The original documents are located in Box C25, folder “Presidential Handwriting, 8/7/1975” of the Presidential Handwriting File at the Gerald R. Ford Presidential Library.

THE WHITE HOUSE

WASHINGTON

August 7, 1975

MR. PRESIDENT -

It is recommended that you read the attached before the Economic/Energy Meeting at 2 P.M. today.

Jim Connor

THE PRESIDENT HAS SEEN....

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: FRANK G. ZARB

SUBJECT: WINDFALL PROFITS TAX

BACKGROUND

In your January State of the Union Message you proposed immediate decontrol coupled with a windfall profits tax (WFPT). Since this original proposal, a number of events have occurred which necessitates modifying your proposal.

- Congress repealed the depletion allowance.

- The Senate Finance Committee has reported a windfall profits tax in the event of immediate decontrol.

ADMINISTRATION'S NEW WFPT

Your advisors have reviewed the current situation and have developed a recommended WFPT which closely follows the Senate Finance Committee bill. The basic features of the deregulation tax are:

- Tax both old oil and uncontrolled oil (including oil from stripper wells), at 90% of difference between base price of about $5.25 per barrel (increasing 0.5% per month) and the sales price.

- Provide constructive base price for uncontrolled oil equal to about $11.25 per barrel.

- Phase out the WFPT tax over 67 months by reducing the amount of taxable oil by 1.5% per month.

- A plowback credit which offsets up to 25% of the tax. The credit is dollar for dollar for the amount of qualified investments in excess of a threshold. The threshold is 40% of the base price for old oil produced during the taxable period (i.e., average of $2 per barrel). There is no threshold for the credit with respect to uncontrolled oil.

The recommended deregulation tax differs from the Finance Committee bill by:

- Providing individualized base price for uncontrolled oil depending on grade, quality and location rather than flat $11.50 base price.

- Including stripper well production in uncontrolled oil subject to tax.

Both of these modifications increase revenues from the tax particularly in the later years.

CONSUMER COST INCREASES AND TAX REBATES

Your original State of the Union proposals would have increased energy costs by approximately $30 billion and rebated to energy consumers -- corporations, individuals and state and local governments -- all of their increased costs.

Immediate decontrol, coupled with the removal of the import fees of $2.00 and $.60 per barrel on crude oil and petroleum products respectively will cause total energy costs to increase by about $8.0 billion annually. Of these total costs, individuals will pay approximately 5.1 billion directly and the rest will be borne by industry and all levels of government.

The proposed windfall profits tax would collect $7.3 billion directly and result in an additional $1.1 billion of corporate income taxes from oil companies. However, deregulation in the absence of a WFPT would also increase Federal taxes collected. As a result of the Treasury estimates the net taxes collected from the WFPT would be about $5.1 billion.

There is some disagreement over the level of consumer rebates. From an energy perspective, maximum support of decontrol will necessitate rebating the gross tax revenues i.e., $7.3 billion.

On the other hand this will have the maximum negative effect on the budget deficit. Given the removal of the fees, the greatest effect on keeping the deficit as close as possible to $60 billion would argue for lesser rebates. However, any decision to not fully rebate energy taxes is inconsistent with your State of the Union energy proposals and the statements of your advisors during the last several months.

The table below summarizes the budget deficit impact of these alternatives.

	Change in Budget Deficit in C.Y. 1976		
	No WFPT	WFPT with rebates of:	
	No rebates	$5 billion	$7 billion
Same monetary policy	+6.5B	+2.8B	$4.2B
Accommodating monetary policy	+4.5B	+0.8B	$2.2B

The increased budget deficits are due in large part to the loss of over $3 billion of expected Federal revenues when the tariffs are removed. The larger deficits with no WFPT or rebates are due to the adverse economic impact and resulting loss of tax receipts if revenues are not recycled. The deficit impacts in succeeding years may be somewhat larger.

The basic issue is the tradeoff between your basic energy and economic policies.

- Raising energy prices, but maintaining consumer purchasing power.

- Holding the line on the budget deficit.

The ERC recommends that all gross revenues collected from the WFPT be rebated. Your other advisors will present their views at the energy meeting later today.

STRUCTURE OF CONSUMER REBATES

If you decide to provide rebates of the WFPT, the structure of such rebates should be modified. With the much lower levels of total rebates, two basic questions should be asked.

- Should the rebates for industry and S&L governments be dropped?
- Should the rebates to individuals be on a per capita basis or only for low and middle income individuals?

It is the consensus of your advisors that general rebates to industry and state and local governments should be dropped and only targeted rebates such as for farmers be included. The issue of consumer rebate structure is still under review and a decision paper will be prepared for you.