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THE FEDERAL ENERGY ADMINISTRATION
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REMARKS OF THE HONORABLE FRANK G. ZARB
ADMINISTRATOR, FEDERAL ENERGY ADMINISTRATION
BEFORE THE

NATIONAL EXECUTIVE CONFERENCE OF WASHINGTON
THE DOLLY MADISON ROOM
MADISON HOTEL
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"Energy and the Economy" -- the subject of this conference -- couldn't be more appropriate. Certainly, it's the topic of the year; probably the topic of the decade; and, quite possibly, in an evolving form, the topic for the last quarter of the Twentieth Century.

And, certainly, energy and the economy, have dominated agendas in corporate boardrooms throughout the country over the past year. You know far better than I the extent to which executives who used to worry about the problems of marketing soap or streamlining an R&D operation, have had to become instant experts on petrodollars, natural gas and the Outer Continental Shelf.

The vastness and complexity of the subject matter could keep us talking for days, weeks and years. But none of us has that kind of time. So, for the next fifteen or twenty minutes, I would like to limit myself to one -- admittedly broad -- aspect of the energy problem that probably deserves more discussion than it has received: specifically, the prospect of increasing government regulation in the energy sectors of the economy.

Of course, government activity in the energy marketplace isn't a new idea by any means.

During World War II, for example, the Federal Government came into the marketplace as a regulator of an entire segment of an energy industry. It established a rationing program for allocating and distributing every gallon of gasoline consumed by private businesses or private citizens.

Then, a few years later in 1946, the Government created the Atomic Energy Commission, which has been directly involved in the research, development, manufacture, operation and regulation of nuclear powerplants and all atomic energy projects since that time.

Each of these examples of direct government involvement in energy was limited in a way that set it apart from other, more pervasive government involvement in other areas of the economy.

Gasoline rationing was an offspring of World War II and the temporary need to allocate short supplies of gasoline. Its temporary nature brought it to a close after 38 months. The Atomic Energy Commission was an offspring of the atom bomb and the need to safeguard classified information. And, although its special mission continues today, its influence in the private sector of the electric utilities has been limited primarily to assuring safe use of potentially dangerous materials.

Of course, direct government involvement in energy hasn't always been so circumscribed. During the 1930's it entered the marketplace, not just as a regulator, but as an actual or prospective competitor, with the creation of the Tennessee Valley Authority. The TVA -- by its lights -- has prospered; it now produces electric power from 29 dams and 12 coal-fired power-plants to supply some two million customers in seven states. TVA's critics -- including environmentalists who claim its plants are responsible for more than half of the sulphur dioxide pollutants in the Southeast -- are not exactly delighted with its growth. As one commentator recently put it: "TVA, once the shining dream of idealistic reformers, will stand as a premier example of why Americans have become so disillusioned with bigness in government and business."

Now, as Administrator of the federal government's biggest energy agency, perhaps I shouldn't be citing quotes like that one.

But I do think that I can come into court with clean hands -- because my basic philosophy, and that of the President, is that the marketplace, not the government, is the best regulator of our economic affairs. Yes, the FEA is big. Yes, it has broad powers. Yes, it has, is and will continue to regulate.

I said that rationing in the early '40's was the offspring of the War and that the AEC was born with the atom bomb. Similarly, the FEA is the fall-out of the energy crisis. Each of these intrusions of the government into the marketplace were justified by the events that surrounded their creation. In times of war, in matters of national security, in circumstances of grave economic dislocation, the government <u>must</u> step in.

But the goal -- which we seem to have so much trouble achieving -- should be to minimize government intervention and, once government presence is no longer necessary, to withdraw from the marketplace and let the forces of competition operate.

This is not to suggest that government doesn't have a continuing role to play. But the role should be that of a referee or umpire, whose function is to see that the rules are obeyed -- that the marketplace remains open, fair and free. That is precisely the role that the FEA is currently playing in our much-publicized investigation of overcharges for crude oil, propane and other petroleum products.

Far too often, long after the rhubarb is over the umpire is still right there in the center of the field, instead of on the sidelines where he belongs. And far too often the umpire becomes a player. And the history of the Federal government as a player in the marketplace is not good.

Let's look at some past examples of what direct pervasive and continuing Federal involvement in the marketplace has done to various sections of the economy.

The Interstate Commerce Commission was created in 1887, when people like Jay Gould controlled the nation's railroads and were literally earning their title of robber barons. The ICC was established to protect shippers against the monopolistic powers of the railway tycoons, and, for a period, both shippers and consumers were benefited.

But by 1935, development of a national network of highways and a growing trucking industry had taken a big chunk of the transportation market away from the railroads.

With the railroad monopoly broken and the trucking industry still wide open to competition, it was a logical time to dismantle the ICC.

Unfortunately, logic had nothing to do with what actually took place: Congress passed a new law that not only did not dismantle the ICC, but expanded its regulatory authority to cover interstate trucking as well as the railroads.

In addition to its control over our deteriorating railways, today the ICC also dictates how many new trucking firms can enter the interstate markets, thus restricting competition, while at the same time, giving carriers already in the market anti-trust immunity to set freight rates. The result is a non-competitive price fixing system that gouges the shippers and consumers ICC was established to protect.

And, let's consider the airline industry.

The Civil Aeronautics Board controls the entry of new air carriers into the interstate market, controls the distribution of routes, and has the power to disapprove or modify proposed changes in airline rates.

The result is that, in the areas of rates and routes, there is virtually no competition at all. The CAB has not approved a new trunk carrier for entry into the market since 1938. And, the higher prices that consumers pay because of CAB regulation of air fares are clearly illustrated by what has happened when interstate carriers must compete with intrastate carriers that are outside CAB authority. When Pacific Southwest Airlines entered the Los Angeles-to-San Francisco market as an intrastate carrier, it did so with rates more than 50% lower than those being charged by the regulated airlines. After attempts to ignore PSA's lower fares failed, the CAB carriers were forced to cut their rates to meet the competition. Today, as a result, it costs only about half as much to fly from L.A. to San Francisco on a per-mile basis, as it costs to fly from Washington to New York.

Another example of government regulation that often defeats its purpose is in the utilities area. The big difference here is that the problems are being caused largely by state rather than federal regulatory policies. But the end result is the same: the utilities are saddled with a rate-making system that does not respond to their needs, and the industry and all of us who depend on that industry are in trouble.

Although most government regulation was enacted with the honest goal of protecting the consumer from abuse, much of today's regulatory machinery does little more than shelter business from competition in a free and open marketplace.

In some cases, like the ICC's regulation of the railroads, this is true because circumstances have changed. In other cases, either the regulatory machinery has become perverted or regulation was a mistake from the beginning.

Whatever the case, the consumer generally winds up paying plenty for government-sanctioned price-fixing.

On the other hand, as I said before, government has a legitimate and vital role: to ensure that competition in our free enterprise system remains both free and fair.

In a free economy, competition is the only assurance that scarce resources are allocated according to the value priorities of society. When prices are administered rather than determined by the market, the consumer pays for what he receives without receiving any additional value for his money. This is true for price-administration by the private sector as much as for price-setting by government fiat.

And there are at least as many historic examples of consumer savings that were achieved by antitrust enforcement against private manipulation of the market-place as there are examples of higher consumer costs from government regulation.

So where do we draw the line?

When does government regulation become so heavy-handed that the activity being regulated becomes little more than a ward of the state and market dislocations become worse rather than better?

I recently read that there have been at least six major studies of Federal regulatory agencies since the late 1930's. These studies have all resulted in some highly critical reports, and yet there has not been a perceptible change in either our regulatory programs or the way they are administered.

Probably every President in history has complained at one time or another that the bureaucracy is impervious to change because it has a life of its own. Agencies somehow seem to be indestructible, even after the rationale for their existence has disappeared.

This is one reason why last October, President Ford asked Congress to take a long, hard look at the regulatory process. He said then that "the Federal Government imposes too many hidden and too many inflationary costs on our economy."

Later in the fall, recognizing that regulation is also a large part of state government authority, the President also sent a message to the Governors urging them to eliminate costly and unnecessary regulatory practices wherever possible.

My old associate at the Office of Management and Budget, Walter D. Scott, told an interviewer recently that he didn't believe that the government was getting its money's worth from regulation.

That feeling is being voiced more and more by senior people in government, including those who run the regulatory agencies, as well as by public spokesmen who are generally viewed as interventionist in their economic outlook -- most notably -- and perhaps, surprisingly -- by Ralph Nader, in some recent comments on the Food and Drug Administration.

The Administration will soon be presenting proposals to Congress to streamline many of these regulatory procedures — to make them more responsive to public needs and to eliminate those that hinder rather than help the operation and growth of a productive economy.

There are indications that Congress -- and, particularly, the Senate Judiciary Committee -- are receptive to such reforms. Hopefully, at long last, some of the regulatory barnacles can be removed that over the years have impeded development in so many areas.

There is the danger, however, that in the energy field -- where we have faced, and will continue to face, a crisis situation -- the popular inclination will be to pile on the regulations and the controls.

To many Americans, if the private sector isn't functioning smoothly, ~~a strong dose of medicine in the form of~~ government regulation is called for to straighten things out. And that's a feeling that prevails today about energy.

We see this type of thinking displayed by private citizens, by economists, by news commentators, and most importantly, by some members of Congress. Some propose increased or tighter regulation of energy industries. Others call for outright government take-over of many of the functions that have in the past been the sole province of private firms.

This tendency must be resisted.

It is true that certain practices of major oil companies, or utilities, for example, might be viewed by some as an open invitation for wholesale government involvement in their affairs. That is a political reality.

But there is also the economic reality that I've been discussing this afternoon -- the unpleasant reality of too much government intrusion into the marketplace, leading to inequity, inefficiency and stagnation. Those are characteristics, in the field of energy, that we must make every effort to avoid.

Government regulation cannot protect energy consumers for every minute from every abuse. We would be far wiser to recognize this fact and proceed with caution in formulating our energy policies than to opt for an energy Morgenthau plan -- a plan that would not only stifle competition and vital energy development, but would distort our national economy and the very underpinnings of our free enterprise system in ways that we can't even begin to measure.

The Administration will do its utmost to avoid such consequences -- to read the lessons of the past and exercise restraint and forebearance when called on to delve deeper into the marketplace.

Thank you.

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