached \$2.5 billion. Most of this trade is with the U.S. Mainland. In 1966, shipments from the States amounted to \$1.4 billion, making Puerto Rico the Mainland's fifth largest customer—exceeded only by Canada, Japan, West Germany and the United Kingdom. We estimate that these shipments were responsible for some 180,000 jobs on the U.S. Mainland.

B. Achievement during fiscal 1966

During the past year Puerto Rico once again experienced an overall growth rate in excess of ten percent. Gross product rose by some \$317 million and per capita net income rose to \$950, a level exceeded in this hemisphere only by the United States and Canada.

During 1966 Puerto Rico can be said to have entered the third stage of its development. The year marked the coming on stream of significant new ventures in petrochemicals and formulation of plans by private firms for the creation in Puerto Rico of substantial industrial complexes.

Overall, 1966 was a year of substantial economic expansion: some 29,000 new jobs—one-third of them in the island's new and rapidly expanding industrial plants were created; 22,353 new dwelling units were constructed; 15,000 additional telephones were installed; 87.6 kilometers of new highways were constructed; 16,277 new sewer and 26,733 water customers were added to the island-wide networks; electricity was made available to 11,277 additional rural families.

Total external trade expanded by \$325 million; exports to foreign countries rose by 50 percent. An additional 117,000 persons visited the island and visitor revenue rose to \$140 million.

Accompanying these indicators of continued economic growth was an increase in the number of unemployed—the unemployment rate rose by well over a full percentage point. There was also an increase in the number of public welfare beneficiaries.

C. A look into the future (1967-73)

The employment outlook in Puerto Rico for the next five to six years calls for action. Even though net migration to the Mainland rose significantly last year—after five years of stagnation—the island's population increased by 2.2 percent. The formidable dimensions of the task force the development agencies is illuminated by consideration of the number of jobs which would have to be created to reduce unemployment to what might be termed "acceptable" levels by 1970. The Commonwealth's recent Overall Economic Development Program, prepared in response to the program requirements of the Economic Development Administration, U.S. Department of Commerce, reveals that if one assumes that the currently low Puerto Rican labor force participation rates will respond to an increasing availability of jobs, it is then foreseeable that during the second half of the decade it would be necessary to create 343,000 new jobs; some 66,000 jobs annually or slightly over twice as many as have been created annually during the 1960's to date—a period of substantial employment expansion.

The report goes on to state that the computation tends to understate the additional job requirements because no account is taken of the effects that changes in the structure of the economy, higher wages, and improved productivity will have on the number of existing jobs.

Since October 1960 industrial wages in Puerto Rico have increased at an annual rate of 5.6 percent largely as a result of legislative and administrative pressures on the wage structure. The immediate outlook is for an accelerated rate of increase, as a result of the implementation of the 1966 amendments to the Fair

Labor Standards Act which will increase manufacturing payrolls in Puerto Rico by some 14 percent within the next twelve months (as minimums are raised by 12 percent in April 1967 and an additional 16 percent one year later). The U.S. Secretary of Labor's recent decision to deny appealing Puerto Rican industries legislatively provided-for relief presages even greater job losses than had hitherto been anticipated.

Other factors which will adversely affect the level of existing employment and the future rate of industrial growth include the expiration of tax exemption grants which, given the provisions of the U.S. Internal Revenue regulations, require firms to liquidate their operations on the island in order to maximize their benefits from the tax concessions granted by Puerto Rico. Over the next four years the tax grants of 216 concerns, currently employing some 19,000 persons, will expire. In the following three years, by 1973, an additional 218 firms, with 21,000 employees, will lose their tax-exempt status. Unless the current peculiarities in the U.S. tax regulations are satisfactorily resolved a large number of these enterprises will probably be forced to abandon the island leaving behind them a small army of unemployed.

Probably Puerto Rico's gravest social problem is the under-utilization of its human resources; a matter of the gravest concern given the extreme youth of its population and the resulting high number of dependents for each citizen who is actively employed.

A staff paper prepared for the U.S.-P.R. Commission on the Status of Puerto Rico makes the following relevant observations. "During the past 20 years, between 3 percent and 7 percent of the members of the U.S. labor force have been totally unemployed. These unemployment rates are higher than in most of the developed countries but far below those prevailing in Puerto Rico. Underemployment rises and falls along with unemployment, thereby compounding its effect on output."

"... Since the 1920's, when Puerto Rico's land resources were sufficient to provide subsistence to those who could not be more productively employed elsewhere, the Island has never known even nominally full employment of its human resources. According to the conventional labor force statistics, unemployment in Puerto Rico has been roughly three times higher than in the United States, ranging between 11% and 16% of the labor force ever since 1948. The degree of under-utilization of human resources in Puerto Rico, or in any other undeveloped country, cannot be adequately measured, however, by the methods appropriate for advanced economies. In the more backward of the under-developed countries, the concept of 'looking for work', a key element in conventional labor force statistics, is practically meaningless. . . . [Rather] to measure the true extent of unemployment in an economy where it is chronically high, there must be a more stable concept of labor force from which to subtract the recorded figures of employment."

"The key assumption made in calculating the labor force base . . . is that, if work were available, Puerto Ricans in each specific age and sex group would be working or looking for work, in the same proportionate numbers as in counterpart age and sex groups in the United States. This is statistically equivalent to assuming that, except for differences in the age and sex structure of the population, the overall labor force participation rate in Puerto Rico would be the same as in the United States, *if jobs were available*. This assumption cannot be verified because nowhere in Puerto Rico have there been enough job openings to test it pragmatically. There is, however, substantial evidence in its support."

On the above premise, the author proceeds to calculate that in April 1960 Puerto Rico had a total numerical job deficiency of 243,000 (and in April 1965, despite a sizable increase in jobs, the deficiency had nevertheless increased to 263,000). The conventionally calculated unemployment estimate for April 1960 was only 56,000. The 1960 calculation shows a job deficiency equal to 30 percent of the calculated labor force. "This approximate measure of true unemployment is eight times greater than the current rate of unemployment in the United States and considerably above the highest rate of unemployment ever recorded during the depths of the great depression of the 1930's. There is perhaps no area within the United States that has ever experienced a period of unemployment of comparable duration and severity." Nevertheless, even conventionally computed unemployment estimates show several labor market areas within Puerto Rico with unemployment rates in excess of 20 percent. This demonstrates why a major objective of the Commonwealth Government must continue to be industrial decentralization.

II. NEED FOR RESTRUCTURING THE ECONOMY OF PUERTO RICO

The essential effect of Puerto Rico's industrialization efforts over the past fifteen years has been to restructure Puerto Rico's economy—from an agricultural economy to a diversified economy. In fiscal 1950, 36.3% of Puerto Rico's jobs were in agriculture; 17.8% of Puerto Rico's jobs were in manufacturing. By 1965, manufacturing employment for the first time surpassed employment in agriculture. By 1965, employment in plants sponsored by the Economic Development Administration of Puerto Rico had reached 71,000—and is was up to 84,000 in fiscal 1966. These increases in manufacturing employment opportunities had, by 1966, served to offset the losses in employment opportunities in agriculture.

While pursuing industrial development, the Commonwealth Government is by no means abandoning agriculture. As stated by Professor Gottfried Harberler of Harvard University:

"It is true there may not yet exist an underdeveloped country that is highly industrialized. It is an extremely important fact that there exists no highly developed country that has not also a highly developed agriculture . . .

"The fact that in developed countries not only industry, but also agriculture, is more highly developed than in under-developed countries lends further weight to the warning that development policies should not concentrate exclusively on industry." *

The Commonwealth Government is, therefore, pursuing vigorously the development and improvement of the island's agriculture. This is necessary to provide sufficient food production at home to reduce rapidly rising and costly import demand. This effort is necessary to boost exports of processed and unprocessed farm products, and thereby further contributing to absorption of surplus labor. This effort is, in sum, needed to raise employment and living standards in Puerto Rico's more impoverished areas.

But Puerto Rico's agriculture cannot be the mainstay of the island's economic growth, for several fundamental reasons:

Cultivable land is scarce.

Soil has been depleted.

Necessary capital investment funds simply do not flow into agriculture in sufficient amounts.

Prior to World War II, Puerto Rico's economic development was, in fact, directed primarily at exploitation of natural resources, with sugar, of course, as "King." In the late 1930's, most people—including technicians and policy makers—still believed that agriculture was the key to Puerto Rico's development. Even during the formative years of "Operation Bootstrap"—from 1950 to 1965—Commonwealth Government appropriations for agricultural development exceeded those for industrial development by about \$13 million.

As a result of Puerto Rico's efforts in agriculture—and while much work remains to be done—the fact is that the island's agricultural resources have to a large degree been exhausted as far as major employment opportunities are concerned. For example, Puerto Rico has more of its land in farms, more of its farmland in cropland, more agricultural net income generated per acre either in farmland and cropland, and more employment per acre of farmland than does the United States. Yet while mechanization of Puerto Rico's agriculture has caused rising productivity within limited farming areas, it has also caused a decline in employment in agriculture—from 214,000 in 1950 to 124,000 in 1960, and down to 110,000 in 1966. It is expected that the decline in agricultural employment in Puerto Rico will continue, and that the total number of workers employed will not exceed 100,000 by 1975. Income per farm worker should then be substantially higher, but for an island-wide labor force that will then be in the neighborhood of one million people, agriculture can provide only a small and relatively inflexible part of the total employment opportunities required.

Other natural resources of the island are even more limited than farmland. Much of the interior is wooded, but it is mostly second-growth timber, having been cut over for fuel. So far, no substantial forestry operation has proven economically feasible. Similarly, the waters around Puerto Rico have not proved suitable for large-scale commercial fishing. There is a relative abundance of clays, sands and stones, but they can serve as a base for relatively few export products. And their use will probably expand at about the same pace as the

**International Trade and Economic Development*, National Bank of Egypt, Fiftieth Anniversary Commemoration Lectures, Cairo, 1959.

economy as a whole. Metallic minerals exist, but no deposits are known to be commercially exploitable. An exception is found in two deposits of copper around which efforts now center to develop a copper mining and fabricating complex to provide employment for, hopefully, up to 4,000 people.

Of Puerto Rico's known physical resources, only its combination of fine weather and beaches seems capable of supporting expansion of a large primary industry. External tourism has been one of the most rapidly advancing sectors of the economy, and it seems likely that its growth will continue. But among the sectors of the economy on which economic growth is so dependent, tourism still accounts for *only 6.5 percent of total Commonwealth gross product*, only about one-eighth as much as manufacturing. Employment in Puerto Rico attributable to tourism is less than 10,000 jobs.

The Commonwealth of Puerto Rico is by no means so poorly endowed that an adequate level of living cannot be achieved for its people. Its resource limitation implies, however, that Puerto Rico must bring from abroad—mostly from the United States—the full range of materials and products it needs. To pay for these, it must be able to produce and ship out a necessarily much narrower range of products but in comparatively larger volume. Its shipments of agricultural and industrial products, and its income from non-resident tourists, must be of sufficient value to pay for the thousands of products that cannot be efficiently produced locally but which are needed for an adequate level of living. Thus, the development strategy for the Commonwealth of Puerto Rico *must* be specialization in the crops, products and services in which nature or man-made conditions give production in Puerto Rico a cost advantage in its own or other penetrable markets.

The significant growth of the Puerto Rican economy during the last 15 years is, of course, attributable almost entirely to the fourfold increase in the value of merchandise shipments out of Puerto Rico, mainly to the continental United States. The investment needed to produce this export increase also came mostly from the United States. Thus, a penetrable "outside" market, plus an inflow of investment funds, had enabled and has largely financed a fourfold expansion of total production—destined for use or consumption outside Puerto Rico. This, in turn, has financed an approximately equal expansion of merchandise shipments into Puerto Rico originating in the Mainland, and results in more than a tripling of the economy as a whole.

The factories which have to date been responsible for Puerto Rico's economic development are not a cross-section of manufacturing in the United States. They are concentrated in industries in which production and distribution from Puerto Rico can be at a lower cost than in competitive areas in the United States. Their characteristic difference is that they are concentrated in the production of nondurable goods, especially apparel and foods, where comparatively low wages are paid even in the United States. Except for petroleum and stone, clay and glass products, every industry group in Puerto Rico with a greater concentration of employment than in the United States is a relatively low wage industry in the United States as well as in Puerto Rico. This partly explains the vulnerability of most Puerto Rican manufacturing industries to the wage increases that are necessary to provide an adequate standard of living. At the same time, many industries that are of great importance in the United States manufacturing scheme are entirely absent from Puerto Rico. Among the durables, there are many absentees including all smelting and refining of metals. Lack of these basic metal industries largely accounts for other "absentees" from Puerto Rico's industrial base, such as ordnance, autos, aircraft and many other heavy machinery and fabricating industries.

The heavy and more highly technical industries which abound in the States typically pay higher than average wages. They require more fixed capital per worker, and thus may be considered more permanent than the light industries in which Puerto Rican employment has been concentrated. Throughout the world, metal-based heavy industry is concentrated where ores and usually coking coal are also concentrated. Petroleum, however, may be shipped economically over greater distances. Petroleum refining and related chemical industries are, except for a few industries based on locally available raw materials or scrap materials, the only heavy, capital-intensive industries which are demonstrably feasible in Puerto Rico.

The Commonwealth of Puerto Rico now has a higher concentration of employment than the continental United States in only two basic industries: oil refining, based on imported petroleum, and cement manufacturing, based on local

limestone. The cement industry has limited possibilities for forward integration and a limited export potential. Petroleum and petrochemicals provide Puerto Rico's main hope for the development of a heavy industry base which can be integrated forward through fibers and plastics to support the existing light industry concentrations in apparel and plastics fabricating.

III. PETROLEUM REFINING AND PETROCHEMICALS; PROGRESS AND PROBLEMS

A. Initial promotion of petroleum refining and petrochemical facilities (1950-55)

At the time of the establishment of the Economic Development Administration Puerto Rico had neither petroleum refining capacity nor facilities for the production of synthetic organic chemicals.

Demand in Puerto Rico for petroleum products at that time amounted to approximately 14,400 b/d broken down as follows:

Product:	Quantity (b/d)
Gasoline -----	5,300
Kerosene -----	1,700
Distillate -----	800
Residual -----	6,400
Other -----	200

It is relevant to note that the 1950 makeup of product demand in Puerto Rico differed markedly from that on the U.S. Mainland. In the former case demand for heavy products amounted to 46 percent of the total while in the latter case the comparable percentage was 25 percent.

Satisfaction by source of local demand for petroleum products in 1950 was governed by the import tax structure of the U.S. Internal Revenue Code: heavy materials were imported into Puerto Rico from foreign Caribbean sources; light products were shipped into Puerto Rico from the U.S. Mainland.

An early and prime objective of the Commonwealth's development effort was the promotion of petroleum refining capacity in Puerto Rico. The fruits of this effort were establishment of the Caribbean Refining Company and of the Commonwealth Oil Refining Company. The plant of the former company came "on stream" in May 1955; that of the latter in December 1955.

The early promotional efforts of the Commonwealth Government in this area are relevant to present purposes for two reasons.

The first of these reasons is derivative from the composition of petroleum product demand (noted above) as it existed in Puerto Rico in 1950. Should this demand have been viewed in isolation (which it was not) it would probably have suggested promotion of a "topping" plant involving an investment of, say, \$1,500,000. Instead, however, the basic concept was that of a common Puerto Rico-U.S. Mainland market (free movement of goods, capital and persons) which would warrant investment in refining capacity to produce a full range of the major refinery products: production of any product in excess of local demand would be shipped to the U.S. Mainland.

The second of the reasons concerning this early and prime promotional effort of the Commonwealth Government which is relevant to present purposes relates to the importance which government attached to this promotional activity. The best measure of a sense of urgency and importance in this context is a willingness to commit resources to the purpose at hand; in this case scarce governmental financial resources.

In the matter of such a commitment outside, expert advice, contracted for by the Commonwealth Government recommended caution, delay and, in effect, inaction. Despite this, the Commonwealth Government made the largest single financial commitment it has ever made to an industrial facility to bring into being the first petroleum refinery in Puerto Rico (the governmental line of credit established was 50 percent of the estimated cost—\$12 million—of building the refinery of the Caribbean Refining Company).

The interest of government in local production of synthetic organic chemicals dates from this early period of the Economic Development Administration and is also attested to by the fact of the willingness on the part of government to commit scarce resources to such an end.

Specifically, the Government Development Bank and the Puerto Rico Industrial Development Company subscribed to bonds in an amount of approximately \$5 million which made possible the construction of a synthetic ammonia plant

(González Chemical) at Guánica, P.R., with an initially estimated total plant cost of slightly in excess of \$12 million. As a consequence of production and marketing difficulties which need not be detailed here these government investments in González Chemical subsequently had to be written off as a total loss. However, the plant continues to be operated under different management (1960) primarily as a consequence of government intervention directed at keeping the plant in production.

B. Great expectation and crises (1956-60)

The beginning of the second half of the decade of the 1950's was one of great expectations in government circles in the matters of growth both of petroleum refining and petrochemicals production (for a concrete expression of these expectations see the annexed paper (1957) titled: "Puerto Rico's Industrial Future"). Both refineries were "on stream;" the fertilizer plant of González Chemical was under construction; Commonwealth Oil was engaged in the doubling of its facilities based primarily upon a long-term (20 years) supply contract with the Union Carbide and Carbon Corporation.

A series of events demolished these expectations. In chronological order these events were as follows:

First, Commonwealth Oil experienced severe start-up difficulties (1956-57) with consequent heavy financial losses.

Second, González Chemical experienced severe start-up difficulties (1957-58) with consequent heavy financial losses.

Third, the U.S. Government instituted mandatory oil import controls (1959).

Fourth, Union Carbide's investment at Peñuelas, P.R., was jeopardized because of the fact that Commonwealth Oil was able to supply only a fraction of the feedstock required by Carbide (1959).

Government's responses to these several developments were as follows:

First, the Government Development Bank and the Puerto Rico Industrial Development Company extended three lines of credit aggregating \$3¼ million in an effort to prevent the threatened insolvency of the Commonwealth Oil Refining Company.

Second, the Government Development Bank and the Puerto Rico Industrial Development Company waived their rights as bondholders in González Chemical so that emergency financing could be obtained to keep the plant in operation.

Third, in the matter of mandatory oil import controls the Commonwealth Government sought recognition of the fact that, both for reasons of geography and a lack of indigenous natural resources, Puerto Rico should be established as a wholly separate importing district.

In summary, the second half of the 1950's which began as a period of great expectations in fact turned out to be a "salvage operation" by government so far as petroleum refining and petrochemicals production were concerned.

C. Laying a foundation for growth (1961-65)

During the first half of 1961 three things became apparent.

First, Commonwealth Oil's financial solvency was assured.

Second, continued operation (though only marginally attractive financially) of the fertilizer plant (now known as Caribe Nitrogen under W. R. Grace management) at Guánica, P.R., was assured.

Third, with the active cooperation of the Interior Department's Oil Import Administration, a "permanent" solution to Carbide's feedstock problem was in sight: creation of a foreign trade sub-zone which would enable Carbide to execute the necessary long-term supply contracts for importation of naphtha from the foreign Caribbean area.

With these problems resolved and/or in process of resolution the Commonwealth Government (second quarter of 1961) began to work actively in an effort to realize, at least partially, the great expectations of five years earlier. This effort became known, colloquially, within the Commonwealth Government as the "third refinery project." That is, Puerto Rico's economic growth could be greatly stimulated if the ban on entry of new refiners into Puerto Rico could be eliminated.

Specifically, the effort, which lasted some 2½ years, was concentrated on identifying someone prepared to invest in an unconventional refinery—one which would maximize the output of basic petrochemical streams. Discussions were held with representatives of many companies, oil and chemical, culminating in early 1964 with the formal endorsement by the Commonwealth Government of the project of the Phillips Petroleum Company.

Meanwhile, numerous discussions were taking place between government representatives and representatives of the two existing local refining companies looking toward development of plans by them for production of petrochemical streams. The position (1964) of Gulf Oil was that the firm had no plans for production of petrochemicals in Puerto Rico. The position at the same time of the Commonwealth Oil Refining Company was that it was going to enter the petrochemicals field. This decision was taken in the absence of a commitment by the Commonwealth Government to endorse any oil import quota request which the company might see fit to file.

To summarize, the foundation for growth of an integrated petrochemical industry was "triggered" by decision in 1961 of the Commonwealth Government to promote the "third refinery project" and reinforced by the decision of Commonwealth Oil to commit substantial sums for chemical production.

IV. DEVELOPMENT OF AN INTEGRATED CHEMICAL INDUSTRY IN PUERTO RICO (1966-1972/73)

The basic objective of the Commonwealth Government in matters of petroleum refining and production of basic petrochemicals during the next 5-6 years is development in Puerto Rico of an integrated chemical industry. What precise content can be given to this highly generalized objective?

First, it means the strengthening of our weak industrial base for the purpose of overcoming what now appears to be an intractable unemployment problem.

Second, it means maximizing the integration potential of existing and prospective producers of basic petrochemical streams. We visualize the desirability of an exchange of streams as among the existing and proposed petroleum refining and petrochemical plants in Puerto Rico. Such interchanges as we visualize pose difficult but, we hope, not insoluble problems of effecting the necessary contractual agreements.

Third, it means maximizing the further fabrication on the island of basic petrochemical streams.

Fourth, achievement of the objective stated immediately above will in turn require promotion of inorganic as well as organic chemical operations. Specifically, our first priority in this area is promotion of a substantial chlorine-caustic soda industry.

Fifth, achievement of an integrated chemical industry in Puerto Rico during the next 5-6 years will require an increase in imported feedstocks. The basic requirements are now embodied in applications pending before the Department of the Interior. The dimension of this increase can and, we hope, will be reduced to the extent that integration among the producers of basic petrochemicals in Puerto Rico can be maximized.

Mr. HERLONG. Are there questions? Mr. Bush.

Mr. BUSH. Mr. Camero, I feel very much about your testimony as I did about Congressman Matsunaga. It is an excellent presentation representing your area, your Commonwealth; and certainly you have highlighted the tremendous economic problems that you have there.

However, the thing that troubles me that I would just like to ask a question or two about is, in terms of national policy to this country, does it make sense to take a program whose basic justification lies formulated upon the concept of defense of this country and the vital necessity of a strong domestic oil industry in this country, and then use that program for social or economic goals no matter how justifiable. My question would be, suppose we just eliminated the oil import program; do you think that under that condition any refinery would make the kind of deal with you that they have done or do you think the program should be kept on and then have it used as a mechanic through which to further the economy of Puerto Rico on a special interest basis? That is a rather complicated question, but you know what I mean.

Mr. CAMERO. I understand, sir. First of all, I don't think that Puerto Rico would want to propose anything that in any way, shape, or form would weaken our national security structure.

The second point that I would say is: Yes, since we have a tool which we have been using successfully within this 12.2 accommodation that, at the same time, has been providing the security that we are concerned with; and, at the same time, helping your 2.7 percent fellow citizens in Puerto Rico to lift themselves up by the bootstraps, that this should be used for this purpose; yes, sir.

Mr. BUSH. The only question I have is this. If we are going to be lifting up our 2.7 percent fellow citizens—which I think we have to do something about—the question I would raise for the committee's consideration is whether the way to do it is through jimmying it around, as I would call it, the existing oil import program.

You mentioned for example, several incentives or several collateral advantages to Puerto Rico that come from granting Sun, Phillips, and some of these companies the right to do this, you see.

I am wondering just how did that work out. You mentioned that there is a deal with one company which agreed to build a harbor over there.

Mr. CAMERO. That is correct, sir.

Mr. BUSH. One you said gave money to a conservation fund. Who negotiates that? Does the Secretary of the Interior say, "Look, Phillips, if you build a harbor or conservation program, we will give you a loophole through which you can import oil"? How does that work?

Mr. CAMERO. First of all, I don't think that Puerto Rico is using loopholes. Nor do I think that we have used any kind of gimmickry. I think we have used the tools at our disposal.

Mr. BUSH. I am not criticizing what you are doing. I am saying: Should we on this committee take a fresh look at it and recognize that there is a subsidization for Puerto Rico, clean up the program, and then go about the Puerto Rico situation in another way?

I think you would agree that there is a special interest here. Could you answer the question for me?

Let's take the harbor deal for example. Who negotiated that deal? Was that at arm's length between Puerto Rico and the oil company, or did the Secretary of the Interior come into that? How did that work out?

Mr. CAMERO. This was arm's length between the Commonwealth and the oil companies.

Mr. BUSH. In other words, this wasn't an incentive to the Secretary. The Secretary of the Interior had absolutely nothing to do with this special arrangement; is that correct, sir?

Mr. CAMERO. Well, I think that the Secretary of the Interior looks at an overall picture and has been conscious of the creativity that we must have in Puerto Rico in order to eliminate this poverty that we are in right this moment, this unemployment problem. I think these are facts that enter the picture.

Mr. BUSH. Would you say, "Look, Phillips, if you want to go into Puerto Rico I would suggest to you that you go down there and negotiate a deal and do something about poverty at the same time"?

I am not clear on these various incentives. Normally I have never found business people overly excited about—just for no reason, for just the good of their hearts, dealing in a tightly competitive business as this is, being willing to build the harbor and so forth.

Go over to the Middle East for a minute. When you build over there part of the action is you have to build the hospital. It is put into the deal. I am not clear on how these collateral advantages are developed between Phillips, the oil company, and Puerto Rico, and what role the Interior Department played.

Mr. CAMERO. I think this is part of our negotiating process and I think possibly the Interior Department entered it. I am new in this, but I will say, yes, I know that any company doing this will do it with a profit motive in mind.

Mr. BUSH. And they should.

Mr. CAMERO. At the same time our Commonwealth government has as its main interest to eliminate poverty and increase employment.

If we can negotiate ourselves into a beautiful position with a company by having them help us with a harbor that will be used for multipurpose later on, we feel that without hurting the security of the United States and at the same time being able to do for us by using of tools that are at our disposal, it is much better than having to be down there sitting there taking handouts.

Mr. BUSH. I commend you for that. You have my admiration and gratitude because you have taken a project and done wonderful things for your people in this area. I think this is fantastic. The thing we have to consider is: Is this to the best interests of all the American people?

I understand that the companies get foreign tax credits for some of this work there and that, therefore to the degree that they get a foreign tax credit for operating in Puerto Rico, we are paying for it.

I am paying for it, Mr. Conable is paying for it, all the American people are paying for it.

My basic question is, Mr. Chairman, whether this program should be used as a social program. I just want the record to be very clear that these gentlemen are doing what they should do, they are trying to better Puerto Rico.

My question is, is there a better way to do it? Should it be done directly rather than through this indirect use of a national defense program really to be used for social purposes? Are we kidding ourselves or are we concealing various things when we permit this?

I would predict, sir, that if an import program were eliminated and this was on a pure economic basis people wouldn't build refineries in Puerto Rico. The only question I raise is, is this the way to do it?

Mr. CAMERO. Possibly not, but if we recall back in 1955-56 we started our first refinery from Puerto Rico and didn't ask for this import program.

The next thing that is very important here is that when this thing started out in 1959 we were actually frozen. We were actually frozen until 1965 when by this proclamation we were able again to start developing our petrochemical industry.

What I am saying in essence is that we have had anywhere from 33 percent to 32 percent unemployment for 7 years without being able to do anything because of this freeze that we had during that time. I say

that before we had an oil industry. Maybe we would have had one anyway. Maybe not. I don't know.

Mr. BUSH. Mr. Chairman, the only thing I hope we have brought out is the basic philosophical question that this committee should among many others address itself to. That is should the program be used as a social and worthy job program in this very important area of Puerto Rico or should it be a uniform program—that was the dialog I was trying to develop with Mr. Matsunaga; not that he doesn't have a problem, but should it be uniformly used—and then address ourselves to these inequities and these terrible problems faced here. Thirty-two percent is fantastic. If any one of our States were that high we would be desperately trying to solve it but I, for one, question whether the program should be used this way.

I have had this feeling and I think you have allayed my fears a little but not altogether that a great deal of this is done by the Secretary of the Interior, well intentioned as he is, but I am not sure that this should be a tool for social reform.

If it is, I think we ought to define it and get it out in the open and spell out the ground rules so that everybody who has a poverty problem could participate. I don't want the record to show lack of concern for Puerto Rico.

Mr. CAMERO. Thank you very much, sir. I appreciate that very much. I simply say if to arrive at in Puerto Rico what we are trying to do you have other ideas that you can legislate to help us to change the name of this thing, I have absolutely no objection.

On the other point, we bring the companies into Puerto Rico. We take them up to the Interior Department and we do the basic negotiating.

Mr. BUSH. But they give you something that nobody else has. They give you an advantage over any other, they give you the quota, and that is the bargaining. That is the power you have. So it is a key thing.

I commend you for your fantastic trading ability. I wish when I was in business I had you with me.

Mr. CAMERO. I wouldn't complain about that myself. Thank you, sir.

Mr. HERLONG. Mr. Utt will inquire.

Mr. UTT. You refer to the Phillips agreement to reinvest their profits for 10 years.

Mr. CAMERO. That is correct, sir.

Mr. UTT. Were they given a 10-year income tax or tax concession in Puerto Rico in exchange for plowing back the profits?

Mr. CAMERO. No, sir; 17 years.

Mr. UTT. What.

Mr. CAMERO. No, sir; 17 years.

Mr. UTT. 17 years.

Mr. CAMERO. Yes, sir.

Mr. UTT. That they don't have to pay taxes.

Mr. CAMERO. They don't have to pay taxes.

Mr. UTT. During that time were you not shipping several thousand barrels of refined gasoline into the west coast of California for the purpose of breaking the price of gasoline in California?

Mr. CAMERO. I am not an expert on that. I will ask my attorney to answer. It was the Commonwealth Co. that was involved in sending to California. If the Congressman would like I will pass the question to my attorney Mr. Rigby.

Mr. UTT. It was what company?

Mr. RIGBY. Commonwealth Oil Refining Co. gasoline to the west coast to district V. I don't know their motives.

Mr. UTT. Did they also have a tax concession?

Mr. RIGBY. Commonwealth Oil does have a Commonwealth Government tax concession, that is correct.

Mr. CAMERO. Let me add something.

I should say that Commonwealth had because their area was 12 years and it is over, sir. They are paying taxes now.

Mr. UTT. The thing that I am questioning is the use of a tax concession to send a refined product into the continental United States which was used for the purpose of breaking the price of gasoline.

Mr. CAMERO. I don't know what their motive was for sending it to the United States, sir.

Mr. UTT. I think that is something that we ought to know and that there should be a supplemental statement on that.

Are you still sending refined products back into the United States from Puerto Rico?

Mr. CAMERO. Oh, yes, sir. There is a certain amount being sent back to the United States.

Mr. UTT. How much?

Mr. CAMERO. Within this 12.2. I think it runs less than 5 percent. It's approximately 50,000 barrels a day which is about 5 percent.

Mr. UTT. I know if I were a domestic refiner I would be a little unhappy with the Commonwealth of Puerto Rico sending subsidized merchandise into the United States in order to compete with the other companies.

That is all I have, Mr. Chairman.

Mr. HERLONG. Are there any further questions?

If not, thank you so very much for your appearance before the committee. We appreciate your cooperation and your contribution.

Mr. CAMERO. Thank you for this honor.

(The following telegrams, letters, and statements were received, for the record, by the committee:)

July 8, 1968.

Congressman WILBUR MILLS,
Chairman, House Ways and Means Committee, House of Representatives,
Washington, D.C.:

Let me urge favorable consideration of bills limiting import of oil and especially those which will set 12.2 percent ration into law. I am convinced that we must provide adequate assurances of domestic oil for national security and this can only be accomplished under a stabilizing program as offered under the present bills before your committee. Our country must in order to prepare for the future know the quantity and location of its oil reserves. Without this knowledge, our position is weak and our potentialities are unknown. The oil industry needs this law in order to fully serve our Nation.

Sincerely,

ALBERT P. BREWER, Governor.

STATEMENT OF HON. ROBERT B. DOCKING, GOVERNOR OF KANSAS

PRODUCTION DECREASE

The oil and gas industry problem in Kansas is manifested in many ways. One of the most striking ways that the problem can be shown is to review the trend of production in Kansas. Kansas' production in 1956 was 124,204,000 barrels. In 1967 it was 99,199,810 barrels, for a percentage decrease of 20.13% for the 11 year period. Even since 1964 the production has dropped from 106,252,025 barrels to its present level. This is approximately a 6.6% drop in production per year in just three years. In fact, production has dropped off so much that Kansas produced 8,386,190 barrels less in 1967 than it did in 1950.

Another very graphic example of the reduction of production in Kansas is the decline in the number of producing wells in the state of Kansas. In 1964 there were 48,297 producing wells, whereas in 1967 there were only 46,125. This constituted a decrease of 2,172 wells or a percentage reduction in the number of producing wells of 4.5% in three years.

This would indicate a reduced daily production capacity for the state of Kansas, and the figures bear out such an indication. In 1964 the average production per day throughout Kansas was 290,306 barrels while 1967's average was 271,780 barrels. This is a decrease in the State's daily production average of about 6.4%.

RESERVE SHRINKAGE

The figures just related become even more impressive when they are correlated with the decrease in the amount of proven crude reserves. In 1964 Kansas possessed 796,541,000 barrels of proven crude oil reserves. On December 31, 1967, it possessed 625,121,000 barrels. This means that Kansas' capacity to support the nation in a time of emergency has been reduced by 171,420,000 barrels of oil in three years under a program designed to accomplish the opposite result.

EXPLORATION CURTAILMENT

The exploration for oil is to say the least a high risk venture. By way of illustration the percentage of successful wildcat wells in Kansas last year was about 16%. The number of wildcat wells completed in 1964 was 3,131 while the number completed in 1967 was 2,572. This reflects a decrease in exploration of 559 wells.

Another persuasive and valid index on the future outlook of the industry is the development that oilmen are undertaking on present fields. That is, how many pool and service wells are being drilled. In 1964, 2,182 pool and service wells were drilled. This number decreased until in 1967 when only 1,748 were drilled.

A third set of figures dramatizing the problem of the oil industry in Kansas is that of rig activity. In 1964, the oil industry had 87 rotary rigs active in Kansas. On June 17, 1968, there were only 32.

All of the above analysis points to one conclusion. That is, that there is still oil to be found and developed in Kansas but that the oil industry is slackening its efforts to find it. Why? The reason must be economic. This must be so as the State of Kansas has certainly not dissuaded exploration and development.

STATE REMEDIAL ACTION

The State of Kansas has always recognized the problems inherent in the industry in question. It is interested, as a state should be, with the conservation of its wealth and the development of this wealth so that the maximum may be gained by it.

As an example of Kansas' efforts along this line, it was noted just recently in the Oil and Gas Journal that at a meeting of the Interstate Oil Compact Commission—

"Jack Graves, General Counsel of the Kansas Corporation Commission, said that compulsory unitization of oil fields is working well in the state under a law adopted last year. There are seven units operating under the new Kansas law. They are expected to result in the production of an extra nine million barrels of oil and eight million Mcf of gas."

Kansas continually supervises its oil industry with the thought in mind of how most economically and feasibly it can develop its wealth.

PRODUCTIVE CAPACITY

A continuation of all of the aforementioned circumstances has resulted in the State of Kansas declining from its traditionally fifth place in the nation in the production of oil. This fifth position was held until 1959 when Kansas fell to sixth and finally arrived at its present position of being a weak seventh. In ten years, in spite of Kansas' arduous efforts, the production has fallen from around 340,000 barrels a day to a present approximate 260,000 barrels.

INCREASED DEMAND

An argument might be advanced that the productive capacity fall off in Kansas is due to reasons other than economic. I would take issue with such a contention. As a basis for disagreement, I would point out that the oil is there. It just has to be discovered by people willing to accept a sixteen percent success rate.

Now the reasons for this failure to keep Kansas' reserves up must be attributed to facts such as the price index of oil being at the same level as it was in 1957, while the price index of tubular goods has risen from 1.000 to almost 1.200.

Another indication that the problem is economic is reflected in the demand for oil in Kansas that existed in 1964 as contrasted against that demand in 1967. In 1964 Kansas produced 106,252,025 barrels and imported 40,575,900 barrels. During that year Kansas used 110,877,265 barrels and exported 35,950,660 barrels. In 1967 Kansas produced 99,199,810 barrels and imported 49,231,817 barrels. Of this amount the State used 129,414,517 barrels and exported 19,017,110 barrels. These figures reflect that in three years Kansas' oil needs have risen 14%, its imports have risen 17.6%, its production has fallen 6.6% and its exports have decreased 47%.

FOREIGN COMPETITION

It is obvious that the cause for our situation is economic, resulting from inadequate incentive due to a price structure affected by foreign oil. For example, the 1957 price of \$3.07 per barrel to a low of \$2.92 per barrel during 1964, 1965, and 1966. Only recently has the price returned to the same level that prevailed in 1957.

One basic reason is the number of exceptions that have been granted to the ceiling percentage of 12½% placed on crude oil imports. These exemptions have brought about a situation where the United States imports 250,000 barrels daily more than it would have had the ceiling not been subjected to these exceptions.

NATIONAL SECURITY

Extrapolating the figures and trends indicated thus far it would appear that these exceptions negate the reason for the ceiling on imports. This influx of oil has driven and will drive the yearly production down. It tampers with the initiative of the oil industry as regards their exploring and seeking out new sources of oil. This has resulted and will continue to result, in a steady decline in known reserves.

Only by aggressive exploration can we reverse the trend toward declining reserves. The reversal of this trend is imperative if our nation is to avoid the peril of being subjected to the whims of the possessors of foreign reserves. The security of our nation should not and cannot depend on externally made decisions.

KANSAS LABOR AND TAX PROBLEM

Not only does the United States have a problem with the program under discussion, because of the national security question, Kansas has a problem with it in that it affects the state collaterally. Mainly, Kansas is affected because of the decrease in production but so also, is the State's labor market and tax base.

In 1960, Kansas had 19,600 employees in the petroleum industry. As of May, 1968, it had 13,400. This is a 38.6% drop in this area of the Kansas labor market.

Concomitant with the decrease in the employment is the steady decrease in the assessed valuation of oil and gas in Kansas subject to the ad valorem tax. In interpreting these figures I would like to point out that they contain both oil and gas valuation, and that the valuation of gas has remained fairly constant in the last few years.

From a period starting with 1957 and ending with 1964, the assessed valuation of oil and gas decreased 8.3%. This decrease was in the face of a gas production

increase during that time of approximately 28.4%. This trend continued as is shown by the fact that in 1965 there was a further decrease of 2.1% and in 1966 the decrease was 11.9%. In 1968 there was a \$75,355,401 increase but this was due to a required reassessment.

My concern is exemplified by the fact that the valuation of Kansas oil and gas dropped 35 million dollars in one year and by the fact that in 7½ years 6,200 jobs have been lost.

CONCLUSION

For these reasons, I would ask this committee to assist the domestic industry to get the domestic production of oil back into such a position that the trend is toward a self-sufficiency in time of need, rather than the present trend that could jeopardize the security of our nation because of dependency of foreign oil.

The nation must have an effective oil import control program. No additional exceptions should be effected and we suggest that those that have been granted should be reviewed to the end that they be canceled or phased out in order to restore industry confidence in the program.

At the present time market demand for Kansas crude is good and we have been able to maintain production from semi-depleted fields; we have been able to promote efficient drilling in newly developed pools by adopting wide spacing patterns; and with the aid of unitization statute which became effective on July 1, 1967, we have approved the unitization of pools for pressure maintenance and secondary recovery projects. With sufficient market demand these conservation measures have all been possible. Any increase in imports of foreign crude and refined products which would result in a decrease in market demand for Kansas crude would have an adverse effect on our ability to most efficiently produce the oil already found and further have an adverse effect on stimulating the search for new reserves.

STATEMENT OF HON. BOB DOLE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. Chairman, this Nation is drifting toward an unprecedented dependence on foreign oil. The serious economic decline of the domestic oil industry is a result of the systematic dismantling of the mandatory oil import program.

The United States is currently importing almost 3 million barrels of foreign oil per day. Options available to the Department of the Interior could increase that flow to flood-tide proportions in the months ahead.

BASIS OF MANDATORY OIL IMPORT PROGRAM WAS DEFENSE

When the mandatory oil import program was initiated under President Eisenhower in 1955, the Congress and the Administration recognized the crucial position the domestic oil industry held in the defense of the Nation.

Since that time, international developments have documented the soundness of that reasoning. The Vietnam war, the closing of the Suez Canal, renewed pressure on Berlin, periodic Red Chinese attacks on her neighbors, the illegal seizure of the United States warship Pueblo, the French upheaval, increased Soviet presence in the Mediterranean, and a host of other occurrences all serve to underscore the precarious political balance abroad.

A sustained United States response to all these pressures demands many things. Our response demands resolve, fortitude, military flexibility; and—equally important—a totally reliable petroleum supply.

The domestic oil industry is the *only* oil industry not subject to the vicissitudes of international politics.

IMPORTS HAVE CAUSED DECLINE AT HOME

Most regrettably, Mr. Chairman, the domestic oil industry is subject to the vicissitudes of the import policies of the Administration. This Administration's policies have created the most serious decline in the domestic oil industry since the depression. This is happening, I might point out, at a time when a reliable fuel supply was never more essential.

Let me document our decline at home. The following facts demonstrate the extent and gravity of the crisis:

Exploratory wells drilled in 1967 are down 35.1% from the 1957-1959 averages. Employment in the domestic industry is down 18.6% from the 1957-1959 levels. Crude oil prices—in the face of gross inflation—are down 1.4% from the 1957-1959 levels.

Oil profits have consistently run below manufacturing industry's profit margin for over a decade.

LEGISLATION IS NEEDED

The guidelines of the mandatory oil import program are being ignored. Loopholes in the program are currently allowing an average of 180,000 barrels per day. Petitions for increased imports are receiving favorable consideration by the Department of the Interior with alarming frequency.

Mr. Chairman, the defense of this Nation is our first consideration. The economic health of those vast areas of the United States where the domestic oil industry is predominant is of vital concern to all of us.

In my opinion, the only way to assure proper import controls—the only way to assure proper safeguards for the defense of the Nation's fuel supplies, is for the Congress to enact legislation pending before your committee writing the import limitation into law.

DOLE BILL PENDING

I have introduced H.R. 10689, now pending before your committee. This legislation would write the 12.2% of consumption import limitation into statute law. The loopholes would be closed. Hopefully, the economic revitalization of the domestic oil industry could begin.

Mr. Chairman, I urge this committee to report a bill which will assure such economic revitalization. Much of my State of Kansas is economically dependent on oil. Hundreds of counties across America are in a decline because of the stagnation of this once vibrant industry.

For our economy at home, for our defense abroad, I recommend enactment of meaningful legislation to reverse these alarming trends.

STATEMENT OF WILFRED H. HALL, EXECUTIVE VICE PRESIDENT, NATIONAL OIL JOBBERS COUNCIL

Gentlemen, The National Oil Jobbers Council is a non-profit business trade association located in Washington, D.C. It is composed of 35 State or regional associations covering 41 States (see Appendix #1). Our membership of approximately 9,600 individual firm members is composed entirely of distributors who handle petroleum products at wholesale and retail levels. This segment of petroleum distribution handles 24% of the gasoline sold to service stations, 74% of the heating oil sold to households. Also, a substantial percentage of residual oil sold in the nation today is handled by them. This group has serious interest in U.S. tariff and trade regulations which bear upon petroleum, since it is the raw material on which their business and livelihood depends.

The Council has been concerned with the import program since 1955 when we objected to the so-called "National Security Amendment" to the Trade Agreements Act. We objected to federal pressures invoked during the so-called "voluntary" plan of quotas. We again testified in 1958, 1965 and 1968 in various Congressional committees against aspects of import programs under discussion by the Senate Finance Committee and others. Again, we wish to voice our opinions concerning the oil import program as it is presently constituted. Further, we wish to propose ideas which we believe will strengthen the Nation's security while preserving vital inter-fuel competition. The future of our members depends upon adequate energy resources, not only in the short run, but in the long view as well.

OIL AS A PART OF TOTAL IMPORT POLICY

Liberalization of modern trade between the U.S. and other nations began, perhaps, during the Trade Agreement Act of 1934. Some 11 extensions of the basic authority have been granted to the President up to 1962. The Trade Expansion Act of 1962 further liberalized Presidential authorization to negotiate multi-lateral trade. The so-called "Kennedy Round" of negotiations aimed at further liberalization of trade and took into account an emerging European Common

Market concept and the need for encouraging industrialization to insure a solid financial base for non-communist countries like Japan and West Germany.

Thus, since 1934, our country has grown and prospered simultaneously with a trend to reduce trade barriers, war time years excepted. On July first, 1968, the six countries in the European Common Market lowered tariffs on six commodities, further evidence of a trend toward international lowering of tariff barriers. Oil logically must fit into the total trade and tariff policy of the United States unless there is some excellent reason why it should not do so.

REVIEW NEEDED

Now, in 1968, oil imports, as one factor in the total trade and tariff problem, need review. World conditions have changed. Prior to World War II, the U.S. had over $\frac{2}{3}$ of the free world's petroleum reserves. In 1968, we find the Middle East enjoys this position. U.S. foreign policy and U.S. activity in various parts of the globe during 1968 dwarf activities of 1955 and certainly 1934 when liberalization of modern trade was embodied in the Trade Agreement Act. Also, unlike even five years ago, domestic petroleum reserves have ceased to grow in absolute terms. Our number of drilling rigs no longer shows an increase each year. Recognizing the problem, Congress has appropriated funds to discern the best way to make gasoline out of coal, and oil terminals have experienced a "tight" supply of heating oils during the 1967-1968 heating season. All of these trends are new since the National Security clause was invoked.

Also, substantial oil discovery in Canada, potential reserves on the Continental Shelf and shale oil research all have become factors requiring examination as policy on imports is discussed. The growing number of mergers of refining companies has avalanched, bringing benefits of favored quotas into the hands of fewer and fewer business organizations, which in turn affects inter-fuel competition.

Review is clearly called for by each and all of the factors indicated.

BASIS FOR THE PROGRAM

The National Security clause was invoked, according to news releases, to keep a "healthy domestic oil industry" in connection with the defense requirements of the nation. This statement presupposed attendant encouragement of domestic production, U.S. refining capacity, improvement in U.S. petroleum reserves, and prevention of price deterioration due to foreign competition so that we could fuel our war and non-war economy without interruption of supply due to shrinking reserves, or curtailment of foreign sources upon which dependence had been established. The import quota system was clearly established to achieve these ends.

HOW HAS IT SUCCEEDED?

Domestic production is up.—Table No. 1 shows crude oil run by refineries up from 2,789,404,000 barrels in 1958 to 3,447,193,000 barrels in 1966.

Domestic drilling is off.—Table No. 2 shows well drilling activity declined steadily in numbers of wells drilled and footage drilled during the period of 1958 to 1966.

Refining capacity has increased.—Table No. 3 shows refinery capacity increased from 9,812,248 barrels per day in 1962 to 10,412,447 barrels per day in 1967.

Proved Reserves are not keeping pace with demand.—Table No. 4 shows ultimate recovery from new wells discovered during the year steadily decreasing from 1958 to 1966 and proved reserves in 1966 were less than in 1959.

Price of domestic crude oil has held relatively stable in the face of the world market.—Table No. 5 shows stable prices since 1959.

During the Suez Crisis of 1968, domestic users were relatively unaffected by dislocation of world petroleum supply so that our country's economic, or war time needs were met.

In summary, the program succeeded in the short run to increase refinery capacity, domestic production, it held domestic prices up and insulated us against supply interruption during Suez.

However, it has failed to encourage domestic drilling, nor has it improved domestic reserves. Both items were basic objectives of the program. Moreover, investigation should be made to see just how much of our war needs are met through U.S. oil vs. foreign oil. This element is in serious question. Global operations require global resources. The peril of short supply for war uses should

not depend upon refinery capacity located, to a significant extent, on the U.S. Gulf coast.

Reserves are not increasing and drilling is off, even under price protection. We may have achieved some short run benefits. However, if our reserves cannot keep up under such protected conditions, our security in the future is indeed in question, notwithstanding other temporary benefits enjoyed.

NATIONAL SECURITY OBJECTIVES

As indicated earlier, our national security objectives should be re-examined. Several searching questions must be dealt with. Some of these questions are not ones which the National Oil Jobbers Council can definitively answer. However, we feel that even in such cases the questions may have value to the Committee in its deliberations. They are as follows:

1. *Has the time not arrived to take a Hemisphere approach in dealing with Imports of petroleum products?*

Energy studies by experts in the field indicate that the U.S.A. will use *all* of its capacity of coal, oil, gas, water power and nuclear energy by 1980. This use will be prompted by growing demand for energy due to increasing energy use per capita and increased population. It is forecast* that we will use 73 quadrillion Btu's of energy in 1980 versus 44 quadrillion Btu's used in 1960. This is an increase of 65%. Beyond 1980, it is estimated that 114 quadrillion Btu's will be needed by 2000.

Continental oil and gas reserves are limited. New fields of major significance are as scarce as hen's teeth. Water power contributes less than 4% of the total energy used and experts say that we should not count on added capacity to solve the energy gap ahead.

Recently, the adequacy of natural gas reserves has been questioned. Coal reserves are proliferous. Yet, because of degradation or waste and the difficulty of transport, coal will likely be used at mine mouth to generate electricity. But, transmission of electricity has practical limitations. (Offshore oil and shale will be dealt with separately elsewhere in this paper.) Thus, it does appear that, given some new and dramatic turn of events, we will find ourselves major importers of energy sometime within the next two decades. Some say it will be ten years, while others say it will be 30 years. Few experts feel that we can avoid this eventuality. If these experts are correct, it would appear that the U.S.A. should now consider liberalization of imports on a systematic basis from neighbors in this hemisphere.

Our war and peace security will require us to depend more and more on imports as the years progress, and sources within this hemisphere are obviously better than those across an ocean. An orderly program which slowly escalates petroleum imports as it is called for by expanding demand will strengthen neighboring countries in this hemisphere. It will keep domestic petroleum running to its capacity and will diversify our reserves in times of global conflict. Also, it will make us less vulnerable to disruption of supply by making us less dependent upon the U.S. Gulf Coast area.

2. *Should geographic dispersal of refining capacity be encouraged?*

Currently, 40-50% of refinery capacity is located in the general Oklahoma, Texas and Louisiana area (see Table #6). These states have obviously been logical locations for refining since they are close to domestic supply, close to tide water, and because, until recently, mass destruction of U.S. docks and pipe line terminus facilities was remote. Of course, there is no suggestion here that such facilities be moved, nor that growth in refining capacity should cease in these areas. Yet, it would seem wise, in the interest of national security, to encourage refining capacity to be well dispersed so that distant U.S. markets could be served. In time of attack, the Northwest and New England areas might be able to use Canadian crude oil if the Gulf were out of commission. In fact, in a pinch, they might get crude oil from a variety of sources which could enhance domestic security, and this could help fuel a globally dispersed war machine.

Advanced technology in using "all the barrel" for profitable by-products together with improving transportation facilities makes the movement of crude more feasible than in the past. Indeed, refineries in the Northwest and Northeast areas might well find it profitable to make more fuel oil, which those markets use.

*"Natural Resources for U.S. Growth," Landsburg.

3. *Should we start now to more fully encourage shale oil and offshore drilling efforts?*

Some, in government particularly, are prone to rely for expanded petroleum needs exclusively on oil shale and offshore drilling.

Oil shale is centered in the far west. Unfortunately, the material is located in an area which makes delivery of the finished products to markets most costly. Also, facilities are experimental at this writing. Government policies with respect to leasing properties is clouded.

This type of operation requires that reserves and manufacturing be contiguous (because of degradation). This is potentially dangerous to security since one bomb destroys both the reserve and the manufacturing process. Nevertheless, encouragement of the development of these facilities is wise since they tend to diversify supply sources, and therefore, might relieve those western states east of the Rockies and west of the Mississippi from almost complete reliance on distant sources. Therefore, we must conclude that limited dependence on shale oil would be useful and that Federal policies should be tailored to encourage private investments to be made in these areas. Because of the uncertain future of this new process, we should not count much on its solving problems of supply in the Eastern, Western or Central business corridors. Indeed, commercial production of shale oil, is at best, 10 years distant.

Offshore oil developments have been principally in the Gulf. Unfortunately, this does little to diversify our petroleum reserves. Other offshore areas on the Continental Shelf are being investigated. This is wise since we will need all the product available in years to come. Again, the cost is high and technology uncertain. We should encourage private enterprise to develop these resources through clear Federal and state leasing laws. But, again at this point in history, we cannot depend heavily on this source of petroleum products.

4. *Should we import finished products into the U.S.A.?*

Reliance upon foreign refineries is to be avoided, unless domestic refineries fail to produce adequate finished products to meet demand.

U.S. refineries have an obligation to produce needed products and ordinarily would do so. However, if various profit incentives are not available leading to production of one particular product, then it should be freely imported. While one can argue that the same security considerations would apply to crude imports as apply to products, there are significant differences. A U.S. refinery can accept crude from a variety of sources. Canada, Venezuela, Mexico, Central and South America, Sumatra, the Persian Gulf and Alaska are but a few sources. This crude can be made into various products as are needed at a particular time in a particular area where the need exists, i.e. fuel oil, or jet fuel, or gasolines of various grades.

If we depend to a significant degree on products manufactured in other countries, we automatically are reliant on the option of some third foreign party for a particular product at a given time which they may not wish to manufacture because of economic or other reasons. Quality may be a problem and it is far safer to transport crude, than for example, aviation gasoline. Also, the shutting down of a particular refinery could leave us without needed supply. Therefore, possessing the refinery capacity on U.S. soil allows us greater flexibility of end product supply.

Dependence upon foreign crudes from nations in this hemisphere carries some risk. Whether or not this risk is meaningful when considering Canadian, Mexican or Venezuelan reserves as compared with Gulf States reserves is debatable. Yet, the fact is that this risk is far less than it would be if we depended upon foreign crude, plus foreign crude transportation to refineries, plus foreign nationals to refine crude. The maintaining of U.S. refinery capacity cuts down overall dependence by scaling down functions performed to that of crude gathering alone.

However, if U.S. refineries *do not* produce adequate products to meet demand, the import program should be geared to import finished products to make up this deficit. Products should be brought in during these periods in a manner which will prevent wind-fall profits and/or give one set of marketers undue competitive advantage over the others. Products entering this country might come into a commodity exchange where buyers bid up to U.S. price levels, thereby ironing out price differentials. This needs study.

If such a system is not available, tariffs should be investigated which would allow products to flow in at price levels which are established by competition in the market place. Such systems will encourage refineries to meet future shortages with added capacity as demand increases for particular products. If such plans are not feasible, an equitable quota system should be established which gives all similar type marketers equal advantage.

In order to quickly compensate for deficits in product supply arising for a variety of reasons at the domestic refinery level, pre-established criteria should be set. Such criteria would establish existence of a critical point at which products imports would be encouraged. Inter-fuel competition, the non-convertability of heating plants and the very existence of the independent marketer's business entity require that shortages be properly classified and acted upon sufficiently in advance to avoid dislocation.

5. Who should be permitted to import crude?

The current system of quotas runs counter to the free enterprise concept. Basically, a refiner must have had "inputs" before quotas can be established. While exceptions are granted and a "newcomer" pool established, the system is mainly geared for existing refiners. The centralization of refining capacity into the hands of fewer and fewer companies (see table #6) clearly indicates that some thought should be given to encouraging new refineries to enter the scene so as to preserve inter-fuel competition at the primary level. For example, a chemical company might establish an oil refinery in Seattle, Washington. This group might use Canadian or Alaskan crude for manufacture of fuel oil and gasoline for the Pacific Northwest. Such activity would diversify refining capacity, bring new competitiveness, and allow the "local" refinery to meet product demand for that particular area. Latest moves by Interior in this direction are encouraging. These moves should be amplified by placing more crude in this "newcomer" category.

SUMMARY

We feel that the Nation's security requires analysis of several factors dealing with petroleum imports which were not prominent at the time import controls were imposed on this industry. Also, we have had over 10 years' experience under the quota system which proved some short run benefits are present. Yet, the basic increasing of domestic reserves and "a healthy domestic" drilling program has not been achieved.

We feel that the future demand for energy requires that U.S. policy encourage development of offshore and shale oil technology. However, we should not gamble on these sources alone to meet the energy gap which is certain to arrive. Therefore, we feel a systematic increase of crude imports, to be initiated as supply is needed to meet demand is in order. This precludes rigid control. Also, we feel U.S. security would be assisted by encouragement of diversified refinery locations which could serve individually dispersed markets.

Finally, if U.S. refineries fail to produce various products to fully meet demand, that such products should be brought in, but under a system devoid of discrimination.

Our proposals are geared to increase imports only as needed to meet demand. If oil shale or offshore activities do prove to be adequate, foreign imports would be minimized. Our program of encouraging refinery building near markets appears worthy of consideration for security reasons alone. Also, if domestic refiners do produce adequate products, no finished goods of major proportion would be brought in. However, flexibility is needed to meet these problems and plans should be incorporated to allow quick implementation if and when the need arises.

Attached are the basic policies of the National Oil Jobbers Council which underlie this report. These policies have been passed by the Council's Board of Directors.

APPENDIX No. 1

LIST OF NATIONAL OIL JOBBERS COUNCIL ASSOCIATION MEMBERS

Alabama Petroleum Jobbers Association
 Arkansas Oil Marketers Association
 California Oil Jobbers Association
 Colorado Petroleum Marketers Association
 Connecticut Petroleum Association
 Empire State Petroleum & Fuel Merchants Association
 Florida Petroleum Marketers Association
 Georgia Oil Men's Association
 Illinois Petroleum Marketers Association
 Independent Heating Oil Dealers Association of Maryland, Inc.
 Independent Oil Marketers Association of Indiana
 Independent Oil Men's Association of New England
 Intermountain Oil Marketers Association
 Iowa Independent Oil Jobbers Association
 Kentucky Petroleum Marketers Association
 Louisiana Oil Marketers Association
 Michigan Petroleum Association
 Mississippi Oil Jobbers Association
 Missouri Oil Jobbers Association
 Nebraska Petroleum Marketers Association
 New Jersey Fuel Merchants Association
 New Mexico Petroleum Marketers Association
 North Carolina Oil Jobbers Association
 Northwest Petroleum Association
 Oklahoma Oil Marketers Association
 Oregon Oil Jobbers Association
 Pennsylvania Petroleum & Fuels Association
 South Carolina Oil Jobbers Association
 South Dakota Independent Oil Men's Association
 Tennessee Oil Men's Association
 Texas Oil Jobbers Association
 Virginia Petroleum Jobbers Association
 Washington Oil Marketers Association
 Wisconsin Petroleum Association
 Wyoming Oil Jobbers Association

TABLE No. 1.—Crude oil run by refineries, 1958–1966

[Thousands of barrels]

1958	2,789,404	1963	3,170,652
1959	2,917,661	1964	3,223,329
1960	2,952,534	1965	3,300,842
1961	2,987,158	1966	3,447,193
1962	3,069,631		

Source: API Petroleum Facts and Figures, 1967.

TABLE 2.—TOTAL WELLS DRILLED AND TOTAL FOOTAGE OF WELLS DRILLED IN USA, 1958–67

Year	Total number feet (in 1,000 of feet)	Total wells drilled
1958	198,224	50,039
1959	209,231	51,764
1960	190,703	46,751
1961	192,116	46,962
1962	198,559	46,179
1963	184,357	43,653
1964	189,922	45,236
1965	181,484	41,423
1966	159,377	37,881
1967	144,235	33,558

Source: "API Facts and Figures 1967", with 1967 figures obtained by phone interview, July 2, 1968.

TABLE NO. 3.—*Refinery capacity operating Jan. 1, 1962–67*

[Barrels per day]			
1962	9, 812, 248	1965	10, 161, 311
1963	9, 814, 791	1966	10, 171, 159
1964	10, 063, 164	1967	10, 412, 447

Source : API Petroleum Facts and Figures, 1967.

TABLE 4.—1966 ESTIMATE OF ULTIMATE RECOVERY FROM FIELDS DISCOVERED DURING YEAR AND PROVED RESERVES AT END OF YEAR IN THE UNITED STATES, 1958–67

[Thousands of barrels]		
	Ultimate recovery from fields discovered during year	Proved reserves end of year
1958	871, 013	30, 535, 917
1959	627, 778	31, 719, 347
1960	633, 255	31, 613, 211
1961	444, 326	31, 758, 505
1962	679, 264	31, 389, 223
1963	403, 723	30, 969, 990
1964	513, 275	30, 352, 391
1965	363, 350	31, 352, 391
1966	250, 784	31, 452, 127
1967	136, 472	31, 376, 670

Source: API Reserves of Crude Oil Natural Gas Liquids, and Natural Gas in the United States and Canada.

TABLE 5.—SELECTED CRUDE OIL PRICES 1958–67

[Dollars per barrel]		
	36 gravity crude East Texas, flat price	January 1 mid- continent 36 crude
1958	\$3. 25	\$3. 07
1959	3. 05	3. 00
1960	3. 05	2. 97
1961	3. 10	2. 97
1962	3. 10	2. 97
1963	3. 10	2. 97
1964	3. 10	2. 97
1965	3. 10	2. 92
1966	3. 10	2. 92
1967	3. 15	3. 00

Source: Platt's Price Service.

TABLE NO. 6.—*Refinery capacity by selected districts, Sept. 30, 1967*

[Barrels per day]	
Texas Gulf Coast	2, 468, 000
Louisiana Gulf Coast	1, 048, 750
Louisiana Inland and Arkansas	257, 500
Texas Inland	389, 350
Oklahoma, Kansas, and Missouri	873, 750
Subtotal selected	5, 037, 350
Total United States	10, 781, 020

Source : API Petroleum Facts and Figures, 1967.

POLICY STATEMENT

IMPORT QUOTAS

The National Oil Jobbers Council vigorously opposes the granting of favored import quotas on number two fuel oil to selected independent terminal operators since such will create an unreasonable market advantage and discriminate between the favored quota recipients and others with whom they compete. This can only interfere with historical marketing patterns which will interfere with free and open competition. If and when financial hardships, dislocation, or shortages can be factually established and importation of number two fuel oil is required, then allocation of quotas should be granted to all independent terminal operators equally on a historical basis. Such allocation should benefit all marketers and consumers equally on a non-discriminatory basis.

PURPOSES OF COUNCIL

To establish a National Council of state and regional trade associations whose memberships are composed of independent oil jobbers and marketers of petroleum products;

To establish, maintain, and promote systems of education and instruction for independent petroleum marketers throughout the United States to the end of assisting such independent marketers in the more economic distribution and sale of petroleum products for the benefit of themselves and the general public;

To create and foster a cooperative spirit between independent marketers and distributors of petroleum products, to advocate and encourage the adoption of practices, customs, and legislation affecting the marketing of petroleum products to the end of maintaining fair practices and a system of free, competitive enterprises, as well as to oppose customs, practices, regulations, and legislation contrary to such purposes; and

To perform generally all services for and on behalf of independent petroleum jobbers and distributors in a manner similar to that engaged in by boards of trade and chambers of commerce to the extent that such activities are consistent with the laws of the United States, the State of Tennessee, and the Charter of the Council, but under no circumstances to be contrary to the general welfare of society or to be for the individual profit of its members.

STATEMENT OF EDWIN JASON DRYER, COUNSEL, INDEPENDENT REFINERS
ASSOCIATION OF AMERICA

My name is Edwin Jason Dryer. I appear here on behalf of the Independent Refiners Association of America of which I am counsel.

The Association for which I speak is composed of, and represents, domestic independent oil refiners. It includes independent refiners of all types—in all parts of the country and of varying size—representing their common interests as independents.

The members of this Association have an enormous and common stake in the success and integrity of the oil import program—a stake measured by the simple fact that, in the absence of their quotas in that program, most of them could not survive. This is because they do not have the large non-refining resources, typically including substantial quantities of crude oil, both foreign and domestic, enjoyed by their integrated major company competitors. Essential to their survival is the distribution of the competitive advantage of such foreign oil as enters the domestic market in a manner which, in its practical economic effects, will foster competitive equality between independent refiners, with costs based upon domestic crude oil prices, and their integrated major company competitors.

Independent refiners are therefore critically concerned with an aspect of the oil import program which does not specifically appear in the legislative proposals before the Committee for a quantitative limit on imports—namely, the way in which quotas, within the overall limit, are actually distributed. This aspect of the program is important not only to independent refiners but also to the success of the program as a whole. This is because of the role of the independent refiner in maintaining a competitively healthy petroleum industry and his special role in the mobilization base for national security.

First, the national security aspect. The independent refiner is typically found at dispersed inland locations as contrasted with the coastal concentrations which typify much present-day major company refinery construction. In terms of a national emergency, therefore, the independent refiner occupies a critically important role as a dispersed, protected and technically flexible source of oil for war. This has been repeatedly recognized by all branches of the government concerned with industrial mobilization. It need not be developed further here.

But the independent refiner's national security role goes beyond his own production capability and extends to his part in preserving competition and thereby a healthy and viable petroleum industry. For many years the anticompetitive forces in the petroleum industry, and the tendency toward concentration of refining capacity and resources in the hands of a few major oil companies, have been a major concern to the Congress and the Executive Branch and even the courts. Suffice it to say here that the independent refiner provides the thrust of real competition in the refining industry, upon which the interests of the consumer and the health of the oil industry itself ultimately depend.

For these reasons it was of major concern to the government to observe at the outset of the mandatory oil import program that the independent refining companies were rapidly disappearing. In the brief span of years from 1951 to 1956 the total number of refining companies declined from 223 to 159. This decline in numbers was wholly in terms of independent refining companies of course—no major company disappeared.

Due to this alarming statistic and the serious consequences which it foreshadowed, special steps were taken at the very outset of the Mandatory Oil Import Program to bolster the independent refiner's chances for survival. The sliding scale, with its preference in quota distribution to independent refiners in relation to refinery size, was instituted and it has been an essential part of the program ever since.

Attacks have been launched by some major companies against the sliding scale ever since its inception. These attacks have failed, however, because the case for the sliding scale has been clear and convincing. It is no windfall or special deal such as those with which the program has recently become infected. The sliding scale is instead merely responsive to that widely recognized industrial fact of life that larger enterprises can and do wield disproportionately greater economic power. The sliding scale is also responsive to an important fact which is not so obvious, namely, that all of the major oil companies have large crude oil resources, which the typical independent refiner does not. These major companies therefore benefit directly in their crude oil operations from the import program's beneficial effect on domestic crude oil prices. In short, the sliding scale is only a partial offset to the double-barreled advantage of the major oil companies in the oil import program.

The case for the sliding scale has been well documented in each of the many Congressional and Departmental hearings held in the last nine years on this subject. I particularly call this Committee's attention to the report of hearings on "Oil Import Allocations", August 10 and 11, 1964, by the Senate Select Committee on Small Business and the Annual Reports of that Committee from 1964 to date. And, for a single, concise statement on this critical point, we refer to the explanation of the government's decision to distribute quotas in this way, given by Under Secretary of the Interior Elmer Bennett on April 21, 1960, a full copy of which is attached hereto. He said in part:

Caught in the two-fold squeeze of declining general business and the competitive pressures from large importers with access to lower-cost imported crude, the domestic refiner was faced with serious problems. I would be less than frank if I did not point out there was grave concern within the Federal Government about the future of the independent refining segment of the industry.

* * * * *

The independent refiner was threatened with extinction by those integrated companies whose refinery locations gave them access to lower-cost raw materials but whose marketing areas everywhere permitted fullest use of this competitive advantage.

Although the needs of the independent refiner have been recognized in the program as developed until recently, we are deeply worried about recent trends. After years of careful development, the Department has launched in the last two years a series of special deals unrelated to the program's national security

objectives and which, if continued, threaten to reduce the benefits of the program for independent refiners. This is because, as the quantity of imports allocable to the refiner class is reduced by these special deals, pressure will be generated to reduce quotas in the lower brackets of the sliding scale also.

These aberrations, this tinkering with the program, have been described by other witnesses and need not be described further by me. In respect to these special deals and loopholes, suffice it to say we share the concerns expressed by the producer groups to this Committee and we seek with them a return to the oil import program as so carefully developed up to two years ago.

As to the means to accomplish this result, we think some affirmative and forceful action by this Committee *now* is more important than delay while specific legislation is sought defining precise details such as the overall level of imports.¹ In this connection, the statutory basis of the program *has been* adequate—the deficiencies noted are recent and concern the implementation of the statute, rather than its content. We think therefore that the most immediate, simple, specific and effective step which the Committee on Ways and Means could take on this important subject would be a clearcut and affirmative report condemning recent aberrations in the oil import program.

Such a report could and should restate and confirm the original basic purposes of the underlying legislation and the manner in which those purposes have, until recently, been carried out. Such a report could and should expressly endorse the sliding scale method of distributing these valuable import rights—a matter on which existing legislative proposals are silent. Such a report could and should confirm the quota treatment which the independent refiner has had and must continue to have if the program is to succeed. In these respects such a report could deal effectively not only with the items in pending legislative proposals but with other aspects not covered in such proposals but of equally critical importance.

We say “deal effectively” because such a report from this important Committee must necessarily influence not only the current Administration but the Administration which will have the responsibility for the shape of oil import controls beginning next year. Furthermore, this action by this Committee can be accomplished without arousing some of the objections which proposals for a statutory mandate have inspired—especially the objections of the Administration that a precisely detailed statutory mandate would be too inflexible. We urge such an affirmative report by this Committee.

In the interest of completeness, and at the same time brevity of this statement, I call to your attention and ask that there be incorporated by reference here two basic documents setting forth the views of independent refiners and our concerns with the current state of the oil import program. One of these documents is the Association's statement of April 19, 1968, to the Department of the Interior on the imports auction scheme proposed by the Department. The other document to which I refer is the statement of this Association on October 31, 1967, to the Committee on Finance, United States Senate, regarding oil import quotas. This statement has been published under date of February 7, 1968, in the so-called “compendium” of industry comments with respect to import quotas and U.S. trade policies generally in connection with hearings proposed by that Committee.² We shall, for the Committee's convenience, furnish copies of these statements directly to you.

STATEMENT OF INDEPENDENT REFINERS ASSOCIATION OF AMERICA, COMMITTEE ON
FINANCE, U.S. SENATE, REGARDING OIL IMPORT QUOTAS, OCT 31, 1967

SUMMARY

Independent refiners share the concern of independent producers with regard to recent changes in the oil import program which are designed for purposes other than the national security and which threaten the effectiveness of the program in maintaining a healthy producing and refining industry. They endorse S. 2332 which seeks to confirm and tighten the established oil import program.

¹ We endorse, of course, prompt passage of the extension of the Trade Expansion Act of 1962 which is the legislative basis for the oil import program and sets forth its national security purpose.

² Committee on Finance, United States Senate, 90th Congress, 2d Session, “Compendium of Papers on Legislative Oversight—Review of U.S. Trade Policies.”

IRAA points out that the real success of the program depends not only on the overall quantitative limit on imports but also significantly upon the way in which quotas are actually distributed. This aspect of the matter, which is not touched by the presently proposed legislation, is of particular concern to independent refiners because the very survival of most independent refiners today depends upon their oil import quotas.

There was carefully developed over several years and under three Presidents a method for distributing import quotas which has been highly effective, namely, to refiners on a sliding scale basis in inverse relation to refining size. To discourage further deleterious tinkering with the program, IRAA urges the Senate Finance Committee to express its endorsement of this method of distributing these valuable import rights and to confirm the quota treatment which the independent refiner has had and must continue to have if the import program is to succeed.

Detailed reasons and views in support of IRAA's position are set forth in the current statement and in several prior IRAA statements at Congressional and Administrative hearings. These are submitted and also incorporated by reference.

STATEMENT

This statement is submitted by the Independent Refiners Association of America for two purposes. The first is to express the views of this Association in connection with the Committee hearings of October 18-20 on specific import quota proposals including oil. The second is to express IRAA's views with respect to the Committee's general review of U.S. trade policies, and the proposed extension of the trade agreements statutes, as to which hearings are yet to be convened and the Committee has asked that papers be filed in advance.

It is appropriate at the outset to identify this Association and the companies it represents. The Independent Refiners Association of America consists solely of independent oil refiners. It includes independent refiners of all types—in all parts of the country and of varying size—representing their common interests as independents.

A word about the independent refiner. The independent refiner characteristically owns or controls little of the crude petroleum which he processes and except in rare instances, has little control over the markets in which he sells the products which he manufactures. Yet without a refining element in the petroleum industry crude oil cannot be transformed into consumable products and without the independent refiner, the competitive elements in the market place which provide such products to the consumer will be removed. Moreover, the independent refiner by size and location possesses facilities not readily susceptible of destruction, in even the most grave national emergency. Further, an excess refining capacity upon which this country must depend in times of national peril exists in operable condition, immediately available, only by virtue of the existence of the plants of the independent refiner. The independent refiner is, therefore, critically important to competition in the domestic economy and to our national security in emergencies.

Because of their position, dependent upon the purchase of crude oil for their raw material supply, independent refiners have had from the inception of oil import controls a special concern with the measures proposed to allocate foreign oil to firms in the United States. From the outset of import controls in 1959, this subject has been a matter of major interest to the Association and its members. The current importance of import controls to independent refiners is most simply illustrated by the fact that, absent the share in foreign oil which the import control program allocates to independent refiners, most independent refiners in the United States would be operating at a loss today.

As a result of IRAA's deep concern with oil imports we have testified at all of the Congressional hearings bearing on this subject and all of the administrative hearings on this subject since the inception of the program. The impact upon independent refiners of alternative control measures and the facts in support of independent refiners' proposals (which have been largely embodied in the program as developed until recently) have been set forth previously in these various statements. The most recent of these, submitted in the Department of the Interior's general hearings on the oil import program in May 1967, brought these facts up-to-date. In the interest of brevity we incorporate by references and attach herewith certain of these key statements, to wit: Statement of May 10,

1961, before the Department of the Interior Oil Import Hearings; Statement of September 2, 1964, to the Senate Select Committee on Small Business; Statement of March 10, 1965, before the Department of the Interior Oil Import Hearings; Statement before the May 22-24, 1967, Department of the Interior Oil Import Hearings, and the Statement of Under Secretary Elmer Bennett dated April 21, 1960, explaining the fundamental premises of the import program, and referred to in the last mentioned IRRA statement.

We should like, however, to highlight certain aspects of the matter of direct and immediate significance for the legislation currently under review.

1. *Oil Import Controls Differ from General Protectionist Legislation.*

The pending oil import legislation (i.e., S. 2332) differs greatly from the pending bills of a general protectionist nature considered by the Senate Finance Committee in the hearings of October 18-20, 1967. It is most significant that the existing oil import program (which it is the purpose of S. 2332 to confirm) has its statutory origin and basis in the several trade *expansion* acts. Oil import controls are there authorized—under the national security exception to the general program for unrestricted trade. A national security exception was recognized as a necessary part of this country's trade expansion policies. National security has been and should continue to be the basis and the objective and correspondingly the limit of the oil import program.

The other protectionist bills pending before the Senate Finance Committee represent instead a direct collision with the policy of free trade which so recently was pressed to significantly new accomplishments in the so-called "Kennedy round". This difference between the oil import control legislation and the bills of a general protectionist nature should be recognized in the consideration of these bills by the Congress. The national security exception to free trade, which has been an essential part of the free trade policy since its inception, should meet with the approval of even the most vigorous free trade advocates who otherwise would oppose general protectionist legislation.

The oil import proposal now before the Committee reflects essentially the concern of its sponsors that recent administrative actions are tending to twist the program toward objectives other than the national security (specific instances are discussed separately below. It represents a tightening of the program to its national security purpose. As such, the legislation deserves the endorsement of everyone including those favoring the original trade expansion legislation now up for further extension.

2. *Recent Steps to Subvert the Oil Import Program.*

S. 2332 is a response, in effect, to recent steps by the Administration, some accomplished and others still proposed, which would have the practical effect of subverting the oil import program as it has been so carefully developed over the years under three different Presidents. The recent measures which would use the import program for purposes other than the national security include:

(a) The grant of special import treatment to the Phillips Petroleum Company to encourage it to make investments in Puerto Rico which would help the economic development of that territory. Following this special deal, other companies promptly sought similar treatment with proposals to stimulate the economic development of Puerto Rico, the Virgin Islands and even Guam in exchange for the grant of valuable import rights. All these proposals are extraneous to the national security. Worse, they will weaken the program and thus thwart the national security. As desirable as the economic development of these territories may be, it is not an objective of the Congressional mandate on which the oil import program is based.³

³ Trade Expansion Act of 1962, Pub. Law 87-794, 19 U.S.C. § 1862. Nowhere does the statute contemplate grant of quotas for foreign oil for the purpose of improving economic welfare or unemployment which has not been adversely affected by excessive imports. The lawyers who prepared the Presidential Proclamation legitimatizing the special deal for Phillips apparently recognized this because the special quotas for Puerto Rico there authorized were expressly limited to "instances in which the Secretary determines that such action would not impair the accomplishment of the objectives of this Proclamation . . ." (Section 3(b)(2) of Proclamation 3279, as amended.) The Secretary has authorized the Phillips deal; impliedly he has determined that this one special deal will "not impair the accomplishments of the objectives of this Proclamation." But what about the host of applications for similar treatment now pending! Also interesting: the case for quotas for Puerto Rico and the Virgin Islands is completely at odds with the statute's concern for *excessive* imports in that it relies on alleviating unemployment by *increasing* imports into these areas, and thence to the mainland.

(b) The grant of special import quotas to promote air pollution control. The President on July 17, 1967, authorized changes in the oil import program designed to aid in air pollution control. The Secretary of the Interior thereby was authorized to grant *additional allocations* "notwithstanding the levels established in Section 2 of this Proclamation [the limitation on oil imports (except for residual fuel oil) to 12.2% of domestic production in accordance with a careful Cabinet Committee study and Presidential determination that imports above that level would threaten the national security]." A breach of the 12.2% limit by the Secretary is there clearly authorized.

In the same Proclamation and again for the express purpose of aiding air pollution control, the definition of residual fuel oil (which is outside the 12.2% limit) was redefined to include No. 4 fuel oil. The net effect was to remove No. 4 fuel oil from the 12.2% limit and to authorize an increase in overall imports beyond the 12.2% limit as previously applied by and undetermined amount of No. 4 fuel oil imports. As desirable as the control of air pollution may be and as desirable as strenuous efforts in aid thereof by the Government may be, there is still, however, no connection between air pollution and the national security. Significantly none was even asserted.

(c) Expansion of asphalt imports in excess of the 12.2% overall limit. The President on April 10, 1967, authorized changes in the oil import program which would permit imports of asphalt "without respect to the levels of imports prescribed in Section 2 [the limitation on imports to 12.2% of domestic production]." Again, a breach of the 12.2% limit by the Secretary is clearly authorized.⁴

(d) The Administration's threat in February 1967, released through "briefings" by federal officials, to use import controls as a threat or sanction to enforce compliance with the Administration's desire to roll back gasoline prices. No hint of any national security connection appears here and none was even suggested. The Administration merely found its control over valuable import rights a most powerful tool. It felt no restraint in using this powerful tool for objectives completely unrelated to the national security.

(e) There is under consideration by the Administration at the present time (by reason of its affirmative sponsorship by key members of Congress from New England) a proposal which would in effect accord to No. 2 fuel oil (the prime heating oil) a relaxation like that for No. 4 oil, permitting imports beyond the existing 12.2% overall limitation. It remains to be seen whether if done, it will be done by "redefinition" as in the case of No. 4 oil or by authorization "notwithstanding" the 12.2% limit as in asphalt, and the air pollution bonus quotas. But it is obvious that one breach easily begets another. The express purpose of this proposal is to reduce home heating oil costs for consumers in New England. No hint whatsoever of a national security purpose appears.

With such steps already taken and proposed, the present legislative proposals to restrict such adventurous toying with the program make sense.

3. *Significant Aspects of the Oil Import Program Not Dealt With In Proposed Legislation—To Whom Shall Quotas Go?*

While the limitation of oil imports quantitatively (heretofore to 12.2% of domestic production plus residual as required) is a substantial part of the oil import program and the present bill is concerned solely with tightening such quantitative restrictions, it is important to note that the real success of the program and attainment of its national security objectives depends significantly upon the manner in which quotas are actually distributed.

Because of the large price differential between domestic and foreign oil, these quota rights are valuable. To whom shall these valuable rights be granted and on what basis? This matter, which is not touched by the present legislation, is of particular concern to independent refiners. As noted above, the very survival of most independent refiners depends upon their oil import quotas.

For reasons which are developed in detail in the prior IRAA statements attached hereto, the carefully developed system of distributing import quotas to refiners and on the basis of a sliding scale in inverse relation to refinery size⁵ serves best the objectives of the oil import program. For reasons there docu-

⁴ The Proclamation does limit the Secretary's authority to circumstances which "he determines to be consonant with the objectives of this Proclamation" thereby preserving the national security objectives as a matter of legal draftsmanship and thus keeping technically within the Congressional mandate. The fact remains, however, that breach of the 12.2% limit, as previously determined necessary for the national security, was authorized and authorized prior to and in the absence of any real study of the national security impact of asphalt decontrol, i.e., one inviting industry comment such as the Director of the Office of Emergency Planning subsequently initiated, 32 Fed. Reg. 6155, April 19, 1967.

⁵ In short, the system as developed over many years prior to the recent grant of quotas to petrochemical companies and for the several other purposes noted above.

mented, that system best serves to maintain a sound producing industry, a sound refining industry, a wholesome competitive environment and the health of the small companies in the oil industry upon which national security especially depends. For a single concise statement on this critical point we refer to the explanation of the government's decision to distribute quotas in this way, given by Under Secretary of the Interior Elmer Bennett on April 21, 1960, a full copy of which is attached hereto. He said in part:

Caught in the two-fold squeeze of declining general business and the competitive pressures from large importers with access to lower-cost imported crude, the domestic refiner was faced with serious problems. I would be less than frank if I did not point out there was grave concern within the Federal Government about the future of the independent refining segment of the industry.

* * * * *

The independent refiner was threatened with extinction by those integrated companies whose refinery locations gave them access to lower-cost raw materials but whose marketing areas everywhere permitted fullest use of this competitive advantage.

The facts and factors there set forth still exist and are still relevant.⁶ Extinction of the independent refiner has been averted and this is due directly to the method in which import quotas have been distributed. By that very token, any steps which threaten the independent refiner's quota position, threaten his survival.

IRAA'S RECOMMENDATION

We urge that the Senate Finance Committee's Report on S. 2332 include not only an endorsement of the quantitative limits heretofore in effect (which S. 2332 would confirm and tighten), but an endorsement also of the method by which quotas have actually been distributed prior to the recent administrative aberrations herein noted, i.e., quotas to refiners and on the basis of a sliding scale in inverse relation to refining size. We urge that the Senate Finance Committee also express clearly its disapproval of the recent steps which have provided for quotas outside of the refiner-sliding scale system and for purposes unrelated to the national security. (If and to the extent that some of the recent steps cannot now be reversed, we urge Congressional recognition of the special role of the independent refiner and Congressional endorsement of the rule that any reductions in refiner quotas (needed to pay for special quota deals and stay within the 12.2% limit) shall be borne by the major oil companies.) Such Congressional expression confirming the skillful administrative development of the import control machinery until recently will discourage further tinkering with the import program. This tinkering, if continued, will soon defeat that program's basic objectives and ultimately destroy both the independent refiner and the independent producer.

In taking this position the Senate Finance Committee will also confirm the position and views of every Congressional Committee which has considered this subject.⁷

INDEPENDENT REFINERS ASSOCIATION OF AMERICA,
Washington, D.C., April 19, 1968.

Mr. ELMER L. HOEHN,
Administrator, Oil Import Administration, Department of the Interior,
Washington, D.C.

Re comments of IRAA on Imports Auction Proposal.

DEAR MR. HOEHN: I submit herewith six copies of the comments of the Independent Refiners Association of America with respect to the Department's import auction proposal, set forth in the release of March 20, 1968. I wish specially to call your attention to the fact that the position of IRAA was *unanimously* adopted at a meeting attended by independent refiners of all sizes in Houston, Texas, on April 1, 1968.

If and when hearings are scheduled on this—or any other aspect of import controls—we wish, of course, to be heard.

Sincerely,

EDWIN JASON DRYER,
Counsel for Independent Refiners Association of America.

⁶ See IRAA Statement, May 22-24, 1967, p. 12.

⁷ See especially the report of hearings on "Oil Import Allocations", August 10 and 11, 1964, by the Senate Select Committee on Small Business and the Annual Reports of that Committee from 1964 to date.

COMMENTS OF INDEPENDENT REFINERS ASSOCIATION OF AMERICA ON IMPORTS
AUCTION SCHEME PROPOSED BY THE DEPARTMENT OF THE INTERIOR

I. PRELIMINARY STATEMENT

These comments are submitted pursuant to the release of the Department of the Interior on March 20, 1968, inviting comments with respect to "a proposed system for auctioning oil import licenses" with particular reference to "the scope of such a system and . . . areas of exclusions and inclusion, date of implementation, types of auction, etc."

The tenor of the Department's release implies that an auction system has been at least tentatively decided upon and industry comments are primarily invited with regard to how such a scheme could be carried out. We have carefully reviewed the matter and have concluded that such an auction scheme would be completely unworkable in terms of accomplishment of the objectives of the Mandatory Oil Import Program. Accordingly, our comments are directed to this point rather than to the mechanics by which an auction scheme might be instituted.

This position was approved by the Board of Directors of this Association at a special meeting in Houston, Texas, on April 1, 1968, which was also attended by a large number of the members of IRAA. Furthermore, this position was approved *unanimously* by all Directors and all members there present, including independent refiners of all types, both as to size and geographical location.

II. THE OIL IMPORT PROBLEM AND THE PRESENT PROGRAM AS A SOLUTION THERETO

Because the imports auction scheme constitutes a complete revision of the present oil import program, it is in order to restate at the outset the nature of the problems which the oil import program has been intended to solve. These problems are, of course, well known to the Department and throughout the oil industry but restatement is necessary to serve as the basis for analysis of the imports auction scheme. That scheme must stand or fall as it helps to solve those problems.

A. *The Background of the Problem*

Crude oil imports into the United States mounted rapidly in the 1950s. Such foreign oil was (and is today) available at costs substantially below the cost of domestic crude oil. The net effect was severe pressure on the prices of domestic crude oil and refined products and derivatively on oil exploration. The rate of oil drilling slowed substantially threatening the maintenance of reserves essential to national security.

Because much of our domestic crude oil reserves are in strong hands, e.g. the major oil companies, the impact of low cost foreign oil was evidenced even more severely in reduced product prices than in reduced crude oil prices. As a result, the number of independent refiners—whose survival depends upon operating within the margin between raw material costs and product prices—declined alarmingly, from 203 in 1951 to 139 in 1956. This threatened another aspect of our national security—the need for widely dispersed refining plants away from vulnerable coastal areas. These are typically inland independent refining plants and their importance in our industrial mobilization base had been repeatedly affirmed.

By 1957 both the oil industry and the government were deeply concerned. A Special Cabinet Committee in 1957 reviewed the matter. It found that the mounting level of oil imports threatened our national security and it recommended import limitations to the 12.2% level which, with modifications, has continued in effect to now. These limitations were applied in mid-1957 and 1958 through the Voluntary Oil Import Program, but that program did not succeed. Its failure was not due merely to its voluntary nature, which permitted violation, but more importantly to the keen competitive imbalances which it created and which, unresolved, spelled inevitable collapse of the system.

B. *The Key Element in Its Solution—Fair Distribution of the Foreign Cost Advantage to All Refiners*

Prior to the promulgation of the present Mandatory Oil Import Program, extensive hearings were conducted by the Department of the Interior in which the nature of the problem was fully explored. The key fact emerging from those hearings and testified to repeatedly, so that it is beyond peradventure, is that the cost advantage of foreign oil spreads competitively throughout the

entire national oil market and those enjoying this cost advantage are enabled to and do sell their products at prices lower than those which a refiner using domestic crude oil alone must charge to cover his costs. Obviously a refiner using domestic crude oil alone could not survive (in the absence of other resources such as those available to the major oil companies) and, as noted, many did not. This competitive pressure would extend in turn to domestic crude oil prices, and as noted these had declined—although not enough to maintain adequate refining margins or prevent the decline in independent refiner numbers.

In sum, the key to a solution was recognized to be a fair distribution of the cost advantage of foreign oil—a fair spreading of this cost advantage among all refiners. Only this would eliminate the competitive distortions which had resulted from the availability of this cost advantage to a few coastal refiners.

C. The Present Program

The basic design of the Mandatory Oil Import Program which emerged from those hearings and which has been in operation for over nine years was directly responsive to the problem.

1. A quantitative limitation was, of course, an essential element.

2. But clearly a quantitative limitation alone, however achieved, was not enough. It had been demonstrated that even a *limited* amount of low cost foreign oil in the hands of a few coastal refiners could still upset competitive relationships throughout the national market. Accordingly, the limited amount of low cost foreign oil was distributed to *all* refiners and in relation to their size.

3. But even this was not enough. It was recognized that competitive distortions would be eliminated and the ability of all refiners to purchase domestic crude oil would be maintained only if proportionately greater quotas, in relation to their size, were granted to the nonintegrated refiners. The graduated scale has therefore been a key element of the mandatory program since its inception. The shortest and simplest citation to the need for the graduated scale is the fact that, without the import quotas assigned to them on the graduated scale. Most independent refiners would operate at a loss today at today's prices for domestic crude oil and today's prices for their refined products.⁸

D. The Key Elements of the Problem Have Not Changed

After more than nine years of operation, it is clear that the mandatory program albeit short of its goals has been, at least until recently, in substantial measure successful. The decline in crude prices has been arrested if not significantly reversed. While the refining margin, within which nonintegrated refiners must operate, remains inadequate, its further decline has been halted.⁹ The decline in independent refiner numbers has been slowed, if not arrested.¹⁰

At the same time, it should be emphasized there has been no favorable change in the basic forces at work which suggests relaxation of the control program. If anything, the pressures of foreign oil have intensified as world supply outstrips demand, and the differential between domestic and world crude oil prices has grown.

Accordingly, the imports auction scheme must be tested, in comparison with the present program (and other alternatives), as a solution to the same problems and as a means to the same objectives with which the Department has been so carefully working in the past ten years.

III. THE IMPORTS AUCTION SCHEME WILL NOT WORK

Instead of the present system the Department now proposes that "Quotas under an auction system would be obtained by means of competitive bidding." The Department states that it will preserve the overall level of import quotas but,

⁸ The underlying circumstances are more complex, of course. A principal circumstance is the fact that the major integrated oil companies, by reason of their ownership of domestic crude oil reserves the price of which is supported by the oil import program, enjoy profits from that program in their crude operations which are not available to the nonintegrated refiner. There are also strong forces at work in the impact of the tax laws to allocate integrated company profits to their crude oil operations, thus creating a price structure for crude oil and refined products in which the refining margin is artificially reduced, with serious effects upon nonintegrated refiners. This is not the place to analyze these circumstances. They have been developed at length in the numerous hearings by the Department of the Interior as well as those conducted by the Federal Trade Commission. For the present purposes it is sufficient to state merely that the graduated scale is indispensable to the survival of independent refiners and their refining facilities so essential to the national defense.

⁹ See Appendix A.

¹⁰ See Appendix B.

as noted above, this is only part of the problem. The new method of distributing import quotas is completely unworkable in terms of any actual solution to the oil import problem.

A. The Auction Scheme Will Produce Competitive Distortions as the Cost Advantage of Foreign Oil Goes to a Fortunate Few, Rather Than Being Shared by All Refiners

The auction scheme will not accomplish the fair distribution of the foreign cost advantage among refiners which, as noted above and as demonstrated by its absence during the period of the voluntary oil import program, is absolutely necessary. Instead import quotas will go to those who bid the most—presumably those companies with the lowest cost foreign oil and refining plants on tidewater. It is obvious that the bids which these companies can make successfully will still leave in their hands a substantial measure of the cost advantage of their foreign oil. With this cost advantage one can expect a return to the situation immediately preceding the Mandatory Oil Import Program when the few companies with the advantage of low cost foreign oil pressed their advantage throughout the national market, depressing the price of domestic crude oil, dampening exploration, and decimating the independent refiner. We have been there before. Why should we return?

Some of the fuzzy thinking behind the imports auction scheme may be based upon the assumption that with competitive bidding for import quotas, the price therefor would tend to rise to the differential between domestic and foreign oil, thus equating the cost of domestic and foreign oil in the United States. There are two serious defects in this assumption. One defect is that in practice such parity will never be realized. Unless there is some substantial cost advantage remaining with the bidder, why should he bid? Look one step beyond—to the nature of the companies who will have the incentive to bid—a handful of major companies with large foreign crude oil holdings. It does not take an antitrust conspiracy to keep the lion's share of the foreign cost advantage in their hands—self-interest alone will lead to restraint in the bidding. The other defect will be discussed under the next heading.

B. The Auction Scheme Will Deny the Inland Refiner Any Share in the Cost Advantage of Foreign Crude. Without a Fair Share in the Cost Advantage of Foreign Oil, Most Refiners Cannot Sustain Present Domestic Crude Oil Prices—So the Auction Scheme Will Fail to Maintain Those Prices

Even if the bid prices equalled the general cost differential between foreign and domestic crude, the auction program will not work. This is because the present important program distributes to *all refiners* a portion of the foreign cost advantage and, under the auction scheme, this cost advantage would be distributed to the Federal Government (and selected refiners) instead. The practical consequences of this change from the present program is that, to that extent, most refiners will be less able to pay the present prices of domestic crude oil.

The sums involved are significant, especially for nonintegrated independent refiners. In the aggregate they are estimated in the hundreds of millions of dollars. The diversion of these vast sums to the government and a few bidders must inevitably be offset elsewhere—by pressure upon domestic crude oil prices, or an increase in product prices, or most likely both.¹¹ If domestic crude prices decline, the program fails. If product prices are increased, the government's anti-inflation program and consumer interests will be dealt a severe blow.

C. The Auction Scheme Will Doom the Graduated Scale

The need for proportionately larger quotas for nonintegrated independent refiners has been noted above. It has been demonstrated to the government and seems to be accepted by the government up to now. The need has been met through the graduated scale.

But the auction scheme must inevitably end the graduated scale. Nor can we conceive of any means by which an adequate substitute for the graduated scale

¹¹ This brings into focus a frequently misunderstood (and more often misrepresented) aspect of the present program—the oft-repeated claim of a “windfall” to inland refiners. It is true that a share of the foreign cost advantage is distributed to inland refiners by the present program (and would be denied them under the auction scheme) but this is no windfall in the sense of an unfair addition to earnings. Instead this is a cardinal feature of the present program which maintains a competitive equality among refiners and which permits the present level of reasonable product prices to be sustained without reduction in domestic crude oil prices. Absent this equality, product prices paid by consumers must increase or domestic crude prices must yield, or both.

could be implanted into any auction scheme. By definition, an auction treats all bidders with the severe equality of equal opportunity to use sheer financial power in bidding.

Even if an effort is made to accord some form of special treatment to those refiners classified as "small business" by the Small Business Administration,¹² it is doubtful that a graduated scale can be applied, since the Small Business Administration makes no distinction between refiners of different size within its definition. Also, clearly those independent refiners not classified as "small business" would be placed in the same bidding category as their major company competitors even though they are much smaller in size and lack the resources of their major company competitors. However, the essential overriding economic and national security fact that has consistently been recognized is the distinction between *all* nonintegrated independent refiners and the major oil companies, and a graduated scale, inconsistent with auction procedures, has consistently been recognized as the way to preserve the distinction.

IV. THE IMPORTS AUCTION SCHEME IS BAD POLICY IN OTHER SERIOUS RESPECTS

A. The Auction Scheme Constitutes a Tax Ultimately Payable by the Consumer

A prime purpose of the auction scheme is to transfer the huge values involved in the price differential between domestic and foreign crude oil to the Federal Government. As noted above, these values will only be partially transferred to the Federal Government—the rest being transferred to the few companies who will gain most by imports and thus bid the highest. But one thing is clear—a transfer of vast sums from the rest of the oil industry will be accomplished.

How will the transfer of such vast sums be offset? Like any other tax or cost of doing business, the exaction of this huge sum from the oil industry must inevitably be borne by higher product prices paid by the consumer. The other alternative would be for domestic crude oil prices to yield and this would strike directly at a fundamental objective of the program.

Insofar as this sum is to be assessed against the consumers of petroleum products we submit that it is bad policy (in view of the large tax burden already imposed on oil users) as well as devious administration (avoiding the normal Congressional approval required for the imposition of taxes).

B. The Imports Auction Scheme Is a Breach of Faith With the Industry Which Will Hurt Our Mobilization Base

While no person or industry has a vested right in a certain type of government action (in the absence of a contract therefor) it is still sound public policy to avoid drastic shifts in programs regulating activities where substantial investments are involved. The auction scheme is a drastic change in the rules of the game rather than a further step in improvement. Plant construction and modification have proceeded for almost ten years on certain assumptions as to the nature and direction of government action which must now be jettisoned.

Besides its disquieting influence generally inhibiting plant construction, if the auction scheme is to be the new policy, it will encourage the very type of refinery construction in the future which is *least* desirable as a matter of national security—on tidewater.

It is pertinent to note that the government's reluctance to effect drastic alterations has justified the persistence for almost ten years of the "historical" quotas. But what about the position of those refiners who relied on express government policy as it has developed in the last ten years? Are they to be treated any less favorably?

C. The Imports Auction Scheme Is Contrary to Trade Expansion Policy

An auction price is for all practical purposes a duty or tariff, albeit variable, and as such contrary to the trade expansion policies. It is much more than an "adjustment" of imports so as not "to impair the national security", which is what, and only what, the statute permits. It is inconsistent with the status of import controls as a very limited national security exception to trade expansion policy.

V. THE IMPORTS AUCTION SCHEME IS PROBABLY ILLEGAL

While we appreciate the present-day tendency to give the Executive maximum leeway within the scope of his statutory authority and we recognize also that

¹² Discussed in some of the press reports on this subject.

the Department would not have proposed the auction scheme without at least a tentative conclusion that it had authority so to do, nevertheless we submit that this proposal transgresses the President's and the Department's existing statutory authority for import controls. The proposal is probably illegal on at least three grounds.

(1) It is contrary to and in excess of the limited *national security* basis and purpose in the underlying statute. For the reasons shown above, it will actually frustrate attainment of purely national statutory objectives. We see no other national security interest, certainly for example, not in the mere sale of quota tickets.

(2) The auction scheme is in substance and effect a tax without compliance with the basic rule that all taxation originate in the House of Representatives. While the price paid by the bidder may be described or labeled under some other name, the simple fact is that the government can collect money by three principal means: a) the sale of government-owned goods or government-rendered services, b) the acceptance of gifts, and c) the imposition of taxes. The payments proposed to be made for import quotas are clearly not in the first two categories. The cost advantage of foreign crude oil is not property of the Federal Government; it cannot be sold; it can only be regulated or taxed.

(3) The government's expressed intent to permit Phillips and Hess to continue to ship petroleum products into the United States under the agreements in respect thereto between those companies and the Secretary raises still further legal questions. While this intent does not expressly appear in the release of March 20, 1968, it has been reported on more than one occasion in the trade press. The agreements with Phillips and Hess did not exempt those companies from payment of import duties, fees and other charges incident to shipment into the United States. Therefore, if the auction scheme should become a reality, it would appear that these firms should be required to pay whatever fee is assessed against other importers under the auction scheme. If not, there will exist the basis for a serious charge of administrative discrimination.

While it may be that these legal defects could be cured through appropriate legislation, such legislation is apparently not intended by the Department's proposal. In the absence thereof, the legal difficulties are so great as virtually to assure a legal challenge to the auction scheme and to place the program in doubt while that legal point is settled.

VI. IMPROVEMENTS, WITHIN THE BASIC STRUCTURE OF THE PRESENT PROGRAM, ARE IN ORDER

We are mindful of the many serious complaints which have been made, and recently in increasing number, with respect to the present oil import program. Indeed, this Association has itself been critical of certain recent tendencies to depart from the essential basis of the Mandatory Oil Import Program in such matters as the special deals for Phillips and Hess, petrochemical plants, etc. Such deviations from a sound, regulatory structure properly invite criticism from those who are otherwise most interested in its integrity.

We are afraid, however, that the present volume of criticism, from friends and foes alike, has been misconstrued by the Department. What is needed to quiet these criticisms is a return to the basic essentials of the original program and the gradual, evolutionary improvement in that program. By basic essentials we mean quotas to all refiners on the basis of refinery inputs and with the graduated scale. By improvements we mean the prompt elimination of historical product quotas (which have been continued for all these years without even partial phaseout) and the correction as soon as possible of the petrochemical aberration—and an end, of course, to other special deals such as Phillips and Hess.

DEPARTMENT OF THE INTERIOR—INFORMATION SERVICE

(For release on delivery)

ADDRESS BY HON. ELMER F. BENNETT, UNDER SECRETARY, DEPARTMENT OF THE INTERIOR, TO THE NATIONAL PETROLEUM ASSOCIATION, CLEVELAND, OHIO, APRIL 21, 1960 AT 2:30 P.M.

THE FIRST YEAR OF THE MANDATORY OIL IMPORT PROGRAM

It is indeed a pleasure to be here. I want to thank your president, Mr. Blazer, your eminent counsel, Mr. Dow, and your presiding officer, Don O'Hara, for

this opportunity to discuss some aspects of the Department's interest in your industry.

Your association constitutes the first successful cooperative effort toward industry organization in the petroleum field. While the National Petroleum Association is not the largest trade association today, it is second to none in reputation and integrity.

This is your 56th mid-year meeting, but it would seem that the petroleum industry faces many of the same problems it confronted in 1902—when the National Petroleum Association was founded.

Then as now, the industry is in transition.

Old markets cannot fully absorb the output of your refineries, and the markets of the future have not yet been fully developed.

The future economic problems of oil—even in the midst of general prosperity—are unpredictable. Competition is keen. The prices which you receive for your products—so I am told—are close to safe operating margins.

The problems of today may seem insurmountable to some. I imagine the problems of 1902 seemed equally insurmountable to many, except perhaps to the 20 independent refiners who gathered in the Hotel Lincoln in Pittsburgh in June of 1902 to organize this association.

The National Petroleum Association will be 58 years old in June. It spans the years of transition from a kerosene-based industry to its present status as a modern industrial giant without which our way of life would be impossible. Historians often refer to the Stone Age, the Bronze Age, and the Iron Age. Because of its importance in the industrial and personal lives of all of us, the oil industry truly has made this the Petroleum Age.

You here today have blazed the trail from yesterday to today—a trail which others have followed. I am sure that this leadership, mature and forward-looking in its judgment, will help to find a constructive path through the mists of the future as it has the fogs of the past.

When Mr. O'Hara suggested that I speak about the first year of the mandatory oil import program, my initial inclination was to suggest another topic. The subject is highly controversial—as we all know. I imagine a poll of the views of those present would divulge many conflicting opinions. No matter what I say—I cannot possibly please all of you. But that, my friends, is the inevitable price of public life.

As you know, the President has given policy and operational responsibility for the oil import program to the Department of the Interior.

"To place the first year of the mandatory oil import program in proper perspective, one must review the developments which led to the President's decision last year to impose mandatory controls on oil imports.

"In 1944, the United States became a net importer of petroleum—after 85 years of world leadership in the export of oil products. Since that time, segments of the refining industry have been dependent—in varying degrees—on oil imports to meet a portion of refinery demand.

"The reasons for this dependency are manifestly economic. To the best of my knowledge, however, shortage or unavailability of domestic petroleum has never been a major factor in the import programs of the Nation's oil companies.

"By 1954, a short span of ten years, oil imports had risen to a level which evoked concern, and in early 1955, the President's Committee on Energy Supplies and Resources Policy reported that oil imports would endanger the national security if they should significantly exceed the 1954 ratio of imports to domestic production. There seems to be little controversy on the principle that a healthy rate of domestic exploration and development is essential to the defense security of our Nation.

"We entered a period of 'industrial statesmanship' in which the Government requested the major importers to restrict their imports voluntarily. There were no levels, no quotas. To the credit of many, I must say that this plea was honored by most of the industry.

"There were, however, a few whose actions made it clear that this approach would not achieve the fundamental aim of a stable, healthy domestic petroleum industry, financially and technically capable of exploring for and developing new domestic petroleum reserves.

"As a result, another committee—composed of the heads of six major Federal departments—developed a voluntary program for the control of oil imports based on individual recommended levels. Most of you no doubt are familiar with that program.

"This voluntary program worked reasonably well, considering its many inherent limitations. The vast majority of importers, as they had done earlier, adhered voluntarily to their recommended allocations.

"Again, however, the actions of a few, often for reasons beyond their control, undermined the effectiveness of the voluntary program, and the enforcement weapons of education, persuasion, and public opinion proved inadequate to do the job.

"Other factors were also at work, sounding the deathknell of the voluntary program.

"Some importers limited their imports of crude oil as requested, but at the same time increased their imports of unfinished oils and finished petroleum products. Imports of finished products, in fact, jumped slightly over 100 percent between 1957 and 1958. In unfinished oils, the increase skyrocketed some 2900 percent in the same period.

"Caught in the two-fold squeeze of declining general business and the competitive pressures from large importers with access to lower-cost imported crude, the domestic refiner was faced with serious problems. I would be less than frank if I did not point out there was grave concern within the Federal Government about the future of the independent refining segment of the industry.

"I think we will all agree that the independent refiner—as well as the independent producer—plays an essential part in a healthy domestic petroleum industry.

"The stage was set for a change. The ingredients were there.

"First, there was noncompliance by a few companies in observing recommended crude oil import levels.

"Other firms were indirectly threatening the program by increasing their imports of other products to avoid the impact of the crude controls.

"The independent refiner was threatened with extinction by those integrated companies whose refinery locations gave them access to lower-cost raw materials but whose marketing areas everywhere permitted fullest use of this competitive advantage.

"Domestic exploration and development had not responded to the stimulus of the voluntary program and was still headed downward. The Administration warned that mandatory controls were the likely alternative in event of failure of the voluntary approach. Top officials of the Department of the Interior pleaded publicly and privately for support and cooperation.

"The rest is history, and I am sure you are familiar with its pages. I must say at this time that those who dislike the mandatory program must look to their industrial neighbors—and in some instances to themselves—in placing responsibility for mandatory oil import controls. Only with the greatest reluctance and after most careful consideration did Secretary Seaton and I concur in the conclusion that the time had come for the government to interfere in the normal processes of competition and the marketplace.

"Once the need for such controls became apparent, the problem then was clearly one of how best to allocate allowable imports of crude oil. Unless it is refined, crude oil has little economic or utilitarian value. Unless it is changed into products for the marketplace, crude oil is merely another mineral substance of the earth.

"The key, of course, is the refining process. Here man's technology and labor add the economic and useful value. Crude oil—foreign or domestic—must be refined. In further seeking the impartial standard against which all could be measured, it became obvious that refinery inputs were again the common denominator, and as a logical consequence, crude oil allocations have been based on such inputs. The very bedrock of the program had to be a fair sharing of the competitive advantages of imported oil. Our only practicable alternative would have been a steeply reduced quota level which might well have had severe international and domestic repercussions.

"The adoption of the impartial standard of refinery—a standard based on common ability, rather than special circumstance of one form or another—would indeed be a hollow mockery without adequate and fair provision for the exchange of foreign oil for domestic oil.

"Exchanges of petroleum are not a peculiar monster of the import program. Rather, they are historic devices of mutual benefit within your industry. And in the marketplace there has never been a distinction between exchanges of purchased oil and oil produced by parties to the exchange.

"I am sure that many of you have heard—even possibly support—the sentiment that an allocation granted to an inland refiner is a "windfall" or unearned gift from the Federal Government.

"This conclusion overlooks, first, the fact that the inland refiner meets the impartial test I have set forth earlier as leading to selection of the refinery input criteria.

"Secondly, I prefer to think that a real windfall, a really unfair competitive advantage, would result if the Federal Government conferred exclusive crude oil import rights based solely on geographic location.

"Before accepting the "windfall" statement, I think a little examination of the nature and mechanics of exchanges should be considered.

"It takes two parties to make an exchange. We assume that these parties, in business transactions, are dealing with each other at arms' length. We also assume that each has weighed the advantages and disadvantages of the exchange and have concluded that the former outweigh the latter. We further assume that each party enters into the agreement in accord with his concept of his own best interest.

"Secondly, the producer of the foreign crude is not required to sell to the inland refiner. The tanker owner is under no obligation to transport the oil. Nor is the major company under any compulsion to exchange domestic crude oil for the inland refiner's foreign oil.

"On each count, the transaction is entirely voluntary—and, from one point of view or another, advantageous.

"By common definition, a windfall is generally considered as an unexpected legacy or profit or preferred position. If such a windfall accrues to one party to an exchange, it must necessarily be given to him by the other party on a voluntary basis.

"The real windfall would, in fact, accrue if the Federal Government by administrative decree protected the import position of a refiner because of geography or overseas productive capacity and denied access to all others.

"Actually, the system adopted is of mutual benefit to all. The inland refiner is not discriminated against, nor is he subject to unfair competitive conditions from which he has no recourse. The coastal refiner has the opportunity to obtain additional quantities of imported crude oil—over and above his own allocation—which he would not otherwise get in the absence of the exchange. Many of your members are taking advantage of this benefit.

"The windfall idea may possibly arise because some importers believe that, in the absence of the exchange provision, they would get the imported oil now allocated to the inland refiner. If any of you subscribe to this view, let me assure you that it is probably erroneous. If exchange agreements were not allowed, the coastal refiner would not receive any larger allocation than under the existing program, because we would then be under tremendous pressure to allow unused quotas to expire or to set total quotas at sharply reduced levels.

"Actually, there is an important aspect of the exchange-agreement provision which directly supports the policy objective of the mandatory oil import program. It would appear logical to assume that a domestic producer who cannot sell his product also would be unable financially to seek new domestic reserves. Similarly, domestic refiners required to use only high-cost raw materials cannot live in today's highly competitive conditions.

"The stability of the market which is necessary to provide the financial incentive for new exploration and development is a basic objective of the oil import program. During the first half of this year, in excess of 280,000 barrels per day of domestic crude oil will find a market in District I-IV because of the exchange-agreement procedure. This, as well as the basic limitation on imports, is in direct support of the President's national security policy.

"The security of our people and our Nation dictate that we maintain a stable, healthy petroleum industry—and a stable, healthy industry requires a stable market."

We have now just completed one year of operation under the mandatory oil import program. What has been accomplished?

According to the impartial and authoritative *Oil and Gas Journal*, there were 50,893 oil wells drilled in the United States in 1959. Completions averaged 3.6 percent higher in 1959 than in 1958.

Of the total wells drilled, 25,379 were crude wells, 1,255 were condensate wells, 3,761 were gas wells, 1,397 were service wells, and 19,101 were dry holes.

The decline in exploratory work which began in 1957 was halted—permanently we hope. There were an average of 2,074 rotary rigs operating in the United States in 1959, about eight percent higher than the previous year.

There were 10,073 wildcat wells drilled—about 19.8 percent of all wells drilled and about five percent greater than the 1958 level.

Proven reserves of liquid hydrocarbons registered another record high, with more than one and one-half billion barrels added to the Nation's proven reserves over and above the production for the year.

We would not be so foolhardy as to claim that the mandatory oil import program is entirely responsible for this modest, but encouraging, upswing. However, in fairness, we do claim it has been an important contributing influence, both materially and psychologically.

In retrospect, I think it fair to say that the present program is succeeding where—despite a valiant effort—the voluntary program was doomed to failure.

Crude oil markets have been influenced by the stabilizing effects of the program—and, while these markets do not fully meet the desires of the domestic producers, many have frankly stated that the market conditions would probably be far worse without the program.

Well completions and wildcat activity have moved modestly upward.

There are more crews in the field seeking oil.

The possibility of economic extinction no longer faces the efficiently operated independent refinery.

The oil industry—indeed, each company—can properly assess the impact of imports on over-all business activity.

These achievements provide a firm basis—a foundation—upon which another advancing era for the oil industry can be built.

Many problems face you. Consumer demand is not rising as rapidly as it has in past years. Your refining capacity outstrips the demand for products. As a consequence, inventories are high.

You will note, however, that excessive imports are not generally listed in the table of contents of today's problems.

From the beginning, we in the Department of the Interior insisted that crude oil imports were not the sole cause of the problems faced by the petroleum industry. Today, we insist with equal vigor that mandatory controls on oil cannot solve all of the current problems of the Nation's fuel industries, nor should they be expected to. These controls will play only a supporting role in your future stability.

Initiative, ingenuity, business acumen, and sound judgment gave this Nation its magnificent petroleum industry. To these positive values—as distinct from governmental action—you must look to find the answers to the full scope of the problems of the industry.

In this effort we seek to be helpful.

PETROLEUM INDUSTRY RESEARCH FOUNDATION, INC.

New York, N.Y., July 2, 1968.

Mr. LEO H. IRWIN,
Chief Counsel, Ways and Means Committee,
U.S. House of Representatives,
Washington, D.C.

DEAR MR. IRWIN: As part of the hearings on foreign trade legislation currently held by your Committee, the dates of June 27th and 28th were set aside for the U.S. oil industry. While our organization did not participate in these hearings, we had expressed our views on the subject of oil imports on May 16, 1968 before the Subcommittee on Mines and Mining of the House Interior and Insular Affairs Committee.

We would like to submit a copy of the testimony given by our organization on that occasion for inclusion into the record of the hearings held by the Ways and Means Committee. We understand the records of your Committee are being kept for such additional submissions until July 3, 1968.

Sincerely,

JOHN H. LICHTBLAU,
Director of Research.

STATEMENT OF PETROLEUM INDUSTRY RESEARCH FOUNDATION, INC. (PIRINC)
 PRESENTED BY JOHN H. LICHTBLAU, RESEARCH DIRECTOR, BEFORE THE SPECIAL
 SUBCOMMITTEE ON OIL IMPORTS OF THE COMMITTEE ON INTERIOR AND INSULAR
 AFFAIRS, U.S. HOUSE OF REPRESENTATIVES, MAY 13-16, 1968

Few policies of the Federal government have been the subject of more controversy than the mandatory Oil Import Control Program in existence since 1959. The reasons for this controversy are manifold. One factor is that both the cost of the import restrictions to consumers of oil and the benefit of the restrictions to the domestic producers of this commodity are truly gigantic. With the exception of residual fuel oil whose importation is more or less unrestricted, the control program has largely insulated the U.S. oil business from foreign competition. As a result every major oil product sold in the U.S. is significantly more expensive than it would be in the absence of the federal import controls. Estimates of the total cost of the controls to the American consumer vary from \$3 to \$4 billion per year, depending on the assumptions made regarding the penetration of foreign oil into the U.S. market under conditions of free entry. The benefits of the import controls to U.S. oil producers are of course on the same order as the cost to consumers.

Overriding both of these is the significance of the restrictions to the U.S. national security—the sole reason for their imposition and continuation. It would be difficult to assign a dollar value to the national security benefit of the oil import restrictions. However, we can say that, everything else being equal, in the world we live in domestic oil is safer than foreign oil and oil coming in overland from adjacent countries is safer than oil brought in from overseas, from the point of view of our national security. We have seen a clear demonstration of this principle during the Middle East crisis of last summer when Western Europe and Japan came dangerously close to a serious oil shortage while we replaced our own import fallout with ease and were even in a position to export substantial quantities of oil to Europe throughout the emergency. In the absence of the imports restrictions the oil aspect of the Middle East crisis would undoubtedly have been a matter of major domestic concern for us. In addition, our import dependency would probably have aggravated the scope of the potential oil shortage for Europe and Japan.

Thus, we do have tangible evidence of the benefit of U.S. import controls. But it should never be forgotten that the cost of these benefits to U.S. consumers is extremely high and has been rising since 1959 as U.S. and foreign oil prices have tended to move in opposite directions.

On the West Coast (District V) total oil imports have been declining in the last several years, both in actual volume and as a share of total demand. This is in accordance with the import formula for that area. In the rest of the country (District I-IV) imports—except for residual fuel oil—have been held to the ratio of 12.2% of the estimated domestic crude and natural gas liquids production in that part of the country. Since 1960 actual oil imports in District I-IV have never varied from that ratio by more than a small fraction of 1%. Thus, the government has successfully held the line on total oil imports throughout the existence of the Control Program.

But the figure of 12.2% is not a magic number, necessarily superior to any other. It was adopted as a matter of practical policy to maintain the status quo on U.S. oil imports and as long as it is desirable to continue maintaining the status quo the 12.2% ratio is a useful tool. But we do not believe it should be accorded the force of law, as has been advocated by spokesmen of some domestic oil producers. For the time may come, when we will have to liberalize our oil import policy to prevent the cost of the program from becoming oppressive relative to its benefits.

We would now like to address ourselves briefly to the distribution of oil imports within the 12.2% limit. It is this aspect of the imports program, rather than the overall volume of foreign oil entering the U.S., which has drawn most of the criticism and controversy in the last couple of years. A few statistics will illustrate the reason. In the first half of 1960, total imports, other than residual fuel oil, into Districts I-IV amounted to 847,000 barrels daily. In the first half of 1968 comparable imports will amount to 1.1 million barrels daily, an increase of nearly 30%. Yet, during the same period crude and unfinished oil imports allocated to companies classified as refiners in Districts I-IV declined from 719,000 barrels daily to 592,000 barrels daily—a drop of 18%.

Even more telling is the decline in quota allocations to the twelve refiners located at the Eastern Seaboard. These refiners who are the only ones to process their allocated import quotas in their own plants, saw their allocations cut from 432,000 barrels daily to 279,000 daily between 1960 and 1968, or from 51% to 25% of total imports brought in under the 12.2 ratio.

There are several reasons why refiners in general and East Coast refiners in particular did not participate as a group in the growth of oil imports. The principal ones are a) a substantial increase in shipments from Canada to refiners with plants near the Canadian border, accompanied by reduction of their overseas import licenses; b) the inclusion of petrochemical manufacturers in the Import Control Program; c) the granting of special import quotas to refiners with offshore plants in U.S. possessions and territories and d), in the case of East Coast refiners, the phasing out of historical quotas, based on imports before March, 1959 and their replacement by an input formula which discriminates against large companies such as most East Coast refiners.

The special status of Canadian oil imports has been included in our import regulations since almost the beginning of the Program and is based on our national security requirements. The other three features, however, have little or nothing to do with national security. These features have caused most of the criticism of and loss of confidence in the Interior Department's handling of the Oil Imports Program. For each new inclusion into the Program and each special quota issued under it reduces the quotas available to all other participants. This, in turn, has caused some of these others to seek similar special privileges. The result has been a serious general undermining of the whole Import Program. The Interior Department's oil import policy in this regard seems to be based on a belief that the import quotas represent a federal bounty which the government is free to dole out at its discretion to what it considers deserving parties and causes.

The request for expansion of the Program to non-refiners has by no means come to an end. At the moment the petrochemical industry is arguing for an Import Program for petrochemical feedstock to be kept "separate" from oil imports reaching the U.S. energy market. However, the petrochemical industry's "separate" import quota system includes the provision that petrochemical plants may transfer their import quotas to domestic refiners in exchange for the delivery of domestic petroleum feedstock. The recipient refiners would be free to use these quotas just as they do their own. This obviously makes nonsense of any separate petrochemical Import Program. If the quotas transferred by petrochemical producers to their refiner-suppliers are given within the 12.2% limit, all existing quotas would have to be reduced to make room for the petrochemical industry's quota. If they are given outside the 12.2 limit, more domestic crude oil would be displaced by imports than is presently the case. Either way, the supply of oil for the production of energy products would be affected by this scheme.

The petrochemical industry has originally asked for a share in the Oil Imports Program on grounds of competitive equity with refining companies, many of which produce also petrochemicals. By now the petrochemical industry receives import allocations equivalent to 10% of its feedstock inputs whereas those oil refiners who also have a significant petrochemical production receive on the average import quotas equivalent to only about 4.5% of their total inputs. Under the Chemco plan, forwarded by a group of major petrochemical producers, the industry's input of foreign feedstock would rise to a theoretical 100% by 1972. If this plan is implemented it cannot help but wreck the entire Oil Import Program.

The petrochemical companies contend that they must have access to foreign feedstock to be internationally competitive. If this contention is correct they should be satisfied with import quotas limited to petrochemical feedstock which cannot be exchanged but must be processed in the importer's own plant. Apparently the petrochemical producers are not interested in this type of import quota. Up to now nearly all petrochemical imports have consisted of foreign crude oil which was traded off against domestic feedstock at the standard profit for import quotas of about \$1.25 per barrel. This amounts to a subsidy, paid out of the pockets of the U.S. refining industry. The Interior Department should not increase this subsidy by accepting the Chemco plan in its present form.

We would like to conclude our testimony with some comments on the question of distillate heating oil imports into the U.S. East Coast, a subject which has

been under active debate since last summer. Since this is a sensitive issue with many different views and non-views, I would like to stress that the views stated here represent only the thinking of PIRINC.

The question of distillate heating oil imports must be related to the availability of supplies during the past heating season. Given the facts that a) the last heating season was 8% colder than normal from September through February, b) that the refinery runs of East Coast plants were below that of the previous year from the end of June 1967 through April 1968 as a consequence of the temporary decline in imports brought about by the Middle East crisis and c) domestic-flag tankers were in short supply due to strategic reasons, it is not surprising that some sporadic local shortages developed in the course of last winter. However, there was no evidence of a general shortage in any East Coast State nor were there complaints from end users of heating oil about inability or even difficulty to obtain supplies. Thus, oil heat suppliers and distributors have weathered a most difficult winter without any hardship to their customers.

At the moment distillate oil inventories are considerably higher than a year ago and the outlook is for adequate supplies to continue. In our view there is no sign whatever of a structural shortage of distillate oil in this country. True, distillate oil yields east of California have shown a modest decline from 22.75% to 22.21% of total refinery runs from 1965 to 1967, reflecting the fact that demand for this product is growing more slowly than for gasoline or jet fuel. But during the same period the volume of distillate fuel oil output east of California has increased from 689,000 barrels daily to 732,000 barrels daily or by 6.2%.

Thus, distillate fuel oil continues to be the second largest product made by domestic refiners. Unlike domestic residual fuel oil, distillate heating oil is neither a by-product of refinery operations nor is it an unprofitable product. Refiners have therefore always geared the supply of this commodity to its demand. There is no reason to assume they will not continue to follow this practice in the future.

However, the next winter could conceivably be even colder than the last one while domestic-flag tankers might again be in short supply for any number of reasons (a fact which would particularly effect New England which is not supplied by long-distance products pipelines and has no local refineries). Any such temporary supply dislocation on the East Coast might create temporary shortages possibly at the peak heating season. The result could be further price increases of distillate heating oil to the detriment of consumers who cannot switch to other fuels and as well as the detriment of independent heating oil marketers whose sales are already under heavy pressure from competing utility fuels.

Despite its recent price increases, distillate fuel oil is still a bargain. In New York and Boston, for instance, it sells now 14% and 18% respectively above the 1957-9 price level, according to the Bureau of Labor Statistics' consumer price index. By comparison, all consumer products and services in the same two cities show an increase of 21% and nearly 22% respectively. But the price gap between distillate fuel oil and natural gas has significantly narrowed in the last two years, a fact which is of major concern to many fuel oil marketers. Future shortages, even of a very temporary nature, might cause it to narrow still further.

Given these circumstances a limited volume of distillate fuel oil imports might be desirable under certain conditions as a balancing item. However, they must be distributed equitably and kept to a minimum in order not to violate a basic tenet of our oil imports policy which hold that as long as imports restrictions are required the U.S. should import crude oil rather than finished products available domestically, in order to maintain a healthy domestic refining industry.

In our opinion the Oil Imports Appeals Board is not the correct agency for allocating such imports, since by its very nature the O.I.A.E. is set up only to distribute import quotas on a special hardship basis. Temporary distillate oil dislocations are likely to affect all marketers in a given area. It would therefore be inequitable to give some of them access to lower-cost foreign distillate oil to offset the dislocation, while others are denied this privilege.

In view of the sharp cost differential between the foreign and domestic product we also doubt the equity of giving permanent import quotas to some marketers of this product while their competitors have to continue to purchase all their

requirements from domestic sources. Furthermore, the need for import quotas may vary from heating season to heating season.

We would therefore like to suggest an approach which is based on the principle that under normal conditions U.S. refiners are willing and able to supply all the distillate heating oil required at the East Coast. Under these conditions the Interior Department would only need to provide for possible temporary shortages. This could be accomplished by letting refiners bring in a fixed small share of their quota imports in the form of finished products, similar to the fixed share of unfinished oil which they may bring in under existing quotas. This provision would, in our opinion, have the following advantages:

1. The imports would be distributed equitably, since the distribution channels would be exactly the same as those through which the domestic oil (which accounts for 96% of total supplies) moves to wholesalers and retailers.

2. The requirements to give up an equal amount of crude oil would assure that refiners would import distillate oil only to the extent to which an actual shortage may exist, since they would have no other incentive to exchange crude oil for distillate oil.

3. The proposed plan would minimize the drain of distillate oil imports on the U.S. Balance of Payments, both because refiners could be expected to minimize their volume of imports and because the requirements to give up crude oil would reduce the net dollar outflow per barrel from what it would be if there were no offsetting reduction in crude oil imports.

The plan suggested herein may require a slight modification of the Presidential Proclamation on oil import controls. But this should not present an obstacle to its adoption, if it is otherwise found acceptable.

OHIO OIL AND GAS ASSOCIATION,
Newark, Ohio, May 27, 1968.

COMMITTEE ON WAYS AND MEANS,
U.S. House of Representatives,
Longworth House Office Building, Washington, D.C.

GENTLEMEN: The Ohio Oil & Gas Association sincerely appreciates this opportunity to comment briefly and specifically on the subject of oil import quotas. We are an association of over 900 members representing the drilling and producing segments of the petroleum industry operating in Ohio. Our Association has supported the Mandatory Oil Import Program since its inception and for several years prior to that we advocated the need for such a program.

OIL IMPORTS PROGRAM—EXEMPTIONS

The present oil import program has undoubtedly served to some degree to help insure our nation's security the past ten years but we are extremely disturbed by certain tampering with the program in the last two years. This has taken the form of special exceptions, or exemptions, to the import program that are economically selfish and politically inspired but that in no way serve the basic purposes of the program; the safeguarding of our nation's security with a strong domestic petroleum industry.

The exemptions being granted by the Secretary of Interior are best illustrated by new import allocations going to certain companies with new refineries in Puerto Rico and the Virgin Islands; quotas being granted, and more contemplated, for petrochemical companies; and just last week the issuing of a new proposal designed to provide bonus imports of crude oil for the manufacture of low-sulphur residual fuel oil. The concern by Interior for the economic well being of these islands and the desire to help in the air pollution problem are admirable and have merit, but to use the national security based oil import program as the vehicle for such plans is inexcusable. These kind of actions will eventually be the cause for the program's demise and will assuredly cause irreparable damage to our domestic petroleum industry, particularly the drilling and production segments.

DAMAGE TO INDUSTRY

Our industry cannot stand much more of this abuse. Statistics will be furnished you showing that drilling for new oil is down critically from ten years ago and that the price for crude oil has never really regained the overall levels it reached in 1957. In our own case, the price for crude oil in Ohio is lower now for

all grades of oil than it was in 1948. This does not take into account any adjustment for cost of living increases and obviously we are paying much more for all our goods and services. How much longer our people can endure such a situation is not known but we have already lost many of them and more are leaving. Is this building a strong domestic producing industry to help assure our national security?

RECOMMENDATION

The imports program has never been perfect but it is now being rapidly turned into a disgraceful sham. Something must be done soon to bring the program back to its relative stability of a few years ago with adequate safeguards to assure that necessary changes will be made on an equitable and meaningful basis, always keeping in mind the original intent of the program. The Ohio Oil & Gas Association endorses the twelve point program on oil imports of the Independent Petroleum Association of America with particular emphasis at this time on point number XII: "Immediate support of legislative action to provide long-range stability in the import program to assure both the funds and incentives for finding and developing adequate domestic reserves." Experience dictates the need for this type of legislation, which is now pending in Congress, since the basic levels of imports supposedly allowed under the program have been circumvented on many occasions.

SUMMARY

It is obvious that the administrative fiat being used to grant the special treatment to a few will certainly be harmful to the majority. We do not doubt for a moment that such actions are putting our country on a direct course of dependence on unreliable foreign oil and will further aggravate by several hundred million dollars the present \$2 billion annual deficit in our balance of payments from oil imports. This necessary legislation will establish a reasonable level of oil import quotas that will assist our domestic petroleum industry in finding and producing adequate reserves as needed for the security and economic well being of our great country.

Sincerely,

DAVID H. BELL, *President.*

STATEMENT OF ROLAND A. WHEALY, VICE PRESIDENT, ASHLAND OIL & REFINING CO.

Mr. Chairman and members of the committee, my name is Roland A. Whealy. I am a vice president of Ashland Oil & Refining Company, a Kentucky corporation, with its principal office at 1409 Winchester Avenue, Ashland, Kentucky. I reside in New York, New York.

The company (herein called "Ashland") is engaged in all phases of the oil business, including production, refining, transportation and marketing. It is a largest net purchaser of crude oil.

We appreciate this opportunity to express our views as to the Mandatory Oil Import Program, a program limiting the importation into the United States of very low-priced foreign-produced crude oil, unfinished oils and certain petroleum products to such a level as to maintain a strong and vigorous domestic petroleum industry capable of meeting any national emergency. Evidence of importance of that capability was clearly demonstrated last summer when U.S.-produced crude oil not only met additional domestic demands due to interruption of supplies from the Eastern Hemisphere, but also supplemented requirements in Europe and Canada. Had not such a program been instituted in March 1959 there is no doubt our petroleum producing capabilities would have been in such a state of deterioration as to have been unable to meet the challenge. We are in full accord with the original objectives of the program, that is the legal and public policy to maintain a healthy and vigorous petroleum industry in the United States in the interest of national security.

In expressing our views to the Committee we wish to convey to you our deep concern, particularly as it applies to the administrative deviations from these objectives, which we believe are gravely undermining its effectiveness, and to urge corrective action which we consider essential if the program is to serve its proper purpose. We believe that Congressional action is needed to provide definite and meaningful guidelines to restore the program to its original national

security objectives and to assure the required stability. The continuous manipulations of proclamations and regulations are threatening its ultimate destruction.

We shall address our remarks primarily to the area east of the Rocky Mountains (District I-IV).

FIRST.—THE LEVEL OF IMPORTS

Based upon careful investigation, it was determined that the level of oil imports (not including residual fuel to be used as fuel) should be 12.2% of the estimated domestic production of crude oil in Districts I-IV. As a result of administrative action, serious departures from this formula have occurred, which have increased imports to volumes in excess of this level. These departures have taken the form of exemptions of certain petroleum products from controls. Moreover, by amendment to the governing President Proclamation, the Secretary of the Interior has been authorized to provide such an exemption for asphalt. An amendment to the regulations recently proposed for comment could create additional overages associated with bonus allocations for production of low-sulphur fuel. We understand that a plan involving bonuses for exports is also under consideration.

SECOND.—INEQUITIES IN ALLOCATION OF CRUDE OIL IMPORTS

Initially, crude oil imported were allocated in a generally equitable manner based upon refinery inputs of crude oil. Some recognition was given to historical import position, under arrangements which called for a gradual phasing out of higher quotas, (other than those for refined products) derived from historical experience. This system of granting quotas creates the medium through which the benefits to holders of the licenses are used to average down the cost of the higher priced domestic crude oil they refine. In this manner domestic crude prices have been supported.

The program was effectively administered in substantial record with this principle until 1965. During that year a large allocation was made to an oil company with respect to refining and petrochemical facilities in Puerto Rico, including permission to import large volumes of finish petroleum products (principally gasoline) into the continental United States. In addition, the petrochemicals made from this low-cost raw material have ready access to the U.S. market. This was for the announced purpose of supporting the Puerto Rican economy. This allocation not only diminished benefits originally intended for the domestic industry, but conferred upon the oil company so favored a significant competitive advantage in the U.S. market.

A dangerous precedent was set, with no end in sight. Thus, a similar special arrangement has been made in the Virgin Islands and additional allocations of the same type have been made to two other oil companies and a chemical company in Puerto Rico this year. Special interest proposals of the same kind are pending with respect to two more Puerto Rican ventures, and others in Guam, the Virgin Islands, and Newfoundland. The volumes involved are of such magnitude that, unless this trend of discriminatory administrative action is reversed, the basic purpose of the program will be subverted, with the result that imports of finished products will be substituted for crude oil. This would mean serious impairment of the capability of the domestic refining industry to supply domestic demand in times of emergency and an excessive dependence upon offshore manufacturing facilities, with grave implications for the national security.

THIRD.—ALLOCATIONS TO THE PETROCHEMICAL INDUSTRY

Beginning in 1966, petrochemical and chemical companies were granted allocations to import crude oil and unfinished oils, based upon the use of domestically produced unfinished oils as feedstocks, thus causing the pyramiding of inputs for purposes of earning crude import allocations. Even though these companies rarely use crude oil as a feedstock they are now enjoying the benefits of crude import allocations out of all proportion to their contribution to the well-being of the domestic petroleum producing industry. This is manifestly unfair to domestic refiners whose import allocations are based upon inputs of domestic crude and clearly impairs the effectiveness of the Oil Import Program in relation to its primary purpose.

Notwithstanding the preferred position already achieved, the chemical industry now seeks, with strong support from the Department of Commerce, unlimited

access to foreign hydrocarbon feedstocks. If granted, this special privilege would gravely undermine, if not destroy, the Oil Import Program.

FOURTH.—QUOTA BIDDING

Earlier this year the Secretary of the Interior announced that consideration was being given to a proposed system for auctioning oil import licenses and invited comments. Ashland vigorously opposes such a system. A copy of our letter of April 17, 1968, to the Oil Import Administrator on this subject is attached as Exhibit A.

FIFTH.—A CONTINENTAL APPROACH

It is increasingly clear that domestic supplies of crude oil are becoming inadequate to meet long-range domestic demand. Even last year production of crude in the United States exceeded the additions to proven reserves. The interruption of supplies from the Middle East and from Nigeria as a result of disturbances in those areas highlights our ultimate dependence upon all North American sources of crude oil. There is no doubt that every appropriate step should be taken to encourage domestic exploratory effort, particularly through restoration of the central purpose of the Crude Oil Import Program. We believe, also, that the time has come for full integration of United States and Canadian sources into a single supply system and that Canadian crude should be given the same consideration as domestic in all respects.

SIXTH.—STABILITY OF THE OIL IMPORT PROGRAM

In recent years, the Oil Import Program has been subjected to frequent alterations and manipulations to achieve a variety of purposes unrelated to, and often in conflict with, its fundamental objectives.

Special allocations granted by the Appeals Board in the absence of clear criteria and to serve purposes outside the proper scope of the program, frequent changes in definitions of terms of regulations with a mounting complexity and confusion in interpretation, resulting in near administrative breakdown, discriminatory arrangements for offshore facilities and chemical operations, bonuses for low-sulphur products, and the prospect of import quotas as rewards for exports—all these create a basic instability and a lack of confidence in the integrity of the program. The impairment of the fundamental purpose resulting from these deviations, distortions and confusions, already operates to deprive the oil industry of intended benefits. Thus pressure is exerted to depress the price of crude oil and to increase refined products prices, at a time when the nation urgently needs additional crude oil supplies and when inflation threatens the national economy. Moreover, the oil industry is seriously handicapped in the long-range planning of its operations by such rapid and unpredictable fluctuations in the permitted level of imports and in the system of allocations. We would not, of course, dispute the obvious fact that flexibility is required in administration to deal with novel situations and to adjust to changing conditions. But the need for flexibility cannot justify the chaos which now threatens to overwhelm this program and to defeat its central purpose. We urgently recommend that the Committee give consideration to the establishment by statute of definite and meaningful guidelines and standards governing executive discretion to assure adherence to the original national security objective of the oil import program—a healthy and vigorous petroleum industry in the United States—and essential stability in administration of the program.

We are most grateful for the opportunity to express our views on this vitally important matter.

(Exhibit A)

ASHLAND OIL & REFINING CO.,
Ashland, Ky., April 17, 1968.

Mr. ELMER L. HOEHN,
Oil Import Administrator, Oil Import Administration, U.S. Department of the
Interior, Washington, D.C.

DEAR MR. HOEHN: Pursuant to a March 20, 1968 news release by the Department of the Interior, entitled "Department of the Interior Announces Oil Import Proposals," we wish to submit our views applicable to that portion of the release concerning a proposed system for auctioning oil import licenses.

It would appear that over the last eighteen months the original justification for the Oil Import Program has been lost in a maze created by special interest groups seeking to subvert the interest of the Program to their own special benefits. The authority for the Oil Import Program is derived from a finding by the Office of Civilian Defense Mobilization that crude oil and its principal derivatives were being imported into the United States in amounts which impaired the national security by adversely affecting crude oil production and its derivatives within the United States. The intent of the Oil Import Program was to benefit the domestic crude oil producing segment of the petroleum industry by controlling the overall level of oil imports and by helping to maintain the price for domestic crude oil through a system of quotas which offset the difference between the cost of foreign and domestic oil.

The granting of quotas to inland refiners who receive and exchanged import licenses created a medium through which the benefit of the licenses was used to average down the cost of the higher priced domestic crude oil. This system of exchange has supported the price for domestic crude oil. The proposed auction program will destroy the principal method by which the level of domestic crude oil prices are supported and the price for crude oil will naturally gravitate toward the lowest price level of any crude oil moving into the market.

Few refiners, regardless of size or location, are able to operate profitably on domestic crude oil charged at posted prices. The mechanics may be different but the result is much the same whether it is a seaboard refiner using his low cost foreign oil in his own refinery to average down the cost of domestic oil to his refinery or an inland refiner who exchanges his quota and uses the profit for the same purpose as the seaboard refiner. The coastal refiner who acquires extra import quotas through exchanges in order to refine more foreign oil and less domestic oil is merely reimbursing the inland refiner for processing for him those exchange barrels of higher cost domestic oil.

If the auction system is established, the import program will distribute the entire benefits of import controls to those few companies having large, low cost sources of foreign crude oil. There will be no flow through of benefits to the domestic crude oil producing industry. The foreign crude oil producer with a cost of oil delivered into tankers of less than 10 cents a barrel will have as his cost of crude oil delivered to the United States this minor charge for crude plus tanker charges, taxes in country of origin, and the price paid at the crude oil auction.

It is no accident that since the advent of the Oil Import Program there have been no major reductions in prices for domestic crude oil. A material deterioration in the price for domestic crude oil would have occurred had conditions continued as they were prior to the Oil Import Program with a concentration of the right to import in the hands of a few large, low cost foreign producers.

We are convinced that the proposed auction system would subvert the original intention of the Oil Import Program so as to remove it from the scope of the legislation upon which it is based. We have received from leading law firms opinions that without specific legislation from Congress this proposed change cannot be legally placed into effect. Should the auction system be brought into being, we are prepared to give extremely serious consideration to the filing of a suit seeking an injunction to prohibit the Secretary from implementing the program in question.

Aside from the considerations mentioned above, there are a number of very practical considerations which would make the auction system practically unworkable.

In addition to the very serious realignment of economics within the industry, quota bidding would likely cause frequent violent upheaval of domestic operations. For example, a large east coast refiner who may have been successful in his previous bid and is the holder of 100,000 barrels per day of import license could during the next bid period be completely shut out. Under these conditions, he would have to renegotiate his entire position, release tankers carrying foreign crude and replace them with American flag tankers, and establish domestic crude supplies to fill the gap. Obviously, this would have an impact throughout the industry and on the supply of any number of other refiners, large and small. Domestic crude postings could be expected to fluctuate widely. Under these conditions, no one would have a secure supply since it would be impossible to enter into crude sales and purchase agreements of any duration longer than the periods between license auctions.

Country of origin quotas would probably be necessary, else Canadian oil would undoubtedly be foreclosed from importation and continuous supplies from other

countries would be vulnerable—most particularly to tanker rates. Various producing countries might feel compelled to enter the bidding in some capacity (nationalization, subsidy, tax rebates) in order to protect their market from wide swings between auction periods.

An auction system would offer the greatest opportunities to corral imports by those companies with the lowest cost foreign oil and with lowest cost transportation. Recently a large number of companies, both large and small, have ventured into foreign areas and have been more or less successful in finding oil. This quite frequently is not low cost oil, but at least the present allocation system provides the opportunity for an allocation holder to integrate a portion or all of that production with his domestic supply; otherwise, he may be faced with foreign marketing with necessary foreign expenditures for downstream facilities.

In a serious effort to be constructive, we are still convinced that the Oil Import Program as originally conceived and administered most clearly supports a strong, vigorous domestic petroleum producing and refining industry. Allocations should only go to those persons who are in fact processors of crude within the continental United States. Any other allocation is a subsidy by an indirect method and contributes nothing toward the purposes for which controls were intended. The Program in the future should distribute its benefits to the domestic oil industry in an equitable manner. Certainly, additional innovations which affect such equitable distribution should not be made. The program should not be exposed to radical changes.

Cordially yours,

ORIN E. ATKINS, *President.*

ASHLAND OIL & REFINING CO.,
Ashland, Ky., July 5, 1968.

Hon. WILBUR MILLS,
Chairman, House Committee on Ways and Means,
Longworth House Office Building,
Washington, D.C.

DEAR SIR: Ashland Oil & Refining Company was encouraged to see a report in "The Oil Daily" for Monday, July 1, 1968, that the Office of Foreign Direct Investment of the Commerce Department is considering a proposal permitting all exploratory expenditures on foreign oil concessions, whether or not ordinarily capitalized or expensed, to be made free of the restrictions of the Foreign Direct Investment Regulations until the properties reach the development stage.

The Foreign Direct Investment Regulations are set up, in general, to allocate foreign direct investments quotas arbitrarily on the basis of historical investments made in past years and therefore tend to discriminate unfairly against newcomers to the field of foreign operations. It is encouraging to see that the new proposal relating to foreign oil and gas exploration expenditures departs from this historical approach which benefits longtime foreign operating companies. The new proposal apparently would not penalize companies such as Ashland which has newly obtained oil concessions in Libya and Indonesia, but no substantial historical base for exploration expenditures in foreign countries.

We believe that the long-term United States balance of payments would not be adversely affected by a program which would permit unrestricted expenditures for exploring and discovering oil in foreign countries provided once oil has been discovered further investments for development and exploration be treated as restricted transfers of capital during the year involved. Perhaps such program could include equitable provisions for retroactively treating pre-discovery exploration costs as transfers of capital after oil in commercial quantities has been discovered.

On the other hand, if the Office of Foreign Direct Investment changes its approach so that expenditures for foreign oil and gas exploration will be based on the amount of a company's expenditures in a given past year or years, this would unfairly penalize companies such as Ashland which have obtained desirable foreign petroleum concessions only at great trouble and expense and, if not permitted to make expenditures to explore and develop those concessions, stands the risk of losing the concessions with the consequent loss of income to the company and to the long-range detriment to the United States balance of payments picture. At the same time, this approach would favor the companies which have operated in the foreign area for a longer period of time and would give them an undue competitive advantage over Ashland and other companies which are relative newcomers to the field of foreign investments.

We sincerely hope that the Office of Foreign Direct Investment adheres to the approach first discussed so that Ashland, and similar companies, with valuable properties and investments in foreign countries will not have the retention of those properties and their investments jeopardized by regulations which have the effect of favoring certain companies for no other reason than the fact that they have made large foreign investments in the base year or years.

We also submit that the current program for restricting American companies from investing in and expanding operations in foreign countries should be temporary and that consideration be given to enacting appropriate legislation to terminate, or at least limit, at the earliest practical date restrictions on foreign investments by American companies. The current restrictions seriously hamper American companies in maintaining their competitive position in the face of increasing competition from foreign companies. The long-range result of such restrictions will be to seriously and adversely affect long-term United States balance of payments.

We respectfully request that this letter be included in the record of the proceedings in the hearings on tariff and trade proposals.

Cordially yours,

ORIN E. ATKINS, *President.*

STATEMENT OF CONTINENTAL OIL CO.

Continental Oil Company is broadly engaged in the petroleum, chemical, coal and related businesses, both foreign and domestic. We are vitally concerned with legislation and regulations relative to the imports of hydrocarbons into the United States.

We strongly support the provision of the Trade Expansion Act which permits the President of the United States to establish limitations on such imports, upon request, but only after determination that circumstances exist which threaten or impair our national security.

In accordance with this legislation, the Mandatory Oil Import Program was instituted by Presidential Proclamation 3279, issued on March 10, 1959. We believe that the limitation of oil imports continues to be essential in order to assure adequate producing, transportation and manufacturing capability to meet our petroleum energy requirements during a national emergency.

We feel that the Mandatory Oil Import Program can be properly administered provided that national security is the prime consideration in determining quota levels and the allocation thereof. We sincerely believe this to be the intent of Congress under the "national security" provision of the Trade Expansion Act under which the program is authorized.

Many administrative interpretations since 1965 have departed from the national security basis or concept, and we are seriously concerned that these departures dilute the program as to render it ineffective in providing for national security. We are attaching a detailed analysis of the oil import program and recent administrative interpretations. This analysis, dated May 13, 1968, was filed by Continental Oil Company before the Subcommittee on Mines and Mining of the House Interior and Insular Affairs Committee.

We urge that existing legislation be amended to require that in the administration of the oil import program national security will be the sole consideration in determining quota levels and the allocation thereof.

STATEMENT OF CONTINENTAL OIL CO., PERTAINING TO THE BASIC OIL IMPORT PROGRAM BEFORE THE HOUSE INTERIOR AND INSULAR AFFAIRS COMMITTEE, SUBCOMMITTEE ON MINES AND MINING, MAY 13, 1968

Continental Oil Company strongly supports the fundamental purpose of the Mandatory Oil Import Program which is to adjust "imports of crude oil and unfinished oil and finished products . . . so that such imports would not threaten to impair the national security." Renewed efforts should be directed toward the preservation of the successful aspects and correcting the proven shortcomings and inequities of the program as it now exists.

To accomplish this goal, we would make the following general observations:
First: So many changes and special provisions have been made in the recent past as to place the entire program in jeopardy of complete breakdown through administrative confusion and complexity.

Special grants and exceptions as well as certain basic changes in the program itself have endangered the national security capability of the program, introduced gross inequities, generated a chaotic situation and caused considerable inefficiency in the planning and operations within the entire petroleum industry.

Second: Proposed changes are being initiated in such rapid fire order that it becomes impossible to comment constructively on any particular change since one is unsure whether his comments relate to the program as it then exists or to the program as may be altered by interim proposed changes that have not as yet been made.

Viewing the Oil Import Program in today's perspective and desiring to work constructively to realize a program that will most nearly meet our national security requirements, achieve maximum equity and at the same time result in a program that is viable under today's political and operating situations, Continental suggests the following major points:

(1) For rule-making and administrative purposes, the United States should continue to be subdivided into PAD Districts I-IV and PAD District V. Puerto Rico, the Virgin Islands or other island possessions of the United States should each be considered as a separate unit for these purposes.

(2) The maximum level of crude oil and unfinished oils import quotas for Districts I-IV should be 12.2% of the estimated production of crude and natural gas liquids during the allocation period.

Crude oil and unfinished oils imported into District V should be established at the excess of requirements over supply available from District V and Districts I-IV but should be no less than 12.2% of the estimated production of crude and natural gas liquids during the allocation period.

(3) Overland imports of crude oil and unfinished oils in to the continental United States should continue to be exempted from import license. Overland imports should be included within the 12.2% total imports allowed for Districts I-IV and the quota as determined for District V.

(4) All historical quotas for crude oil and unfinished oils, including Northern Tier, should continue to be phased out.

(5) No special licenses should be granted for importing refined products (ex-residual fuel oil). Existing term agreements for importing products from Puerto Rico and from the Virgin Islands should continue *only* for the term of the existing agreements. No license for the 10,000 barrels daily additional products to be imported from Puerto Rico into Districts I-IV should be issued for 1968 or subsequent years.

The additional 10,000 barrels daily referred to were transferred from District V to Districts I-IV with Secretary Udall stating that its import into District V in 1967 was possible due to a "loop-hole in the regulations". The loop-hole should be corrected, but the importer should not be rewarded for discovering it.

Product imports adversely affect the development of producing and refining capacity in the continental United States which detracts from the objective of adequate capability to meet an emergency. Use of the import program to distort the free play of product prices will have undesirable long range consequences.

(6) There should be no refined products imported under bond for use in the United States and no non-quota imports by the Department of Defense for use in the United States.

(7) No bonus licenses should be granted for the production of low sulfur residual in a domestic refinery or for the importing of low sulfur oil. The laudatory goal of clean air can be achieved through programs designed to encourage the development of other means and methods of reducing pollutants.

(8) Crude oil and unfinished oil imports should be permitted into Puerto Rico, the Virgin Islands or other island possessions of the United States to the extent products therefrom are utilized for local consumption or for exports other than to the United States. Refined products imported into each of the above should be allowed to the extent production therein is inadequate to meet demand.

(9) Refineries or petrochemical plants should be permitted in "free trade zones" provided the total product equivalent of all imported hydrocarbon feedstocks would be exported. No import quotas should be generated by such plants.

(10) There should be no import of crude oil, unfinished oils or finished products based on exports of petroleum products or petrochemical products. Such exports have been developed under the present program and will continue. Licenses issued under such a concept introduce an inequity of financial benefit to a limited group of refiners or petrochemical plants permitting them a competitive advantage in domestic markets.

(11) No new or rehabilitated refinery or petrochemical plant nor enlargement of any plant should qualify for quota until qualified under the provisions that quota will be determined for any years based on runs for the first 12 months during the 15-month period preceding the quota period. This regulation has worked satisfactorily in the past. Problems of both equity and identity between plant enlargements and new or rehabilitated plants would be introduced.

(12) Refinery inputs should be as defined in the Oil Import Administration proposal released March 15, 1968, except that overland imports of crude oil and unfinished oil and liquid feedstocks, normally referred to as "synthetic oils", which are produced from shale oil, tar sands or coal in Districts I-IV or District V or imported overland or pursuant to an allocation should be added to the list of qualifying inputs.

(13) The sliding scale method of allocating licenses to refiners should be discontinued. By administrative decision this device has been utilized to grant increasing benefit to small plants to the point of maintaining grossly inefficient plants in operation. We think it is extremely inequitable to grant one barrel of refining runs 19% of a barrel of quota and another barrel of refining runs only 2.74% of a barrel of quota in Districts I-IV and a variation of from 45.0% to only 2.2% in District V. The sliding scale has also been responsible for spawning a number of plants which are merely a subterfuge to obtain a high quota allocation through qualifying a small plant "legally" as a small refiner.

Continental strongly urges discontinuance of the sliding scale but if it is to be continued the variation of grants to refiners should be sharply reduced.

(14) A barrel of hydrocarbons should qualify as a basis for import quota only once. Consequently, petrochemical plants should qualify for quota only if they are the first domestic processor of a barrel that meets the definition of qualified refinery input. If petrochemical plants are eligible to receive quota under the regulations, we suggest the following basis:

(a) Each plant should be qualified as either a refinery or petrochemical plant but not both.

(b) Refinery inputs should be as indicated in No. 12 above. Petrochemical plants inputs should be as defined in the Oil Import Administration proposal released March 15, 1968, except that overland imports of crude oil and unfinished oil and liquid feedstocks, normally referred to as "synthetic oils" which are produced from shale oil, tar sands or coal in Districts I-IV or District V or imported overland or pursuant to an allocation should be added to the list of qualifying inputs. Petroleum coke should be eliminated as input for petrochemical plants.

(c) Total available crude oil and unfinished oil quota for Districts I-IV and District V should be prorated between refiners as a group and petrochemical plants as a group in each area in the same proportion as the total qualifying inputs for each bears to total inputs for both for that area.

(d) Refinery quota allocation for Districts I-IV and District V, as determined under (c) above, shall be allocated among refiners in each area on the basis of refinery inputs.

(e) Petrochemical plant quota allocations for Districts I-IV and District V, as determined under (c) above, shall be allocated among petrochemical plant operators in each area on the basis of *outputs*. Output to qualify for this distribution of quota should be limited to hydrocarbon content on a weight basis of products produced which will not enter the energy market. No barrel of output should count more than once so output should be limited to the initial processing of a qualifying input barrel.

(f) If a sliding scale is continued for refiners, a comparable system should be applied for petrochemical plants.

(15) An auction system for crude oil import licenses should not be established. The uncertainties of the proposed auction system make it difficult to assess its impact on sources of supply. It seems likely, however, that distortions in established logistical patterns would occur. At any given auction, a company will secure a larger proportion of import licenses than at other auctions. Their supply arrangements could favor one producing country at the expense of others. Thus, markets for a particular producing nation could be distorted temporarily, leading to serious international relations problems. Should efforts to control this situation be attempted by placing limitations on the volume of import licenses any one company may purchase or that could be used to import crude from any one producing country, the plan becomes subject to administrative decision and

the probable confrontations between the United States and the producing countries.

Under a system which would provide for auction of less than 100% of the import licenses, the magnitude of the exceptions and the disposition of such licenses becomes an administrative decision and introduces new avenues for special grants and privileges which have been so harmful to the present program. On the other hand, if 100% of the licenses were auctioned, many new factors could be introduced which would be disruptive to stable supply patterns developed under the present plan. In either event, an auction system would make it extremely difficult for any company to plan and carry forward a sound, efficient program of operation or to make rational decisions for domestic development and expansion.

An auction system would increase the total raw material costs to refiners. Under the present program, the financial benefit of import licenses for refiners in reality amounts to a reduction in costs. In our free enterprise economy, this is translated into reduced prices for the products sold and in this manner the consumer of refined products is properly the real beneficiary.

(16) Quotas should be determined and announced two months prior to the beginning of each quota period to permit efficiency in planning and operations.

(17) Any changes in the program should be done through a review of the total program periodically but no more often than once a year.

STATEMENT OF WARREN B. DAVIS, DIRECTOR, PLANNING & ECONOMICS,
GULF OIL CORP.

This statement will be limited to comments on the Oil Import Control Program and to the mandatory controls on direct foreign investment and their effect on trade.

Gulf Oil Corporation believes that the United States should follow a policy of encouraging freer trade except when free trade would adversely affect the national security. We believe that controls on oil imports are essential to national security. The Oil Import Control Program in effect since March 11, 1959, in our opinion, has been successful, to date, in controlling the overall level of imports in keeping with its national security objective. We have been concerned, however, since the control program was first established with the use of the program to accomplish objectives in addition to its basic objective. This has been done by granting special privileges to some firms and, consequently, have made the program inequitable in the awarding of allocations to individual importers. In the last three years, the use of the Oil Import Control Program to accomplish purposes beyond its basic objective has been intensified, and now even threatens to prevent the program from accomplishing its primary national security objective. We believe it imperative that no additional special privileges be granted under the program, and that a plan be devised to phase out the special privileges that now exist.

We are also concerned with the mandatory controls on direct foreign investment. Direct foreign investment consistently makes a positive contribution to the balance of payments, and restrictions on capital outflow for direct foreign investment now will reduce income on investment in future years. We believe controls on direct foreign investment should be removed, if not at once, at least by the end of the year. Aside from military expenditures, the major weakness in our balance of payments is the deterioration in the balance of trade. We believe it imperative that this balance be improved through fiscal measures to stem inflation, export promotion, and actions to offset promotion of exports by foreign countries.

GENERAL POSITION ON TRADE

Gulf Oil Corporation believes in freer trade, and has consistently supported programs to promote it. We believe, however, that restrictions on free trade are necessary whenever it threatens national security. We recognize that our national security is complex. It includes the security of all free nations of the world and our ability to conduct military operations in all areas of the world as well as the physical security of mainland United States. It involves economic and other factors as well as purely military considerations. We believe it would include maintaining the soundness of the dollar.

THE NEED FOR AN OIL IMPORT CONTROL PROGRAM

Gulf Oil Corporation believes that an Oil Import Control Program is necessary to our national security. In fact, we are convinced there is more need for the program now than when the voluntary program was established in 1957. We were doubtful of the need for a mandatory control program at that time, but the world oil industry has undergone significant changes since 1957. On January 1, 1957, petroleum reserves in the Free World outside the U.S. were estimated at 177 billion barrels, or about five times the 36 billion barrels of the United States. On January 1, 1968, Free World reserves outside the U.S. were estimated to be 341 billion barrels, or about 8.5 times the 40 billion barrels of U.S. reserves. Since 1957, eight countries which had no crude production in 1957 have become producing countries. Also, some countries with insignificant production in 1957 have had new discoveries which have resulted in a sharp increase in production. The number of companies with substantial petroleum production outside the United States has also increased sharply in the last ten years, and in view of the number now exploring for oil, the number of producers is almost certain to increase further. The desire of each producing country to maximize production and the necessity for each new producing company to develop its reserves and sell some oil to recover its large investments caused crude productive capacity to increase even more rapidly than the substantial growth of demand. This surplus has brought about a sharp drop in the price of foreign oil, and without controls foreign oil would displace much of the U.S. crude in U.S. markets or else force its sale at prices substantially below cost and thus discourage the exploration necessary to maintain productive capacity essential to national security.

BASIC OBJECTIVES OF AN OIL IMPORT CONTROL PROGRAM

The basic objective and only legal basis for the Mandatory Oil Import Control Program is to prevent the importation of petroleum and petroleum products in such quantities as to impair the national security. However, as already pointed out, our national security is complex. Consequently, we believe more specific objectives are necessary. At the Department of the Interior Oil Import Hearings in March, 1965 and again in May, 1967, we listed eight specific objectives that should be continually considered in designing the import control program. We think these objectives are still sound. They are:

1. Provide sufficient protection for the domestic production industry to prevent a decline in its share of U.S. petroleum requirements in areas where it can develop sufficient capacity to enable it to share in future growth.
2. Provide for participation in the U.S. market of crude petroleum produced by friendly foreign nations, particularly those of the Western Hemisphere, to keep those nations and their resources oriented to the Free World.
3. Prevent increases in the prices of petroleum products not in keeping with our national security objective.
4. Prevent in any way a shift of control of U.S. foreign-producing operations to foreign countries.
5. Provide the necessary encouragement to investment in a refinery, transportation, and distribution system which will be prepared to utilize most efficiently the nation's changing oil supply in the years to come.
6. Provide protection for the foreign investment of U.S. oil companies.
7. Be oriented to the long-range economic and defense needs of the nation, and not tailored to immediate and temporary factors.
8. Interfere no more than absolutely necessary with the competitive structure of the industry which would develop under free enterprise.

SUCCESS OF THE OIL IMPORT CONTROL PROGRAM

The Mandatory Oil Import Control Program has been successful in its basic objective of protecting our national security, and it has met reasonably well the first four specific objectives we outlined above. Imports of crude petroleum and unfinished oils in 1967 in Districts I-IV were 8.4% of the total of these imports and domestic production of crude petroleum and natural gas liquids. Although 1967 was affected by the Middle East crisis, this percentage was 9.8% in 1966 and significantly lower than the 11.5% in 1958—the year before the mandatory program began. The share of the domestic producer in Districts I-IV crude requirements has actually improved somewhat. Imports of residual fuel and imports of crude oil and unfinished oils into District V are set to meet demand and

have increased only because of the inability of domestic production to meet demand. Production of friendly foreign nations has participated in the growth in the U.S. market, and production of Western Hemisphere nations has maintained its share. The Oil Import Control Program has been a success in controlling the overall level of imports, and we see no reason to change this part of the program.

WEAKNESS IN THE OIL IMPORT CONTROL PROGRAM

The weakness in the Oil Import Control Program has been in the inequitable allocations to individual importers. The provisions of the program pertaining to the awarding of allocations to individual importers has been inequitable from the start and has grown increasingly more inequitable over the years of the program. It has consistently ignored the planning and investment of existing importing firms through changes in the program which have eroded the position of these existing importers. Allocations were granted to firms with no importing history and special bonuses were bestowed upon a few firms in order to accomplish a purpose not related to the basic objective.

We believe that the strength of America lies in its free enterprise system under which individual firms plan their investment in competition with other firms both within the United States and outside it. We are convinced that the success of this system is dependent on the confidence of the investing firm that will realize an adequate return on its investment. The Oil Import Control Program has largely ignored existing investment, and has seriously affected the return on that investment through reducing the import position of existing importers to grant a special import privilege to some in order to accomplish purposes with no relationship to the basic national security objective of the control program.

We believe that national security is dependent not only on productive capacity, but also on a refining, transportation, and marketing complex which will efficiently utilize the crude petroleum produced. To assure that the investment necessary for this refining, transportation, and marketing complex is made, it is essential that plans can be made with some assurance of stability in the Import Control Program.

We are aware of the desirability of designing any program so that it will, if possible, contribute toward the easing of as many problems as possible. We also recognize the desirability of using government programs to provide incentives to industry. However, we are also aware of the dangers in such efforts that the ability of the program to meet its basic objectives can be limited or destroyed. We are concerned, because we believe this is happening to the Oil Import Control Program.

The Oil Import Control Program, as it was originally designed, was inequitable because it provided import allocations to all refiners regardless of whether they had invested in the facilities to utilize foreign crude and allowed them to "exchange" this allocation for domestic oil realizing a profit which they had done nothing to earn. The inequity was further compounded by allocating, through a sliding scale, a greater relative share to small refiners than to large refiners. This was done to accomplish a purpose not a part of the national security objective—to encourage small business. We are not concerned at this time with discussing the desirability of subsidizing small business, but using the Oil Import Control Program to do it meant that resources were taken from some firms in the industry to subsidize their competitors.

With the precedent set in the original program of some firms receiving a special unearned bonus, nearly everyone has been trying to devise a scheme whereby they can obtain a similar bonus. Fortunately, these efforts have not all been successful, but enough of them have been to reduce further the allowable imports of those who had become importers through their own foresight and investment under competitive conditions before the program was imposed. Significantly, those who were granted the special bonus in the original program and who have made investments under its provisions, have seen their position eroded in order to grant special bonuses to others or to allow for a new group of importers.

Beginning in 1966, import allocations were made to petrochemical producers in what, in our opinion, was a mistaken belief that it would cause an increase in exports and thereby aid the balance of payments. This gave allocations to a large number of new companies at the expense of existing importers. In late 1965, the decision was made to grant permission to Phillips Petroleum Company to ship 24,800 B/D of gasoline from Puerto Rico to Districts I-IV. In 1968, provision has been made to allow shipments of products from Puerto Rico to Dis-

tricts I-IV by Commonwealth Oil & Refining Company of 10,000 B/D and by Sun Oil Company of 29,500 B/D. All of these special provisions were said to be based on actions by these favored companies in providing investment in Puerto Rico which would increase employment there. The special privileges granted these companies not only affects other refiners whose allocations are reduced, but also will weaken the overall control program.

In 1968, an allocation was made to Hess Oil & Chemical Corporation to ship 15,000 B/D of finished products from the Virgin Islands to the East Coast in return for payments to the Virgin Islands which would help their economy. This 15,000 B/D was not deducted from refineries in general, but was subtracted from the finished product allocations. Consequently, it adversely affected a relatively small number of firms, but it affected them significantly.

The effect on small refiners of these special privileges has been minimized by increasing the size of the lower bracket in the sliding scale, and the effect on petrochemical plants has been reduced by increasing the share going to petrochemicals. This means that large and medium-size refiners were affected the most.

Provision was made in the Presidential Proclamation in 1967 to allow for allocations to asphalt dealers, despite evidence that there is no shortage of domestically-produced asphalt. This provision has not yet been implemented, and in our opinion should not be.

Indications are that the Oil Import Administration plans to continue changing the regulations. Recently, at the request of the Administrator of the Oil Import Administration, we submitted comments on three proposals for changing the regulations. The Administrator is currently considering additional petitions for special allocations by refiners in the Caribbean and elsewhere. The Administrator is also under considerable pressure to increase imports of distillate fuel on the East Coast for heating purposes. So far, the Administrator has wisely refused on the grounds that such imports were not necessary, but should he allow these additional imports, it would, in our opinion, further impair the effectiveness of the program.

We do not believe that the contribution made to the other problems for which the Oil Import Control Program has been used were significant enough to offset the serious inequities they caused to existing refiners. These actions threaten the whole program because the gross inequities created and the uncertainty regarding the future of the program will discourage the investment required to provide the necessary refinery, transportation and other capacity necessary to continue to provide the low-cost energy essential to economic growth. We are convinced that others will be presenting new proposals to obtain benefits similar to those already granted. We believe that immediate action is necessary to prevent the granting of additional special privileges and that a plan should be devised to phase out the special privileges that now exist.

DANGER OF CONTINUED CONTROLS ON DIRECT FOREIGN INVESTMENT

Gulf Oil Corporation is seriously concerned with the mandatory controls on direct foreign investment. We realize the seriousness of our balance of payments program, but believe that restrictions on capital outflow for direct foreign investment will have a serious adverse effect on our balance of payments in future years. Direct foreign investment consistently makes a favorable contribution to our balance of payments in that the return on existing investment significantly exceeds the capital outflow for additional investment. The additional investment is necessary both to expand and maintain the return on investment. In 1967, income on direct investment was \$4,445 million. In addition, the direct foreign investment returned \$1,126 million in fees and royalties. Thus, the total return of \$5,571 million exceeded the capital outflow of \$3,026 million by \$2,545 million. This was not only one of the few items making a favorable contribution, but was up \$998 million from the previous year. In addition to the direct favorable contribution to the balance of payments, direct investment is responsible for a significant portion of our exports. Much of the capital outflow is really an outflow of U.S.-made goods. Therefore, the contribution of direct investment is even greater than indicated by the cited figures. Business will try to maintain its foreign investment by borrowing money abroad, but this will raise their costs and adversely affect their competitive position with foreign firms, and will reduce the return on investment, which has been so significant in our balance of payments. We believe it dangerous to restrict even as an emergency

measure direct foreign investment which consistently makes such a strong favorable contribution to our balance of payments. Our efforts should be directed to those areas of the balance of payments showing weakness rather than those showing strength.

We believe the greatest weakness, aside from travel and military expenditures, in our balance of payments is the deterioration in our balance of merchandise trade. This balance in 1967 was \$3,193 million, a decline of \$175 million from 1966, and \$1,274 million less than in 1960. A significant portion of exports is due to our government foreign aid programs. If this is substracted from exports, the deterioration in our trade balance is even more alarming. Our balance on trade in 1967, excluding government expenditure on U.S. merchandise for export, was only \$250 million—\$396 million less than in 1966 and \$2,607 million less than in 1960. It seems imperative that the government adopt a fiscal program which will reduce the excessive inflation of the last three years. It seems highly desirable to do everything necessary to encourage greater exports. The mandatory controls on direct foreign investment actually discourage exports. Although we believe these controls should be removed at least by the end of the year, we urge that the regulations be changed immediately to give credit for export of U.S. made goods. Other actions should be taken to offset the vigorous promotion of exports by foreign countries.

STATEMENT OF C. H. MURPHY, Jr., PRESIDENT, MURPHY OIL CORP.

The theme of the President's message on the proposed Trade Expansion Act of 1968 is "Greater Prosperity Through Expanded World Trade". Murphy Oil Corporation is in agreement with this principle and therefore supports such portions of the Trade Expansion Act of 1968 as promote expanded world trade.

One portion of the Trade Expansion Act now in effect which requires comment, however, is that portion which permits the President to restrict, and therefore diminish rather than expand, world trade. Insofar as this power is concerned, the title of the law is a misnomer, and should be "The Trade Diminution Act". We refer of course to Section 232 of the Trade Expansion Act of 1962, which is not being amended by the proposed bill. This is the Section which authorized the President to limit imports of any particular commodity or article when a determination is made that the further unrestricted importation of such commodity or article will impair the national security. Pursuant to this authority (and similar authority contained in prior legislation) the importation of crude oil into this country has been restricted for some ten years now. It is interesting to note that although the statutory basis for restricting imports of crude oil is national security, the actual program which has been developed has come to be administered more and more on an economic basis and, unfortunately but logically, is now being thought of in economic terms by those affected. Thus, one finds "accommodations" being made in the present Oil Import Program for the benefit of refiners in the Virgin Islands and Puerto Rico which are sought to be justified because of their economic benefit to those locales. No pretense is made that such favoritism improves the Nation's security.

So, the President's authority to impose restrictions, which began with a wholesome purpose, the security of the United States of America, has now become a fact of life which is being used to accomplish economic ends never intended by the Congress.

We believe that a healthy domestic industry is one which can compete fairly with its world competitors without any artificial trade barriers to protect it. Therefore the aim of this nation and every nation should be to encourage the development of such healthy industries. It is not necessarily inconsistent with this view for a nation to accord temporary protection to a particular industry to avoid long term damage which might be caused by a sudden turn of world events. We should never, however, be content with such temporary protection continued on a permanent basis. Rather, we should always be striving to eliminate the need for such protection. This is our basic criticism of the Oil Import Program. It came at a time when the domestic industry was thought to be in need of protection from the greatly expanded producing capacity developed in the Middle East. It would be pointless to argue now whether that decision was wise. Our criticism today is therefore no longer directed to the original basis for the protection, but rather to the fact that this temporary protection has

existed for ten years and no effort has been made either to eliminate the necessity for the protection by strengthening the domestic industry or to find a more appropriate and equitable means of administering the protection plan. A temporary measure intended to shield a vital domestic industry from exposure to suddenly increased world wide competition is becoming a permanent crutch not intended by the Congress. Does the industry in fact need a crutch? If it does, then it should have one designed for permanence, not the present patchwork system.

Oil is today one of the most abundant and useful, and therefore one of the most important, commodities in the world. Its importance to the industrialized nations cannot be overemphasized and its importance to the industrialized nations makes it important to all others. It would therefore be foolish to suggest that this nation should not have a national policy with respect to its own supply of this important material just as it would be unrealistic to suppose that each of the other nations of the world is not going to have for itself its own self determined national policy with respect to the acquisition, disposition and/or use of oil. Among the producing nations, oil is a vital instrument of national ambition, to be used to promote all foreign and economic policies. It is their sword in the economic battle of nations. To the consuming nations, oil is an essential source of energy, to be acquired in ever increasing quantities to further industrial development. Little wonder that both sets of nations necessarily have policies on oil. Recognizing that this nation, like the others, should also have a national policy on oil is what prompts us to be critical of the present situation, because what we have today is not really a policy, but a collection of makeshift rules and loopholes. Here then is our criticism of the proposed Trade Expansion Act of 1968—*not based on what the Act does but on what it does not do. It does not provide a way to eliminate the "temporary" artificial trade barrier of the Oil Import Quota System nor does it establish a national policy for oil.* It might well be argued here that the power to eliminate the import quota rests with the President since he is the person authorized by Congress to institute the quota. However, we suggest that since the import quota has been administered in a way *not intended by the Congress, namely as an economic measure rather than a national security measure,* it well behooves the Congress to alter the form of the protection being afforded the domestic oil industry and at the same time begin to develop a national oil policy.

What should our national oil policy be and what should it strive to accomplish? We believe the two long range objectives of such a policy should be—

1. To assure this nation of an adequate supply of petroleum for national defense.

2. To promote the peaceful economic growth of this nation by assuring an adequate continuing supply of petroleum at a reasonable cost.

It appears at first blush that these two objectives are opposed, the first pulling toward a higher price for petroleum to stimulate domestic production and the second pulling equally hard to keep petroleum prices lower, but this apparent conflict of objectives only seems so because it is impossible to accomplish both under the present Import Quota System. They can, and must, be reconciled.

The stop gap Import Quota System has more or less preserved the status quo but has not contributed to a permanent solution of either of objectives one and two. Ten years of Import Quota have not served to expand or strengthen the domestic industry to any great extent nor rendered the domestic industry any more able to compete in world markets. The decline in domestic drilling simply does not correlate with the amount of oil imported into the country, and it must therefore be conceded that the cause of that decline is found elsewhere. In any case the Import Quota has done little in the way of a long range solution to objective one. Similarly, the Import Quota has done little to achieve objective two, that of providing an adequate source of petroleum for expanding the domestic economy. Contrarily, the Import Quota may have actually inhibited expansion of the domestic economy by imposing an artificial limit on the amount of petroleum available. Thus, when measured against these objectives for a long range oil policy, the Import Quota System must be termed at best a temporary holding action. If the quota system is to be scrapped, what can be used to replace it that will accomplish the objectives a national oil policy should have? We are going to have to work to find an answer. If the answer were easy it would

already have occurred to someone in the ten years which have gone by. We do know this, that the quota system has not accomplished the objectives that a national oil policy should have accomplished and, speaking as part of the industry most affected by it, we can state that it has aroused intense feelings of disgust. *The first criterion for a government policy is to be fair to all of its citizens and we say frankly that we are incensed to see our competitors being handed an unfair advantage over us pursuant to the Oil Import Policy now in effect.* The record our Company has made with the Oil Import Administration on these matters is lengthy. That is an administrative matter. We will not burden this Committee by repeating the statements, protests and appeals which we have made to the Oil Import Administration but merely point out that the record is there for those who have any interest in it.

We do have suggestions to put before the Congress. What sort of program can be developed which would accomplish the long range objectives we have outlined and would meet the furthest test of being fair to all? *Since any artificial trade barrier is, in essence, a discrimination against goods, it could be accomplished most equitably by a tariff, or border tax, if you prefer.* A tariff is impartial because it applies to goods and not to persons, companies, plants or refineries. This at least would spare us the semi-annual spectacle of oil companies fighting over their quotas like dogs over a bone, or another disgraceful episode such as that involving the petrochemical quota issued Standard of Indiana, then withdrawn by the Interior Department on a spurious excuse because of the adverse publicity when the "loophole" was discovered, and finally reinstated when the company filed suit against the Secretary of the Interior.

In addition to the tariff, if it is judged necessary, in the national interest to afford the domestic industry some further economic inducement to compete against foreign industry the most equitable way to it is by a subsidy. While we do not deem it necessary or desirable at this time, a subsidy has something to recommend it. It is at least forthright and honest. It admits weakness and inability to compete on equal terms. And, best of all, it provides a means for continuous review, because it requires an appropriation, and the Congress will have an opportunity to look at it every year. This means at least that it can be adjusted to meet challenging situations, and, hopefully, eventually done away with altogether.

The right combination of tariff and subsidy, if necessary, could be evolved to accomplish both of the long range purposes which a national oil policy should seek to achieve. A tariff could be adjusted to take into consideration the quantity, availability, and cost of the foreign product and to recognize the relative safety of various sources of supply for national defense purposes. A subsidy or bounty could be based on the development of oil resources vital to this country's defense. Both flows of economic benefits could be appropriately adjusted from time to time to assure an adequate supply of petroleum for the expansion of this country's economy.

Sound policy includes continuing Congressional review of all governmental activities and we believe the Oil Import Quota System to be now ripe for such review. It is a program authorized several years ago which the Executive branch of the government has permitted to develop into something different from the program originally sanctioned by the Congress. When this happens it is not just the prerogative, but also the duty, of the Congress to re-examine the program and take what ever steps are necessary to re-establish the Congressional purposes. We have no particular quarrel with the proposed Trade Expansion Act of 1968 which the Committee has before it for hearing except to say, as we have already done here at some length, that its shortcoming is in *not* providing for a change in the Oil Import Quota System. We are confident however, as we believe the Committee is also, that the whole subject of foreign trade, tariffs, border taxes, and import quotas will not be laid to rest by the Trade Expansion Act of 1968. It is our purpose here to sound the call for a thoroughgoing re-examination of the portion of law which authorizes the Oil Import Quota, and we will be pleased to be available to this Committee when it is ready to conduct a detailed inquiry into this subject.

STATEMENT BY STANDARD OIL CO. OF CALIFORNIA

OIL IMPORT CONTROLS

Oil import controls were imposed in 1959 as a national security measure under authority of what has since become the Trade Expansion Act of 1962. Standard herewith presents its views on this subject.

In the early 1950's oil imports into the United States, aided by the clear-cut cost advantage of foreign over domestic production, began to accelerate rapidly. Mandatory controls were imposed finally in 1959 to prevent their attaining proportions which would threaten national security by undermining incentives for domestic exploration and production. Standard believes this was wise.

The events of 1967 in the Middle East served to illustrate the importance of the program. The oil supply crisis brought on in the middle of that year by the Arab/Israeli conflict could not have been surmounted had not adequate domestic reserves been available to supplement the reduced flow of oil from the major foreign producing centers. The crisis clearly demonstrated that some restriction on oil imports—in order to stimulate domestic exploration and development—is essential to the national interest.

This does not mean that the program must be administered rigidly and without regard for other desirable objectives such as air and water pollution control. Nor does it mean that every effort to relax controls should necessarily be resisted. There is good reason, for example, to support relaxation of control when it can be demonstrated that a product shortage exists.

It does mean, however, that every administrative policy or contemplated change in policy should be examined closely for possible conflict with the programs' primary purpose.

Considered within this framework, and insofar as the problem is one of establishing overall limits on crude oil and product imports, we think on the whole that the program as constituted today does meet its primary objective.

There is no longer a threat that imports will gain a major share of the domestic market. Almost 90% of the market for crude oil and natural gas liquids in Districts I-IV is reserved to the domestic industry, and in District V imports are permitted only as needed to offset domestic shortages. There is little more that controls can do to protect the incentives needed to encourage domestic exploration and development.

Once the overall level of import control has been decided upon, of course, it becomes necessary to devise an equitable basis for allocation of quotas among eligible importers.

We think the effort here should be to achieve a pattern of allocation paralleling as nearly as possible that which would have existed in the absence of controls. There should be no attempt to interfere with normal competitive forces by conferring advantage on any group. The import control program, after all, is not intended to promote any economic philosophy. It is concerned with national security and security is a function of the overall limits placed on total imports. The connection, if any, between national security and methods of quota allocation is remote.

An area of particular concern to Standard currently is the petrochemical import quota plan. We were among those who opposed its adoption initially. We did not then, nor do we now, believe that petrochemical manufacturers suffered any significant competitive disadvantage in the domestic market under the original oil import control program. Furthermore, we seriously question the assertion that petrochemical exports can be stimulated simply by awarding oil import quota to petrochemical manufacturers. A quota system designed simply to equalize foreign and domestic feedstock costs will not overcome the other economic advantages enjoyed by large-scale plants located abroad near the markets they are intended to serve. We think any expansion of the petrochemical program would be a mistake.

We would suggest finally that the oil import control program be reviewed from time to time to be certain that it is serving the national interest most effectively.

STATEMENT OF TEXACO, INC.

ROLE OF THE UNITED STATES IN THE WORLD ECONOMY

During the past thirty years the volume of international trade has more than tripled. The United States has played an important role in creating the conditions that have made this expansion possible. It has followed policies that have helped to reduce trade barriers and to promote the growth of foreign trade on a non-discriminatory basis. Under its leadership, other nations have been encouraged to move in the same direction. The benefits to the United States have been substantial. Its volume of exports has quadrupled and its economy has been strengthened. Furthermore, our trade policies have supported the national security interests of the United States as well as those of its free world allies. In view of these benefits, Texaco endorses the extension of the Trade Expansion Act and continuation of efforts to reduce foreign trade barriers to expansion of U.S. exports.

The House Ways and Means Committee is holding its hearings on tariffs and trade at a time when the United States is facing its greatest challenge of the post-war period. Confidence in the dollar has steadily been eroded as the result of continuing large deficits in the country's balance of payments. This has led to recurring crises which threaten to undermine the very basis of the international monetary system. The United States has responded to these developments by adopting direct controls on foreign investment that can only be regarded as shortsighted and expedient. The history of the post-war period clearly shows that direct controls have never solved any country's balance of payments problem. Instead, they narrow the opportunities for further expansion of trade and investment, serve to invite retaliation from foreign countries, are a serious handicap to American business in maintaining its competitive position abroad and in carrying out foreign concession obligations, and, if continued, will result in irrevocable loss of potential investments by American-owned companies to foreign firms.

As a major international trader with over 60 years of operating experience abroad, Texaco is keenly aware of the dominant role and influence that this country exercises in the free world economy. It is, therefore, urgent that the United States re-examine its position or risk a return to more restrictive trade practices elsewhere in the world as well as further damage to its own balance of payments.

MEASURES TO IMPROVE THE BALANCE OF PAYMENTS

We are aware that the House Ways and Means Committee is considering only certain aspects that bear on the balance of payments' problem. Proposals to improve the commodity trade balance are important. The causes of the balance of payments' deficit, however, are rooted in a broader economic context that has to be considered if the deficit is to be substantially reduced. And the deficit must be reduced since we cannot allow it to continue at the rate of recent years without further undermining international confidence in the dollar.

In a statement submitted to the Trade Information Committee of the Office of the Special Representative for Trade Negotiations, Texaco reviewed the overall U.S. balance of payments' problem and recommended several measures to improve the deficit. A copy of this statement is attached. It is worthwhile to reiterate our major recommendations since we firmly believe they provide the only way to improve our international payments position.

(1) The first essential is the restoration of domestic price stability as there is a direct connection between inflation at home and the balance of payments' deficit. Our trade balance, which the House Ways and Means Committee is now considering, has steadily declined as the result of the accelerating inflation that has been fueled by the substantial federal budget deficits of the past few years. The most effective way of restraining inflation is to cut Government non-defense expenditures as this will have more of an immediate impact in reducing consumption than a rise in income taxes.

(2) The increase in Government spending and lending abroad in the last few years is a big factor in the balance of payments' deficit. It is imperative that the Government re-examine its commitments abroad and reduce them to a level consistent with our national security. Low-cost government loans to foreign countries, furthermore, may encourage them to enlarge the public sector of their economies to the detriment of U.S. exports.

(3) Specifically, in regard to the commodity trade balance, we recommend accelerated efforts to reduce existing quantitative and tax barriers to expansion of U.S. exports. This is an area that has been relatively neglected in previous trade negotiations. Particular attention should be given to the trade-restrictive effects of state trading enterprises and other non-conventional types of quantitative controls.

These recommendations deal with the fundamental causes of the balance of payments' deficit rather than with its symptoms as do direct controls. Only action along these lines can reduce the deficit. Trade and investment restrictions are contrary to the foreign trade policies we have followed in the past and can do irreparable harm to the U.S. balance of payments and American industry abroad.

MANDATORY INVESTMENT PROGRAM

As we indicated in our statement to the Trade Information Committee, the Mandatory Investment Program is particularly inimical to the interests of this country. The program was imposed as an expedient in the hopes of some short-term gains to the balance of payments. These gains, if any, are far outweighed by the longer-term harm to the country's international payments' balance and to the position of American industry abroad.

As is commonly known, direct investments abroad return substantial funds to the United States far in excess of the capital outflow for such investments. This has been true for every year during the entire post-war period. In 1967, for which data have recently been released, the capital outflow totaled \$2.7 billion (excluding \$290 million of funds obtained abroad), while dividends, profits, fees and royalties remitted to the United States by direct investors increased to \$5.6 billion, more than twice the outflow. This is an outstanding performance by any standard, but it would not have been possible had mandatory restrictions on capital outflow been in effect for an extended period in the past. By their continuation, we face the risk of a slow-up in American business expansion abroad, the loss of markets to foreign competitors, and even ability to replace and modernize existing investments. These prospective developments would soon begin to reduce the substantial benefits that direct investment now contributes to the balance of payments.

Many in the federal government recognize these facts, but are willing to take the risk in restricting capital outflow for a short-term benefit. The thought that the current substantial return flow of dividends and royalties to the United States will not be adversely affected by reducing capital outflows for a few years overlooks two factors. One is the very short balance-of-payments payback of direct foreign investment. For example, U.S. petroleum investments abroad, as discussed further in Texaco's statement to the Trade Information Committee, have on average a payback of three years or less in terms of benefits to the balance of payments. Secondly, there is a strong possibility of retaliatory action against the United States. Already many foreign countries have indicated growing concern about the effects of U.S. investment controls upon their economies and have threatened to take countermeasures. The consequence would be a reduction of U.S. trade. In view of these factors, the risk of continuing the Mandatory Investment Program for a possible short-term gain is shortsighted. The country cannot afford to run such a risk, particularly since there is no doubt that the U.S. balance of payments will be seriously damaged in the longer term. The continuation of the Mandatory Investment Program will also hamper the ability of American industry abroad despite increasing resort to foreign borrowing. We cannot regard such a development with complacency as American overseas investments strengthen the U.S. political and strategic position in many foreign areas.

CONCLUSIONS

The United States is at a crossroads in regard to its foreign commercial policy. Decisions taken now will substantially contribute to the shaping of the future of the world economy. The country must decide whether to continue to move forward in reducing trade and investment barriers, or return to a period of more restrictive trade practices. While we do not want to minimize the seriousness of the balance of payments' problem, we believe that continuation of the Mandatory Investment Program will not help, but instead harm, our payments position. We urge again that the program be rapidly phased out. The correction of the deficit can be accomplished by other means consistent with maintaining a world trading environment that encourages trade and investment. This is in the best interests of the United States and its free world allies.

TEXACO, INC.,
Washington, D.C., March 13, 1968.

TRADE INFORMATION COMMITTEE,
Washington, D.C.

GENTLEMEN: The study of U.S. foreign trade policy being undertaken by the Office of the Special Representative for Trade Negotiations is particularly timely. In view of recent restrictions imposed to improve the U.S. balance of payments, it is more urgent than ever before that the United States Government clarify its position in regard to the future of this country's foreign commercial policy.

The direction of that policy is now in doubt and has caused apprehension among American businessmen as well as foreign governments. At risk is the loss of American economic leadership abroad and a set back to the U.S. Government's efforts of more than thirty years to reduce barriers to the expansion of international trade and investment within the free world. These long-range objectives of U.S. trade policy will certainly be jeopardized unless we are careful and maintain a flexible position in dealing with the present balance of payments' problem. Direct and rigid controls may be self-defeating as they provoke other countries to adopt similar measures.

Texaco, therefore, welcomes this opportunity to present its views on future U.S. foreign trade policy. As a company whose subsidiaries have operated abroad for more than fifty years and which presently has extensive operations in almost all free world foreign areas, we are hopeful that our experience and views can be of help in the deliberations of the Trade Information Committee.

Our experience with international operations has made us keenly aware of the key position the United States holds in respect to the international economic relations of the free world. United States foreign trade is larger than that of any other single country. And United States influence on the general character of the free world's international economic policies is immense.

We believe that the policies followed by this country under the Reciprocal Trade Agreement Acts and the subsequent Trade Expansion Act have contributed substantially to reducing barriers to international trade and investment. They have encouraged other nations to move in the same direction. The strength of the domestic economy and efficient use of its resources depend upon continued expansion of international trade and investment and upon creation of a free world monetary and trading environment with a minimum of restrictions. It is, therefore, essential that the United States re-assert its traditional leadership in this field.

In the study the Trade Information Committee is now undertaking, high priority should be given to a re-examination of the controls recently imposed to improve the U.S. balance of international payments. These controls represent a serious setback for U.S. trade policy. In addition to restricting international transactions by Americans, they serve to invite retaliation from other countries. The mandatory controls upon direct investments have also raised doubts as to the ability of American companies to carry out obligations incurred as a condition of investment abroad. Already many foreign governments have expressed fears as to the effect of the measures adopted by the United States on their economies and trade, while strongly hinting at possible countermeasures. The consequences may be a return to economic nationalism and protectionism within the free world as occurred during the 1930's. The resulting damage to world trade might take decades to undo.

We do not want to minimize the problem of the balance of payments deficit. Clearly the U.S. dollar must be defended and strengthened. If these new controls could be expected to achieve this purpose, they could be tolerated for a short time despite their adverse effect on world trade. If not, there would be no economic justification for their continuation.

It is, therefore, no light task that the Trade Information Committee has undertaken. Its review and recommendations regarding the future of U.S. foreign trade policy will be awaited with great interest by foreigners as well as Americans.

Texaco is affected by all aspects of U.S. foreign trade policy and is, of course, deeply concerned about the balance of payments problem. During the period of the voluntary program to restrict overseas investments, we complied fully with the requests of the U.S. Government in the hopes our contribution would benefit the balance of payments. This program was successful, as President Johnson has acknowledged, but only because it was considered to be temporary. The mandatory program suddenly changed this prospect. We believe it is not possible to

tighten restrictions still further without damage to the balance of payments as well as to the competitive position of American companies abroad. As this program is particularly inimical to the best interests of the United States, we wish to limit the remainder of this submission to an analysis of its effectiveness and discussion of alternative measures to improve the balance of payments.

DIRECT INVESTMENTS AND THE BALANCE OF PAYMENTS

Much misunderstanding has developed in recent years regarding the effect of overseas direct investments on the balance of payments. While analysis of this problem is admittedly complex, a review of the record and the nature of direct investments will, we believe, generally support the conclusion that such investments are beneficial and tend to strengthen our international payments position.

Besides the original capital outflow, the balance-of-payments effects of direct investments involve evaluation of many factors, of which the following are of major importance:

(1) Direct foreign investments tend to develop new markets for U.S. exports of capital equipment. For example, American enterprises overseas have been in the forefront in adopting new methods of production, which have stimulated demand for U.S. exports embodying a high degree of modern technology. Affiliates of American oil companies alone purchased almost \$350 million worth of capital goods from U.S. suppliers in 1964, equal to over 46% of the capital for foreign petroleum investment in that year (over-all industry and later data not available). Furthermore, in most cases, there is no alternative but to invest abroad because of foreign tariffs and other quantitative barriers to international trade. Thus, direct investments overseas do not, as often alleged, displace American exports, which would have been lost in any case.

(2) The biggest benefit to the balance of payments comes from the dividends, profits and royalties remitted to the United States from American companies' direct investments overseas. Current remittances, of course, represent the yield from past investments, but, as discussed further below, the period between the capital outflow and the return flow to the United States of sufficient funds to pay back the original investment in balance-of-payments' terms is relatively short.

The return flow to the United States (including fees and royalties) of all direct investments overseas has consistently risen every year except two during the postwar period. In 1966 it totaled about \$5.1 billion, over two times the level of ten years earlier, and has remained at this high annual rate during the first nine months of 1967. This increasing contribution to the balance of payments could not have been possible except for the continuing investments made abroad by American companies.

The benefit to the balance of payments of the first factor discussed above is difficult to quantify because of lack of reliable and recent data. But as it is a plus factor, the dividend and royalty return flow for which data are regularly compiled by the Department of Commerce should be considered as the minimum gross benefit of direct investments to the U.S. balance of payments.

As an offset to this gross benefit, account must be taken of the capital transfers from the United States for direct investments overseas. These transfers, however, have risen far less than the increase in the return flow of dividends and royalties to the United States. Over the last ten years, for example, capital outflow increased by approximately 50% to about \$3.1 billion in 1966 (excluding \$445 million of funds borrowed abroad by American companies). The return flow of dividends and royalties, however, doubled over this period so that the net contribution of foreign direct investments to the balance of payments rose from \$450 million in 1956 to about \$2 billion in 1966. In the first nine months of 1967, this net benefit had increased to \$2.8 billion at an annual rate. The foreign operations of the American oil industry accounted for almost half of the net contribution of overseas direct investments to the balance of payments in 1966, the latest period for which such industry data are available.

The increasing contribution of direct overseas investments to the balance of payments has repeatedly been acknowledged by the Johnson Administration. But in imposing mandatory restrictions, the Government contends that the savings now required in foreign investment outlays are beyond the reach of a voluntary program. Furthermore, it believes that restriction of future investments for a short period will benefit the balance of payments without materially affecting the present increasing return flows of dividends and royalties, which are the result of investments made in the past. The Government, in effect, justifies its case for **mandatory restrictions on grounds of short-term expediency.**

The question that must be considered, therefore, is how long mandatory restrictions can be maintained without reducing the balance-of-payments benefits of direct overseas investments. In brief, it is a matter of the payback period of such investments in balance-of-payments terms.

According to a study of The Chase Manhattan Bank based on a survey of 29 major U.S. petroleum companies, the average dollar that leaves this country in the form of new petroleum investments is returned within three years and that thereafter the balance of payments continues to benefit from increased inflows. This is a relatively short payback. It takes account of the many investment-related receipts such as exports of capital equipment and management services to foreign affiliates that, in addition to remitted income, benefit the U.S. balance of payments. It does not include the indirect gains to the balance of payments of new foreign petroleum investment, such as expenditures for U.S. exports by foreign recipients of oil funds, which are not feasible to calculate. The payback period would be even shorter than three years if these expenditures could be taken into account.

The conclusion that can be drawn from the Chase Manhattan study is that restricting direct investments abroad for even a short period of time will not materially help, but rather weaken the balance of payments. Restrictions on such investments have been in effect for almost three years under the voluntary program. During this period, foreign investment opportunities in petroleum have had to be foregone which now would have begun to yield net benefits to the U.S. balance of payments.

OTHER EFFECTS OF INVESTMENT RESTRICTIONS

While the balance of payments is our major problem at the present, a continuation of investment restrictions may also have serious undesirable consequences in other areas that cannot be overlooked.

1. A limitation on foreign investment opportunities could adversely affect the position of American industry abroad. Under the voluntary program to restrict investments, American companies have had to rely increasingly on foreign borrowings. The sharp tightening of mandatory restrictions will force still further reliance on foreign capital markets. But it seems clear that these restrictions will result in a cutback of the foreign investment programs of a number of companies. The result will be a weakening of the competitive position of American firms overseas by a postponement of programs to modernize and expand as facilities required to supply the free world's petroleum requirements either may not be installed, or may be provided by foreign competitors. As a result it will be extremely difficult, for example, for the oil industry to provide the facilities and products necessary to comply with the tighter air pollution requirements being increasingly imposed in many areas.

2. U.S. Government officials have long recognized the need for a high level of U.S. foreign investments to assist in the economic development of the less developed nations. Despite the investment increase scheduled for these countries under the mandatory program, the over-all restrictions in developed areas are likely to limit the benefits of such investments. In many industries, such as petroleum, investment made in producing areas is dependent upon investments made in refining and marketing in the developed areas, where most of the world's oil is consumed. By discouraging investments in the highly industrialized countries, investments in the less developed nations are bound to suffer.

CONCLUSIONS AND ALTERNATIVES

It is obvious that the balance of payments deficit cannot continue at the rate of recent years. Action must be taken to correct this situation and to restore international confidence in the dollar. The problem of the deficit, however, is not one that will yield to easy and expedient solutions. The approach adopted by the U.S. Government in placing the heaviest burden on American direct investments abroad, particularly those of American oil companies, is not a lasting cure for the balance of payments. These controls do not deal with the fundamental causes of the deficit, as many foreign analysts have already been quick to point out. Before irreparable harm is done to the U.S. balance of payments, the mandatory investment restrictions should be immediately eased and rapidly phased out. Other methods to improve the balance of payments should be considered.

First, the Government should not lose sight of the obvious connection between inflation at home and the balance of payments deficit. The excess demand created at home by expansionary fiscal and monetary policies has encouraged a substantial increase in imports, which has reduced the foreign trade surplus of the private sector from about \$3 billion in 1960 to \$700 million in 1966. Only the Middle East crisis prevented a continuation of this deterioration in 1967. The over-all foreign trade surplus has been maintained entirely by an increase in exports financed by tied-in loans and grants of the federal government.

In view of this development, it is more important than ever that we restore and maintain domestic price stability. The most effective step in this direction would be a substantial cut in government non-defense expenditures. These expenditures have increased at an annual rate of almost 13% since mid-1965 when the war in Vietnam was escalated. As a result, the federal deficit has risen to unprecedented levels, which has contributed substantially to inflation and the deterioration in our international payments position.

Second, government spending and lending abroad have increased significantly in the last few years and is a big factor in the payments deficit. While the Vietnam war may prevent a reduction of foreign military expenditures in that area, other overseas government spending should be subjected to continuous review in order to reduce it to a minimum consistent with our national security.

Furthermore, government loans and grants tied to U.S. exports, which the government justifies on grounds that they are not a drain on the balance of payments, should also be thoroughly re-examined since the indirect effects of much of this aid may tend to increase the deficit. Low-cost government loans, for example, may encourage foreign countries to enlarge the public sector of their economies to the detriment of American and other private companies. This could restrict the return which private companies make to the U.S. balance of payments.

Third, U.S. Government efforts should be accelerated to reduce existing quantitative and tax barriers to expansion of U.S. trade abroad. This would be consistent with our foreign trade policy of the last 30 years and held to promote a higher level of exports on a sound basis. The direct controls on investment adopted by the U.S. Government will make this task difficult, as is already evident from the reaction they have provoked in foreign countries. This is an additional reason why these controls should be dropped.

Particular attention should be given to the trade-restrictive effects of state trading enterprises and other nonconventional types of quantitative controls. State trading enterprises pre-empt sizable markets in which private companies are either forbidden to operate or are at a competitive disadvantage because of the strong government support these enterprises receive.

We feel that action along the fronts just discussed will go a long way in reducing the balance of payments deficit. Furthermore, these proposals deal with the underlying causes of the deficit problem, not just its symptoms. The repression of these symptoms—as the mandatory restrictions on investments attempt to do—is not the answer. Direct controls are an expedient bound to provoke countermeasures abroad that will drive the world down the road to protectionism.

It is our hope, therefore, that the direct controls on investments overseas will be rescinded, or, at the very least, substantially eased. We should not lose sight in our present difficulties of a fundamental fact: that freedom of capital movements is necessary to the promotion of international trade and of the economic growth and political stability of the free world.

Respectfully submitted.

JAMES H. PIPKIN.
Executive Vice President.

STATEMENT OF AIR TRANSPORT ASSOCIATION OF AMERICA

The Air Transport Association of America is a voluntary trade and service organization whose membership is comprised of virtually all the scheduled airlines of the United States which engage in air transportation pursuant to certificates of public convenience and necessity issued by the Civil Aeronautics Board. In addition to their domestic in territorial services, these airlines carry the flag of U.S. air commerce to every corner of the world.

The oil import legislation before this committee as typified by HR 10690 would have a direct and critical impact upon the airline industry. Whether inad-

vertently or otherwise, one provision thereof would have the practical and immediate effect of eliminating altogether the source of almost all the jet fuel used in this country by the airlines to operate their international flights. The effect of this particular provision on the overall legislation purpose of encouraging and stimulating domestic oil production in the interests of national security, on the other hand, would be minimal since the jet fuel in question would represent only a small fraction of one percent of total domestic oil production.

To properly understand this problem, we must first review some of the pertinent background.

Under the provisions of Section 309(a) of the Tariff Act of 1930, 19 U.S.C. § 1309(a), fuel and other supplies for aircraft and vessels engaged in foreign trade may be withdrawn from customs bonded warehouses free of all duties and internal revenue taxes. The airlines, both U.S. and foreign flag, rely on fuel withdrawn from bonded warehouses for use in the operation of their international flights. The rationale underlying the long standing statutory provision for such duty free withdrawals is that these commodities never enter into the domestic commerce of the United States, but rather are consumed directly in the course of conducting this nation's foreign trade. This privilege is also granted to foreign ships and aircraft on the basis of reciprocity; being contingent upon the grant of reciprocal privileges by the foreign country involved (see 19 U.S.C. § 1309(d)).

Of more recent origin, the mandatory oil import program was established by Presidential Proclamation No. 3279 on March 10, 1959. It was determined at that time that bonded fuel was outside the jurisdiction of the oil import program. By its express terms, the proclamation specifically excluded from the quotas and other import limitations established thereunder "... free withdrawals by persons pursuant to Section 309 of the Tariff Act of 1930." This executive determination has never been changed. Thus, the bonded fuel used by the airlines has never been covered by the mandatory oil import program and no basis has been established for the changing of its status in the present legislation.

The various sponsors of the legislation referred to have enumerated in some detail the exact nature of the special exemptions and exceptions which they felt were now threatening the mandatory oil import program. Absolutely no mention was made by anyone of bonded jet fuel withdrawals from customs' warehouses which, as we have seen, have never been encompassed within this import program and thus could not constitute a newly arisen threat to the program.

Furthermore, while the proponents of the legislation state that present levels would be preserved this is not the case. Airline bonded fuel would be affected by the peculiar language proposed.

These bills as presently drafted would have the effect of bringing bonded fuel under the existing oil import quotas for the first time. This results from the use of a definition of the term "imports" which is based on a statistical reporting practice of the Bureau of the Census. That agency includes within its "imports for consumption" statistics, the free withdrawals from bonded warehouses under the provisions of Section 309. (This Census Bureau practice is itself open to serious question since both Section 309(b) and 317(b) of the Tariff Act of 1930 clearly classify as *exportations* the loading of such supplies aboard ships and aircraft engaged in foreign trade.)

The bills in their present form would not simply bring bonded aircraft fuel within the oil import quotas for the first time; they actually would have the effect of eliminating altogether the availability of such fuel. This would be the practical result of the fact that import quotas for finished oil products (into which category jet fuel would fall) have always been a very small proportion of the overall total and have long since been allocated to other uses. Airline bonded fuel requirements in Districts I-IV during 1967 would represent 65% of the total finished products quota for these districts; their 1970 requirement would represent 100% of that quota. Thus, the legislation would override the long standing bonded fuel rights of the airlines under the Tariff Act of 1930—without any regard for the adverse effect on the economy and efficiency of this nation's foreign air commerce.

The bills would also jeopardize reciprocal privileges granted by foreign countries throughout the world. Enactment of such legislation would place the United States in the untenable position of circumventing the provisions of the bilateral air transport agreements which it has signed with over 60 foreign nations. These agreements provide that fuel and other supplies for use on the aircraft of each

signatory country may be brought into the other's country and boarded on such aircraft free from customs duties, excise taxes, inspection fees and other national duties and charges. More recent bilateral agreements further provide that such fuel shall not be subject to otherwise applicable economic prohibitions and restrictions relating to import, export and transit. To effectively end the availability of the bonded fuel used by foreign-flag airlines would certainly be deemed to be a breach by the United States of the spirit, and in some cases the letter, of these international agreements.

The consequent loss of stature in the community of nations would not be the only loss suffered by the United States by such a circumvention of these bilateral air transport agreements. Retaliatory action would surely be forthcoming. Just as our own Tariff Act provides for withdrawal of bonded fuel rights from the aircraft and vessels of foreign nations which do not accord reciprocal privileges, these nations can and would do the same to U. S.-flag carriers. The result would be a substantial net increased cost in the fuel loaded at foreign points—millions of dollars in added costs that would be paid without economic benefit to anyone in this country. The end result would be a total economic waste and a wholly unnecessary addition to the balance of payments deficit. Moreover, the very nature of such a breach of good faith on the part of the United States would likely engender other forms of economic retaliation—all to the detriment of the prime United States interest in the free and unhindered flow of international air commerce.

It is our understanding that other provisions of the proposed legislation would exclude from its coverage the bunker fuel used by ships engaged in foreign trade. To retain such rights for vessels, but not for aircraft, clearly would represent a rank form of discrimination between sea and air transportation—one that is unexplained and, we submit, unexplainable. Since bunker fuel and other residual fuel oils which have not been covered by the mandatory oil import program are to continue to be exempted by this legislation, the same treatment properly must be afforded with respect to the precisely comparable case of bonded fuel used by the airlines.

With the elimination or substantial curtailment of the availability of bonded fuel supplies, these airline fuel requirements would be thrown on the domestic market which already suffers from shortages of jet fuel due to increased military requirements and the rapidly increasing demands of civil aviation. Bonded fuel now supplies about 20% of total airline fuel requirements in this country—much too large an amount for the already tight domestic market to handle. A substantial disruption in jet fuel supplies would be virtually inevitable; curtailment of air carrier schedules might even be required. Moreover, military fuel supply requirements would necessarily be affected adversely by this increased civil demand. And the economic effect on the airlines would be serious—an increase of 10 percent or more in the cost of fuel used on international flights. This latter element would be in derogation of the efforts of our government to attract foreign visitors to the United States through low-cost air services. Again, the balance of payments deficit would suffer.

In summary, this aspect of the legislation would unjustifiably eliminate a traditional right in aid of foreign trade, one recognized throughout the free world and made the subject of bilateral agreement with over 60 foreign nations; it would place the United States in an untenable position with respect to these agreements and would invite wasteful economic retaliation; it would arbitrarily discriminate between air and sea transportation; it would seriously disrupt domestic aviation fuel supplies, with adverse effects on both military and civil aviation requirements; and, in general, would be in derogation of the vital public interest objectives served by the international air commerce of this nation. Moreover, this facet of the bills has no genuine relationship to the announced legislative purpose of the overall proposal, and would have only the most minimal effect thereon in any event. These considerations dictate that the legislation be amended so as to delete from its coverage all bonded fuel withdrawn free of duty pursuant to the provisions of Section 309 of the Tariff Act of 1930.

Attachment.

SUGGESTED AMENDMENT TO H.R. 10690

Revise subsection (h) (2), as follows:

“Imports shall include (A) ‘imports for consumption’ as recorded by the United States Bureau of the Census, *other than free withdrawals by persons*

pursuant to Section 309 of the Tariff Act of 1930, as amended, and (B) shipments (i) from Puerto Rico, the Virgin Islands, and Guam into the United States, and (ii) into any foreign-trade zone located within the United States."

EXPLANATION

This revision maintains the existing exclusion of bonded fuel from the mandatory oil import program. It uses the language of Section 2(e) of the proclamation establishing the mandatory oil import program (Proclamation No. 3279 of March 10, 1959) which has always excluded bonded fuel withdrawals from the quotas and limitations established thereunder.

STATEMENT OF SOUTHERN CALIFORNIA EDISON CO.

The Southern California Edison Company (Edison) is a public utility that provides electric service to an area in central and southern California and central Nevada containing a population of more than 7 million people. This service is substantially dependent upon the continued operation of Edison's oil and gas-fired steam electric generating plants located in southern California. Because of its requirements for substantial amounts of low sulfur Indonesian fuel oil, resulting from the inadequacy of the gas supplies available to it and the need to conform to the strict air pollution control requirements in southern California, Edison is vitally concerned that such imported low sulfur oil continue to be available for its use.

Edison provides electric service to homes, farms, manufacturing and military establishments, food processing and preservation plants, hospitals, schools, churches, railroads, factories, water, fire and sewage services, police departments, cities, counties, unincorporated towns and rural areas and to the public generally in the area which it serves. The public health, welfare and safety in Edison's service area is dependent upon a sufficient and reliable supply of electricity by Edison.

The electric generating capacity available to Edison aggregates 8.9 million kilowatts, of which over 7.7 million kilowatts is thermal generation. Approximately 7.4 million kilowatts of this thermal generation is oil and gas-fired and is located in southern California. In addition, Edison has 1.3 million kilowatts of oil and gas-fired thermal generation under construction in southern California. Two coal-fired generating stations are under construction—one at Four Corners, New Mexico, which will commence operations in 1969, and the other in southern Nevada, which will commence operations in 1970—in which Edison will have an entitlement of approximately 1.6 million kilowatts. The generating capacity being added to the Edison system is required by load growth and the continued operation of its existing plants, as well as the operation of the above mentioned new plants, is necessary to meet the needs for Edison's electric service in its service areas.

In view of the air pollution problems which exist in the southern California area, coal cannot be burned for the generation of electricity, and Edison's oil and gas-fired generating plants use natural gas as their principal fuel supply. There, however, is insufficient gas available to this area to satisfy the fuel requirements of these plants, and fuel oil must be used to supplement the available gas supply.

In the past, California residual fuel oil, used by Edison to meet the deficiencies in the supplies of natural gas, had a sulfur content of approximately two percent by weight. However, as early as 1955, Edison was convicted in criminal actions filed by the Los Angeles County Air Pollution Control District in the Redondo Beach Municipal Court of alleged violations of the California Air Pollution Control laws. These violations were due to the combustion of conventional domestic residual fuel oil. Since 1955, because of its inability to comply with air pollution requirements, Edison has been unable to obtain permits from the Air Pollution Control District of Los Angeles County to operate its steam electric generating stations using such fuel oil, and its operations have been subject to variances.

Edison has engaged in extensive and continuing research and development programs in accordance with the requirements of the variances granted to it. These programs have involved all aspects of power plant air pollution control, ranging from a determination of the kind and amount of materials emitted by oil

and gas-fired boilers to the actual installation and testing of full-scale equipment designed on the basis of pilot plant studies to control these emissions. Edison has employed recognized authorities and consulting organizations in the air pollution control field to supplement the efforts of its own engineering staff and has worked closely with boiler and control equipment manufacturers and with the local air pollution control agencies. No means, however, have as yet been devised which will economically remove from stack gases the substantial quantities of sulfur oxides which are produced whenever California fuel oils are burned.

Recently, with the construction and operation of the two large 450-megawatt generating units at its Alamitos Generating Station and the two large 450-megawatt generating units at its Redondo Generating Station, Edison has been subjected to increasingly indignant public protests and complaints claiming spotting damage from rust and acid allegedly emitted from the Company's plants when burning fuel oil. The Control Officer of the Air Pollution Control District of the County of Los Angeles has announced that he will take every means to restrict the construction of any additional oil or combination oil and gas-fired boilers in Los Angeles County. Also, the Public Information Officer of the District has announced that unusual litigation will be commenced against power plant operators directed toward eliminating objectionable atmospheric emissions from high sulfur fuel oil combustion.

Public mass meetings have been held in the communities in which Edison's generating stations are located, and a large delegation from these communities appeared at recent hearings held by the Hearing Board of the Los Angeles Air Pollution Control District upon Edison's application for a continuance of the necessary variances to operate its plants in Los Angeles County. It seems apparent, from the public pressures being exerted upon the Air Pollution Control District, that the use of the conventional California fuel oils will be even more drastically restricted in the future.

California residual oil is being forced out of use because local air pollution control authorities, as well as the United States Public Health Service of the Department of Health, Education and Welfare, have taken the position that burning high sulfur fuels causes deleterious effects upon the environment. Laws of the State of California prescribe restrictions upon the opacity of power plant stack gases which cannot be met when burning fuel oil produced from California sources. Local regulations adopted to control air pollution outlaw the burning of fuels having a sulfur content in excess of 0.5 percent, except when gas is not available.

On July 17, 1967, by Proclamation No. 3794, President Johnson modified the Oil Import Program as established by Proclamation No. 3279 to provide for the importation of low sulfur crude oil and low sulfur fuel oil as needed to meet air pollution control objectives. Then, on October 3, 1967, Secretary Udall issued oil import regulations implementing Proclamation No. 3794, to permit the importation into District V of crude oil equal in volume to the quantities of low sulfur residual fuel oil sold under contract to meet the requirements of local air pollution control regulations. These regulations have the effect of freeing low sulfur residual fuel oil needed for air pollution requirements from import quota restrictions, but continuing the applicability of such restrictions upon all other products produced from the imported crude oil.

Edison is in the course of converting its facilities to use low sulfur residual fuel oil in place of California residual fuel oil. Such low sulfur fuel oil is processed from crude oil produced in Indonesia. During the past winter's oil burning season, Edison used 1,010,000 barrels of low sulfur oil produced from Indonesian crude oil with such excellent results that both the Company and the Air Pollution Control Authorities are satisfied that the use of such low sulfur oil will meet the needs of air pollution control. Complaints from the public in the vicinity of Edison's Redondo Generating Station dropped from over 300 during the 1966/67 winter to near the vanishing point during the 1967/68 winter when only gas and low sulfur oil were used at Redondo. The Los Angeles Air Pollution Control Authorities have now issued to Edison permits to operate its generating units which previously could be operated only under variances, but such permits are conditioned that fuel oil having a sulfur content in excess of 0.5 percent will not be burned.

The amount of oil that will be needed in any specific future year cannot be definitively determined in advance because the operation of Edison's thermal generating stations is subject to strict air pollution control regulations which, for all practical purposes, have the effect of requiring the use of natural gas whenever available. In 1967 Edison's fuel consumption amounted to 50 million equivalent barrels of fuel oil of which 84 percent, or approximately 42 million equivalent barrels, was natural gas and 8 million barrels was fuel oil. A substantial part of the gas supply is variable and unpredictable because the gas supply available to industry is that remaining after meeting the demands of domestic and commercial gas customers whose demands vary with winter temperature conditions and because of the unpredictability of the certification by the FPC of required new out-of-state gas increments for California, but it has been estimated that gas will supply about 75 percent of the 1968-1972 fuel requirements. Edison's oil requirements for these years, therefore, would vary from 6 to 14 million barrels a year.

Efforts have been and are being made by Edison to increase and stabilize the gas supplies available to it. It is anticipated, however, that Edison will have to use increasing amounts of oil each year as its load growth continues.

The oil refining industry in this area, on the other hand, has underway a program to increase its production of gasoline and other light products from California crude oil, and this is reducing substantially the residual fuel oil produced therefrom. As a result, there is a downward trend in residual fuel oil availability in District V, and under present gas supply arrangements there is no reduction in the magnitude of the seasonal fuel oil requirements. This can result in deficient fuel oil supplies to meet peak wintertime needs for electric generation such as was experienced in the winter of 1964-65 unless appropriate action is taken to offset such a deficiency. The U.S. Gulf Coast or Mid-Continent oil producing areas are not reliable sources of supply for backstopping California fuel oil deficiencies.

Because of the need to backstop fluctuations in available gas supplies with oil, it would not be prudent for Congress or the Administration to prevent the importing of foreign oil to cover gas deficiencies in District V.

Edison's problem of assuring continued access to an adequate quantity of oil fuel to backstop interruptible gas supplies is made more complicated by the circumstance that such oil resources must be of low sulfur and low ash content in order to meet the air pollution requirements in this area and to comply with the operating permits as conditioned by the local air pollution control authorities. While imported low sulfur oil qualitatively meets the air pollution control requirement for our operations, it is quite costly, and as anticipated, we have encountered a severe cost impact upon our operations. Also, it is presently available in limited and uncertain amounts due to the lead time necessary for suppliers to increase production from the oil fields and to build refinery processing and pumping facilities, and because the regulations permitting the importation of oil into District V to stimulate production of low sulfur fuel oil have not as yet been extended beyond December 31, 1968.

Our suppliers are expediting their development work. We expect that the quantity limitations will be overcome during the balance of this year and that for the 1968/69 winter season, supply should be adequate, provided the Oil Import Program is continued in an appropriate manner. Edison's low sulfur oil requirements during the 1968/69 winter are expected to be in the range of 11 to 13 million barrels. Not all of this can be stockpiled before December 31, 1968. It is of crucial importance that we know by July 1, 1968, our supply program for the entire 1968/69 winter. Accordingly, it is imperative that the rules and regulations promulgated October 3, 1967, be extended indefinitely so that the electric generating agencies may prudently plan their future operations in the interest of continued reliable and efficient service.

We believe that the flexible administration of this program in the past by the Oil Import Control Administration demonstrates that it can and will work, and that present procedures for regulating oil imports have adequately protected domestic producers. Evidence that changes and tailoring of the program may be needed in the future is good reason for retaining the present plan. It is founded upon a realistic and workable assessment, by both the Director of Emergency Planning and the President, of the needs for national security, giving consideration to the whole public interest.

INDEPENDENT OIL HEAT DEALERS ASSOCIATION OF MARYLAND,
FUEL OIL COUNCIL OF MARYLAND,
Frederick, Md., July 5, 1968.

HON. WILBUR D. MILLS,
*Chairman, the House Ways and Means Committee,
Longworth House Office Building,
Washington, D.C.*

DEAR CONGRESSMAN MILLS: On behalf of the Independent Oil Heat Dealers Association of Maryland, and the Fuel Oil Council of Maryland, which consists of 121 independent fuel oil merchants in the State of Maryland, we have been authorized to file with you the following statement:

Let us begin with our philosophy. We are not anti-big business, we expect no special treatment, our only interest is to see that fair and equitable treatment is accorded to everyone in the oil industry. This of course is absolutely necessary for our survival.

Your Committee should be aware that our group is not the recipient of any favorable tax treatment, such as, "the oil depletion allowance", or "tax-free foundations", nor do we receive any "grants" or "subsidies", or special legislation, such as "The Oil Import Program". We compete with each other in a fierce, but free and honest market place. The consumer is thereby benefited because they get the lowest possible prices and best service. In order for the independent oil marketer to survive *he must also have access to a free and honest market place.*

We would like to call your attention to the fact that the independent oil man not only competes with "major oil companies" at the retail level, but other forms of energy as well, such as "gas and electric".

We are opposed to the "Oil Import Program". It is not serving its original purpose, it is discriminatory and has created a cartel. It is set up in such a manner as to prevent the small independent companies, such as we represent, from participating. The Import Program has been twisted around to where last winter it created spot shortages, and much higher prices this spring. Besides creating unconscionable profits for the major oil companies, this cartel has reduced the margin of profit for the independent oil distributors. Should this pattern continue, it will be only a matter of time until the independents will be forced to sell out to the major oil companies, or be eliminated by economic cannibalism.

We would like to bring to this Committee's attention an Editorial that appeared in the Journal of Commerce on Monday, May 20th, 1968, which was headlined "The Tangled Webb", and we quote:

THE TANGLED WEBB

The hearings conducted on oil import quotas by a subgroup of the House Interior Committee last week may have been futile in the sense that that committee cannot initiate any legislation dealing with import quotas, but they were useful to the extent that they demonstrated what happens when the Government intervenes in one sector of an industry at the behest of another.

When the import quotas were adopted in 1959 none of their most ardent supporters could quite bring himself to say that his objective was to raise domestic prices. No, their stated purpose was to encourage domestic exploration and development by establishing "a more satisfactory" price level. In other words the price increase was to be merely incidental. Once the drillers found it worthwhile to put their equipment to work in the boondocks again, oil would come gushing forth from new sources and the United States wouldn't have to depend on vulnerable foreign supply lines. The executive order that imposed these quotas had not been signed for very long when it became evident that there was something curious about the whole picture.

First off, they applied to Canada. Since Canadian sources are actually closer to some U.S. marketing areas than are those of Texas and Oklahoma, many people began to wonder how this phase of the program could possibly relate to "vulnerable foreign supply lines" and national defense. After some indecisiveness, an exemption was made for Canada.

Second, it appeared that the artificial boost in the domestic price level forced by the quotas was upsetting other industries.

The American petrochemical industry, for example, was battling in various markets with that of western Europe. As the competition intensified it became

more and more clear that American producers forced to pay inflated prices at home for crude oil were in danger of losing ground to their European competitors who could procure their chief raw material at the world market price.

This became especially apparent in the case of Benzenoid Chemicals, with results that are well known. Having taken the cosmetic petroleum industry under its wing, the government tried to protect local producers of Benzenoids by what amounted to a tariff-on-a-tariff, namely the American selling price system (ASP). At this point things were getting complicated. ASP became, in turn, a major obstacle to conclusion of the Kennedy round and still remains a major obstacle to U.S.-European co-operation in relieving pressure of this Nation's balance of payments.

There was, of course, still more to come. Originally, the quotas were to apply to the whole U.S. market. But that didn't make much sense, either, as it turned out.

Why should they apply to Hawaii, lying far from American oil sources and (presumably at the end of one of those "vulnerable supply lines")? Hawaii had problems of its own. So did Puerto Rico, which has been trying to attract heavier industries (including petrochemicals) via its "operation bootstrap." And then there was Alaska, far closer to Canadian sources of oil than American. Why should these areas find their growth stunted in the interest of domestic producers and refiners within the continental United States?

So some more exceptions were made and there were still more to come. Provision was also made for additional quotas for crude oil imported for use in petrochemicals. (The purpose of this was to help maintain the competitive status of U.S. petrochemicals producers vis-a-vis their foreign competitors.)

In the light of all these complexities, modifications, exemptions and the like it is hardly surprising that inequities and administrative troubles have developed.

It has been charged that some large oil companies have been taking a "double dip" on their quotas, namely, by importing their full quota of fuel oil for refining purposes, then claiming another for petrochemical end uses. This has raised questions of who is a bona fide refiner and distributor and who is not. And of who is in petrochemicals and who is not. To those who had demanded the quotas in the first place—allegedly in the interests of national defense—all these exceptions are now condensed in one word: "Loopholes".

They want a tighter administration of these quotas and, to some extent, they seem to be getting it. And they want various loopholes plugged. Their argument is that the official 12.2 ratio of imports to domestic production really applies to less than half of the total of U.S. imports. And considering the exceptions given to mitigate the effects of the artificial price level maintained by the quotas, they might be right. But that is not the point.

The point is that all these disruptions and some of the dissatisfaction among homeowners with the high price of heating oil would have been absent from the picture today if the quotas had never been imposed at all. We still find no valid case for this special treatment for an industry that does not actually need it and is, in any case, already specially favored in terms of the tax depletion allowance and the like. The best thing Washington could do is admit frankly it made a bad mistake nine years ago and scrap the quotas altogether.

These giants staunchly defend the "Free Enterprise System", and we whole heartily agree that it should be preserved. Yet they seek special treatment from our Government (who incidentally are the people) that is not available to small business and is not in the public interest.

Therefore, we urge you in the interest of everyone concerned to get rid of this monstrosity called the "Import Quota System".

Respectfully yours,

FUEL OIL COUNCIL OF MARYLAND,
JAY D. KLINE,
President.
IRVING HUFELL,
Executive Vice President.
IOHD ASSOCIATION OF MARYLAND,
JOHN M. MYERS,
President.

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., May 28, 1968.

HON. WILBUR D. MILLS,
*Chairman, Committee on Ways and Means,
House of Representatives,
Washington, D.C.*

DEAR MR. CHAIRMAN: Enclosed is a statement, in triplicate, prepared by Mr. George W. Miller, Chairman of the Board of Battenfeld Grease & Oil Corp., in my congressional district, in support of my bill H.R. 2406. I understand this bill will be considered along with other proposals relating to tariff and trade proposals in hearings scheduled before your Committee beginning on June 4, 1968.

In order to save the time of the Committee, we are submitting this written statement in lieu of a request to be heard in person. I respectfully request that this statement be made a part of the hearing record and that it be given full consideration at the appropriate time.

Thank you for your attention to this matter.

Sincerely yours,

HENRY P. SMITH, III,
Member of Congress.

Enclosures.

BATTENFELD GREASE & OIL CORP.,
North Tonawanda, N.Y., May 24, 1968.

AFFIDAVIT OF TESTIMONY PERTAINING TO H.R. 2406

This Bill is an amendment to the Tariff Schedules of the United States to allow containers for certain petroleum products and derivatives to be temporarily imported without payment of duty.

Battenfeld Grease & Oil Corporation of New York is an exclusively wholesale manufacturer of lubricants for the Petroleum Industry. These products are packaged mainly in metal containers of various sizes.

For the past seven or eight years Canadian industry has been producing such containers and our Canadian customers are demanding that the lubricants we produce for them be packaged in Canadian made containers. To aid the Canadian purchaser, the Canadian government has eliminated the duty on such containers when returned to Canada filled. However, we are required to pay 10% import duty on these containers empty. For approximately five years we have been requesting the U.S. government to drop this duty on such containers—that is allow them to be temporarily imported duty free, filled with lubricants we manufacture and returned to Canada. As stated previously, the Canadian government already has eliminated the return duty on Canadian manufactured metal containers.

Our Canadian business represents about 25% of our total output. We have lost about 5% of this tonnage in the past several years because we could not meet Canadian competition.

We cannot purchase metal containers in the U.S.A. at a price (plus Canadian import duty on U.S. made containers) that will allow us to continue this portion of our operation. Also, as stated before, Canadian customers are insisting on the use of Canadian made containers—in many cases it is a necessity, since the large accounts purchase very large volumes of Canadian made metal containers lithographed with their designs. Most of these containers are utilized within Canada for products of Canadian manufacture. The cost of lithographed containers decreases as the total volume purchased goes up. For us to have these same type containers produced and lithographed in the U.S. is an additional expense, due to the relatively small volume we use compared with their total overall volume.

While a 10% saving on package cost sounds small, we work on very close volume margins and this amount is the straw that breaks the camel's back. Unless we are afforded some relief, we will shortly be faced with the loss of the balance of our Canadian accounts. This, of course, would be a Corporate hardship and would undoubtedly mean a reduction in our labor force, resulting in further unemployment in this area. We are what is termed "small business" and 25% of our total volume means considerable to us and this area. Also,