ECONOMIC AND ENERGY MEETING

Monday, June 9, 1975

2:00 p.m.

THE PRESIDENT HAS SEEN. G.F.

THE PRESIDENT HAS SEEN

THE WHITE HOUSE

WASHINGTON

June 7, 1975

ECONOMIC AND ENERGY MEETING
June 9, 1975
2:00 p.m.
Cabinet Room

From: L. William Seidman LWS

I. PURPOSE

A. To briefly review the current state of the economy and the near-term economic outlook.

B. To consider the Labor-Management Committee's tax incentive proposals for electric utility construction.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

A. Background: On May 21, the Labor-Management Committee unanimously recommended a series of legislative and administrative measures to increase electric utility construction and output.

Attached at Tab A is a memorandum outlining alternatives regarding the Administration position with respect to the Labor-Management Committee's proposals.

B. Participants: The Vice President, L. William Seidman, John T. Dunlop, James T. Lynn, Alan Greenspan, Rogers C.B. Morton, Frank Zarb, Arthur F. Burns, Stephen Gardner, Donald Rumsfeld, John O. Marsh, Richard Dunham, Fred Hickman.

C. Press Plan: White House Press Corps Photo Opportunity.

III. AGENDA

A. Review of Current State of the Economy

Alan Greenspan will briefly review the current state of the economy and the near-term economic outlook.

B. Labor-Management Committee Utility Proposals

John Dunlop will review the proposals of the Labor-Management Committee and alternative Administration responses in light of your present utility proposals.

A

THE WHITE HOUSE

WASHINGTON

ACTION

June 6, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: L. WILLIAM SEIDMAN LWS

SUBJECT: Labor-Management Committee's Tax Incentive Proposals for Electric Utility Construction

The Labor-Management Committee (LMC), on May 21, unanimously recommended a series of legislative and administrative measures to increase electric utility construction and output. (Tab A)

This memorandum deals only with the Committee's legislative proposals. It requests your decision regarding the Administration position with respect to the Labor-Management Committee's proposals.

I. BACKGROUND

In your State of the Union Address you acknowledged the financing problems of the electric utility industry, and its adverse impact on the Nation's energy objectives.

Earlier, in October, you proposed that the investment tax credit be increased permanently to ten percent for all businesses, including utilities; that it be made "refundable" (i.e., that it be permitted to eliminate the entire tax liability with any excess to be "refunded" to the taxpayer); and that there be a "basis adjustment" (i.e., that taxpayers no longer be permitted to take depreciation deductions for that portion of the purchase price covered by the credit). These proposals were never acted on, but have not been withdrawn.

In your January tax package, you proposed a temporary one year increase in the investment tax credit from seven percent to 12 percent. The "refundable" and "basis adjustment" provisions in the October proposals were not included. The January proposals did include a permanent increase in the investment tax credit to seven percent for utilities to place them on par with other businesses.

In addition, we submitted a limited Federal override bill for state utility regulations as Title VII of the omnibus energy bill. The intent of the Utilities Act of 1975 is to increase utility cash flow and return on investment to restore investor confidence. The legislation would establish a series of minimum Federal standards for several state regulatory practices, including (a) the elimination of regulatory lag, (b) the inclusion of construction-work-in progress (CWIP) in the rate base, (c) the use of normalized accounting practices, and (d) putting the costs of pollution control equipment into the rate base.

It is estimated that the Federal revenue impact of your utility proposals would be minimal.

The legislation has made little progress in Congress. To date, only three days of hearings have been held in the Senate, and none by the House. In light of Congressional inaction, the Energy Resources Council is preparing national guidelines for electricity ratemaking. To induce state regulatory authorities to incorporate these guidelines, tax incentives may be recommended.

Electric Utility Plan Construction Delays

At the end of 1974, electric utilities had deferred or cancelled the construction of an estimated 106 nuclear plants (114,000 megawatts) and 129 coal-fired plants (74,413 megawatts). This extensive postponement in construction schedules of coal and nuclear power plants seriously jeopardizes our national objective of less dependence on imported oil. It also threatens continued economic growth, restrains essential job creation, and inhibits measures to reduce unemployment. Since a number of years are required to get new plants on stream, the current delays and cancellations of new facilities will likely result in future energy shortages and restrictions to economic expansion. The financial condition of electric utilities has improved somewhat from a bleak picture some months ago.

The Labor-Management Committee's Proposals

The LMC's legislative package includes four tax proposals:

1. Increase from ten percent to 12 percent the investment tax credit for non-oil or gas-fired electric generating facilities; allow cash refunds for utilities with no tax liabilities. 1- $10 ,640

2. Allow depreciation for tax purposes to begin during construction of new non-oil or gas-fired electrical generating facilities provided such costs are included in the regulatory rate base. $220

3. Extend for five years current legislation permitting five year amortization of pollution control facilities and also include the costs of converting electric plants from oil and gas to coal and other fuels. 0

4. Permit establishment of stock dividend reinvestment plans allowing electric utility shareholders the choice of receiving stock instead of cash but fully taxable as ordinary income when any stock is sold. $330 310

The Labor-Management Committee also proposes to extend the Nuclear-Indemnity Coverage Law (Price-Anderson Act).

These proposals are consistent with the Administration's objectives to prevent future power shortages and raise electric rates, but differ in several major respects:

1. The LMC's proposals would result in an estimated net revenue loss of $1.5 billion in FY 1976 rising to $2 billion in FY 1980.

2. The LMC's proposals offer tax incentives to secure limited changes in state regulatory practices.

3. The Administration's energy policy is based on the premise that energy users should pay full energy costs, which will in turn minimize energy use. The LMC's proposals are, in substance, subsidies which shift costs to the public generally.

Pros and cons and costs of the Labor-Management Committee proposals are attached at Tab B. Overall evaluations of the proposals from Treasury and CEA are attached at Tab C.

II. OPTIONS

Option A: Endorse the LMC legislative proposals and present them as an Administration-sponsored bill in place of the present Administration utility proposals.

Advantages: Outright endorsement is a significant opportunity to break the current legislative stalemate. The LMC's proposal permits the private sector to more effectively attack the problems of implementing our national energy policy. Such action, if approved by the Congress, would set the precedent for extending similar initiatives to a broader base of industry later in the Summer. Success of this test case could facilitate our introduction of a broad package aimed at the problems of capital formation, productivity, and job creation.

Disadvantages: An unequivocal, no-strings-attached endorsement would limit your current and future flexibility. It entails endorsing tax policy proposals prior to deciding your final recommendations on general tax reform legislation. The LMC proposal would increase the deficit by $1.5 billion. It is not clear that the LMC proposals will work to increase capacity because it is difficult to insure that all the benefits are not all passed to consumers thus discouraging conservation.

Option B: Endorse the LMC's legislative proposals as acceptable to you and as a significant contribution, making no reference to your existing utility proposals.

Advantages: Same as for Option A but provides you the flexibility to continue support for your present utility proposals.

Disadvantages: It entails endorsing tax policy proposals prior to deciding your final recommendations on general tax reform legislation. The LMC proposal would increase the deficit by $1.5 billion. This approach could generate confusion regarding whether the LMC proposals replace or supplement your present proposals.

Option C: Endorse the LMC's legislative proposals as acceptable to you and as a significant contribution and at the same time encourage support for your present utility proposals.

Advantages: Same as for Option A and B but explicitly acknowledges and supports your present utility proposals. This approach emphasizes the compatibility and complementary nature of the LMC proposals and your present program.

Disadvantages: Same as for Option B except that this approach removes confusion regarding the relationship of the LMC proposals and your present utility program.

Option D: Endorse some of the LMC's legislative proposals but not others.

Advantages: Permits you greater flexibility in advancing new general tax reform and energy proposals.

Disadvantages: Selective adoption of the LMC proposals would likely destroy the willingness of LMC members to press for Congressional support of the proposals you endorse.

Option E: Release the LMC proposals and indicate your appreciation of their efforts and that you will carefully consider their recommendations in the formulation of your general tax reform proposals. This is similar to your response to the December LMC tax reduction proposals.

Advantages: This option provides you maximum flexibility in advancing new general tax reform and energy proposals.

Disadvantages: Such an approach would likely alienate both labor and industry proponents of the legislation. It would possibly serve to discourage labor's participation in supporting programs relating to industry incentives.

Proposed Presidential press releases for the above options are attached at Tab D.

DECISION

Option A __________ Endorse the LMC legislative proposals and present them as an Administration-sponsored bill in place of the present Administration utility proposals.

Option B __________ Endorse the LMC's legislative proposals as acceptable to you and as a significant contribution, making no reference to your existing utility proposals.

Option C __________ Endorse the LMC's legislative proposals as acceptable to you and as a significant contribution and at the same time encourage support for your present utility proposals.

Option D __________ Endorse some of the LMC's legislative proposals but not others.

Option E __________ Release the LMC proposals and indicate your appreciation of their efforts and that you will carefully consider their recommendations in the formulation of your general tax reform proposals. This is similar to your response to the December LMC tax reduction proposals.

TAB A

TAB A

For Discussion Purposes Only

May 21, 1975
After Meeting

Electric Utilities

At the end of 1974, it is estimated that electric utilities had deferred or cancelled the construction of 106 nuclear plants (114,000 megawatts) and 129 coal-fired plants (74,413 megawatts). This extensive postponement in construction schedules of coal and nuclear power plants that are needed to meet the nation's energy demands for 1980 and 1985 seriously jeopardizes our national objective of lesser dependence on imported oil. It also threatens continued economic growth, promises to restrain essential job creation and inhibits measures to reduce unemployment. Since electric utilities require a number of years to get new plants on stream, the current slippage of schedules and cancellation of new facilities may be expected to result in future energy shortages and serious restrictions to economic expansion. It is imperative that there be substantial restoration of construction of electric utilities at once. Special measures are needed to shorten significantly the very long lead time which now exists between the design of a project and its completion.

The President's Labor-Management Committee recommends a number of administrative and legislative measures to get this basic and strategic sector of the economy moving.

Special Legislative Proposals

1. The President's Labor-Management Committee earlier recommended that the investment tax credit for utilities be increased from 4 percent to 12 percent a year. The Congress increased the investment tax credit to 10 percent for a two-year period. The Committee still believes the 12 percent figure is appropriate and, in the case of electric utilities, this credit should be extended indefinitely and apply to construction work in progress to stimulate this vital sector which promises to present capacity problems for many years. This proposal is designed to stimulate non-oil and non-gas facilities.

2. In view of the length of time required to complete the construction of electric utility installations, the Federal government should permit depreciation for tax purposes on construction expenditures as made, provided such costs are included in the rate base.

3. The five-year, fast write-off of pollution control facilities should be extended by legislation beyond its present expiration date of December 31, 1975. The fast write-off of pollution control facilities reduces the financing costs of the construction of electric utility units. Fuel conversion costs should receive the same treatment.

4. The Nuclear-Indemnity Coverage law (Price-Anderson Act) should be extended.

5. The urgent need for equity capital in the electric utility industry should be met by a legislative provision that dividends which are reinvested in new issue common stock of the company have tax deferred.

The Committee recommends that the above legislative proposals be incorporated in a single piece of legislation in view of the special need for greater electric utility capacity and the long lead time required to complete plants and get them in operation.

Administrative Action

The Federal government should establish a small task force of experts, with assistance drawn from labor and management with experience in the field of utility construction, to serve as troubleshooters, to discover the impediments to the completion of electric utility plants and to take steps to relieve the particular situation wherever possible. The difficulties will vary from case to case; the problems may include unreasonable environmental restrictions and delays in processing papers, financing, regulatory delay, collective bargaining disputes, production delays in component parts, scheduling of manufactured components, design issues, etc. This task force can expedite the completion of electric utility plants and getting power on stream.

Immediate Improvement in the Policies and Actions Regarding the Usage of Coal and Nuclear Energy

1. Coal

   a. Make a major effort toward increasing the domestic production use of coal to generate power, including the development of economic means of moving either western low-sulphur coal, or the generated power, to the required market areas.

   b. A timetable should be considered for the conversion of oil/gas fueled power plants to coal.

   c. The government should reduce the uncertainties on coal usage by encouraging the development of technology to minimize pollution and environmental concerns regarding coal mining and coal use and by reducing the economic uncertainties in the mining and use of coal. This should encourage increased long-term investment in mining which in turn should stimulate employment.

2. Nuclear Energy

   a. The nation should make every effort to capitalize on the benefits of two decades and billions of dollars of public and private efforts in nuclear power development. While the initial investment costs for nuclear energy are high, it offers the cheapest form of electricity in the long run. Every effort must be made so that the percentage of electric power generation derived from nuclear sources by 1980/1985 is greatly increased from current levels. It is estimated that 10 to 15 million construction labor hours are required for each nuclear unit installed.

b. Specific government action is required in the following areas:

-- Promote the public acceptance of nuclear power.

-- Resolve the uncertainties regarding the nuclear fuel cycle, e.g., long-term nuclear waste disposal, plutonium usage, spent fuel storage and reprocessing.

-- Streamline the nuclear regulatory licensing process to reduce the lead time for getting plants into production. The current lead time is about 8 to 10 years.

<u>Review and Articulate the National Energy Interest with State Regulatory Agencies</u>

a. The Federal government needs to find an appropriate and realistic approach to get the national energy issues and interests before state regulatory agencies when they have their hearings on utility needs.

b. We must provide for prompt and reasonable action on rate applications.

c. New and innovative rate schemes, such as peak load pricing and rates designed to foster conservation, should be thoroughly studied and evaluated to determine the true impact on the various sectors of the economy.

Environmental Considerations

Stretch out, as necessary, present environmental restrictions on energy production and use to reduce energy consumption and facilitate expansion of domestic energy output. This is basically a matter of time-tables, not of objectives. The advance of technology and development of clean energy sources can permit realization of environmental objectives.

The President's Labor-Management Committee

Labor

I. W. Abel, President, United Steelworkers of America
Murray H. Finley, President, Amalgamated Clothing Workers of America
Frank E. Fitzsimmons, President, International Brotherhood of Teamsters
Paul Hall, President, Seafarers International Union of North America
Lane Kirkland, Secretary-Treasurer, AFL-CIO
George Meany, President, AFL-CIO
Arnold Miller, President, United Mine Workers of America
Leonard Woodcock, President, International Union of United Automobile, Aerospace & Agricultural Implement Workers of America

Management

Stephen D. Bechtel, Jr., Chairman Bechtel Group of Companies
Richard C. Gerstenberg, Chairman, General Motors Corporation
John D. Harper, Chairman, Aluminum Company of America
Reginald H. Jones, Chairman, General Electric Company
R. Heath Larry, Vice Chairman of the Board, U.S. Steel Corporation
Rawleigh Warner, Jr., Chairman, Mobil Oil Corporation
Arthur M. Wood, Chairman, Sears, Roebuck & Company
Walter B. Wriston, Chairman, First National City Bank

TAB B

PROS AND CONS OF LABOR-MANAGEMENT COMMITTEE'S LEGISLATIVE PROPOSALS

Item 1. Increase Investment Tax Credit

Prior to 1975, the investment credit was 7% generally and 4% for utilities, subject to the limitation that the credit could not exceed 50% of the liability for tax.

Last October you proposed that the investment tax credit be increased permanently to ten percent for all businesses, including utilities; that it be made "refundable" (i.e., that it be permitted to eliminate the entire tax liability with any excess to be "refunded" to the taxpayer); and that there be a "basis adjustment" (i.e., that taxpayers no longer be permitted to take depreciation deductions for that portion of the purchase price covered by the credit). These proposals were never acted on, but have not been withdrawn.

In your January tax package, you proposed a temporary one year increase in the investment tax credit from seven percent to 12 percent. The "refundable" and "basis adjustment" provisions in the October proposals were not included. The January proposals did include a permanent increase in the investment tax credit to seven percent for utilities to place them on par with other businesses.

Even when applied uniformly, the investment credit helps some taxpayers more than others, which causes inequities that become serious as the credit gets to a large percentage. Thus, we have never proposed a credit as large as 12% on a permanent basis, and even the 10% credit proposal was accompanied by proposals for structural changes to reduce the inequities inherent in the credit.

The present proposal would permanently increase the credit for non-oil and gas electric utilities to 12%. It would also make the credit "refundable," but without the offsetting basis adjustment.

The estimated revenue loss is $995 million for FY 76; $770 million for FY 77; $768 million for FY 78; $722 million for FY 79; and $640 million for FY 80. The FY 76 loss would exceed the $60 billion deficit point.

Pros:

- Provides direct cash benefits to marginal and unprofitable electric utilities (providing the "refundable" feature is retained).

- Improves balance sheets of hard-pressed utilities and their ability to attract equity and debt capital.

- Channels benefits to utilities constructing non-oil and gas generating facilities.

- Alleviates unemployment caused by cancellation and deferrals of nuclear and coal-fired generating facilities if and to the extent that relief causes construction to resume.

- Stimulates accelerated construction of non-oil and non-gas generating facilities and shut down of oil and gas-fired plants.

Cons:

- Is a subsidy rather than a tax adjustment, when confined to a single industry and divorced from tax liability.

- Violates principle of uniformity in tax policy by conferring special and major benefits to utilities on a permanent basis to alleviate particular and temporary problems. (Our prior proposals made only minor and transitional departures from uniformity.)

- Cannot be justified as a special benefit on the ground that it will cause construction to resume, because most of the dollars will go for construction which will occur in any event. (The present credit is subject to the same criticism, but it is available equally.)

- To extent utility investment is increased, some capital will be drawn away from other industries; thus intensifying any "crowding out" problem for the non-electric utility sector.

- The "refundable" feature will be attacked as a "negative income tax" for poor utilities and will highlight the subsidy nature of the proposal. Without it, on the other hand, assistance to wealthiest companies would be even more lopsided.

- Opens doors to other industry pleas for special credits.

- Congress has already provided tax benefits for utilities in the 1975 Tax Reduction Act, which was as much as we recommended on a permanent basis.

- If this is a subsidy, rather than a tax adjustment, municipally and state-owned facilities, TVA, etc., will also expect help. They pushed for benefits in the March bill, but were successfully resisted on the ground that we were only making equitable adjustments in tax liabilities, and they already paid no taxes. Since the LMC's proposal has a negative income feature, their arguments will be more difficult to resist.

Item 2. <u>Extend Depreciation to Period of Construction</u>

Under present law, depreciation commences at the time an asset is placed in service. A part of the gross income from the asset represents the cost of the asset wearing out and becoming obsolete, and must be deducted from the gross income in order to determine the net profit. Depreciation deductions cannot be justified as a cost until the asset has been placed in service.

The proposal is to permit depreciation deductions to be taken while the asset is under construction, before it is placed in service and - obviously - before it is wearing out. The additional deductions proposed are not justified as a proper cost, but rather as a special incentive provision for utilities.

The estimated revenue loss in millions is: $220 for FY 76; $460 for FY 77; $660 for FY 78; $860 for FY 79, and $1060 for FY 80.

<u>Pros:</u>

- To the extent the tax credit acts as an incentive, it can be a potent inducement to state regulatory agencies to include construction work in progress in the rate base.

- Provides needed and more equitable financial relief during long-construction lead times.

- Adds, together with tax credits, to the financial attractiveness of electric utilities to investors.

- Adds an incentive (like the tax credit proposal) to construction of needed new non-gas and non-oil power generating facilities.

Cons:

- Present ADR depreciation rules are in political trouble and face cut-back, primarily because depreciation is not adequately perceived as a real cost and is often regarded as an "incentive gimmick." We increase that problem and risk losing ADR if we transform the deduction into something we can no longer justify as a cost, Treasury tax people regard the danger as very real.

- If depreciation comes to be regarded primarily as an incentive, rather than a cost, it will become a political item, to be turned on and off like the investment credit. The resulting uncertainties over the stability of tax law may dampen capital formation in the long run.

- Proposal does not help utilities with little or no taxable income; benefits those in better financial condition.

- As a special incentive, it violates free credit market principles by distorting normal investment decisions.

Item 3. Extend Fast Write-off of Pollution Control for Five Years and Expand to Include Fuel Conversion Costs

Present fast write-off law for pollution control costs expires on December 31, 1975. A five-year extension is proposed plus expansion to include fuel conversion costs.

Revenue losses are estimated to be negligible because no significant use is expected in light of the more attractive tax credit alternative.

Pros:

- Allows recovery of cash more rapidly than alternative methods.

- Accelerates environmental compliance and conversion to non-oil and non-gas fuels for power generation.

Cons:

- Use of this provision unlikely since election of 5-year amortization precludes claim for investment tax credit for those facilities.

- Makes tax law more complex and, because of its lack of significance to taxpayers, should be eliminated, not extended.

Item 4. Stock Dividend Reinvestment Plan

A shareholder of an electric utility may elect to receive a dividend in stock of the utility rather than cash. In that event, the shareholder would pay no tax on the dividend until the stock represented by it was sold, at which time, the stock would be taxed as ordinary income rather than capital gain.

The estimated revenue loss in millions is: $330 in FY 76; $300 in FY 77; $300 in FY 78; $300 in FY 79; and $310 in FY 80.

Pros:

- Increases supply of equity capital for electric utilities to the extent shareholders leave dividends in utility and take stock in exchange.

- Provides most cost/effective way of rechanneling investment equities into utilities. Minimal cost to Treasury offset several times by equity inflow to utilities.

- Increases balance sheet attractiveness of utilities to new equity and debt security investors by improving equity debt ratios and cash position.

- Provides incentive for accelerated construction of non-oil and non-gas generating facilities and unemployment.

- Offers opportunity to open door early to Congressional consideration of tax reform concepts emphasizing capital formation.

Cons:

- The proposal is fundamentally in conflict with proposals for integrating the corporate income tax:

  The purpose of integration is to make the tax system neutral as between debt and equity. Depending on the length of the tax deferral and the taxpayer's tax bracket, this proposal may increase the ultimate penalty on equity investment because the ultimate gain on reinvestment in stock is taxed as ordinary income rather than capital gain.

  Integration would remove the existing tax penalty on equity investment. This proposal would create a new and additional penalty on those who fail to increase their equity investment in a particular company.

  Adoption of the proposal will siphon away utility support for integration. Utilities would benefit greatly from integration because it would remove an existing discrimination against them. However, they will be unwilling to trade this proposal for integration because this proposal goes beyond neutrality and discriminates in their favor.

- The proposal will be a very bad precedent. It will open the door to income deferrals for other industries which are in trouble - usually because they are not successfully competing. The tax deferral of interest on savings accounts is exactly analogous. We had a hard time defeating that proposal last year. How will we stop it the next time if we have ourselves proposed to defer tax on dividends?

- This proposal will be generally perceived as "anti-tax reform." It has already been defeated on this ground in the Ways and Means Committee. It would undo a tax reform which the Administration itself proposed and Congress enacted in 1969.

- The proposal is intentionally inequitable to other types of investments in other industries. This creates a serious problem of tax fairness. To the extent more investment in electric utilities occurs because of this provision, the cons with respect to the investment credit are relevant.

- The proposal is technically very complex and can never work really well. The record-keeping difficulty for shareholders and audit problems for the Internal Revenue Service are significant.

TAB C

TAB C

June 6, 1975

TREASURY COMMENTS ON LMC ELECTRIC UTILITIES PROPOSALS

The proposals bear a superficial resemblance to proposals advanced by the Administration in the past, as they would liberalize the investment credit and depreciation allowances. There is, however, a fundamental difference. The prior Administration proposals were designed to keep the tax system neutral as it bears on the free market system and to treat everyone as equally as possible. These proposals, on the other hand, would use the tax system in an unneutral way-- to tilt economic decision making.

The aim of the proposals is pragmatic: to provide money through the tax system for an industry that is short of money for nontax reasons.

The question is whether that pragmatic goal outweighs the disadvantages of the particular proposals. The Treasury believes that the proposals represent bad tax policy, detrimental in the long run. It makes the following general arguments:

1. The proposals are fundamentally contrary to free market principles. As such, they are a move in the wrong direction. Each of them uses the tax system to rechannel normal market forces and to distort the price system. Once in place, they are likely to be permanent clogs on the system.

2. The proposals are contrary to the underlying principle of the Administration's energy policy that the users of energy should pay the price for it. The proposals are subsidies, which shift the cost to the public generally.

3. The proposals will not produce any results to the extent that regulatory commissions do not permit the benefits to remain with the companies. They will be under political pressure to pass the benefits through to consumers, and there is no practical way to know whether that has happened, to keep it from happening or to police it afterwards.

4. None of the proposals deal with the fundamental problem of utilities. Utilities can't get equity money because equity investors are not willing to buy where state regulation precludes a fair return. Utility equities are not a good investment for the same reason that rent controlled buildings in New York City are not a good investment. At best, special tax relief will only postpone the day of reckoning.

5. The proposed program is vulnerable--correctly--to the charge that at a time when we are unwilling to help New York City over an allegedly "temporary difficulty," we are nonetheless willing to give more than $1 billion a year to relieve private utility investors.

6. The proposed program is very expensive--starting at $1.5 billion and rising over time. It would be in addition to the investment credit benefits for electric utilities voted by Congress in March, estimated to cost $300 million in 1975 and rising rapidly to about $1.1 billion by 1980. It is doubly expensive if we get nothing for it.

7. The proposals are at cross purposes with projected proposals to help capital formation in the economy generally. The revenues available for general reform will be limited, and the proposals would preempt $1.5 billion of them in the first year alone. Further, the proposals would divert capital from other industries, fragment the political support for more general measures, and present conceptual inconsistencies with other proposals.

June 6, 1975

CEA EVALUATION OF ECONOMIC JUSTIFICATION FOR
SPECIAL MEASURES TO AID THE UTILITIES

While some of the utility construction curtailments and deferrals of 1974 were due to financial causes, the condition of the utilities has now improved substantially. No emergency now exists. There is no requirement that immediate action be taken on economic grounds. There is little likelihood that utility capacity shortages will occur in the next five years or that within the same timeframe, these proposals would lead to reductions in oil imports. Consequently, these measures to subsidize electric utilities should be judged by whether or not they contribute to long run economic efficiency, contribute to substantive tax reform, and are desirable guides against which other legislative actions and requests for special tax treatment or budget expenditures should be judged.

The financial difficulties of the electric utilities were brought on by rapidly increasing costs which they were unable to recover on a timely basis through increased revenues.

The sources of the cost increases were: fuel prices, general inflation, and high interest rates. Revenues lagged because of delays in regulatory approval of rate increases and the leveling off and decline in electric sales.

Recent circumstances have been much more favorable to the financial condition of the utilities. Fuel costs are no longer rising at the rapid rates of 1974. Moreover, virtually all utilities now are under automatic fuel adjustment clauses and thus fuel costs are passed through without time consuming delays. Some jurisdictions allow prospective fuel cost adjustment.

General inflation has fallen from a rate of approximately 12 percent during 1974 to a rate of about 6.5 percent so far during 1975. Moreover, many states now use estimates of future costs in setting rates. In this, and other ways the regulatory commissions have adjusted their procedures so as to shorten the delay between cost and rate increases.

Interest rates have fallen, representative short term rates, relevant to utility construction financing, have dropped from an average of about 9.9 percent during 1974 to approximately six percent now.

Utilities are now receiving rate increases based upon earlier cost increases. The table below shows the rise in the level of rate increases granted.

Annual Rate Increases Taking Effect ($ Million)

Quarter	1974	1973	1972	1971
I	$ 671	$ 295	$ 174	$ 238
II	645	191	187	211
III	602	256	91	266
IV	599	385	154	206
Year total:	$2,517	$1,127	$ 606	$ 923

Source: FPC

Electric utility sales are expected to rise with the recovery in economic activity. The reversal in the 1974 no growth experience will greatly improve the utility revenue picture.

TAB D

The President's Statement on the Labor-Management Committee's Recommendations for Legislative and Administrative Measures Concerning Electric Utilities - June 5, 1975

On December 30, 1974, the Labor-Management Committee presented its unanimous recommendations concerning economic initiatives for personal and business tax cuts and national energy policies.

Today I am releasing those recommendations for legislative measures to increase electric utility construction and output.

For Option A.

Having carefully reviewed these recommendations, I accept and endorse them because they can make a significant contribution toward reducing the nation's dependence on oil imports and conserving scarce natural gas supplies. I accept them in place of existing Administration proposals and will present them to the Congress as an Administration bill.

Additionally, the needed resurgence in electric utility construction and production will provide the kinds of jobs which are most beneficial to the country. An undertaking to increase electrical utility generation capacity also will create the capacity to facilitate economic expansion.

For Option B.

Having carefully reviewed these recommendations, I accept and endorse them because they can make a significant contribution toward reducing the nation's dependence on oil imports and conserving scarce natural gas supplies.

Additionally, the needed resurgence in electric utility construction and production will provide the kinds of jobs which are most beneficial to the country. An undertaking to increase electrical utility generation capacity also will create the capacity to facilitate economic expansion.

For Option C.

Having carefully reviewed these recommendations, I accept and endorse them because they can make a significant contribution toward reducing the nation's dependence on oil imports and conserving scarce natural gas supplies.

At the same time, I urge swift action by the Congress on my existing utility proposals incorporated in the proposed Utility Act of 1975.

Additionally, the needed resurgence in electric utility construction and production will provide the kinds of jobs which are most beneficial to the country. An undertaking to increase electrical utility generation capacity also will create the capacity to facilitate economic expansion.

For Option D.

These proposals work toward the attainment of goals which we all share -- greater energy independence, and higher employment. In particular, I endorse the Committee's recommendations for ______________, ______________, ______________, ______________ and ______________.

The Administration already is taking important initiatives or has proposed further action by the Congress to carry out a good number of the Committee's proposals to increase use of coal and nuclear energy and to balance our energy and environmental objectives.

I will take steps promptly to create the task force the Committee recommends to tackle the problem of delays in the completion of utility plants. In view of the long lead time on utility construction, completion of plants already in advance stages of planning or already in construction must have a top priority.

The Administration already is taking important initiatives and has proposed further action by the Congress to carry out a good number of the Committee's proposals as to increased usage of coal and nuclear energy and balancing our energy and environmental objectives. I have instructed the Energy Resources Council to evaluate these initiatives and proposals against the points made by the Committee in order to determine gaps in our efforts.

For Option E.

I fully endorse the concepts underlying these proposals:

-- that utilities must be allowed to earn a rate of return after taxes sufficient to attract the vast amounts of capital they will require over the next decade if this nation is to avoid costly shortages of electric generation capacity,

-- that we must accelerate our efforts to uncover and, wherever possible, take steps to relieve other impediments to completion of utility plants,

-- that no stone should be left unturned toward bringing about substantially greater utilization of coal and nuclear energy,

-- that the Federal Government must work closely with State and local regulatory agencies on utility rate matters, and

-- that we must look closely at ways of harmonizing our energy and environmental objectives.

When I signed the bill providing for the tax cut in March, I asked the Congress to work with me on a comprehensive review of our tax structure to eliminate inequity and to assure adequate revenues for the future without crippling economic growth. Utility construction is vital to our economic growth, and the Committee's tax incentives for utilities deserve most careful consideration by both the Administration and the Congress. In addition, I support the Committee's recommendation that the nuclear indemnity coverage law be extended.

I will take steps promptly to create the task force the Committee recommends to tackle the problem of delays in the completion of utility plants. In view of the long lead time on utility construction, completion of plants already in advanced stages of planning or already in construction must have a top priority.

The Administration already is taking important initiatives or has proposed further action by the Congress to carry out a good number of the Committee's proposals as to increased usage of coal and nuclear energy and balancing our energy and environmental objectives. However, I have already instructed the Energy Resources Council to evaluate these initiatives and proposals against the points made by the Committee in order to determine gaps in our efforts.

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I thank the Committee for its continuing work and appreciate the constructive contribution of labor and management working together in the national interest.

Gerald R. Ford

(A list of Committee members and a copy of the Committee's statement of May 21, 1975, are attached.)