The original documents are located in Box 1, folder: "Memoranda to the President, April 1975" of the Frank Zarb Papers at the Gerald R. Ford Presidential Library.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

April 1, 1975

MEMORANDUM FOR JERRY JONES

FROM: FRANK G. ZARB

The attached memorandum for the President has been reviewed by OMB and the Domestic Council.

Attachment

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

APR 1 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: Frank Zarb

THRU: Rogers C.B. Morton

SUBJECT: Auto Efficiency Status Report

Background

The 40% voluntary improvement in new auto fuel efficiency by 1980 announced in your State of the Union Message is adversely affected by two events:

- EPA's newest emission standards recommendations, which are different from those which were the basis for the auto companies voluntary efficiency agreement.

- Impending Congressional action on fuel efficiency taxes and/or mandatory fuel efficiency standards.

The responsible committees are moving rapidly to develop specific legislation and our ability to argue effectively against these mandatory approaches is hampered by the uncertainties introduced in your voluntary agreement by the lack of clear direction on emission standards.

Status

We are moving on two fronts to resolve the uncertainties with respect to auto fuel efficiency:

- OMB is coordinating an interagency review of auto emission standard alternatives and their environmental, economic and efficiency implications. It will be completed by April 7.

- FEA is working with the key committees to ascertain the specific tax or other legislation they favor. More details will be available by the end of April recess.

By April 11, the ERC will submit to you a new decision paper on auto emissions and fuel economy based on these efforts.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

4/1/75

OFFICE OF THE ADMINISTRATOR

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THRU: Rogers C.B. Morton

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Dispatched by
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did not come thru E.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 3, 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: FRANK ZARB

SUBJECT: Strike by the United Mine Workers of America

At midnight April 1 the United Mine Workers of America struck the anthracite coal industry. They have a separate contract from that of the bituminous coal industry, which was ratified and signed last December. Some 2,900 anthracite miners - seventy-five percent of the work force - are involved. Sixty-five percent of production or 4 million tons per year is affected.

Major areas of concern are wages, the pension fund, and sick and accident pay. Their demands are similar to the bituminous miners' except for payments to the pension fund which would triple to $2.70 per ton. The bituminous settlement had doubled the royalty to $1.60 per ton. Unpublicized bargaining sessions have been underway for some time and the Federal Mediation Service believes there is hope for an early settlement.

Because most anthracite is used for space heating, the strike's impact will not be as immediate as the bituminous strike last fall. Current stocks of anthracite appear to be sufficient to satisfy industrial and institutional needs for at least 3 to 6 weeks, although individual consumers may be hurt earlier.

No further action by the Administration is required at this time.

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ANTHRACITE STRIKE FACT SHEET

Current Situation

At midnight, April 1, 1975, collective bargaining agreements expired covering approximately 2,900 employees or nearly three-quarters of the production workers in the anthracite mining industry. The United Mine Workers of America (UMWA) ordered a strike to begin April 2, 1975. Contract negotiations which had been going on before the strike were broken-off April 3; but there is hope for early resumption. Major producers affected are: Beltrami Enterprises, Inc.; Bethlehem Mines Corporation; Jeddo-Highland Coal Company; and Reading Anthracite Company. Bargaining is conducted on an industry-wide basis, through the Anthracite Operators Negotiating Committee and the Union's Negotiating Committee.

Impact

Because most anthracite is used for space heating, the impact of the strike will not be as immediate as the UMWA strike last fall in the bituminous coal fields. Current stocks of coal appear ample to satisfy industrial and institutional needs for at least 3 to 6 weeks. Individual consumers, however, may be hurt earlier.

Previous Settlement

During the 1972-1973 contract negotiations, wage and price controls were in effect, and the parties settled on a 71 cent per hour increase for the first year, and 21 cents in each of the second and third years. However, the Wage and Price Board cut the increase back to 51 cents. Litigation initiated by the union resulted in a 10 cent retroactive increase. These actions did not satisfy the union membership which included a sizeable militant group. This background affects the present militant position.

Initial Union Demands

There are three major areas of bargaining concerned: (1) wages; (2) sick and accident pay; and (3) Anthracite Health and Welfare Pension Fund.

The union lists wage demands as the first priority. The following demands, if written into a final contract, could raise anthracite prices up to ten dollars per ton.

- Wage increase of approximately \$2.70 per hour immediately; 50 cents additional in six months.

- o Increase in Anthracite Health and Welfare Fund payments by the operators from 90 cents per ton to $2.70 per ton.
- o A full year of sick or accident benefits at $150 per week.
- o Triple pay for Sunday work.
- o Fully paid major medical and dental insurance.
- o Five paid personal days.
- o Raise in vacation pay from $250 to $500.
- o Annual, graduated, paid vacation scale starting with 2 weeks vacation after an initial work period.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

April 14, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: FRANK G. ZARB

THROUGH: ROGERS C.B. MORTON

SUBJECT: RECENT CONGRESSIONAL DEVELOPMENTS

Senate

The Senate is not as far along on comprehensive energy legislation as the House. Last week, however, the Senate did pass by 60-25 a standby energy emergency bill. There were several disturbing amendments added to the standby authorities legislation on the floor. The amendments adopted in the Senate set a mandatory conservation goal to be achieved by the following undesirable measures, even without an emergency:

- o Bans or severe restrictions on residential or commercial lighting.
- o Curtailment of "non-essential" private automobile transportation.
- o Limitations on industrial energy use.

While we have no major objections with their conservation goal, we believe the methods for implementing the goal and the inclusion of mandatory implementation of conservation in a standby authorities bill will have unforeseen economic consequences and is an unwarranted Federal intrusion into the daily lives of our citizens.

In addition, a price ceiling was established for all domestic crude oil not classified as "old" oil. This oil is now uncontrolled. The price ceiling is set at the price which was charged for this oil as of January 31, 1975 (approximately $11.25 per barrel). Another amendment established a $7.50 price ceiling on oil produced with advanced recovery techniques. The effect of both these amendments is to establish four price levels for crude oil, even more undesirable than our current two tier system. We will strongly oppose these amendments. Both Ullman and Dingell agree with us concerning the defects of the Senate bill.

House

While no legislation has been reported by the House, both House Commerce and Ways and Means Committees are now marking up "comprehensive" energy legislation. We have continued to maintain close, cooperative relationships with the Chairmen and staff, but major problems are being generated by the liberal elements of both committees.

In the Ways and Means Committee, it is now apparent that a fully operational quota could be imposed, probably with quantitative limits set each year. The level of the gasoline tax is likely to be much lower than the $.37 originally proposed by Mr. Ullman and it is possible that it will be at a very low level combined with Presidential authority to raise it higher.

The House Commerce Committee is considering proposals which are very objectionable, including:

- A rollback of old oil to $4.25 per barrel coupled with a 5-8 year decontrol schedule.

- Use of the allocation program to cut gasoline supplies by 2% per year from 1972 levels.

Many of these provisions are not desired by the Committee Chairmen but reflect the general sentiments of the Committee members and their influence over Committee affairs.

On the plus side Chairman Dingell is prepared to support language which would provide the effects of decontrol of old oil within three years. Ullman, of course, has supported this notion right from the beginning.

Recommendations

The situation, particularly in the House, remains very fluid and predicting the form of final legislation is difficult. We are taking a strong public position concerning the recently passed Senate bill pointing out wherever we can its major defects.

We will be providing you within the next week a more complete and detailed breakdown of the shape that the House legislation is taking. We will at the same time submit for your consideration options concerning actions you may wish to impose on May 1, the deadline previously set for the Congress.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 15, 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: FRANK ZARB

SUBJECT: Strike by the United Mine Workers of America

On April 15 the strike of the anthracite industry by the United Mine Workers of America entered its third week. The loss of production is estimated to be 120,000 tons weekly, although the independent segment of the industry is expanding production as rapidly as it can. Normally, the independents account for 35 percent of total anthracite output.

Governor Milton Shapp of Pennsylvania has established an anthracite hotline for consumers who may be running out of fuel. Commonwealth officials have been successful in arranging deliveries from independent mines and from stockpiles at State institutions.

Negotiations between the mine operators and the union, which broke off April 3, resumed April 14 at the urging of the Federal Mediation Service.

Negotiations seem still to be far apart on many issues. Central is the desire of the union to obtain a settlement similar to the one negotiated with the operators of bituminous coal mines last winter. The mine operators are resisting such a settlement as being too costly.

No additional action by the Administration is required at this time.

[co 4/17/75]

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: Frank G. Zarb

THROUGH: Rogers C.B. Morton

SUBJECT: Energy Program Modifications

BACKGROUND

There remains substantial concern about the economic impact of your administratively imposed import fees. While concern is expressed by many sectors, strong opposition is coming from energy intensive industries such as airlines, and from farmers and nonprofit institutions. Two modifications to your current proposals might substantially weaken some congressional opposition during the important days and weeks ahead.

FARMER RELIEF

Treasury and FEA have been exploring alternatives to provide the relief to farmers you outlined in Topeka, Kansas. Rather than a full rebate for all farmers, the following is recommended:

- a 10¢ per gallon rebate for all offroad use of gasoline and diesel fuel.

- if a tilt to gasoline is used, the rebates can be adjusted for both gasoline and diesel fuel.

- a $1000 limit annually per farmer to allow all to benefit, but not provide full rebates to large and corporate farms.

- a three-year phase-out of the rebate program.

- total revenue loss from the program is $350 million in the first year and then phases to zero.

Tab A provides more details.

GASOLINE TILT

FEA currently has the regulatory authority to determine what percentage of the increased import fees are passed on to each petroleum product. Currently we expect that all products would increase proportionately or about 4.3¢ per gallon once the $3.00 crude oil and $1.20 product import fee is fully felt.

The regulations can be modified to disproportionately increase gasoline prices by 6.0¢ per gallon while allowing other products to increase by only 2.9¢ per gallon. Such an action will reduce the economic impact on energy intensive industries and in the Northeast, while increasing the impact on the heavy gasoline use areas of the West. This program would be carried both during the period of the administrative fees and phased out during the period of your short term program, 1975-1977.

It should also be noted that this action is an alternative to giving case by case exemptions to many individual industries.

See Tab B attached for more details.

RECOMMENDATIONS

ERC recommends that both the gasoline tilt and the specific farmer rebate program be approved and announced on Wednesday, during the House hearings and prior to the Senate vote on the 90 day delay of the import fees.

Other agency views are recorded below.

	Gasoline Tilt		Farmer Relief	
Agency	Approve	Disapprove	Approve	Disapprove
EPB	X		X	
OMB				
Treasury		X	X	
Domestic Council	X		X	
Agriculture	X		X	
FEA	X		X	

TAB A

ISSUE:

What actions should be taken to deal with the impacts of increased fuel costs on farmers?

BACKGROUND

Energy costs comprise about three percent of total farm production costs of about $80 billion. The President's energy tax and fee proposals increase energy costs by about $30 billion, of which about 2.5 percent (750 million) is for agricultural purposes. These energy cost increases would increase total farm production costs by about one percent in 1975. This effect indicates that farming is much less energy intensive than many other industries where total production costs would increase by 3-20 percent due to the President's program.

Farmers account for about 3.3 percent of gross domestic product. Seventy percent of farm production is from farms which have gross sales of over $40,000 annually. (See Table 1) The remaining 2.25 million farmers with lower incomes account for 30 percent of farm production and would incur increased costs of about $200 million or an average $100 per farm. These costs for lower income farmers are deductible in computing their income taxes. Any net amount remaining would be wholly or largely offset by the President's tax rebate program.

If tax concessions are given to farmers or others because they are unable to pass their costs on, our $30B revenue and two percent CPI estimate increase must be revised downward.

OPTIONS:

There are two basic options to relieve the farmer situation:

Option 1: Provide all farmers with rebate for increased energy costs.

PRO:

- dramatic exception for an important socioeconomic group
- food production costs would be lowered

CON:

- farmers are no worse off than many other groups
- would result in a revenue loss of about $750 million annually
- would primarily benefit large farmers and major corporations

Option 2: Provide a 10¢ per gallon tax rebate on off-road use of gasoline and diesel fuel for farmers, limited to $1,000 per farmer (would more than cover costs of farmers with sales up to $100,000 per year). The 10¢ and $1,000 could phase down and out over, say, three years: 10¢/$1,000; 7¢/$700; 4¢/$400. If a gasoline tilt is used, the 10¢ rebate can be modified to provide rebates which actually coincide with the different taxes paid on gasoline and diesel fuel.

PRO:

- would result in only about $350 million in revenue loss initially, phasing down to zero after three years

CON:

- roughly same as Option 1 except would confine major benefit to smaller farmers

RECOMMENDATION:

Choose Option 2. A 10¢ gallon/$1,000 tax rebate with a phase-out for gasoline and diesel fuels would help farmers adjust gradually. It would also compensate them for costs which cannot be recovered through higher prices. Such a program would be administered through the existing income tax rebate system farmers now use for Federal gasoline and diesel excise taxes on fuels for off-highway use. Initially, the rebate would cover about half of farmers' total increased costs due to the energy program. The rest of the increased costs -- due to electricity, fertilizer, etc. -- would be offset by tax rebates and minor food price increases.

The revenue cost and the favoritism shown farmers would phase out over a period during which farmers could make a gradual transition to less fuel consumption.

It should be recognized that if a tilt towards gasoline is also adopted as part of our regulations, the rebates, revenue effects, and levels of consumption will change.

Percentage Distribution: Income and Production Expense of Farm Operations from Farming, by Value of Sales Classes, 1973

	less than $2,500	$2,500 to $4,999	$5,000 to $9,999	$10,000 to $19,999	$20,000 to $39,999	$40,000 to $99,000	$100,000 and over	Tota All Farm
Number of Farms	26.4	17.2	9.2	11.7	19.8	11.9	3.8	100%
Cash Receipts 1/	1.0	2.1	2.4	5.9	19.1	23.8	45.7	100
Production Expenses	1.4	2.4	2.3	5.5	17.4	22.7	48.3	100
Realized Net Income	2.5	3.2	3.2	7.5	23.3	25.5	34.8	100

1/ Includes other income

Source: Farm Income Situation, July 1974

GASOLINE TILT

ISSUE

Should the proposed cost pass-through regulations be tilted more heavily towards gasoline?

BACKGROUND

The currently proposed regulations for cost pass-throughs from the import fees would restrict price increases on heating oil and other products while allowing greater than the proportionate share of costs to be placed on gasoline. While the proposed program would allow higher costs on gasoline, it would not require disproportionate pass-throughs. As a result, as the administratively imposed fees are increased, all petroleum products will experience about the same increase in prices.

OPTIONS

Option 1: Adopt the currently proposed regulations.

PROS

- allows greater freedom for pass-throughs
- does not result in disproportionate regional impacts
- provides equal incentive for conservation of all products and industrial sectors
- will not be interpreted as a roundabout way of imposing a gasoline tax

CONS

- places a heavy burden on certain industries (e.g., airlines, petrochemicals) and non-profit institutions
- There is limited capacity to shift from oil to other fuels for heating and industry; whereas gasoline use tends to be more discretionary

Option 2: Require a disproportionate pass-through of costs to gasoline through April

PROS

- maximizes demand reduction on gasoline which seems to be regarded positively as the least essential area of consumption.
- reduces burden on industrial consumers, airlines, and users of electricity and heating oil

- would further reduce effects of program on the Northeast and mid-Atlantic states where more support exists for gasoline tilt

- indirect consumer costs would decline
- this represents an alternative to taking special actions to help individual industries, such as the airlines

CONS

- would disproportionately affect regions of the country more dependent on gasoline (Mountain States, Midwest, and Southwest - See Figure 1). These are the areas in which the greatest support for the program now exists.

- would have larger impact on leisure industry, automobile industry, and farmers (without compensating rebates)

- would create small pricing differentials on products other than gasoline, which could negatively affect the competitive posture of small and independent refiners.

- could be viewed as indirect support for gasoline tax and cast minute changes in a program which we say is well thought out

Option 3: Require higher gasoline pass-throughs until the end of 1977, by extending price and allocation authority

PROS

- provides for orderly phasing back to equal conservation incentives on all products

- continues the other positive effects cited in Option 2

CONS

- requires long-term controls -- counter to our current policy and would have administrative costs
- would create pressures to maintain price controls and allocation from those benefited by this action
- does not allow free market system to work
- could have significant impacts on small and independent refiners
- could have significant effects on refinery expansion plans and operating efficiencies
- could stimulate gasoline imports

ANALYSIS

The average domestic refinery yield is:

Gasoline	45%
Distillate	22%
Residual Oil	9%
Jet Fuels	7%
Other	17%

Thus, for each 1¢ increase in gasoline there would be approximately a 1¢ decline in the price of other products.

Administrative Program

The effect of the administratively imposed $3 per barrel fee on crude oil imports and $1.20/bbl. on product imports would be to increase prices for all fuels by 4.3¢ per gallon. The program could be modified as follows:

	Current Program (¢/gallons)	Proposed Gasoline Tilt (¢/gallon)
Increase in gasoline	4.3	6.0
Increase on other products	4.3	2.9

The effects of the gasoline tilt would be to increase direct consumer costs mostly in the Mountain and Southern states and decrease total costs along the East Coast. It would help the airlines.

The program could be implemented under existing FEA price controls by issuing new regulations.

Legislative Program

In the longer-term, the gasoline weighting could be accomplished by allowing a 15¢ passthrough for gasoline and about 6¢ on other products. Such a shift would have the following regional impacts:

- New England, Mid-Atlantic, and East North Central (Ohiom Indiana, Illinois, Michigan, and Wisconsin) regions would experience small increases in direct energy costs (less than $25 per household/year) and offsetting decreases in indirect costs.

- Mountain, South, and rest of the Midwest would experience large increases in direct costs (about $50 per household/year) and smaller decreases in indirect costs. These regions are heavier users of gasoline.

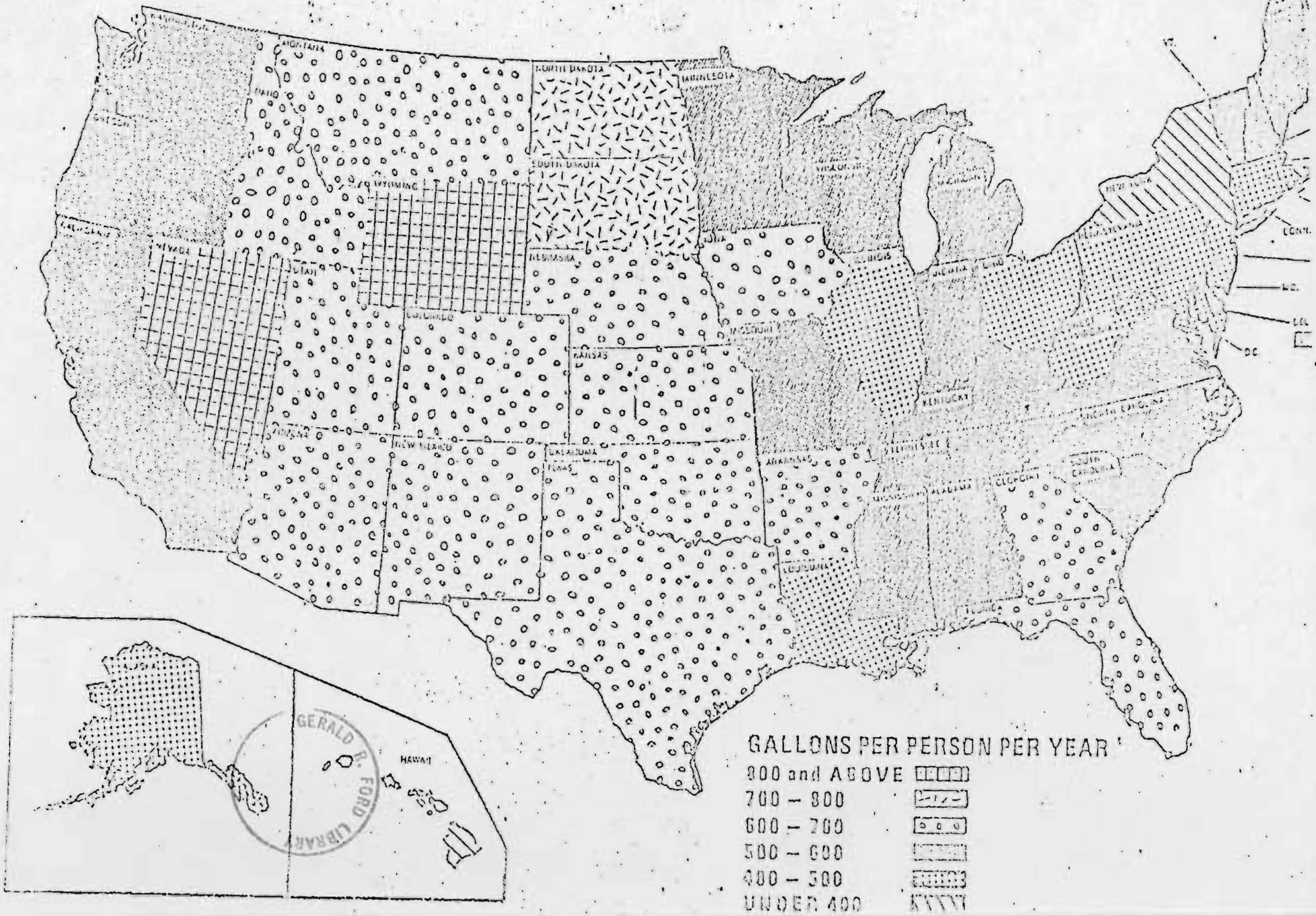
RECOMMENDATION

The ERC recommends that Option 3 be adopted to deal with special industry problems.

Federal Energy Administration

FIGURE 3

PER CAPITA GASOLINE CONSUMPTION 1973



FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 17, 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

SUBJECT: Energy Options for May 1

THROUGH: Rogers C.B. Morton

FROM: Frank G. Zarb

BACKGROUND

The foundation of the short-term energy program you proposed in your State of the Union Message is contained in the following goals and actions~~:~~

- Reduction of oil imports by 1 MMB/D in 1975 and 2 MMB/D in 1977.

- Immediate decontrol of old oil prices coupled with a windfall profits tax.

- Deregulation of new natural gas.

- Excise taxes and tariffs on oil and natural gas.

- Reliance upon the market forces to cause energy conservation.

The decontrol of oil prices and deregulation of natural gas are the most important elements of your short-term program.

Since the January message, there have been several developments that affect our energy policy. First, the continuing softness in the economy has reduced projected demand for energy in 1976 and 1977 (last quarter of 1975 demand will remain about as projected because of the tax cut stimulus). Nevertheless, import levels will continue to grow, although probably to about 7.5 MMB/D in 1977 (rather than 8.0 MMB/D previously forecast). These projections indicate that smaller excise taxes or tariffs could be used to achieve our goal of stemming rising vulnerability. Tab A contains an assessment of 1977 import levels in greater detail.

In addition to the changing economic forecasts, the Congress has enacted a tax cut bill which contains a much larger stimulus than that requested by the Administration. The bill also removes the depletion allowance for major oil companies and contains other provisions that can adversely affect domestic production. The effect of the depletion repeal is to add about $1.00 per barrel to the cost of producing old oil and over $2.00 per barrel to new oil.

When you announced a delay in the imposition of import fees for two months -- from March 1 to May 1 -- it was with the hope and stated goal that Congressional compromise could be achieved. It is now obvious that a full compromise cannot be reached in either House by that date. The most progress we could expect by late April in the House would be marked up bills in the Ways and Means Committee and House Interstate and Foreign Commerce Committee. In the Senate, with the exception of standby authorities, and perhaps a couple of conservation measures, it is unlikely that any bills will be reported out of Committee. It is also possible that we will have major problems with most of the legislation that will emerge.

CONGRESSIONAL ENERGY ACTION

Because the House is much further along, it is the content and status of their legislation which must be the basis for your decision on May 1.

In both the Ways and Means and Dingell Committees, the situation is very fluid and predicting the form of the final legislation they will report is very difficult. Nonetheless, there are several very positive signs as well as very troublesome proposals which are starting to emerge. Summarized below are the key elements on both sides.

Positive House Legislative Possibilities

- Many Ways and Means members support the use of the price mechanism as an important strategy for achieving conservation.

- Your administratively imposed tariff will not be rolled back, but the second dollar you requested in your permanent program may not be allowed.

- There is agreement by the Committee Chairmen in the need for decontrol, possibly as quickly as 3-4 years.

Undesirable House Legislative Possibilities

- There are many amendments by some House members to roll back the price of either controlled or uncontrolled oil which may be introduced.

- Quotas and allocation are still seriously being considered by some members of both Committees to achieve conservation.

- Auto efficiency excise taxes and gasoline taxes are still being favorably considered.

Generally the two Committee Chairmen would arrive at a position that the Administration could accept, but their more liberal Democratic colleagues who dominate the Committee are pushing them away from price effects, and towards more government controls and a slower phase in the program. Tab B explains the current status of the House legislation in more detail, although the next week of markups are likely to change this legislation substantially.

The Senate deliberations are less focused than the House. Senate Bill S.622, passed last week, started as standby authorities legislation and was amended to include mandatory conservation measures for residential or commercial lighting, private automobile use, and industrial energy use. It also sets a price ceiling for new oil at about $11.25 per barrel and a $7.50 ceiling on old oil produced with advanced recovery techniques. The effects of these ceilings is to establish a four-tier price system for oil.

Further, the Senate seems very likely to pass legislation placing further restrictions upon our ability to effect decontrol and may enact natural gas legislation to place a ceiling on new gas and to regulate intrastate gas for the first time.

OPTIONS

We will continue to work with the Ullman and Dingell Committees through April 25 to improve their pending legislation. Although communication is open, significant progress may not be made or the legislation may be locked into very objectionable directions. Therefore, action on May 1 may be needed.

There are really only two broad options available -- either a further extension of the May 1 deadline to allow conciliation and compromise or greater confrontation by taking further administrative actions.

Option 1. Postpone Imposition of Additional Import Fees and Decontrol

Postpone fees for one more month as evidence of movement towards compromise and to allow the House to report out and vote on their major bills.

PROS:

- Maintains deescalation of conflict and positive public posture.
- Avoids another round of counter-productive actions on veto override and possible loss of control over any energy legislation.
- Could be used as bargaining chip for prompt floor action and substantive modifications to the House legislation.
- The energy situation is not in the forefront of public perceptions and additional delay might not be viewed adversely.

CONS:

- We are still not close to compromise and further delay may give a false impression.
- Removes the impetus for action.
- Does not achieve conservation savings we desire.
- You have already set a deadline once for action, if you defer again, it could be viewed as lack of leadership.

Option 2. Take Additional Administrative Actions

There are essentially three major alternatives here -- either add the second dollar of tariffs, take some decontrol action, or do both. By moving forward administratively we can implement a major part of your legislative program. These actions, combined with the tax cut already enacted and only modest new legislation can yield most of the results of your omnibus energy bill.

Option 2a. Add the Second Step to the Import Fees

Add $1.00 to the fee on crude oil and $.60 on products as of May 1, 1975. This could be accompanied by a statement that the $3 fee will be postponed for three months.

PROS:

- Maintains some pressure for action and Presidential leadership.
- Only represents an additional 1.5¢ per gallon.
- Results in further conservation.
- Collects an additional $1.8 Billion annually in revenues.

CONS:

- Could divert the Congress from considering a permanent legislative package.
- Would require action on requests for exemptions from the fee.
- There is a likelihood of a swift Congressional rollback of your fees.

If you decide to proceed with this option, the vote on overriding your veto of the import fee restriction would occur very quickly and there is a good chance your veto would be sustained. Since the veto, the tax cut and removal of depletion allowance have been enacted, and the Middle East situation has deteriorated. Hence, the possibility of an override may be less. If the fee is increased, a number of decisions on exemptions or rebates that were put off in January should be made. These exemptions could gather support for sustaining your veto and should be announced simultaneously with imposition of the next fee increase. The following tabs briefly discuss the issues involved in deciding on any further exemptions to the import fee:

	Possible Action	Recommendation
Tab C:	Rebates for Nonprofit Institutions	No rebate
Tab D:	Modifications to the Previously Announced Farmer Rebate	No modification
Tab E:	Extension of the Farmer Rebate to Fishermen	Rebate
Tab F:	Gasoline Tilt	Postpone decision

Option 2b. Take Administrative Action to Decontrol Old Oil

In your State of the Union Message you announced that you would implement complete decontrol of old oil on April 1, 1975 and then delayed this one month along with the increased tariff. Given that the Congress has not enacted a windfall profits tax and recognizing the current state of the economy, complete and immediate decontrol is unwise. Further, it would be subject to a simple majority veto by either House within 5 days. The likelihood of such a veto is very great, unless parlimentary tactics are used to prevent a vote. As a consequence, phased decontrol is much more desirable and the recommended option is as follows:

- Provide new incentives for secondary and tertiary recovery by phasing out old oil controls in equal steps over the next two years, i.e., 25% of old oil decontrolled every 6 months. This would require FEA hearings prior to submission to Congress for the statutory 5 day review.

- Administratively raise the base price to $6.25 to compensate for increased costs for old oil due to the depletion allowance repeal and inflation. It is estimated that depletion repeal would represent a loss of $1.00 per barrel on old oil and over $2.00 per barrel on new oil.

It should be noted that either of these actions can be implemented separately, or they can be implemented sequentially if this has some strategic advantage. In any event about 4-6 weeks would be needed for the required FEA hearings, findings and implementation.

PROS:

- Begins major movement to decontrol.
- Provides new production incentives and compensates for adverse effect of depletion repeal.
- Provides some conservation effect.
- Substantially relieves FEA of litigation threat from unilateral action without Congressional review.
- Would let Congress acquiese to President's program.
- Part of program can be done without Congress chance for disapproval.
- Could improve chances of getting a reasonably rapid decontrol program from Dingell Committee.

CONS:

- Congress could block phased decontrol.
- The $1.00 per barrel increase could be viewed as attempt to circumvent Congressional intent on depletion repeal and is subject to court challenge.
- Provides additional revenues and windfalls to oil producers.

Option 2c. Implement Both Partial Decontrol and the Second Dollar of Import Fees on May 1

PROS:

- Carries through earlier promise to act if no compromise is reached by April.
- Provides strong conservation effect.

CONS: - Would result in certain confrontation.

- May raise consumer prices too much without any mechanism to rebate money.

Tab G provides more details on all the decontrol options considered.

RECOMMENDATION

The basic choice which we must make is whether to avoid confrontation or put additional pressure on the Congress. In general, the Congress is moving about as rapidly as we can reasonably expect. The problem we have is not with its speed, but with possibilities of direction. It is clear that there is still much sentiment in the Congress to not move for major savings in the early years and to reject the price mechanism in favor of greater government controls.

Proceeding with any option other than further deferral only heightens the differences, makes even marginal improvements in their program harder to achieve, and may result in a Democratic backlash and counter-productive legislation. On the other hand, if we feel that their program is not going to be productive, this might be the right time to attack it and force greater confrontation. Such action may mean that we would achieve little more than your administrative actions in this session of Congress (and maybe not even that if veto is overridden). But, compared to some alternatives, this may not be that bad.

The ERC recommends that you do not make any final decisions on these options until about April 25 and that you meet with the key minority members of the Congress and the key House Committees to inform them of your decision.

Unless good progress is made by April 25, that is we have a reasonable expectation that floor votes will occur within 30 days on Committee bills which we find acceptable, the ERC recommends Option 2c, the increase in tariffs and partial decontrol. If you agree we will begin to prepare the necessary paperwork to implement this decision by May 1.

CONCURRENCE

Treasury
CEA
OMB
FEA
Interior

TAB A

NEW ECONOMIC FORECAST

FEA's current short-term petroleum forecast, adjusted primarily for worsening economic conditions and the recent tax cut indicates a reduction in petroleum demand in 1977 when compared with the forecast prepared in December and used in the State of the Union Message.

The changing economic assumptions include a number of consumption and output indicators as well as updated estimates of the cumulative price effects. For example, real disposable income in 1958 dollars for the two forecasts is summarized as:

Disposable Income
(1958 dollars)

	Old Forecast	New Forecast	Percent Difference
1975	605.5	611.3	+1.0
1976	643.8	643.2	0.0
1977	672.5	678.6	+1.0

Forecasts of industrial production have been also revised as follows:

Federal Reserve Board Index
of Industrial Production
(1967 = 1.0)

	Old Forecast	New Forecast	Percent Difference
1975	1.290	1.125	-12.8
1976	1.348	1.194	-11.4
1977	1.439	1.318	- 8.4

The effect of the downward revision in the production estimates is larger than the effect of the slight increase in the disposable income forecast (due to the tax cut). The resulting reduction in 1977 demand is given below.

	1977 Consumption (MMB/D)	1977 Imports (MMB/D)
Base Case, State of the Union	18.3	8.0
Base Case, Latest Estimates	17.9	7.5

In summary, the slower economic recovery even with the tax cut will probably mean less vulnerability in 1977 by about 500 MMB/D. This has important implications:

-- It indicates that the import level we set as a goal by saving 2.0 MMB/D in 1977 could now be reached with a saving of about 1.5 MMB/D.

-- We could conceivably reduce the "bite" of our program as follows:

Measure	1977 Impact Before (MMB/D)	1977 Impact Now (MMB/D)
Elk Hills	0.3	0.3
Coal Conversion	0.2*	0.2*
Insulation Tax Credit and Auto Standards	0.3	0.3
Other Conservation Measures	1.2-1.3	0.7-0.8

---

* 0.2 MMB/D from coal conversion appears more realistic than previous estimates.

Thus, we could reduce the price effects by more than 1/3 and still achieve our results. This could form the basis for compromise, as we could accept lower fees and taxes while maintaining our objectives. For example, decontrol and a $1 per barrel import fee by 1977 could achieve our goals.

TAB B

SYNOPSIS OF HOUSE ENERGY LEGISLATION

House Ways & Means Committee (Ullman) Energy Bill

Title I -- Import Treatment of Oil

Quotas

- Imposes quantitative limitations on imports ranging from six million barrels per day in 1975 to five and a half million barrels per day in 1979 and thereafter.
- Import licensing system with entitlements distributed by sealed bid.
- Separate entitlements for small and independent refiners.
- Amendments to this section may add further exemptions and set aside for New England and other special interests.

Duties

- Specifies ad valorum duties on oil - two percent of the price of crude and five percent on product. This approach would work contrary to conservation goals by reducing import duties as world price lowers, rather than raise the fees.
- Further increase of duties (up to 10% ad valorum) must be submitted to Congress and would be effective after 60 days unless the Congress passed legislation to ban it.

Office of Petroleum Import Licensing and Purchasing

- Establishes a standby Federal Purchasing Agency which would have exclusive rights to purchase imported oil. Such an agency would always be under pressure to become operational.

Other Provisions

- Extends the Emergency Petroleum Allocation Act providing allocation on a regional hardship basis.

Title II - Gasoline Conservation Program

Gasoline Tax escalating from \$.07 per gallon in January 1976 to \$.37 in March 1980. An income tax credit would offset the tax on nine gallons a week. This provision is likely to be watered down to 5¢ per gallon, with discretion for additional 5-15¢ increase by the President.

Title III -- Other Energy Conservation Programs

- An auto fuel mileage efficiency tax is phased in over five years, starting at \$200 per year for cars getting less than 14 miles per gallon and increasing to \$1000 for cars getting less than 16 miles per gallon.
- Other excise taxes are imposed on auto air-conditioners, and repealed for radial tires.
- Tax credits up to \$300 (compared to \$150 proposed by Administration) would be allowed for home insulation, and up to \$600 on solar energy equipment.

Title IV -- Energy Conservation and Conversion Trust Fund

A trust fund is established from energy taxes (up to \$5 billion a year) and would be used to finance energy research and development.

Title V -- Windfall Profits Tax

Bills assume deregulation system from Dingell Committee; windfall profits tax is imposed and phased out over 16 2/3 years.

Title VII -- Excise Taxes on Industrial and Utility Use of Oil and Natural Gas

An excise tax on oil beginning at \$.11 per barrel and increases to \$.66; natural gas tax begins at \$.03 per mcf and increases \$.03 per year until \$.12. They do not apply to feedstocks or farm use.

House Commerce Subcommittee on Energy and Power
(Dingell) Energy Bill

Title II -- Standby Energy Authorities and National Strategic Petroleum Reserve

- Rationing and conservation plans may be implemented in an emergency only after they have been approved by each House within 60 days and such implementation has not been vetoed by either House within 15 days of the President's request for action. This could effectively tie the President's hands in an energy emergency.

- Strategic Reserve plan authorized, but any programmatic actions are subject to congressional disapproval (one House veto). Drawdowns of reserves are subject to similar congressional disapproval.

Title III -- Measures to Increase Energy Supplies

- Decontrol would be achieved through use of decline curves in existing fields. The minimum time for full decontrol would be 3 1/2 years; but could be as much as 5-6 years.

- Stripper well exemptions not applied to major oil companies.

- Controlled domestic crude price is pegged at $5.25 ceiling with no provision for adjustment.

- Regulatory authorities such as materials allocation, maximum efficiency rate production, and "due diligence" production provisions are contained within the federal leasing section.

Title IV -- Energy Conservations Measures

- Removes expiration date of Emergency Petroleum Allocation Act.

- Establishes a three-year mandatory gasoline conservation program of 2% a year reduction from 1972 base year. This program would result in shortages much worse than those experienced during past year's embargo. A rationing program would almost certainly be required.

- Suggests two alternative industry conservation programs:

  1. Establishes an energy consumption permit for industrial facilities, regulated by Federal energy efficiency standards.

2. Establishes a voluntary standard for industry energy conservation which includes public notification of violators.

Title V -- Improving Energy Efficiency of Consumer Products

- Provides rebates for purchase of energy efficient new cars that are domestically produced.

- Appliance labelling.

Title VI -- Conversion from Oil or Gas to Other Fuels

- Adopts provisions similar to the Administration's Energy Supply and Environmental Coordination Act. Amendments.

- Provides loan guarantees to low-sulphur coal mine operations.

- Allows switching from natural gas to petroleum in boilers.

TAB C

Tab C

CHARITABLE INSTITUTIONS

ISSUE: Should non-profit, charitable institutions be provided rebates for increased fuel costs due to the President's energy program?

BACKGROUND: The President's energy program provides for rebates of a portion of the increased fuel costs to corporate and individual taxpayers and individual non-taxpayers. However, many non-profit institutions do not receive rebates under the proposed system, and have indicated major problems in adjusting to higher fuel costs.

Section 501(c)(3), of the IRS code defines those organizations traditionally as charitable and public service oriented including:

Churches	329,000
Private Foundations	29,000
Private Secondary & Elementary Schools	18,000
Private Non-Profit Hospitals	3,500
Private Institutions of Higher Education	1,480

The Treasury Department is uncertain that a rebate system could legally include churches and institutions with religious affiliation. Rebates to private elementary and secondary schools would face legal and political difficulties. Thus, best judgments suggest that those non-profit institutions to be considered for energy cost rebates be limited to private institutions of higher education and private non-profit hospitals (approximately 5,000 firms).

Issue 1: What, if any, rebates should be provided to private colleges and universities and private non-profit hospitals?

Option 1. Provide no special relief for these institutions.

PRO:

- Hospitals quickly pass-on increased energy costs to individual recipients of health care by increasing prices and fees. Such increases are expected to be small since energy costs are typically a small percentage of total operating expenses.

- Colleges and universities can pass-on the increased costs to students, although with slightly greater difficulty than hospitals. However, a small sample indicates that all energy costs to colleges and universities constitute about two percent of all operating costs.

- Non-profit hospitals and colleges and universities are generally not exempted from other excise taxes, fees and tariffs.

- These institutions already receive considerable financial support from government health and education programs.

- Hospitals especially should be encouraged to reduce energy consumption through price increases since the existing petroleum allocations regulations grant them a special high priority, allowing 100 percent of current energy requirements, and thus at least partially insulate them from the effects of petroleum shortfalls.

<u>CON</u>:

- These organizations may be able to generate considerable pressure for rebates, since the increase in costs of health care and education could disproportionately impact the poor and other economically and socially disadvantaged groups.

- Some of these organizations which have had rapid fee increases in the past several years may have difficulty with additional cost pass-throughs.

<u>Option 2</u>. Provide rebates only for increased fuel costs to private colleges and universities. The rebates could be phased-out over 3-4 years.

<u>PRO</u>:

- Constitutional, legal, and administrative problems would be minimized since these institutions currently receive various forms of federal assistance.

- This policy would be consistent with the government's policy of subsidizing these institutions through tax relief.

- Private non-profit hospitals would be excluded on the grounds that they could quickly recover increased fuel costs.

CON: - The Administration funds higher education through grants, and loans to needy students, not through general institutional support.

- Would set a precedent for the granting of relief to non-profit organizations.

If a rebate is granted, it could cover all fuel cost increases on fuel consumed only for heating purposes. Most of the concern expressed by these institutions is for heating fuel price increases, but such a rebate would be difficult to administer if electricity is included (electricity is used for many other purposes).

RECOMMENDATION: The ERC recommends Option 1 -- provide no special relief for private colleges, universities, and hospitals. If this is not feasible, provide cash rebates to private colleges and universities up to 75 percent in the first year for fuel costs attributed to the energy program and phase-out over four years. The rebates should be for increased costs in heating fuel purchases only, excluding electricity, and based on actual usage.

TAB D

Tab D

FARMERS

ISSUE: Should the rebate to farmers for increased fuel costs be limited to $1,000.

BACKGROUND: Considerable opposition has developed to remove the $1,000 limit and to provide rebates to all farmers. The Administration had previously indicated its intention to propose in the tax legislation a program providing for a 10¢ fuel. The proposal limited the total rebate to $1,000 annually (assuming no gasoline tilt).

The current plan is to offer parts of our tax legislation as amendments to the Ways and Means Committee's energy tax proposals. The Ways and Means draft bill contains a provision for providing full rebates to farmers for the increased costs for gasoline used for farming purposes.

The intent of the proposed rebate scheme was to provide relief from increased energy costs to the small farmer.

At present there are about 2,850,000 farms in the U.S. On the average, it takes between 12-14 gallons of gasoline and diesel to service one acre per year. With a rebate of 10¢ per gallon on gasoline and diesel, farms ranging from about 715 acres to 830 acres would receive a rebate of 100% of their increased energy costs. The $1,000 cutoff would thus encompass farms with sales of about $50,000 to $75,000 per year. Less than 250,000 farms would be impacted by a $1,000 maximum rebate, although these farms account for more than 50 percent of the total cash receipts.

OPTIONS:

Option 1: Maintain the $1,000 limit.

PRO:
- Would result in about a $330 million revenue loss for the first year with a phase-out over three years.
- Would provide full rebates for increased diesel and gasoline costs to about 95% of all farmers (about $100,000 a year or more in sales).

CON:
- Arbitrarily cuts off rebate at $1,000 and could be counter productive to increasing farm output.
- Has drawn opposition in farm states.

Option 2: Provide all farmers with rebates for all increased gasoline and diesel costs.

PRO: - Removes artificial break point.

CON: - Would approximately double revenue loss - $650 million.

- May provide help for large farmers who can benefit from corporate tax cuts.

RECOMMENDATION: Support Option 1 in negotiations on energy tax bill. Energy costs comprise about 3% of total farm production costs. Increased energy costs will increase total farm production costs by about one percent in 1975. This then indicates that farming is less energy-intensive than many other industries.

The intent of the rebate scheme is to provide relief to the small farmer not to the large or corporate farmer. The small farmer is more adversely affected by increased energy costs. He does not have the storage capacity of large farms and cannot take advantage of volume discounts. In addition, the small farmer is less able ~~to~~ use his equipment as efficiently as large farmers.

TAB E

FISHING INDUSTRY

Tab E

ISSUE: Should the marine fishing industry be given fuel rebates to compensate for the costs of excise taxes on fuel.

BACKGROUND: The various segments of the marine fishing industry are in direct competition with agriculture and contend that their treatment with respect to fuel tax rebates should be similar to agriculture.

OPTIONS:

Option 1. Do not provide a fuel rebate for fishing.

PRO:

- Promotes efficient use of fuel and reduces the likelihood of further pleas for exemptions by other industries.

CON:

- Places fishing industry at an increasing economic disadvantage vis-a-vis agriculture.
- Risks political opposition from a large number of states where the Administration's program now has support.

Option 2. Provide rebates to all fishing craft.

PRO:

- Provides equity with agriculture and would be politically popular and relatively simple to administer.
- We have always treated the fishing industry similarly to farming in our allocation program.

CON:

- Reduces the effectiveness of the energy program and would increase pressure from other industries for rebates.

Option 3. Rebates only to boats of 5 net tons or less (est. 71,000 boats).

PRO:

- Would restrict rebates to the really small family operated lobster, crabbing and small fishing entrepreneurs who are mostly low income subsistence types including the Indians and Eskimos in the West Coast salmon industry.

- Might be particularly appropriate if most of energy program costs are loaded on gasoline, because small boats ordinarily use gasoline for fuel.

CON:

- Would exclude most of the Gulf shrimp industry and all of the larger commercial operations which are politically the most active and influential.
- Would subject a large share of the commercial value of fisheries production to added fuel costs resulting in smaller production, higher prices and a worsened competitive position for the fisheries industries vis-a-vis agriculture.

ANALYSIS:

Fuel accounts for about 3 percent of production costs for agricultural production versus 6 to 25 percent or more for fishing and shellfishing activities. Thus, the very considerable increases in fuel costs since the Arab embargo (50-70 percent) have had a greater adverse effect on the costs and competitive position of the fishing industry than on agriculture. Fish and shellfish must compete directly with meat, poultry and other agricultural protein food products for the consumers food dollar.

The proposed increase in fuel costs which would result from the President's energy program would have a greater impact on fishing than on agriculture, because any given increase in fuel prices affects heavy users more than light users. For efficient allocation of resources, the full costs of seafood, as well as other products, should be reflected in its price, but the added impact of an excise tax would raise the price of seafood substantially more than it would raise meat prices.

RECOMMENDATION:

Adopt Option 2, rebates to all fishing craft if rebates are given to farmers or other industries. This option would provide the fisheries industry with economic equity with agriculture and avoid administratively and politically difficult task of trying to divide the industry into separate segments deserving of rebates and undeserving of rebates.

The fishing industry uses an estimated 250-280 million gallons of gasoline. Thus, assuming a gasoline tilt and \$2.00 per barrel import fee, the total cost to the Treasury for Option 2 would be \$10-15 million. If a rebate is given under the full Administration program (10¢/gallon), the costs would be about \$30-35 million.

TAB F

GASOLINE TILT

ISSUE: Should be adopt the gasoline tilt previously announced?

BACKGROUND: The Administration has publicly committed itself to a modification of the import fee program through the application of a gasoline tilt. The currently proposed FEA regulations would modify current regulations to restrict to less than a volumetrically proportionate share, the cost increases which could be allocated among products other than gasoline, in order to place a heavier burden on gasoline. The amount of cost increases remaining for allocation to products other than gasoline will, however, maintain incentives for conservation of other products.

The effect of the $1.00 administratively imposed import fee would be to increase prices of all products by about 1.4 cents per gallon. The gasoline tilt would modify this as follows:

	Current Program (¢/gallon)	Proposed Gasoline Tilt (¢/gallon)
Increase in gasoline	1.4	2.0
Increase in other products	1.4	0.9

With a $2.00 import fee, the average price increase without a tilt would be 2.8¢ per gallon; a tilt would modify this to 4.0¢/gallon on gasoline and 1.8¢ on other products.

The gasoline tilt accomplishes the following objectives:

- Maximizes demand reduction on gasoline which seems to be regarded as the least essential area of consumption.
- Reduces burden of increased fuel costs on industrial consumers, airlines, and users of electricity and heating oil.
- Reduces indirect consumer costs (ripple effects).
- Reduces the overall effects on the East and West Coasts.

The gasoline tilt also disproportionately impacts regions of the country more dependent upon gasoline (such as the Mountain, Midwest, and Southwest). Its greatest impact would be on the leisure and automobile industries.

As a result of the tilt, product import fees for fuels other than gasoline would have to be adjusted to preserve current cost relationships between domestic and foreign products. For example, if a short-term tilt of 4¢/1.8¢ is implemented, the import fees should be adjusted as follows:

$2.00 on crude oil
$2.00 on gasoline
$0.35 on other products -- primarily heating oil and residual oil.

The proposed gasoline tilt regulations have drawn considerable criticism from the groups that will be adversely affected, while gaining little support from groups it was intended to help. These latter groups, such as utilities and airlines, feel that the gasoline tilt does not go far enough.

TAB G

DECONTROL

ISSUE: Technical Adjustments to Crude Oil Pricing Regulations

BACKGROUND: The two-tier pricing system was established in 1973 by the Cost of Living Council for the purpose of stimulating production of domestic oil. In particular, it provides incentives for secondary production by allowing each "new" barrel from an existing field to release an "old" barrel from price controls. Nevertheless, declining production in existing fields has eroded the level of old oil compared to the 1972 base period from which new production is measured. At present, about 60 percent of domestic production is under price controls, and the average price for all domestic crude oil is $7.25 per barrel and for imported oil is $12.00 per barrel. Thus, the average price for all oil is about $9.20 per barrel.

In December, 1973, the Cost of Living Council permitted old oil to rise one dollar to approximately $5.25/bbl. This increase caused considerable controversy and no further increases have occurred. Court action is currently challenging our authority to have adopted this increase and litigation is also pending regarding fundamental aspects of crude oil price controls and structure of the two-tier pricing system.

Under the Emergency Petroleum Allocation Act, all major changes in price controls must be submitted to the Congress for possible override by majority rule in either House within five days. With the current Congressional opposition to higher prices, it is very likely that Congressional disapproval would be swift.

The law does allow for administrative change without Congressional approval if cost increases can be justified. The recent appeal of depletion allowance, declining production from existing fields, or inflation could conceivably justify changes in the regulations. If administrative actions are taken, Congressional disapproval could only occur through passage of new legislation and override of a Presidential veto (2/3 vote needed). However, litigation by consumer groups is almost certain if such steps proceed.

OPTIONS

There are three primary options available to modify current pricing regulations to recognize changing economic conditions. The first involves working with the Congress to develop a regulatory strategy which would be aimed at decontrol, while the second may be implemented administratively.

Option 1. Submit a decontrol plan for Congressional approval.

PROS:

- Involves the Congress in the decision making process.
- Mitigates possible ambiguities with respect to the intent of the law.
- If submitted as a phased plan, could result in Congressional agreement with the entire decontrol strategy, and make future price changes easier to implement.

CONS:

- Decontrol is unlikely to be accepted due to the majority override provision.

Option 2. Take administrative action to begin decontrol process.

There are several ways in which administrative action could be taken to implement partial decontrol:

Sub-Option A. Reduction of Base Period Production Levels to Adjust for Declining Production.

Oil fields reach their peak production levels shortly after development is complete and then, as pressure is reduced, gradually decline in recovery (at a fairly constant rate) for the remainder of the life of the field. The decline rate varies from field to field according to geology and other technical factors, but generally lies within the range of 6% to 16% per year. Thus, a well which produced 100 barrels per day in 1972 might produce only 88 barrels per day in 1973 and 68.1 in 1975. In light of the two-tier pricing system, it becomes increasingly difficult to surpass 1972 production levels as time goes on. The introduction of secondary or tertiary recovery provides only a temporary respite from this problem, as decline soon resumes after the new peak is reached. Under this option, the base period production level would be reduced by about 12% per year from 1972. Including released oil in this proposal would enable total decontrol to be achieved sooner and would provide a greater incentive for enhanced recovery.

PROS:

- Will provide incentives for improvements such as workovers or enhanced recovery which would otherwise be uneconomical.
- Provides a vehicle for phased decontrol.

CONS:

- Could lead to litigation from consumer groups or an unfavorable Congressional reaction.
- The exact extent of the adjustment should be unique to each reservoir and would be extremely difficult to establish in a general and universally equitable fashion.

Sub-Option B. Restoration of Production Incentives Reduced by Repeal of Depletion Allowance.

The removal of the depletion allowance could have serious implications in terms of production incentives, especially for old oil producers. Specifically, 22% of previously excluded production revenues will become subject to income taxes. In the case of old oil, this amounts to about $1.15 per barrel of additional taxable income ($5.25 x .22) and an additional tax liability of $.55 per barrel at the corporate tax rate of 48%. Although many large producers had extensive write-offs and deductions to reduce the effective tax rate below 48%, the impact of depletion repeal will nevertheless directly add to taxable income. This liability may be reduced slightly by application of "cost" depletion allowance. This loss of income could be about offset by allowing an increase of $1.00 per barrel in the ceiling price of old oil.

PROS:

- Adequately protects old oil producers from loss of income due to repeal of percentage depletion.
- Does not create excessive windfalls.

CONS:

- May result in litigation from consumer groups in Congressional action.
- May not sufficiently dampen the incentive to import crude oil at the expense of new oil production. There would be a loss of about $2.00 per barrel in the revenues from sale of new or released oil due to the depletion allowance repeal.

Sub-Option C. Vary Distribution of Old, New and Released Crude Oil as a Function of Increased Operating Costs.

Crude oil price controls have not compensated for increased operating costs during the past year. Operating costs are particularly important with respect to properties which produce primarily old oil. This is because production and per barrel operating costs tend to vary inversely. It may not be feasible to perform a badly needed well workover or similar maintenance, if the resulting incremental production is controlled at the old price. Under this option, the quantity of oil that can be sold at uncontrolled prices would be increased for each producer to compensate for increased operating costs.

PROS:

- Would permit producers to recover incremental costs of actions designed to maintain or increase levels of production.
- Provides incentive to marginal properties whose production is primarily old oil.

CONS:

- Since major oil companies produce the bulk of the old oil, this could be viewed as a concession to them. It may be mitigated, however, since they are required to pass a profit margin test prior to implementing cost adjustments which are not directly related to the increased cost of crude oil or purchased product.
- Could be administratively complex as a result of the number of producers who could potentially take advantage of the provision.

RECOMMENDATION: With the current mood and track record of the Congress, it is unlikely that we would be successful in gaining their approval of any measures which could be viewed as a step toward decontrol and a return to the free market system. Consequently, the administrative method is suggested in order to implement some long overdue regulatory changes. Ideally, all three of the administrative modifications would be implemented. However, if forced to establish priorities they would be:

1. Production decline adjustment
2. Increase price of old oil by $1.00 per barrel
3. Cost pass-through provision

If the first two actions are taken, price controls would be effectively removed by 1979 and the average price of oil would increase to $8.91 per barrel in 1975. (Table 1 shows the percentage of oil under controls and average price each year under these two options.)

HISTORICAL AND PROJECTED CONTROLLED OIL RATIONS
(thousands of bbls/day)

	CONTROLLED OIL	%	UNCONTROLLED OIL	%	TOTAL PRODUCTION	WEIGHTED AVG. DOM. PRICE
72	9480	100	----	0	9480	----
73	6630	72	2580	28	9210	$ 6.86
74	5545	63	3260	37	8805	7.38
75	4645	54	3955	46	8600	8.17
76	3770	44	4730	56	8500	8.91
77	2540	30	5860	70	8400	9.58
78	1310	14	8090	86	9400+	10.34
79	----	+0	9800	100	9800	11.00
80	----	0	10,200	100	10,200	11.00

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FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 21, 1975

OFFICE OF THE ADMINISTRATOR

DECLASSIFIED
AUTHORITY RAC NLG-MISC-COLL-ZARB-10-8-1-1 5/5/08
BY [illegible] NARA, DATE 8/14/09

MEMORANDUM TO THE PRESIDENT

FROM : FRANK ZARB

SUBJECT: INTERNATIONAL ENERGY DEVELOPMENTS

I'd like to supplement the international information in the Bi-weekly Report with some later developments.

<u>Soviet Energy Exploration Activity</u>

Although it was believed that Moscow was not interested in U.S. commercial financing other than long-term, Tokyo has announced, on April 15, that U.S. banks, including the Bank of America, have agreed to provide $100 million in credits for the Yakutsh gas exploration project. A Soviet team will be in the U.S. in the near future to negotiate the terms.

French interest in cooperative arrangements for offshore exploration in the Barents Sea has waned since the Soviets suggested that they wanted to operate equipment to be supplied by the French. Moscow probably wants to keep the Barents Sea, an important Soviet submarine route, clear of Westerners.

<u>Soviet Nuclear Energy Initiatives</u>

Iran and Moscow have agreed to discuss atomic power plant construction in Iran, but not matters such as uranium separation and concentration on which Iran has agreements with the French. Also, the Soviet Atomic Energy Committee should be signing a five-year protocol this summer for collaboration with the European Organization for Nuclear Research.

<u>Other Developments</u>

- In 1974 Peking purchased ten times more working vessels than the year before (100 ships). Japanese firms have reportedly made offers to supply a large variety of oil-related vessels.

- The U.S.-based Sun Marine Drilling Company, the only serious bidder right now, is confident that Sri Lanha will award it the rights for offshore exploratory drilling.

- Trinidad's government announced that it will take over Texaco's marketing operations in Trinidad. Trinidad does not seek to nationalize the company's refinery, but to allow continued operation under a "new relationship."

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4/22/75

MEMORANDUM FOR THE PRESIDENT

FROM: Frank G. Zarb /S/

THRU: Rogers C. B. Morton

SUBJECT: OPEC Countries: Tanker Fleet Expansion

BACKGROUND

You asked us to monitor the activities of OPEC countries in the international tanker market. The following is a preliminary report.

PROBLEM

The international tanker market is severely depressed -- prices for charter are the lowest since the end of World War II. Owners of distressed tonnage are attempting to sell.

OPEC member states are the logical purchasers for these tankers. Saudi Arabia, Algeria, Venezuela, Kuwait, and Libya all either have developed or are developing cargo preference laws. Because of those laws, these countries are in a position to buy distressed tanker tonnage and immediately put it to use.

The market dynamic is such that OPEC countries could in the near future find themselves owning a substantial portion of the international tanker fleet. There is no evidence of an OPEC tanker strategy. The motivation of individual countries appears to be commercial.

After acquiring the tankers, however, OPEC countries could use their fleets to control physical flows of petroleum exports; this would give them the capability of targeting future embargoes with precision.

IEA:JWilhelm/ljb/4-16-75

During the 1967 Suez Crisis, the international oil companies estimated that control of 10 percent of the international fleet would have been sufficient to effectively control the international petroleum transportation system. Because of the current surpluses, somewhat more tonnage may be required today -- but the rough order of magnitude appears to remain accurate.

CIA estimates that 8 percent of the 1980 world tanker fleet would cost $4-6 billion. Such funding is easily within the range of the OPEC member countries. FEA believes that the tonnage could be brought under OPEC flag control with far more modest expenditures.

RECOMMENDATION

The Energy Resources Council working with the EPB will analyze these issues further, and present findings and recommendations to you in 60 days.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

OFFICE OF THE ADMINISTRATOR

April 24, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: FRANK G. ZARB

SUBJECT: SETTLEMENT OF THE ANTHRACITE STRIKE

The Anthracite Strike was settled last night. Production could resume before May 5, although ratification is still required by the union membership.

We do not anticipate coal supply problems before production resumes.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

APR 25 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

FROM: Frank G. Zarb

SUBJECT: Oil Imports

The effect of the Arab embargo in the winter of 1973/1974 and the economic slowdown we experienced in the latter part of 1974 and early 1975 have distorted actual imported oil levels. This memorandum briefly summarizes the key trends.

Historical and Projected Imports (Millions B/D)

	1972	1973	1974	1975	1977
Jan.-March	4.8	6.1	5.2	6.2	
April-June	4.3	5.7	6.2	5.6*	
July-Sept.	4.4	6.2	6.2	5.6*	
Oct.-Dec.	5.2	6.3	6.7	6.7*	
Total Year	4.7	6.1	6.1	6.0**	7.5

* Estimated
**More recent revisions that account for the stimulus of the tax cut adjust this figure to 6.3.

There are several historical patterns to note.

- Imports typically are highest during the winter and drop appreciably during the mid year, as can be seen from the 1972 data.

- The pattern in 4th quarter of 1973 and 1st quarter of 1974 was disrupted by the embargo with resulting lower imports.

- In 1975 1st quarter imports were lower than expected due to weather and the economic slowdown, but are still running above last year due to the embargo.

Projections through 1975 and Beyond

- Through the summer imports will continue to decline following normal seasonal trends.

- By early fall, imports will rise following normal trends of inventory build up.

- With a growing economy in late summer, imports should rise to about 6.7 MMB/D during the last three months of 1975 and peak this winter at an all time high of up to 7.0 MMB/D.

- The yearly average for 1975 will be 6.3 and by 1977 this will rise to about 7.5 MMB/D.

Energy Policy Implications

When discussing these numbers publicly, I would suggest you make the following points.

- While imports are declining now, with the upturn in the economy they will be at all-time highs by year end.

- Even if the Middle East situation was resolved and the chance of an embargo was minimal, increasing dependence would make us vulnerable to further price increases by the Arab nations.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 28, 1975

OFFICE OF THE ADMINISTRATOR

MEMORANDUM FOR THE PRESIDENT

SUBJECT: Energy Options for May 1

FROM: Frank G. Zarb

THRU: Rogers C. B. Morton

STATUS OF NEGOTIATIONS

Since our meeting last week, we have vigorously pursued our negotiations with Congressmen Ullman and Dingell in an effort to reach agreement on basic differences. Both chairmen have been receptive to our concerns and the May 1 deadline and are proceeding in some favorable directions. At the same time, neither chairman seems to have complete control over his committee, overall progress is slow, and significant differences in approach still persist. The situation in each committee is briefly summarized in the following:

Ways and Means

The committee is moving towards a bill that will rely primarily on price effects and market forces to achieve our conservation goals. It is likely that the price effects will be approximately equal to the $2.00 tax fee in our program, but applied in a selective manner and phased in over a longer period of time. Specific provisions include:

- $1.00 per barrel import fee or 10% of the value of imported crude oil, whichever is higher.
- A lower fee for imported products (1/2 the crude oil rate for two years). Although we have argued for a higher fee for imported products to protect and stimulate domestic refining capacity, the committee's approach is a concession to the Northeast.

- An ad valorem tax on new autos, starting in 1976, based on auto fuel efficiency. The tax, which would be between 2-10% in 1977 and rise to 16% in 1980, has strong support in the committee and is viewed by the chairman as being popular throughout the House.

- A gasoline tax of an as yet undetermined amount. The tax is likely to start low in 1976 and rise to the 20¢ level in 1980.

- An industrial fuels tax that rises to $1.00 per barrel over a several year period.

In addition to these market mechanisms, the committee strongly favors the establishment of an import quota system to assure that domestic conservation savings result in reductions in imports and a standby Federal petroleum import purchasing authority. Although our efforts to delete these provisions to date have not been successful, primarily because the chairmen believe that these provisions will have to be included in any legislation that is to be successful in the House, we have been successful in convincing the committee to render the provisions essentially harmless.

Commerce Committee

Progress in the Commerce Committee is much slower and the conceptual directions much less favorable than in Ways and Means. Several important issues have been put off until next week or later, including decontrol of old oil, emergency storage and coal conversion. Although there is a general commitment to decontrol, any decontrol provision from this committee is likely to be phased in over a several year period (e.g. 3-5) and there are disturbing amendments that would roll back the price of new oil as part of any phased decontrol scheme. To date, the Committee has agreed on the following provisions:

- Establishment of a fixed level of consumption of gasoline at 98 percent of comparable months in 1973-1974. Although some Presidential discretion is allowed, this allocation approach could be large enough to result in noticeable physical shortages.

- Standby emergency authorities that require submission of contingency plans to the Congress for approval prior to their implementation.

Action in the Senate remains slow and is tending towards multi-tier crude oil pricing systems and reductions in new oil prices. Active consideration is also being given towards price ceilings on all new natural gas, including the intrastate market which is now unregulated. Unrealistic, mandatory conservation programs are also being considered.

OPTIONS FOR MAY 1 ACTION

Of the basic options regarding the May 1st deadline for the 60 days you provided Congress to develop an energy package, three appear to merit primary consideration:

- impose the second dollar on the import fee,
- take steps towards decontrol, or
- do both.

OPTION 1: Impose the second dollar of the import fee.

Unless the national security proclamation is further amended before May 1, the import fee will rise to $2.00 per barrel on crude oil and $.60 per barrel on products. This action will result in an immediate attempt to override your veto of legislation prohibiting any increase in fees after January 15, 1975. If the veto is not sustained, you will not be able to increase import fees for 90 days, the $1.00 already in existence will be rescinded, and our strength for the rest of the program could be eroded.

If, on the other hand, the veto is sustained, it would be a clear sign of strength and a ratification, however narrow, of the market approach to our energy problems. It is our judgment that the veto could be sustained by a slim margin if an all-out effort is launched, but it could go either way.

Imposition of the second dollar will place additional pressure on Ullman and possibly give the impression that the Administration is not happy with his progress to date or the direction of the Committee's bill, even though the Committee:

- is farther along than any other in the Congress,

- has agreed to let us keep the $1.00 now in effect,
- is moving toward other price mechanisms that would be comparable to your program in both magnitude and philosophy if not in specific application, and
- is likely to produce legislation that has perhaps the highest degree of probability of being acceptable to both the House and the Administration.

In spite of this signal, however, Ullman would be in a position to push his bill as a response to your action, arguing that his bill would effectively roll-back the second dollar while enacting other positive provisions. He might see this as a better response than a negative action to simply negate the second dollar by pushing for an override of the vetoed bill that would suspend your tariff authority for 90 days.

A decision not to impose the second dollar would express general satisfaction with Ullman's efforts, give him additional time to produce a bill, and avoid strong moves/pressures from the New England delegation. At the same time, the viability of one of our major action-forcing levers would be seriously undermined. Failure to impose the second dollar now in the face of a poor performance by the Congress might be an indication of the fact that we do not intend to use it in the future.

OPTION 2: Initiate decontrol procedures.

Under this option, the second dollar would be held in abeyance for an unspecified period of time (an always present threat if the Congress doesn't move) and a phased decontrol plan would be submitted to the Congress within 15 days (to allow for 10 days of public hearings) for its 5 day period to approve or disapprove such a plan. The phased plan, which would be a two year program designed to remove 1/4 of old oil from control every six months, would be comparable in approach if slightly faster in speed, than the approaches that have some support in the Commerce Committee.

Although this action could result in punitive legislation, it is a further compromise from your original proposal of immediate decontrol, it places us on a firm decontrol schedule if successful, and has considerable chances of being viewed as an acceptable solution by the Congress, particularly since it can be construed as an action by the President. As one of the most critical pieces of your entire legislative program, a move on decontrol while holding the second dollar might enhance the chances for the decontrol plan to be approved. The New England delegation, at least, would not actively oppose the plan.

OPTION 3: Impose the second dollar and initiate decontrol proceedings.

This action which combines the basic advantages and disadvantages, opportunities and pitfalls, of options 1 and 2, would be a strong move by the Administration to re-energize the entire Congress on energy legislation.

The basic arguments for this option are two-fold:

- Although Ullman is making some progress, his legislation faces many steps and obstacles before final Congressional action. The likelihood of action on his bill and others by the Congress is remote over the next several months, and the chances of legislation highly objectionable to the Administration are good if we do not maintain a show of strength.

- If successful, this option would represent 90% of the economic components of your energy program, even though achieved in a less efficient manner. All that would essentially be lacking is a windfall profits tax.

The basic problems with this action center in its magnitude and force. Prospects for negative legislation, particularly on the tariff, are higher for this option than options 1 or 2.

RECOMMENDATION

Given the lack of progress by the Congress to date, the need for maximum pressure to keep the Congress from trying to avoid the tough decisions required by the nation's energy situation, and the problems being generated by continued controls on old oil, the ERC recommends that the following actions proceed on May 1:

- Announce the imposition of the second dollar if we are reasonably certain of being able to sustain your veto;

- Initiate decontrol proceedings.

If we cannot sustain the veto, then the ERC would recommend the second option - decontrol with an indefinite hold on the second dollar.

The ERC further recommends the following sequence of events leading up to the announcement of your decision:

1. Monday afternoon - President meets with advisers; no final decisions are made, and public statements indicate only that the President has met with his advisers to review the options.

2. Wednesday morning - President meets first with Republican leadership to inform them of his decision, and then with Ullman and Dingell, separately if option 3, together if option 2.

3. Wednesday afternoon - Public announcement of decision.

4. Thursday - Press briefing by President or by Zarb.

FEDERAL ENERGY ADMINISTRATION
WASHINGTON, D.C. 20461

April 29, 1975

OFFICE OF THE ADMINISTRATOR

MEETING WITH REPUBLICAN LEADERSHIP

Wednesday, April 30, 1975
11:45 A.M.
Cabinet Room

From: Frank G. Zarb

I. PURPOSE

To discuss with the Republican leadership your May 1 energy decisions.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

A. Background: On May 1 your decisions on increasing the import fees on petroleum and administratively decontrolling old oil will be announced. The Republican leadership have been invited to discuss the current legislative status and your options.

B. Participants: Senators Scott, Griffin, Curtis, Stafford, Tower, Stevens, Young, Fannin; Congressmen Michel, Anderson, Devine, Edwards, Conable, Frey, Quillen, Vander Jagt, Cederberg, Brown, Schneebeli; N. Rockefeller, D. Rumsfeld, P. Buchen, R. Nessen, F. Zarb, W. Seidman, A. Greenspan, J. Lynn, R. Morton, J. Marsh, R. Hartmann, M. Friedersdorf, V. Loen, W. Kendall, D. Bennett.

C. Press Plan: None at this time.

III. TALKING POINTS

1. As you know, tomorrow I must make my decision on the second dollar import tariff and my administrative decontrol plan.

2. I would like to review with you my assessment of the Congressional situation and then get your views on my alternatives.

3. There has been significant Congressional progress during the last 2 months, but obviously much less than I had hoped for.

4. On the House side both the Ways and Means Committee and the Commerce Committee have come a long way towards recognizing decontrol of prices and the use of market forces to increase supply and cut energy demand. Nonetheless, there are still many very counter-productive amendments being considered and a long way to go before any legislation is on my desk.

5. Frankly, action in the Senate has been even more disappointing and the mandatory conservation sections of S.622 are particularly burdensome, ineffective and would have unforeseen economic consequences.

6. I would like your views on the situation, what you see happening in the weeks ahead, and your assessment of Congressional reaction should I proceed on the import fees or administrative decontrol.