The original documents are located in Box 33, folder "Transition Reports (1977) - Commerce Department: Consolidated Issues (3)" of the John Marsh Files at the Gerald R. Ford Presidential Library.

ENERGY DEVELOPMENT IMPACT ASSISTANCE FOR INTERIOR STATES

Background

A principal problem cited with regard to additional coal and synthetic fuel development, particularly in Western States, involves the socio-economic impacts which would result from additional employment and attendant population increases involved in such development. Many of the areas to be developed are sparsely populated, and lack the infra-structure and tax base necessary to support such additional population. In addition, there are special peak problems with regard to influx of construction workers who later depart, leaving smaller operating crews to manage the energy development project. The argument is made by the States that, given the national goal of accelerated energy development and the involvement of Federal lands, the Federal Government should provide front-end money to assist States and communities in providing necessary infrastructure (i.e., schools, hospitals, roads, etc.).

A $1.2 billion coastal energy impact fund was enacted in July 1976 to provide such assistance to coastal States in connection with coastal energy activities. Prior to 1976, States received a share (37½%) of the Federal leasing revenues from mineral development on Federal onshore lands for schools and roads. As a result of enactment in 1976 of the Federal Leasing Amendments Act, this share was increased to 50% and the uses to which such funds could be put expanded. In addition, the Federal Land Policy and Management Act of 1976 provided for loans to States at a rate of interest not to exceed 3% of up to 50% of the anticipated mineral revenues under the Federal Mineral Leasing Act to be received by the recipients of such loans. The loans are to be repaid from the mineral revenues to be derived thereafter.

The problem with the Federal Coal Leasing Amendments Act provisions and the advancement provisions provided in the Federal Land Policy and Management Act is that they are not necessarily related to need. Wyoming gets a disproportionate share, and the revenues for all States involved from this source are likely to be insufficient in terms of dealing with the impacts involved. Further, being based on what are in effect grants, they do not provide, as in the Coastal Zone Management Act Amendments, for repayment out of tax revenues generated as a result of energy development employment and growth, thus over time providing windfalls to States with Federal lands located therein. Further, current legislation does not provide for adequate State and local planning on which such infrastructure development can be rationally provided. Finally, an anomaly exists in that the Federal Government provides impact assistance to coastal States (where, except perhaps in Alaska, the need is less) and does not provide a systematic program for inland States.

In October, Senator Hart introduced S.3899, an energy impact assistance bill for inland States similar to the Coastal Zone Management Act. While there are some problems with the bill, it provides an approach parallel to the coastal States. It also includes a planning process. Jurisdiction for the program would be in the Department of Commerce, thus enabling one Department to administer impact assistance and planning for the Nation.

Issue

Should the Department of Commerce and the Administration work with the Congress to provide inland States legislation along the lines of S.3899?

Analysis of Issue

Coal and synthetic fuel development in Western States, a good proportion of which will be on Federal lands, is an essential part of any policy to reduce energy import vulnerability. An important impediment to the development of Western energy resources involves the concern of the States and communities that Federal energy development will result in boom-town conditions, as occurred in Colstrip, Montana, and Gilette, Wyoming. Local opposition is in large part predicated on this concern.

While some monies are already provided through Federal mineral leasing revenue sharing, no comprehensive program exists to assist States and communities in dealing with the problem. While, to be sure, it would be unfair for inland States, particularly States like Wyoming, which receive a large share of the mineral leasing revenues, to obtain double benefits from an additional Federal program, one should be able to structure a program (along the lines of the Coastal Zone Management Act) in which Federal impact assistance is offset by receipts as a result of advances under the Federal Land Policy and Management Act. From the point of view of general impact assistance and economic development planning, it would also make sense for one Department (i.e., Commerce) to administer the national program. Commerce also has considerable experience in its Economic Development Administration in planning for and dealing with economic development.

If such a national program came into existence, it would be necessary to link the current NOAA Office of Coastal Zone Management with the new program. A variety of managerial options are possible. These could be explored in a later issue paper, if it is decided to proceed in exploring with the Congress development of such legislation.

Schedule

Congress reconvenes January 4. Congressional staff and representatives of Western Governors have indicated an interest in exploring these issues with us.

ENERGY CONSERVATION
CONTINGENCY AND RATIONING PLANS

Background

The Energy Policy and Conservation Act (EPCA) requires that the President transmit to the Congress one or more energy conservation contingency plans and a gasoline and diesel fuel rationing plan in preparation for any future embargo. Although due in June 1976, the ERC only finally reviewed the plans in mid-November. They are now in the process of being presented to the President. Once transmitted, the Congress must approve the plans by resolution of both Houses within an expedited time schedule before they can be implemented. However, according to EPCA, additional plans "may be submitted at any time."

FEA has prepared five energy conservation contingency plans, which, in total, have the estimated potential of achieving approximately a 3.5% reduction in energy demand,* as follows:

1. Mandatory turning down thermostats in nonresidential public buildings.

2. Requiring firms with over 100 employees and educational institutions with over 100 students to set up a system for carpooling through limiting the number of parking spaces provided to a certain percentage of employees or enrollees.

3. Restricting sale of gasoline on weekends to reduce weekend pleasure driving.

4. Mandatory boiler inspection to insure that boilers are operating at optimum efficiency.

5. Eliminating oramental gas lights and restricting the use of illuminated advertising signs during nonbusiness hours.

The rationing plan, which is designed to distribute equitably a given supply of gasoline and diesel fuel (not to bring about additional demand restraint), provides for a white market system in which coupons would be transferable

*Based on 17 million barrels/day consumption and could be bought and sold. Business firms (including part-time businesses, those that use automobiles as well as trucks, and those that reimburse employees for use of privately owned automobiles) would be given coupons on the basis of historical use reduced by some percentage. Diesel fuel would be allocated by a separate system using credit cards and historical quotas. Gasoline for personal use would be allocated on the basis of a fixed number of gallons for every licensed driver (regardless of whether he had an automobile). In addition extra coupons would be provided for low-income long-distance commuters, handicapped individuals, migrant workers, and those moving their residence.

Issue

1. Which of the five contingency plans should be transmitted to Congress?

2. Should these plans be used before we resort to rationing in accordance with FEA's interpretation of the Act?

3. Assuming the Ford Administration has sent the Rationing Plan to Congress, should Congress be urged to approve it, or should amendments be sought to the EPCA provisions with regard to rationing plans?

Analysis

1. Contingency Plan Transmittal to Congress

EPCA requires that one or more contingency plans be submitted to Congress for approval. The greatest opposition to the FEA plans has come from the tourist industry which opposes weekend gasoline station closings and from the illuminated sign industry which in the name of small business opposes restrictions on illuminated signs.

The tourist industry's problems are self-evident, although a large proportion of the losses involved are likely to take place in an embargo in any event. (Overall estimated losses amount to $4.2 billion in revenue and sales losses in an assumed 9-month period.) The argument against signage restrictions is that it saves only a small quantity of energy and unnecessarily penalizes small business which for cost reasons relies on illuminated window signs rather than media advertising to attract customers. Further, most of the energy used to generate off-peak electricity is in the form of coal which will probably not be in short supply in a future embargo.

2. Timing of Implementation

It is anticipated that a Strategic Petroleum Reserve (see separate paper) will be in place in the early 1980s. At that time, there will be a question as to whether energy conservation contingency measures should be put in effect to reduce the drawdown of the Strategic Petroleum Reserve (SPR), or whether the SPR should be used early to avoid the disruptive effects of the conservation measures.

In its analysis of the economic impact of these conservation measures, FEA asserts that the impacts would be small since the measures would only be implemented in the event of severe petroleum shortages. However, in such a situation, implementation of these measures might have little impact since they would not significantly change total automobile and truck usage.

In the SPR plan, FEA indicates that it expects to achieve 3.5% conservation by using these contingency measures and that the SPR would be used to make up some or all of the remaining shortfall. A policy of eliminating weekend trips by closing gas stations, combined with forced carpooling, would undoubtedly cause much resentment by those affected and would probably result in a public backlash with impacts on our foreign policy if the cause of the shortages were due to an Arab-Israeli conflict in which the U.S. supported Israel. It may well be desirable to use the SPR at least initially and phase in the energy conservation contingency measures gradually in a manner to maximize diplomatic flexibility.

3. Rationing Plan

EPCA requires that any rationing plan include "ordering of priorities among classes of end users" and "consideration of the mobility needs of handicapped persons." For this reason, FEA, with some misgiving, has developed a rationing plan which provides for priorities and hardship exceptions.

The proposed plan will require 87,000 persons and $1.85 billion over a nine month to one year period to administer. But, even at this level of administration, it will be virtually impossible in any meaningful way to process applications from several million business firms which claim to have purchased gasoline for use in their automobiles, or to have reimbursed employees for gasoline used in their personal cars, while at the same time processing applications from several million individuals claiming hardship exceptions.

As a practical matter, the best that can be hoped for is that people can be taken at their word and given whatever number of coupons they request. Every small businessman (including repairmen, farmers, lawyers, part time magazine salesmen, etc.) can be expected to claim as large an amount of gasoline as possible. Since the coupons are marketable, the rationing plan in effect amounts to a program of distributing blank checks, the amount to be filled in by the recipient. In its effort to appear equitable on paper, FEA has designed a scheme which may discriminate against law-abiding Americans in favor of those who cheat.

There is a feasible alternative to the FEA scheme. This would distribute individual allotments on the basis of drivers licenses. Business users would purchase their coupons in the same manner as individuals who have unusual needs for gasoline for commuting or personal use. Personal hardships should be dealt with by tax relief or cash grants.

Such a system, which generally would be viewed in the Executive Branch with greater favor than the current scheme, would require amendments to EPCA. In view of the major problems with the rationing plan as developed by FEA, the Administration should submit it as a response to the legal requirements, but not urge that it be approved by Congress.

Schedule

The conservation and rationing plans have been reviewed in the ERC and will probably be submitted to the Congress by the Ford Administration. The Carter Administration will have to decide immediately whether actively to push Congressional approval of the contingency plans, take no action, or oppose their enactment. It will also have to decide whether to support or oppose the rationing plan. If the new Administration chooses to oppose the FEA rationing plan and substitute a plan more along the lines of that discussed above, it will have to decide whether to seek amendments to EPCA.

STRATEGIC PETROLEUM RESERVE

Background

The Energy Policy and Conservation Act (EPCA) established a Strategic Petroleum Reserve (SPR) program to provide for a national stock of crude oil which can be drawn on in the event of embargo or other supply constaint. The SPR is to consist of an Early Storage Program of 150 million barrels and a Strategic Storage Program of what amounts to three months of imports at 1973 levels (500 million barrels) unless the Executive Branch recommends another level. A storage plan for the 500 million barrels is to be sent up December 15, 1976.

The most efficient way to store large volumes of petroleum is in salt domes. A substantial number of salt dome cavities already exist in the Gulf Coast area of Texas and Louisiana as a by-product of producing salt brine for chemical plants. At somewhat higher cost, abandoned mines can also be used. Fortunately the Gulf Coast region is well supplied with ports, pipelines and refineries, and storage there gives maximum access to areas which would be heavily impacted by a supply disruption.

Issues

1. What volume of oil should be stored?

2. How should the oil be obtained to fill the storage?

Analysis

1. Size of SPR

The FEA economic analysis suggests an optimal storage volume based on economic criteria of about 350 million barrels, but the legislative minimum requirement has been interpreted as 500 million barrels. In its analysis, FEA has assumed that the SPR can prevent economic damage from embargos and that little damage would occur from implementation of emergency conservation plans designed to save 3.5% of petroleum consumption.

In the 1973-74 embargo, few if any losses in production came about as a result of firms being unable to obtain petroleum or petroleum products. The major losses came from the reduction in demand for automobiles, recreational goods (boats, recreational vehicles, second homes) and tourist services. It can be expected that in any future oil supply crisis, given the likely public concern about future shortages and restrictions on driving, consumers would again reduce purchases of these items. Thus, a part of the economic damage which FEA proposes to avoid through the SPR could occur in any event. While this would suggest that the optimal size might be less than FEA's estimate on economic grounds alone, EPCA mandates a higher reserve level unless a different level can be justified, and FEA's plan has been tailored to meet the initial requirements of the legislation.

2. Oil Purchases for SPR

The major cost of a storage program is the cost of the oil itself; storage costs are only $1.50/barrel. The total cost of the program therefore largely depends on how the oil is acquired. EPCA permits the Government to take royalty oil (a 1/6 share of production from Outer Continental Shelf fields which accrues to the Government as partial compensation for the lease) for the storage program. Since such oil is price-controlled, it is possible to acquire it for the storage program at a price of about $7 per barrel less than FEA anticipates paying for that portion of the reserve which it anticipates procuring in the international market. If all 500 million barrels could be acquired in this manner, about $2 billion could be saved. While there may not be enough royalty oil available to realize quite this volume of savings, the savings could clearly be substantial.

Use of such royalty oil has been rejected because of the potential damage to small refiners. These refiners were given preferential access to such oil in 1973 to deal with the physical shortage of petroleum on the world market existing at that time. It is not known how much benefit these small refiners receive from the use of this oil, although the total benefit is likely to be only a small fraction of the potential savings to the Government.

In 1976, however, the Administration rejected using royalty oil, although it is questionable whether the issue was reviewed in depth. The principal value of using royalty oil for this purpose is that it minimizes the budget impact and marginally increases the price of oil generally. It should, however, be noted that new contracts were executed in 1976 and use of such oil before 1979 might require breaking such contracts and paying damages.

Schedule

While the SPR Plan will be transmitted to Congress in December, additional analysis may be needed on the optimal size of the SPR. This analysis could be done in 1977 in time to affect the FY 79 budget cycle.

INTERNATIONAL ENERGY SUPPLY AND DEMAND

Background

The U.S. Government assesses on a continuing basis world oil markets in terms of overall reserves and likely supply and demand conditions. The agencies principally involved are the NSC staff, State, FEA, Commerce, Treasury, CIA, CIEP, DOD, CEA and OMB. Several Congressional Committees, including the Senate Interior and Commerce Committees, the Joint Economic Committee's Sub-Committee on Energy (chaired by Senator Kennedy) and the House Interstate and Foreign Commerce Committee have all indicated an interest in these issues. A classified paper is available on the issues involved.

Three time periods can be distinguished in connection with petroleum supply and demand over the next ten years:

1977-78	Over the next two years, we can expect upward price pressure and a strain on OPEC capacity.
1979-80	During this period, OECD members will be able to meet increases in demand from increased indigenous supply from the North Sea and Alaska. As a result, there will be some excess capacity and real prices may oscillate or even decline slightly.
Early 1980's	OECD demand is expected once again to increase at a rate which exceeds the rate of expansion capacity within OPEC.

While an oil find outside of OPEC of Saudi Arabian dimensions would change the analysis considerably, the probability of such a find appears too low to base U.S. policy on it. Further, it is expected that U.S. imports will not decline and could increase substantially over the next ten years. And, U.S. vulnerability is considerably less than that of Europe and Japan with which the U.S. is essentially interdependent for political and economic reasons.

Most of our European allies and Japan do not have alternative energy supply options other than nuclear. And, even in the case of nuclear, unless breeder technology proves feasible, there is some question as to whether uranium supply and/or uranium enrichment capacity will be sufficient, even if nuclear power plants are constructed on an accelerated basis.

OPEC will probably let revenue hungry members expand production while Saudi Arabia, and to a lesser extent Kuwait, with their enormous reserves and limited development needs, play the balance wheel. And, OPEC current dollar oil prices will probably rise steadily, to the extent this can be done without either depressing the world economy or encouraging development of alternate energy sources sufficient to make OPEC oil export revenues decline. Under this scenario, Saudi Arabia will have to double its current production.

Issue

(1) What should U.S. policy be to deal with this situation over the long term?

(2) How can consuming countries encourage OPEC nations to exercise restraint with respect to both supply and price?

(3) How should we communicate such a policy to the Congress and the public?

Analysis of Issue

1. Long-term solution

With regard to the long term situation, it is clear that we must, together with other OECD countries, decrease our need for imported oil from OPEC countries. This involves domestic energy policies--increasing both indigenous alternative sources of supply and reducing consumption of oil. Each country will have a different set of policies in this respect. We are in the process of developing with other countries oil import targets, and we are committed in the International Energy Agency (IEA) to a sharing scheme and emergency demand restraint measures in the event of supply disruption. Nevertheless, development of alternative energy supplies has so far not materialized to the degree originally projected. This is particularly so of nuclear power which has been beset by environmental and safety concerns as well as accelerating construction costs. There are limits to energy conservation consonant with economic growth. Synthetic fuels and new technologies are unlikely to produce significant relief before 1990 and beyond.

2. Policy towards OPEC Nations

First, it is clear we must do what we can to encourage OPEC nations to exercise restraint. Actions include: industrial-consumer country long term cooperation; emergency protection against supply disruption; actions to affect production and pricing; and actions with regard to non-oil exporting LDC's (EDDCs). Continuing effort is needed to analyze and develop an understanding of what measures are most in the U.S. interest.

3. Policy Communication

The new Administration should explore every possible option if for no other reason than to permit it to say that it considered the possibility and rejected it for good and sufficient reason. We need to discuss the international energy situation on a confidential basis with the Congress.

Schedule

A priority effort of the new Administration should be development and completion of appropriate analysis of this subject. All options should be explored.

ENERGY TRADE WITH CANADA AND MEXICO

Background

The U.S. now imports from Canada 450,000 barrels per day (b/d) of crude oil and almost one trillion cubic feet of natural gas, respectively three and five percent of domestic needs. Mexico ships to us only about 100,000 b/d of crude oil. The U.S. exports 14 million tons of coal each year to Ontario, Canada, where it is used for power generation, and a small amount enters the U.S. from western Canada. Electrical energy crosses both borders, but the net flow is into the U.S. from Canada and out of the U.S. to Mexico. Canada plans to cut down to 255,000 b/d of crude oil next year, and additional curtailments of gas shipments are likely over time. It appears, too, that Canada will be anxious to ship more heavy crude oil than in the past, as it is only the lighter crudes which are in short supply because of increasing domestic demand.

Mexican oil production has been increasing only slowly, and has not reached the target of one million b/d set for the end of the current President's term of office (November 30); Mexican oil production is now about 800,000 b/d. The new President, Lopez Portillo, is reported to want to increase oil production in order to gain more revenue; he is, however, likely to run up against the conservationist group in the State-owned oil company, Petroleos Mexicanos (PEMEX), who want to maximize benefits from Mexican oil resources. Some PEMEX officials are concerned with the Mexican Government's tendency to siphon off PEMEX earnings for general Government use, reducing PEMEX's ability to make the necessary investments to maximize the oil resource for the future. It is also reported that PEMEX wishes to increase refining capacity in Mexico and hence obtain the additional revenues derived therefrom.

Nevertheless, Mexican oil reserves are enormous and capable over time of producing up to 2.5 million b/d in the 1980's. Mexican crude oil is generally of low gravity and is heavy and of high sulfur content, although lighter oil has been found in some of the newer fields. For example, the old Ebano-Pinuco field near Tampico, the field closest to the U.S., yields crude of No. 12 API gravity and 5.38% sulfur which is usable only for the manufacture of asphalt. Other fields have crude of API gravity up to 35 and of sulfur content in the range of Middle Eastern crude.

Issue

There is a double-barreled issue here:

(1) Can we convince the Canadians to lengthen the timetable for cutbacks on oil and gas shipments to the U.S.?
(2) Can we obtain increased oil shipments from Mexico?

Analysis of Issues

(1) Canada

We are continuing discussion with the Canadians on maintaining as long as possible oil and gas shipments to the U.S. We are also exploring what areas are of major interest to the Canadians. One of the few positive areas involves cooperation with Canada in the study and construction of the so-called Kitimat line from British Columbia to carry Alaskan crude to existing lines running into the U.S. (see Alaska Oil Paper), and possibly an oil and/or gas line from the Alaskan border across Canada, either through the Mackenzie River Valley or along the Alcan Highway (the Arctic and Foothills proposals; see Alaska Natural Gas paper).

(2) Mexico

Mexican oil and gas supplies are of major interest to the U.S. If Portillo implements plans some Mexican officials have proposed, shipments to the U.S. could increase at a rate which would replace imports from Canada, at least on a quantity basis, assuming Canadian shipments decline at the rate planned by the National Energy Board of Canada. On an economic basis, given the lower transportation costs involved, this should also be in Mexico's interest.

At the moment, the main problem facing the Mexicans in oil production is technical. PEMEX is having difficulty obtaining from the U.S. deep drilling rigs (over 18,000 foot rating) and other technical problems. On the other hand, Mexicans have to some extent tried to avoid purchasing U.S. equipment, technology and skilled labor, preferring to "go it alone" in hopes of showing their independence from the U.S.

PEMEX would appear at this point to be somewhat inexperienced in obtaining equipment from U.S. or other markets. For example, while it is true that U.S. manufacturers of drilling rig equipment may be jammed up with respect to some components, there may be ways to obtain equipment through the used drilling rig market on a faster time schedule.

Mexico, in developing its oil reserves, will acquire substantial sums of foreign exchange which it will seek to put to use in accelerating its economic development. The U.S. has an interest in this market as well as access to Mexican crude or product.

Schedule

Early in the new Administration, the Secretary of Commerce should consider making a visit to Mexico City to offer discreetly to discuss the above issues. Official U.S. encouragement and development of enhanced U.S.-Mexican commercial relations is very much in the U.S. national interest if we are to encourage the development of secure sources of crude oil or product and increase our export markets.

U.S. ROLE IN THE INTERNATIONAL ENERGY AGENCY

Background

The International Energy Agency (IEA) was established in November 1974 to deal primarily with future petroleum shortages such as those which resulted from the Arab oil embargo in the winter of 1973-74. IEA is both a consultative and an operational organization. Its consultative activities include demand restraint and international oil market studies, exchanges of information on methods of conserving energy, and cooperation in the development of sources of energy other than oil. IEA's operational purpose is to allocate oil supplies during an emergency based on uniform percentage cutbacks of consumption and stocks.

The IEA is, in effect, the successor to the OECD (Organization of Economic Cooperation and Development) Oil Committee which attempted in the years following the supply interruptions of the 1967 Arab-Israeli War to establish a similar system for dealing with supply shortages. Some OECD members, notably France, chose not to join IEA, which was deemed "confrontational". IEA has just finished running a test of its allocation program involving a simulated emergency. U.S. firms took part in this exercise. Evaluation of the results is now beginning.

Issue

Will the major countries cooperate in sharing oil in a future crisis?

Analysis

The International Energy Agreement requires countries greatly to reduce their consumption of petroleum in order to permit diversion of supplies to other countries that are the victim of a selective embargo or a major cutback in production. For instance, if the United States because of its support of Israel is denied petroleum by the Arab countries and the Arab countries reduce production at the same time, the IEA emergency sharing formula would require Europe, Japan, and Canada to cut consumption in order to divert non-Arab oil to the United States. In certain other scenarios, the United States might have to cut its consumption to supply Europe or Japan.

The political problems involved in doing this can be understood just by remembering the hardships the United States experienced during the last embargo. The United States Government might be reluctant to take political responsibility for shortages caused by emergency sharing. Likewise, a European government might be very reluctant, in the face of Arab opposition, to impose hardships on its people to assist the United States in reducing the impact of its policy of support for Israel.

Schedule

The only action forcing event is a new Embargo. But we should bear in mind the political questions involved in implementing any future international emergency sharing.

U.S. ROLE IN THE CONFERENCE ON
INTERNATIONAL ECONOMIC COOPERATION (CIEC)

Background

In April and October of 1975, representatives of oil-producing and oil-importing countries met to discuss questions of raw material prices, protection of the purchasing power of OPEC members' oil revenues, and the economic health of oil-importing countries hard hit by price increases. At a Ministerial conference in December 1975, it was agreed that meetings would be held during 1976 to discuss these various issues in four commissions: energy, raw materials, development, and finance. At the conclusion of these discussions, termed collectively the Conference on International Economic Cooperation (CIEC), it was planned to hold a ministerial meeting in December 1976 to put the seal of approval on policy recommendations made by the several commissions.

The two major issues which evolved during the year were protection of purchasing power of earnings and of accumulated oil revenues (including the concept of indexation) and debt relief for poor developing countries. Numerous other policy questions were discussed in the various commissions, including proposals for an International Resources Bank (IRB) to assist in financing the production of various raw materials, including energy resources, and an International Energy Institute (IEI) which would provide a mechanism for exchange of technology between industrialized and developing countries.

It is unlikely that the December 15-17 Ministerial will in fact be held, as both sides were unable, at the November session, to agree on commique language to offer their ministers. Instead, it is likely that Co-Chairmen of the four commissions (each commission has both a developed and developing country co-chairman) will meet to tidy up details, postponing any Ministerial, at least for the moment. It is unclear, at this time, whether CIEC will in fact continue. Certainly, its continuation will depend in large part on the nature and level of U.S. support.

Issue

Is CIEC sufficiently useful to expend additional U.S. effort to keep it going?

Analysis of Issue

OPEC representatives in CIEC have implied that action to be taken at the OPEC meeting in December on a price increase will depend in part on whether CIEC deliberations result in concrete accomplishments, in particular in relation to oil price indexation. The U.S. is reluctant to go along with indexation in that it would legitimize the current OPEC cartel pricing, would be difficult to do as a practical matter and would constitute a precedent with regard to other commodities. And, since 1973, OPEC prices have in fact increased at a rate less than the average rate of inflation in the industrialized countries.

From the U.S. standpoint, CIEC may be a limited success if it merely continues a discussion of the well-nigh intractable issues separating the two sides. Perhaps more important is the fact that the U.S. is able in CIEC to expose OPEC countries to the difficulties they impose on non-oil exporting LDCs. Specifically, the developing countries in CIEC ("Group of 19") have been split into oil-producing and oil-importing camps, with the latter disposed to agree with the industrialized countries on the economic dangers of further oil price increases. And, OPEC countries have been exposed to the coordinated views of industrialized countries, which may be helpful in fostering a more responsible attitude within OPEC while providing ammunition to the more moderate OPEC governments.

Despite these positive aspects, the basic confrontations between industrialized countries and OPEC, and industrialized countries and developing countries, have not been modified in any basic way. Nor has there been agreement on the two U.S. proposals of the International Resources Bank and the International Energy Institute. Further, outside of the Energy Commission, the dialogue has either basically ground to a halt in that other fora are involved in the issues in a more detailed way (Raw Materials Commission over commodities) or provided another vehicle for LDC attacks on industrialized countries (Finance Commission over debt relief).

Finally, CIEC has really not been very successful in providing a smaller policy body in which North-South issues can be debated. Countries not included do not consider themselves in any way bound by the discussions and the "Group of 19" representing the developing countries has not moderated its "new international economic order" rhetoric to any appreciable degree.

The Department of State is the most pro-CIEC agency. FEA, Treasury and Commerce have been somewhat skeptical of the benefits from the CIEC meetings held so far, although we are mindful of the positive aspects summarized above.

Schedule

By the end of the year, the issue of CIEC's continuance, at least ad interim, will have been decided. The new Administration will have to decide whether to proceed in this forum or revert to other mechanisms for dealing with OPEC and the various other North-South issues CIEC has been considering. The Canadian-Venezuelan overall CIEC Co-Chairmen are meeting in New York December 1 to discuss next steps in CIEC.

ROLE OF COMMERCE IN ENERGY RESOURCES COUNCIL

Background

The Energy Resources Council (ERC) was established by Section 108 of the Energy Reorganization Act of 1974 and extended to no later than September 30, 1977, by the Energy Conservation and Production Act of 1976 (ECPA). The ERC was activated in October 1974 by Executive Order 11814, now amended by Executive Orders 11819 and 11855. The first Chairman was then Secretary of Interior Rogers Morton. Secretary Morton continued his ERC chairmanship as Secretary of Commerce and was replaced by his successor as Secretary of Commerce, Elliot Richardson. The Administrator of FEA is currently ERC Executive Director.

The ERC has been quite active since its inception--the executive committee (consisting of the principal agencies concerned with energy matters) often meeting on a weekly basis, more often than not in conjunction with the Economic Policy Board. Numerous matters requiring energy policy decisions have arisen and been analyzed in the ERC and appropriate recommendations made to the President. Among those areas to which ERC effort has been directed have been: energy organization, energy legislation, nuclear policy, liquified natural gas import policy, natural gas and oil distribution systems for Alaskan resources, natural gas pricing and many others. ERC currently has task forces involving nuclear policy, utilities policy, and liquified natural gas policy.

The ERC has further been charged by ECPA with producing an energy organization report by December 31, 1976, and an energy conservation analysis report by July 1, 1977.

Issues

1. Should the ERC continue in existence or be replaced by another body?

2. Should it have independent staff capability?

3. What should be the role of Commerce (the present holder of the chairmanship) in the ERC?

Analysis of Issues

1. Continuation of ERC

Since 1970, there has been an official inter-departmental oil policy body of one sort or another. The problem has been lack of continuity of leadership, lack of independent staff capability and a plethora of separate statutory authorities administered by separate agencies subject to Congressional oversight by different Congressional committees. Nevertheless, the ERC has provided a forum in which deliberation of energy issues can take place and disputes be either resolved or referred to the President for decision. Essentially, the ERC has had to rely on FEA staff to perform the bulk of its analysis.

The ERC report on energy reoganization will likely recommend establishment of a Department of Energy including the Federal Energy Administration, Energy Research and Development Administration, Federal Power Commission, Rural Electrification Administration and the power marketing and Bureau of Mines energy functions from Interior. Once such a Cabinet-level agency is established, an ERC as such is probably unnecessary. Pending such a reorganization and consolidation of energy functions, however, some Cabinet-level group is required to assure some degree of coordination between Interior, FEA, EPA, ERDA, and other organizations on specific energy matters.

OMB is negative on ERC. This is both a question of turf and the fact that ERC is perceived as just another voice for FEA. OMB would of course continue budget coordination and its own legislative review process on the details of legislative policy. However, it is preferable for a separate Cabinet-level Council to debate key energy issues at the policy level.

2. ERC Staff

There are arguments pro and con establishing an independent ERC staff. On the negative side, such a staff could isolate the ERC Chairman from agency heads and high level Administration officials responsible under law for energy issues. On the other hand, without such a staff, the Chairman of the ERC is largely dependent upon agency analysis reflecting the bias of particular institutions, and he can only to a limited degree adequately perform required coordination functions, such as bringing together agencies with competing responsibilities in a particular area. On balance, we believe the ERC should have a small independent staff capability to coordinate interagency analysis in key areas and assure that all energy options are, as appropriate and necessary, presented to the President.

3. Commerce Role

With regard to the chairmanship of the ERC, there is no real logic leading to the Secretary of Commerce. On the other hand, choosing a Secretary of Commerce for this purpose is by no means unjustifiable. A great deal depends on the personality, intellect and acumen of the incumbent Secretary. The Department of Commerce, with its broad responsibilities for the economy in general, has major policy interests in energy issues. And, energy policy should be a component of economic policy.

On the other hand, the argument can be made that Commerce, as an institution, is too oriented towards private sector and market solutions to problems which may require positive government intervention. It could further be argued that the ERC Chairman should be a part of the White House or Executive Office of the President staff.

Whoever may be ERC Chairman, the Secretary of Commerce should be an important member of and participant in the ERC. He should be a member of its Executive Committee, and contribute to ERC analysis of issues such as those involving energy pricing, energy conservation, allocations, and outer continental shelf energy development (given the Department of Commerce's oceans responsibilities).

Schedule

ERC functions and leadership should be decided at the outset of the new Administration.

NORTH/SOUTH DIALOGUE ON COMMODITIES -- PROCESS

Background

International commodity trade is a principal issue on the current agenda of institutions involved in developed/developing country discussions of world economic problems -- the North/South dialogue. Following the unprecedented boom in commodity prices in 1973-74, and in light of the success of the Organization of Petroleum Exporting Countries (OPEC) in forming a producer cartel with regard to petroleum, the developing countries (LDCs) began to apply intense pressure on the U.S. and other developed countries (DCs) to obtain international recognition of a "program of action" to establish a "new international economic order" (NIEO).

NIEO was adopted by the U.N. General Assembly at its 6th Special Session in April 1974, despite specific reservations by the U.S. and some other DCs. NIEO has since been pursued assiduously in the U.N. Conference on Trade and Development (UNCTAD) -- the principal LDC-controlled forum on international economic issues. In the field of raw materials and other primary products, the LDCs have pressed in UNCTAD for (1) maximum government intervention in international markets to "stabilize" prices of commodity exports at "remunerative levels"; (2) management of such prices so that they will increase at the same rate as export prices of manufacturerd goods (indexation); (3) maximization of their effective sovereignty over mineral resources within their borders by rejecting traditional safeguards for foreign investment under international law; (4) greater participation in the downstream marketing and distribution of their products; and (5) improvements in the Compensatory Financing Facility of the International Monetary Fund (IMF) that would not only achieve a greater degree of year-to-year stabilization of their export earnings, but would also result in a net transfer of resources to LDCs from the IMF. The LDCs have also, of course, continued to seek more traditional forms of assistance such as increased access to DC markets, especially for more processed forms of their raw materials.

The U.S. position has been to focus on solutions that: (1) emphasize government cooperation in improving and strengthening the functioning of world commodity markets but which fall short of direct government intervention in them across the board; (2) assist LDCs to cope with market instability in individual commodities without government intervention in the market, except in special cases where limited intervention could be helpful without undermining the basic functioning of the market; and (3) discourage solutions that are patently uneconomic or counter-productive in the longer term, or that exclude consumer-country participation.

In this regard, the U.S. has (1) encouraged a commodity-by-commodity approach, both to the analysis of problems and the consideration of possible solutions, including in some cases proposals for individual commodity agreements; (2) supported formation of producer/consumer commodity forums (of which there are already some 20 or more); (3) supported improved market access, mainly through traditional negotiating techniques under the aegis of the Multilateral Trade Negotiations (MTN) now in progress in Geneva, while also seeking ways to improve DC access to supplies; (4) supported improvements in export income stabilization, notably through the recently expanded Compensatory Financing Facility of the IMF; (5) stressed the importance of an improved investment climate and of sufficient investment in commodity production to meet future demand; and (6) participated in broad-ranging, frank discussions in the Raw Materials Commission of the Paris Conference on International Economic Cooperation (CIEC) on all issues affecting commodities, such as the role of transnational enterprises, technology transfer and diversification.

On the other hand, we (1) insist on being convinced, before agreeing to participate in any negotiations, of the need, efficacy and long-term advantages of commodity agreements, while trying to be pragmatic in considering such agreements (we have joined the coffee and tin agreements, negotiated on cocoa but decided not to join, and will negotiate on sugar); (2) have flatly rejected indexation, and (3) have deep reservations on UNCTAD's proposed $6 billion Common Fund (see separate paper).

These issues underlie the ongoing discussions in a large number of international fora: (1) UNCTAD and its Committee on Commodities, where highly politicized discussions revolve around the demands of the LDCs (known in UNCTAD as the Group of 77 (G-77) although they number over 100) (see separate papers); (2) the Conference on International Economic Cooperation (CIEC) and its Raw Materials Commission (RMC), which involves eight key DCs (the European Community counts as one), and nineteen key LDC producers of energy and raw materials; (3) the Food and Agriculture Organization (FAO) in Rome, which has a number of Intergovernmental Groups (IGs) on over a dozen agricultural commodities (e.g., bananas, tea, vegetable oils, meat, jute, hard fibers, etc.); (4) three autonomous international producer/consumer forums, covering cotton, natural rubber, and lead and zinc; and (5) a limited number of international commodity councils which either administer active commodity agreements (coffee and tin), or administer agreements which are currently not active for one reason of another (cocoa, sugar, wheat), but may be in the future.

<u>Issue</u>

What strategy and what fora offer the best vehicles for the U.S. to achieve its international commodity policy objectives?

Analysis of Issue

Beneath all the rhetoric on international commodity policy, the LDCs essentially would like the DCs to help them rig the international commodity markets so that these can become engines for a continuous and increasing transfer of resources based solely on LDC shares in the world trade of the commodities in question and which can be used entirely at the discretion of the LDCs. A small but dedicated number of LDCs with a wide following (notably such countries as Algeria, Indonesia, Peru, Philippines, Mexico and Venezuela) provide leadership in the effort to bring about a world system of government market intervention as a way to increase revenues accruing to raw material producing countries and implement the underlying state-trading philosophy of the NIEO.

Most DCs, and many LDCs, nevertheless, realize that the bargaining power of the NIEO proponents in commodities other than oil is considerably less than that of the OPEC oil cartel. No commodity, other than oil, has the same concentration in the hands of like-minded nations; and few such commodities lack substitutes to the same event. Further, the reserves of no other commodity are uniquely concentrated in the hands of one country lacking the need to maximize current revenues (i.e., Saudi Arabia which is willing to curtail disproportionately its own production in order to maintain the cartel). Therefore, it is most unlikely that cartels in other commodities will in fact materialize. Recognizing this probability, many LDCs find it easier simply to go along with the lowest common denominator among their number, and many DCs find it convenient to pander to ideologically-motivated LDC schemes, however unrealistic, rather than suffer the opprobrium of opposition. These DCs also rely on the unwillingness of the U.S., Japan, and the Federal Republic of Germany (FRG), in particular, to act in the same way.

The DCs are badly divided in their response to LDC commodity initiatives. The biggest commodity importers (the U.S., FRG, Japan) want a basically market-oriented international trading system for commodities, prefer non-market interventionist solutions to temporary market aberrations, and prefer to effect any substantial transfer of resources directly, purposefully, and with specific country targets, through bilateral or multilateral channels, rather than haphazardly through increasingly distorted world trade patterns.

The U.K. is less solid in this regard; but, with its growing financial difficulties, has begun swinging toward the U.S.-German Japanese approach. A number of European DCs--notably France, Belgium, and to some extent Italy and other Mediterranean countries--are intellectually attracted, or have no great objection, to essentially Government-interventionist policies, and are generally amenable to government intervention in commodity markets, especially when their share of the burden would be small; these countries view this approach as a highly visible means to demonstrate DC sympathy for LDC problems at what they feel is a minimum economic cost. These countries are supportered by still others: the Netherlands and the Scandinavians, who, for idealistic reasons, would even go further than the French by trying to insure that a substantial transfer of resources would in fact occur as a result of government intervention.

Under these circumstances, the U.S. and its close ideological allies are constantly in a minority in large multilateral fora where commodities are discussed, such as the quadrennial sessions of UNCTAD, or its annual Trade and Development Board meetings, and the regular and Special Sessions of the U.N. General Assembly. The U.S. has sought, therefore, to favor either smaller bodies, where the more moderate LDCs might have a larger voice (e.g., CIEC) or small expert commodity bodies (e.g., the 20-odd international commodity study groups) where only the major producers and consumers of a commodity are members. Recently, however, the LDC ideologues have found ways to politicize any meeting on commodities by insisting that all UNCTAD meetings be open to all countries and by holding frequent convocations of the Group of 77, which then issue ringing manifestos for the guidance of all LDCs in any body.

Despite these tactics, however, LDCs often are deeply divided on how to deal with problems on a practical level. Fora with limited membership, and especially where criteria for membership specify countries with a real economic stake in the subject under discussion, tend to offer the best climate for developing pragmatic solutions.

The key problem, as has been noted, is that the LDCs want additional transfers of resources from the DCs. A number of DC economies have in recent years encountered difficulties; as a result domestic pressure in these countries has tended to restrict external transfers of resources, even to international financial institutions. The LDCs have, as a result, attempted to find other, less obvious ways to increase their share of the pie. Unfortunately, export earnings from commodity exports cannot be expected to grow steadily or fast enough to match DC export performance, which is the criterion the LDCs apply. Most LDCs have not diversified exports sufficiently (e.g., developed exports of manufactures) to match DC performance. And, in any case, their need for foreign exchange will in most cases outrun their earnings for the foreseeable future.

In addition, both production conditions of and markets for specific commodities vary. It is not possible to assist a producer of a particular commodity without dealing with the very specific production and market elements involved. All of this argues for individual commodity discussions, confined to producers and consumers of that commodity, and, as appropriate, bilaterals between the countries most affected. (See separate paper on Commodities Discussions Under UNCTAD Resolution 93 (IV)).

The current U.S. strategy is to string out the several commodity discussions and force the LDCs to analyze and focus on the real problems in the hope that the analytical effort will bring them to the realization that market intervention by and large will not solve LDC problems. Such a strategy also postpones having to decide as to whether additional resources should be committed to the effort.

On the other hand, the strategy is mainly one of delay. We know what we don't want; but we don't yet know what we do want. We are against a Common Fund (see separate Common Fund paper); we are for being "forthcoming" in individual commodity discussions (see separate Commodities Discussions paper); but we have very little idea of what being "forthcoming" means. Eventually, we must design a real policy.

On the other hand, real solutions to LDC economic problems will require both institutional reform in the LDCs concerned and substantial transfer of resources. Both the reform and the resource transfer will involve considerations much broader than those specifically related to segments of export trade, such as commodities. Therefore, a principal part of any North-South strategy must involve an integrated overall effort by DCs to deal with the general problems of LDC economic development. This will involve substantial sums of money.

This issue is one of the most important which will have to be managed by the new Administration, and must out of necessity be a key part of U.S. foreign policy in the decades ahead. It is not just a question of alleviating Third World poverty; it is a question of overall U.S. political and economic objectives. This set of issues is the subject of a separate, lengthier issues paper.

Schedule

As will be seen from the attached list of meetings, the U.S. faces a full year of multilateral meetings on commodities during 1977. We need to focus a strategy which interrelates our position and that of other DCs in relation to these meetings.

As of November 11, 1976

International Commodity and Commodity-Related Meetings - 1976/77

1976

Int'l Lead & Zinc Study Group	Geneva	Nov. 4-12
Int'l Sugar Organization Working Group	London	Nov. 9-18
UNCTAD Committee on Tungsten	Geneva	Nov. 15-19
CIEC - RMC (Working Group Nov. 12, 13, 15)	Paris	Nov. 12-23
Int'l Coffee Council	London	Nov. 22-23
UNCTAD Intergovernmental Group on IP for Commodities - 1st Session	Geneva	Nov. 24-26
UNCTAD Common Fund Preparatory (1st Mtg)	Geneva	Nov. 29-Dec. 3
UNCTAD Hard Fibers	Geneva	Dec. 6-10
Int'l Tin Council	London	Dec. 6-10
CIEC Ministerial	Paris	Dec. 15-17

1977

UNCTAD Rubber (1st Mtg)	Geneva	Jan. 17-21
UNCTAD Common Fund Preparatory (2nd Mtg)	Geneva	Jan. 24-28
UNCTAD Copper Experts (2nd Mtg)	Geneva	Feb. 7-18
FAO Intergovernmental Group on Tea	London	Feb. 14-25
FAO Intergovernmental Group on Oilseeds	Rome	Mar. 7-11
UNCTAD Common Fund - Negotiating Conference		Mar. 7-Apr. 1
UNCTAD Copper Experts (3rd Mtg)	Geneva	Mar. 14-18
FAO Intergovernmental Group on Hard Fibers	New Delhi	Mar. 14-19
FAO Intergovernmental Group on Bananas	Rome	Mar. 21-26
UNCTAD Oils and Oilseeds	Rome	Mar/Apr
Negotiations for Int'l Sugar Agreement	Geneva	Apr/May
UNCTAD Bananas		2nd Quarter
UNCTAD Tropical Timber		2nd Quarter
UNCTAD Copper Preparatory Mtg (2nd Session)	Geneva	May 9-13
UN Law of the Sea	New York	May 28-Jul. 16
UNCTAD Cotton		2nd or 3rd Qtr.
FAO Intergovernmental Group on Hard Fibers	Rome	Sep.
FAO Intergovernmental Group on Meat	Rome	Sep/Oct
FAO Intergovernmental Group on Jute	Rome	Sep/Oct
FAO Intergovernmental Group on Grains	Rome	Oct. 3-7
UNCTAD Bauxite	Geneva	Second Half
UNCTAD Iron Ore	Geneva	Second Half
UNCTAD Manganese	Geneva	Second Half
UNCTAD Tea	Geneva	Second Half

Rev. 11/76

COMMON FUND

Background

Resolution 93(IV) of the U.N. Conference on Trade and Development (UNCTAD) on an "Integrated Program for Commodities," in which the U.S. concurred with reservations, calls for the Secretary General of UNCTAD to convene, no later than March 1977, a negotiating conference open to all UNCTAD members on the establishment of a Common Fund to finance the creation of buffer stocks for individual commodities.

A buffer stock, usually in combination with a system of export controls, is one of the traditional instruments advocated in international commodity agreements to try to stabilize prices. It usually requires at the outset contributions of both money and quantities of the commodity. The money is used to purchase quantities of the commodity whenever the market price of the commodity falls below a specified level. The theory is that when prices rise above a certain level, sales from the buffer stock will be made so as to reduce pressures on prices going up further.

There are four existing commodity agreements in the world; and of these, only two, on tin and cocoa, have buffer stocks, and the cocoa stock is limited in scope. Based on the performance of these two stocks and general economic analysis, it is reasonably clear that buffer stocks are likely to be useful, if at all, only in connection with a handful of commodities (see Individual Commodities Discussions paper). Nevertheless, the UNCTAD Secretariat with the full backing of the developing countries (LDCs), invented the concept of the Common Fund to promote more use of buffer stocks. From the LDC viewpoint, the Common Fund proposal is another device for pressuring developed countries (DCs) to transfer additional resources to LDCs while also supporting their desire for greater government intervention in commodity trade (see North/South Dialogue paper).

In advance of the March 1977 negotiating conference, preparatory meetings were called in order further to elaborate the details of the Common Fund concept, including buffer stock financing, possible objectives other than its financial needs and structure, possible sources of finance, modes of operation, and its decision-making mechanism.

UNCTAD's hope is that, with a Common Fund to provide the necessary financing, buffer stocks could be established for at least ten "core" commodities (the principal ones among the 18 for which there are individual conferences scheduled). The Fund is presently conceived by the UNCTAD Secretariat as being able to begin with paid-up capital (contributed by governments) totalling $1 billion. In addition, the Fund would borrow capital from market sources, with government guarantees of an additional $2 billion. It is presently estimated that eventually the Fund might need $6 billion. Under UNCTAD's formula for financing the Fund, the U.S. paid-in share would vary from 8 to 11 percent of the initial contribution or tranche--or about $100 million.

Issue

1. What should the U.S. position towards the Common Fund be?

2. What leverage do we have to obtain that position?

Analysis

Since the G-77 success in ramming through agreement on the NIEO in the U.N. General Assembly, the Common Fund has become a major political issue for the LDCs; it is one of the principal political benchmarks by which they will measure progress in the DC/LDC dialogue. The Common Fund concept embodies several major LDC objectives: (1) action in the resource area; (2) a desire for a larger role in shaping the new international economic system; (3) increased resource transfers through both higher commodity prices and pre-financing commitments from the DCs; and (4) a general test of the DC's political will in the DC/LDC dialogue.

The U.S. opposes the Common Fund as proposed by the UNCTAD Secretariat. Apart from serious doubts as to its feasibility and usefulness in addressing the real problems of international commodity markets or for that matter general LDC economic development, we believe the concept is inconsistent with the central elements of U.S. commodity policy. Among these is that commodity problems should be examined and dealt with on a case-by-case basis; that the financial responsibility for developing and implementing solutions should rest with the producers and consumers of the commodity in question, and that buffer stocks represent only one technique among many for improving stability in commodity markets.

The current U.S. strategy on the Common Fund issue is (1) to express analytically our objections to the Common Fund; (2) to attend the preparatory meetings on the Common Fund without commitment on whether or not to participate in the March 1977 conference; and (3) meantime, to undertake an active and positive role in individual commodity consultations.

At the November 29 - December 3 preparatory meeting on the Common Fund in Geneva, the U.S. Delegation will adopt a passive role in the discussions, and will seek to obtain clarification of some of the UNCTAD Secretariat proposed Fund provisions.

1. <u>What should the U.S. do?</u>

We need to develop a thorough consideration and assessment of the real costs and benefits of committing up to $6 billion in financial resources to a Common Fund. We should also try to get countries other than the U.S. to press for serious consideration of possible alternative approaches. Neither the present U.S. strategy nor the U.S. reservations to Resolution 93(IV), of course, foreclose U.S. participation in the March 1977 negotiations without commitment, if, in light of the preparatory meetings, we believe this to be in the U.S. interest.

The issue of the Common Fund has been the subject of numerous discussions in the NSC/EPB Commodities Policy Coordinating Committee; it has also been periodically discussed in the EPB itself. As a result of these discussions, an options paper was prepared by State and Treasury which was reviewed by agency heads concerned and a policy decided upon. Essentially, it was agreed that the U.S. would continue to oppose the Common Fund on a passive basis and participate in the preliminary discussions but not commit to participate in a negotiating session. We also decided not to respond to the UNCTAD Secretariat's request for comments.

Nevertheless, State and Commerce, and possibly even Treasury (which has been the most conservative agency on this issue), are prepared, if necessary, to consider a French proposal (Fourcade proposal) to establish a mechanism which in effect would provide for mutual financing assistance between any buffer stocks which might later be created. Another option which might constitute a bottom line fall-back position would create a package of DC assistance in lieu of a Common Fund. Finally, more thought needs to be given to what would happen if the U.S. and other DCs simply acquiesced in a Common Fund but either did or did not contribute to its financing, in the context of an overall North-South strategy (see separate paper).

2. Leverage

See paper on Individual Commodity Discussions under UNCTAD IV Resolution 93(IV).

3. Schedule

A second preparatory meeting on the Common Fund is scheduled for January 24-27, 1977. If the LDCs insist on holding a "negotiating" session in March 1977 as scheduled, we will have to decide on the advisability of participating, even if the intervening meetings have not by then altered our position of opposing the Common Fund concept. We should begin our analysis now as to what variants of the Common Fund concept might be more acceptable to the U.S.

INDIVIDUAL COMMODITIES DISCUSSIONS UNDER UNCTAD RESOLUTION 93(IV)

Background

The U.S. has consistently indicated its willingness to discuss and evaluate international commodity problems on a case-by-case basis and has objected to any general or uniform market interventionist program covering many commodities as being inefficient and unworkable. Accordingly, in response to the overwhelming consensus among developing countries at the U.N. Conference on Trade and Development in Nairobi in 1976 (UNCTAD IV) as expressed in UNCTAD Resolution 93(IV), the U.S. agreed to participate in preparatory meetings on eighteen individual commodities, but refused to agree in advance that these should necessarily culminate in the negotiation of commodity agreements for each or most of them, with or without buffer stocks, as the preferred solution. The U.S. maintains that a variety of approaches exist, that all should be considered in relation to the problems peculiar to each commodity, and that the expertise of existing intergovernmental commodity organizations should be used in the process. The LDCs, on the other hand, view these meetings as leading directly to negotiations to establish commodity agreements which would feature buffer stocks and which would be linked to and financed by a Common Fund (see separate paper).

The commodities to be considered are: bananas, bauxite, cocoa, coffee, copper, jute and products, manganese, meat, phosphates, rubber, sugar, tea, tropical timber, tin, vegetable oils including olive oil, and oilseeds. The fact that for one reason or another most of these commodities would not be realistic candidates for commodity agreements (including buffer stocks) has had little influence on the enthusiasm LDCs continue to express for buffer stock agreements in general.

Developing countries (LDCs) insist that the case-by-case approach has not produced substantial improvements from their point of view in the benefits to be derived from international commodity trade, and that only by establishing UNCTAD's Integrated Program (the name given to Resolution 93(IV)) will progress be made towards providing them with greater benefits and their goal of a "New International Economic Order" (NIEO). LDCs expect the Integrated Program (IP) to, inter alia, stablize commodity price fluctuations while also raising the average price level for their commodity exports and improving their real income from commodity trade; reduce competition from synthetics; reduce trade barriers in developed markets; encourage research and development on the problems of natural products; and improve the LDC share in the downstream marketing and distribution of their raw materials.

The U.S. and several other developed countries (DCs) maintain that the goals and mechanisms of the IP are sometimes conflicting and counterproductive, conducive to economic inefficiency, and in large part unworkable. In its reservations at UNCTAD IV, the U.S. stated that, with regard to meetings on individual commodities, "...the purpose of such meetings is to determine the nature of the problems affecting particular commodities and to determine, without commitment, the measures which might be appropriate to each product."

Coffee, tin, cocoa and sugar have been removed from the UNCTAD list of commodities to be discussed because international commodity agreements already exist for the first three (the U.S. is a member of the coffee and tin agreements), and a negotiating conference has been tentatively scheduled for sugar. (The U.S. was a member of previous sugar agreements until 1961).

In regard to the other commodities, the UNCTAD objective, as demonstrated in the case of the recent preparatory meetings on copper and jute, is to obtain agreement in the individual commodity consultations on the primacy of buffer stocks as the principal instrument for international action. Success in obtaining agreement to this approach would then be used by the LDCs and the UNCTAD Secretariat to demonstrate a need for a Common Fund to finance these commodity buffer stocks. To achieve this goal, the UNCTAD Secretariat is exercising as much control as possible over the preparatory meetings and the studies for the Common Fund discussions. The Secretariat has attempted to minimize the role of existing commodity organizations. It has also encouraged participation in individual commodity discussions by G-77 members who have little interest in the commodity concerned but are committed to the IP.

<u>Issue</u>

What should be the U.S. strategy in these commodity meetings?

<u>Analysis</u>

To date, the U.S. strategy that has evolved in the IP meetings has been (1) to seek as much involvement as possible by the existing intergovernmental fora for the particular commodities; (2) to insist that all action options be studied, (not just buffer stocks); (3) to insist that basic analytical studies be carried out in parallel with, if not prior to, elaboration of actual action proposals by the UNCTAD Secretariat; (4) to take the initiative in making proposals aimed at attacking the fundamental problems of the commodity in question, such as financing of research and development or obtaining consideration for reducing or removing trade barriers. The U.S. has also supported procedural steps to encourage technical discussions by subgroups of the meetings in order to reduce the influence of politically motivated countries which are neither major producers nor consumers of the commodity in question but are present to ensure that the results of the meeting support their ideological bent in favor of the Common Fund and maximum government intervention in markets.

This strategy has worked fairly well in the copper meetings, where the major producers are deeply divided, and two of the principal producers (Chile and Canada) are sympathetic to the U.S. position of undertaking further analysis of the problems of the world copper market before leaping into specific solutions. Zaire and Zambia are also not militant about creating a copper buffer stock (although it may be that a copper buffer stock would be feasible albeit very expensive). On the other hand, this strategy met with little success in the jute meeting, where the major producers (Bangladesh, India) are highly sensitive to maintaining ideological unity with the most radical G-77 proponents of the NIEO.

Our basic argument is that it is far better to assist LDCs in solving individual commodity problems, even if the solutions involve expenditure of DC resources, than to acquiesce in a new international economic order which, while it might provide a one-time shot in the arm to individual producers, would neither contribute to solving most commodity stabilization problems nor to increasing in any important way LDC economic development. Trade in most commodities is of such a high dollar value that it would be difficult to obtain sufficient commitments to create a buffer stock of sufficient size to have much more than a temporary effect on supply/demand imbalances. And, most LDCs' economic development involves too much more than commodity trade for whatever limited stabilization that might result to contribute greatly to development. In any event, the IMF Compensatory Financing Facility already provides a means to assist producing countries suffering from a major downturn in demand.

American industry's views can be divided into three categories: (1) companies which are producers, (2) companies which are consumers, and (3) commodity traders. Producing companies have little difficulty with commodity agreements as such to the extent that they provide an additional market for a particular commodity. They are, however, concerned by the possibility of production or export controls which would normally accompany any buffer stock arrangement. Consuming companies, on the other hand, are concerned by these elements of buffer stock arrangements and new international economic order rhetoric which would result in a constant upward trend in commodities prices; in most instances, however, such price increases could be passed on to the ultimate consumer. Commodity traders are the most affected by commodity agreements which, to the extent they are effective, tend to dampen speculation. On the other hand, commodity agreements would also tend to create an artificial market force and thus undermine the normal market clearing functions performed by traders.

Commerce has urged that the U.S. develop as many initiatives as possible, which are and can be perceived to be positive approaches to the problems of specific commodities. A major constraint is that such solutions often involve substantial direct costs and agreement within the USG has so far not been achieved on whether to pledge specific amounts for specific purposes. A chart outlining what initiatives should be explored is attached.

It should be noted that the LDCs rebuffed U.S. attempts to be "forthcoming" on jute with respect to measures other than buffer stocks. However, hopefully, this may reflect primarily the present campaign to enforce LDC solidarity in focusing exclusively on the buffer stock approach in anticipation of the Common Fund negotiations in March 1977.

Schedule

The preparatory meetings on individual commodities are scheduled to continue throughout 1977 and to end in February 1978. Resulting negotiations are to be finished by the end of 1978. The UNCTAD Secretariat has scheduled early its major candidates for the buffer stocks approach (copper, jute, hard fibers, rubber) to try to support the alleged need for a Common Fund. Depending on how that negotiation turns out, and the resultant LDC reaction, non-interventionist initiatives may receive a better reception in the later months of 1977.

TABLE OF POSSIBLE COMMODITY INITIATIVES TO BE EXPLORED

Commodity	Principal Exporting Countries	1	2	3	4	5	6	7	8	9	10
Bananas	Ecuador, Costa Rica Honduras, Panama, Philippines		X?	X	X	X			X		E
Bauxite	Jamaica, Australia, Guyana		X?	X	X			X			X
Copper	Chile, Peru, Canada Zaire, Zambia	X	X	X				X	X		X
Cotton	U.S., U.A.R., Mexico, Turkey		X	X	X	X			X	X	E
Hard Fibers & Products	Brazil, Tanzania Mexico	X	X?	X	X	X		X	X	X	E
Iron Ore	Australia, Brazil India, Venezuela, USSR		X?	X	X			X			X
Jute & Products	Bangladesh, India, Thailand	X	X?	X	X	X	X		X	X	E
Manganese	Brazil, Gabon		X?	X				X			X
Meat	Australia, Argentina, New Zealand		X		X						E
Phosphates	Morocco, U.S., USSR, Mauritania			X				X			X
Natural Rubber	Malaysia, Indonesia, Thailand, Sri Lanka	X	X?	X			X	X	X	X	E
Tea	India, Sri Lanka, Kenya, Uganda		X	X	X	X		X	X		E
Tropical Timber	Philippines, Malaysia, Indonesia		X?	X	X			X			X
Vegetable Oils	U.S., Brazil, Malaysia, Australia, Canada		X		X			X	X	X	E

1. Buffer Stocks
2. Export and/or Production Control
3. Encouragement of long term contract
4. Access to Markets
5. Assistance for diversification
6. Assistance for improved productivity
7. Assistance for domestic processin
8. Assistance for market promotion
9. Assistance for R&D
10. Producer-Consumer Forum

Note: "E" indicates producer-consumer forum exists.

FOOD IMPORT POLICIES

BACKGROUND: During the past year, the Administration has been subjected to strong pressures from agricultural interests, and members of Congress, to act under the provisions of existing statutes to restrict imports of certain food commodities, imports of which form a significant part of U.S. supply, and have a considerable impact on domestic prices, i.e. sugar and red meats.

In the case of meats, expansion of herds in the U.S. and abroad over the past few years, plus recurrent droughts in Australia which have forced premature slaughter, has led to severe price pressure on U.S. cattlemen who, in a number of cases, find themselves in a loss situation resulting from low meat prices and rising feed costs.

Domestic beef producers are afforded protection under the 1964 Meat Import Law, which requires the President to impose import quotas when imports rise to 110 percent of a base quantity designed to maintain a steady ratio between U.S. production and imports. Up to this year the U.S. was able to avoid putting quotas into effect, usually by persuading our major foreign suppliers to impose voluntary restraints on their exports. However, this year increased domestic production, aggravated by increased imports from Canada (whose exports were not restrained) and leakages in the export restraint program via one of our Foreign Trade Zones, led to intense cattlemen and Congressional pressures on the Executive Branch. Consequently, on October 9, the President declared import quotas on meat for the first time. On November 26, however, he authorized negotiation of a new series of voluntary export restraint agreements in order to avoid having to extend the import quotas beyond December 31, 1976.

In the case of sugar, extremely high prices peaking in 1974 plus improved weather conditions have led to sharp increases in foreign production at a time when the U.S. had just completed dismantling its 30-year-old sugar program by allowing the Sugar Act to expire on December 31, 1974. The drop in world and domestic sugar prices resulting from the surge in world subsidies has since threatened the economic viability of a segment of our domestic sugar-growing industry, especially the cane sugar growers in the Gulf States. Complicating the problem has been the growing production in the U.S. of sugar derived from a new source, i.e., high-fructose corn syrup (HFCS). This product, which is the laboratory equivalent to sugar, has captured most of the growth in sugar consumption.

As an interim protective measure, the President tripled the duty on sugar imports last October and requested the International Trade Commission (ITC) to determine whether or not the domestic industry is being injured as a result of sugar imports.

ISSUE: How do we reconcile our need for a steady and reliable supply of beef and raw sugar to meet the requirements of U.S. processing industries and the consumers with the necessity of responding to domestic producers who feel they are threatened at home by foreign competition?

ANALYSIS: From the point of view of Commerce, meat and raw sugar imports, and particularly the latter,which historically has accounted for just under half of U.S. sugar supplies, are an important source of raw materials for U.S. industry as well as important items in the consuming public food budget. However, the imposition of U.S. restrictive measures on imports would generate retribution by foreign suppliers which is likely to bear heavily on U.S. exports of manufactured products. Consequently, we have an interest in avoiding actions which would have a serious adverse impact on the achievement of overall U.S. objectives in the current round of multilateral trade negotiations under the GATT.

With respect to meat import policy for 1977, available options will depend on the outcome of U.S. attempts during December 1976 to negotiate a new voluntary restraint arrangement with major foreign suppliers. Should these negotiations prove unsuccessful the U.S. will be faced with the decision whether to continue the formal quotas now in effect or delay imposition of quotas until the situation so warrants during the course of 1977. Because of the rather drastic consequences of either course of action, the Agricultural Policy Working Group will undoubtedly review the entire meat import situation and assess carefully the pros and cons of possible alternative options.

In the case of sugar policy, import options are likely to be limited to: (1) continuation of current policy; (2) a two million ton global quota reduction and no duty change; (3) a restrictive global quota with no duty change; (4) a combination of duty increase and restrictive global quota.

Concurrent consideration must also be given to likely pressure on the Congress for enactment of new sugar legislation to protect the domestic industry, and to the implications arising from the negotiation of a new international sugar agreement with operative economic provisions.

SCHEDULE: The President has instructed the State Department to begin international negotiations for a voluntary restraint arrangement (VRA) below the meat import quota trigger level of 1282 million pounds. State will begin such negotiations in early December and seek to get the arrangement in place by January 1, 1977.

Sugar policy options will be addressed in a number of contexts during the first half of 1977. The International Trade Commission will make public sometime next January its findings on the question of import injury to the domestic sugar industry. A finding of injury by ITC would put pressure on the Executive Branch for remedial action, and also, increase pressure on the Congress for new sugar legislation. On the international side negotiation of a new International Sugar Agreement (ISA) is scheduled for April-May 1977.

APPENDIX - Agricultural Policy Working Group

AGRICULTURAL POLICY WORKING GROUP
(APWG)

PURPOSE: To exchange information and evaluate domestic and international trends or events affecting the world supply of basic agricultural commodities, U.S. agricultural production and trade, farm income, retail food prices, etc.

To undertake analytical studies, and recommend national policy actions for dealing with actual or developing food and agricultural issues both in the short and medium term.

BACKGROUND: The APWG serves as a working group of the Cabinet-level Agricultural Policy Committee. Meetings are chaired by the Assistant Secretary of Agriculture for International Affairs and Commodity Programs. APWG principal members are the Departments of Agriculture, Commerce, State and Treasury, the Office of Management and Budget, the Council of Economic Advisers, the Office of the Special Representative for Trade Negotiations, and the Council on International Economic Policy.

ISSUES: The following topics on the agenda of 1976 meetings are indicative of the range of issues normally considered by the APWG: (1) Grain exports; (2) World grain situation and impact on the U.S. supply-demand balance; (3) Agricultural and retail food prices; (4) Sugar policy; (5) Food aid to LDCs; (6) Financial assistance to foreign palm oil producers; (7) Impact of the EEC non-fat dry milk regulation on U.S. soybean exports; (8) Import quotas for EEC dairy products; (9) CCC credits for sales of agricultural commodities to foreign countries; (10) Meat Import policy for 1977.

SCHEDULE: Issues similar to those listed above are considered at monthly meetings. Special meetings are called whenever required by the urgency of the problem or in the conduct of special studies.

INTERNATIONAL GRAIN RESERVES POLICY

BACKGROUND: Following the mid-1960s drought in Asia, the corn blight in the United States in 1970, the years 1972-73 saw a wave of crop failures around the world--a short grain and soybean crop in the U.S. due to early frost, and the failure of the anchovy catch off Peru. These losses were compounded by the fact that the U.S. had just significantly drawn down its surplus grain stocks for the first time since World War II as a result of heavy sales to the USSR. With international food prices skyrocketing, the poorer developing countries (LDCs) found themselves in danger of being outbid for limited supplies and thus faced with starvation.

To deal with these problems a World Food Conference was convened in Rome at the request of the U.S. under the aegis of the Food and Agriculture Organization of the U.N. (FAO). This conference dealt with a wide range of problems, including both the long and the short term problems of maintaining world food security. Under the category of short term problems, one of the chief results was adoption of a proposed set of guidelines known as the International Undertaking on World Food Security, aimed at encouraging individual countries, especially the developed countries (DCs) and the USSR, to adopt national policies insuring that sufficient grain stocks would be held domestically so that in bad crop years such countries would not place heavy burdens on world food exports and thus give the LDCs a better chance to compete for the smaller export supply. Most major grain trading countries (including the U.S.) have expressed agreement with this general undertaking.

Pursuing this idea, in late 1974, the President, speaking to the U.N. General Assembly, announced U.S. preparedness to negotiate an internationally-coordinated system of nationally-held grain reserves. In September 1975, following numerous informal international discussions, the U.S. convened an ad hoc meeting of the major grain exporting and importing countries to lay a basis for preliminary discussion of a grain reserves negotiation. These discussions have continued under the auspices of the International Wheat Council, but without result.

ISSUE: How can we achieve our objective of obtaining international agreement on a system of nationally-held grain reserves?

ANALYSIS OF ISSUE: In the U.S.' view, an international system of grain reserves should establish a reserve supply of grains in addition to that normally available for world consumption (production plus carry-over). It should make this supply available in years of serious global production shortfall to offset at least a portion of this shortfall, thereby preventing the need for severe reductions in world food consumption, and secondarily undue fluctuations in prices.

In the September 1975 meeting, the U.S. tabled a proposal with those objectives in mind for the establishment of an international system of nationally-held grain reserves. Agreement has never been reached, however. The reason for this is that most other grain exporting countries believe that grain reserves should be part of a new grain stabilization effort, i.e., a commodity agreement on grains, with the double purpose of price stabilization and maintenance of a system of grain reserves. The U.S. has argued that a return to an international wheat agreement is a step backward from liberalization of agricultural trade, and is unnecessary in view of the basically strong position of the world grain market in the wake of a long series of short crops.

Desirous of avoiding resumption of government intervention in our own grain economy, we have also sought to obtain recognition of part of the U.S. commercial inventory of grain as being our contribution to world "reserves" over and above normal trading needs. The U.S. view in effect has been that if all developed countries carried a comfortable level of grain inventories, either in commercial hands or through government stocking, the essential elements of a grain reserve system could be put in place. A consultative forum could then be constructed so governments could make sure that such stocks were drawn upon if the world crop threatened to fall significantly in any given year.

It is clear that the U.S. concept of grain reserves has proven either too sophisticated or not sufficiently concrete to win general acceptance. On the other hand, in a period of relatively lean supplies, the U.S. has had a strong argument against those who have tried to turn the need for adequate grain stocks into an argument for a price stabilization agreement. In view of the excellent grain harvests in 1976, however, the world for the first time in several years can look forward to a significantly improved stock position during 1977. A second good world crop in 1977 could reduce prices to the level where the U.S. Government would have to consider supporting the domestic market through grain purchases. This would increase the likelihood of earmarked grain reserve stocks; however, it would also increase pressure for a commodity agreement on grains.

While the Departments of Agriculture and State have primary responsibility, Commerce has an overall economic interest in grain supply and demand, both under its responsibilities pursuant to the Export Administration Act as well as its role in the formulation of international commodity policy.

SCHEDULE: No action on the food reserves issue is expected in the next half year. Efforts to liberalize the grain trade (the U.S. is a major exporter) are now being made in Geneva in the context of our Multilateral Trade Negotiations (MTN) efforts. Perhaps, by mid-1977, further action will take place in the context of negotiations for a new International Wheat Agreement (IWA) to replace the present Agreement of which the U.S. is a member; the current IWA does not have operative provisions for Government intervention in the market.

STRATEGIC VERSUS ECONOMIC STOCKPILES

Background

As a result of the establishment of the Organization of Petroleum Exporting Countries (OPEC) oil cartel and of widespread short supply and skyrocketing prices in raw materials in 1973-74, considerable interest developed in exploring the desirability of the Federal Government's accumulating and maintaining inventories of industrial raw materials for purposes other than national defense and security. Considerable study has since been devoted to the subject by the joint Executive Branch-Congressional National Commission on Supplies and Shortages, the Office of Technological Assessment, and several Congressional committees. Executive Branch analysis of economic stockpiling has been less intensive, in view of work going on elsewhere, to which it has given staff support. Executive Branch analysis has rather focused on a major review of the U.S. strategic stockpile and its adequacy for possible military emergencies.

The distinction between strategic and economic stockpiles is important. The purposes of the strategic stockpile, as stated in the Strategic and Critical Materials Stockpiling Act of 1946, are (1) to provide for the acquisition and retention of stocks of certain critical and strategic materials within the United States, (2) to encourage the conservation and development of domestic sources of these materials, and (3) to decrease and prevent U.S. dependency upon foreign nations for supplies of such materials <u>in times of national emergency</u>.

Economic stockpiles, on the other hand, would involve the acquisition of commodities for other than defense related purposes to achieve national economic objectives. Economic stockpiles would be aimed at (1) reducing price instability; and (2) hedging against unpredictable supply interruptions resulting from national disasters or the concerted actions of foreign producers.

Issue

Given the existence of the strategic stockpile, could it and should it be used to accomplish some of the purposes of an economic stockpile?

Analysis

It is fair to say that in the case of the U.S., it is easier to see the disadvantages of an economic stockpile than the advantages. As a possible defense against foreign cartels, the concept suffers from two major weaknesses: (1) an interagency study in 1974 showed that effective foreign raw material cartels are not a strong possibility and (2) the U.S., with its huge domestic resource base, would be less vulnerable than most other industrialized countries. As a possible price stabilizer, an economic stockpile would have the weakness of any buffer stock, i.e., the cost of success in such an exercise would probably exceed the benefits to be derived. In the end, a serious Governmental attempt to stabilize prices of raw materials could be highly disruptive of the entire economy.

The operation of the U.S. strategic stockpile has created its own share of problems: its procurement operations helped encourage uneconomic production and world surpluses in some materials in the 1950s; and disposals to reduce excess inventories have periodically brought complaints from foreign governments regarding their disturbing effects on world markets.

On the other hand, it can be said that in some ways the strategic stockpile, when used for economic purposes, has caused relatively little economic disruption. As the various commodity stocking objectives have been raised or lowered, strategic stockpile commodities have been both bought and sold. In the late 1950s, purchases were made for a "supplemental" strategic stockpile as one device in trying to stop a price slide in certain minerals such as lead and zinc. In 1974, large amounts of excess inventories were sold off in an attempt to reduce market price escalation in that period of short supply, as well as in order to help reduce the Government's budget deficit. Recently, the strategic stockpile goals for a number of commodities were increased considerably, and the U.S. could consider the possibility of phasing procurement in meeting these goals in conjunction with dealing with possible price weaknesses in world commodity markets.

Most observers and some interested Government agencies continue to have open minds on the pros and cons of economic stockpiles. Perhaps we should consider, in addition to continued analysis of economic stockpiling, a realistic assessment of how the Strategic Stockpile might be used to provide the U.S. with additional options for dealing with both domestic and international commodity problems.

Schedule

It is our understanding that the General Services Administration is including in its FY 78 budget a request for funds to begin procurement of materials in order to meet the increased stockpile goals which resulted from the November review. If such funds become part of the President's budget request, they will be the subject of hearings by the Armed Services Committees in Congress during the spring of 1977. Review by the Appropriations Committees would follow in the course of the summer.

The National Commission on Supplies and Shortages, which has issued a study on Economic Stockpiling, will complete a Final Report on its activities by December 31, 1976, and be terminated in March 1977. It is possible that Congressional hearings will be held to review this Final Report.

INTERAGENCY DECISIONMAKING ON COMMODITY POLICY

Background

Interagency coordination of the development and implementation of international commodity policy is achieved in a number of ways.

Decisions on overall policy (e.g., with respect to the Common Fund and the UNCTAD Integrated Program) are made by the Economic Policy Board (EPB) after staffing and review in the NSC/EPB Commodity Policy Coordinating Committee (CPCC). CPCC is an Assistant Secretary level body co-chaired by State and Treasury; membership includes Commerce, Agriculture, CEA, OMB, NSC, and CIEP. Informal ad hoc working groups composed of member agency staff prepare the necessary analyses.

U.S. positions and related background papers for specific meetings in connection with specific commodities are normally developed, in accordance with general CPCC guidance, by informal interagency committees which usually include State as chairman, Commerce and Treasury. Interior is included when the commodity in question is a mineral produced in the U.S. Agriculture is included for agricultural commodities, and usually asserts a major interest when the U.S. is a producer or exporter of the commodity in question.

Where commodity issues are discussed as a part of a broader international conference, such as UNCTAD-IV, the U.N. General Assembly or Special Sessions thereof, and the Paris Conference on International Economic Cooperation (CIEP), coordination of non-controversial issues takes place in ad hoc interagency committees convened by State and having broad membership. Where controversial issues arise, they are forwarded to the CPCC, which also may ask for EPB approval.

Once policy is settled, day to day implementing and tactical decisions in line with established policy is made through interagency clearance at the staff level. In the case of international conferences, interagency coordination is effected through membership of most interested agencies in the U.S. delegation. Commerce is normally represented in all commodity-related delegations with some exceptions such as wheat and certain other agricultural commodities where the major U.S. interest is that of an exporter.

Issue

What should be the decisionmaking mechanism for international commodity policy? What should be the role of the Department of Commerce?

Analysis

Prior to November, 1975, there was considerable friction between the Treasury and State Departments with regard to international commodity policy coordination. The State Department, with its control of international governmental communications and U.S. delegations to international commodity discussions, was suspected by Treasury of not taking domestic economic concerns sufficiently into account in negotiating with developing countries on commodities. Under Secretary Simon, Treasury staff have taken a basically free-market approach to commodity discussions and essentially discounted U.S. long term political and economic interests in connection with developing countries (LDCs).

Commerce, while lacking the clout of either State or Treasury, took a middle position, responding to LDC concerns in ways that would both assist them in their development while avoiding market intervention solutions. Commerce, with its U.S. industry contacts, has advocated a careful, step by step approach in which we and the LDCs would develop greater understanding of individual commodity markets and ways to strengthen them.

The CPCC was created essentially to provide a Treasury veto over State Department actions in international commodity discussions. From Commerce's point of view, it makes sense for a domestic agency to exercise such a role, although it need not necessarily be Treasury. There are both domestic and international considerations involved; international commodity discussions should not be the sole province of foreign affairs specialists. And, in our view, the co-chairing arrangement of CPCC (Treasury and State) helps to assure a balance.

On the other hand, from a domestic point of view, Treasury lacks depth and experience in the commodities area. And, both State and Treasury rely on Commerce and to a lesser extent Agriculture and Interior, to provide expertise, analysis on individual commodities, and the experience of long continuity in the field. At the same time, our international commodities staff still lacks depth in policy making; most of it is relatively new and it is thinly spread over a large number of commodities. Equally important, they have not been able to speak with the clout exercised by Treasury.

From an overall USG management point of view, it might make sense to combine the Treasury and Commerce functions in international policy making. On the other hand, if a new Secretary of Commerce wishes to take a lead in this area, he has the beginnings of a staff, and the necessary industry contacts with which to do so.

Treasury involvement in this area has largely been a function of Secretary Simon and Assistant Secretary Parsky. Prior to Simon and Parsky, Treasury had little interest in international economic policy other than international financial policy. While Treasury now has the beginnings of a general international economic staff, it is not sufficiently developed to preclude Commerce from taking a lead role, especially since Treasury does not appear to have plans to develop its underlying commodity expertise. U.S. business and industry would probably welcome such a role. If we are to undertake leadership of this kind, we will need to acquire additional policy oriented staff to build on existing capability.

Schedule

If we wish to take the lead, we should move early in the next Administration.

OCEANS POLICY FORMULATION AND ORGANIZATION

Background

Concern has been expressed by prominent members of both the Senate Commerce and House Merchant Marine & Fisheries Committees with regard to policy direction involving oceans issues and programs. This concern focuses primarily on general ocean issues involving the National Oceanic and Atmospheric Administration (NOAA) and numerous other agencies and Departments--from the Maritime Administration and the Coast Guard, to the Environmental Protection Agency and the State Department.

Many in the Congress feel that our ocean policies, investment and organization are inadequate to deal effectively with ocean problems--ocean pollution and coastal zone congestion, for example; and unable to realize ocean potentials--food, minerals, energy--and international cooperation at the Law of the Sea Conference. The Sea Grant legislation, as it passed the Senate (but not as it was enacted), included a clear direction to NOAA to develop and coordinate its marine and coastal resources programs in light of "national goals and international objectives". The bill would have established NOAA as the "lead agency for certain programs for the United States". These references were consistent with Reorganization Plan #4 of 1970 which established NOAA as the central civilian agency for matters related to oceans and the marine environment.

On September 9 Secretary Richardson testified before the House Committee on Merchant Marine & Fisheries' Subcommittee on Oceanography. Despite vigorous OMB opposition, he stated his firm personal belief that a Cabinet-level oceans committee should be established to assist the President in developing ocean policy objectives and priorities. The Secretary noted that, while ocean questions have been dealt with in a variety of Cabinet committees (e.g., NSC, Domestic Council, Energy Resources Council), and these committees have a large degree of common membership, there is an important need to deal with oceans questions as a whole and not simply as one item on an agenda.

Beyond a Cabinet-level policy body, the Secretary sketched out arguments pro and con the establishment of a separate oceans agency and indicated his belief that if there were to be an oceans agency, it should be either Cabinet-level or a part of a Cabinet-level agency.

In the last days of the 94th Congress, Senator Hollings introduced S.3889, a bill to establish a Cabinet Department of the Environment and Oceans (DEO). The Hollings bill includes in one Cabinet Department, among other entities, EPA, NOAA, the Coast Guard, and the National Park and Fish and Wildlife Services and the Bureau of Outdoor Recreation from Interior. Since the elections, both Office of the Secretary and NOAA staff have met with Senate staff on this bill.

Issue

The issues are (1) how should the Federal Government develop a more coordinated policy thrust for ocean issues and programs; (2) what should be the role of NOAA in this area; and (3) what should be the nature of the eventual organization encompassing oceans issues?

Analysis of Issue

1. Oceans Policy

Ocean activities may be regarded in at least two fundamentally different ways. One philosophy considers ocean efforts functional extensions of land-based efforts; this would group ocean transportation, food production and energy development in the oceans, with their counterparts on land. On the other hand, Secretary Richardson has noted four fundamental qualities which differentiate ocean-based efforts from land-based efforts and indicate that oceans should be treated as unique. First, oceans are not divided by private property rights in the same way as the lands; second, the ecology of the oceans involves closely interrelated phenomena and therefore the impacts of oceans activities on the ocean ecology are more closely interrelated than is the case with land activities on the land ecology; third, the technology for marine resource development is qualitatively different; and fourth, the oceans constitute an area in which U.S. interests butt up against the interests of other countries.

Regardless of our eventual oceans organization, there will be a need to assure cross-cut consideration of ocean issues in relation to each other, as well as in relation to other domestic and international governmental functions. There is a general sympathy within the Executive Branch and the relevent committees of Congress for such an approach, although there are differences of view within the Executive Branch whether the Vice-President, the Secretary of Commerce, or someone else should have the lead.

In addition, the State Department/Defense Department/NSC complex of institutions are concerned that any such Cabinet-level effort might interfere with NSC coordination of Law of the Sea negotiations.

2. Role of NOAA

At present, NOAA is the only agency of Government with general ocean responsibilities. The objective of Reorganization Plan No. 4, in establishing NOAA, was to coordinate and provide cohesion to our ocean efforts. Despite this initial charter, NOAA has not been able to provide ocean policy direction--in part due to opposition at OMB, and basically because of a lack of statutory authority.

NOAA is beginning to augment its policy capability. And, the Office of the Secretary has itself created a focal point for oceans policy in OESRP. It should be noted that, with the possible exception of the deep seabed mining issue (see separate issue paper), the involved Congressional committees generally support a more active leadership role by NOAA and the Commerce Department.

3. Oceans Organization

With regard to eventual reorganization involving oceans issues, the question is: what should be the principal context within which oceans issues are dealt? Essentially, the oceans are a repository of resources (both living and mineral), a medium for transportation, and an important determinant of environmental quality through the interaction of the oceans and the atmosphere. These uses of the oceans involve both developmental and environmental protection interests. Certainly, the environmental protection aspects of the oceans should be dealt with as a whole. This is not the case at present; protection and regulatory functions are widely dispersed and include the Interior Department, the Corps of Engineers, the Coast Guard, and the Environmental Protection Agency. NOAA developmental functions with respect to fisheries, on the other hand, are lodged together with conservation functions in the National Marine Fisheries Service. In addition, a large portion of NOAA's activities can be lumped under the heading environmental services. Many other agencies such as the Geological Survey and the Coast Guard provide related services.

If, as is likely to be recommended, a Department of Energy is established, one could well argue that to complete this change, it would be logical to include ocean conservation and regulatory programs in a strengthened environmental agency, which would generally be concerned with the management of common resource properties. However, the case for including ocean development activities is not as compelling. Indeed, arguments can be made against it, since the pressure for development could compromise conservation interests; the reverse is also true. At the same time, separating these activities would lose the benefits of a single agency responsible for oceans policy.

Schedule

Both the Senate Commerce and Government Operations Committees will consider next year the Hollings bill, which will be reintroduced in the 95th Congress. The House Merchant Marine and Fisheries Committee intends to continue its hearings on national ocean policy as well. This issue should be the subject of immediate Secretarial involvement and leadership, both within the Administration and in concert with the Congress.

IMPLEMENTATION OF THE FISHERIES CONSERVATION AND MANAGEMENT ACT (1976)

Background

The Fisheries Conservation and Management Act of 1976 allows vessels of foreign nations to fish within the U.S. 200-mile fishery conservation zone after March 1, 1977 if their governments have (1) entered into a Governing International Fishery Agreement (GIFA) not rejected by Congress, and a valid permit is aboard the vessel; or (2) have an international fishery agreement in effect on the date of enactment of the Act, along with a registration permit issued by the Secretary of Commerce for each fishing vessel.

A variety of nations have traditionally fished off our shores beyond 12 miles (the width of our fisheries conservation zone prior to enactment of P.L. 94-265) but within 200 miles. This fishing has resulted in serious depletion of certain stocks. Japan and the USSR account for 87% of the foreign harvest.

The principal purpose of P.L 94-265 is to conserve and manage the fishery resources found off U.S. coasts and strengthen domestic commercial and recreational fishing. To achieve this purpose, the Act provides for the establishment of Regional Fishery Management Councils to prepare fishery management plans which will achieve and maintain, on a continuing basis, the optimum yield from each fishery. Among other things, these plans will contain that portion of the optimum yield which, on an annual basis, will not be harvested by U.S. fishing vessels and can be made available for foreign fishing. Based on this determination, the Secretary of State is to allocate the amount available among foreign nations.

The Councils were appointed in August, 1976. It is generally conceded that the Councils will not be able to prepare plans by March 1. Therefore, in accordance with the Act, NOAA has prepared draft preliminary fishery plans which can go into effect, pending development of Council plans, when State notifies Commerce that a foreign nation has submitted an application for a fishing permit.

On the other hand, foreign vessels will not be able to have valid fishing permits on board by March 1, 1977. Four nations have to date signed GIFAs (Poland, German Democratic Republic, Republic of China (Taiwan), USSR). Japan has so far not signed. Negotiations are, however, proceeding favorably with those nations which have not signed. Bulgaria, Romania, and possibly Korea and Japan are expected to sign in December (although special problems remain with regard to Japan). Even if all thirteen countries, which are anticipated to seek fishing privileges in the U.S. fishing zone sign GIFAs by March 1, 1977, they will not have valid permits on board because it takes approximately four months to complete the permit application review and issue a valid permit.

Issue

How do we assure a reasonable process to permit foreign fishing after March 1 which is in accord with the purposes of P.L. 94-265?

Analysis

It is important to assure preferential opportunities for U.S. fishermen within the 200-mile zone and protect the authority of the Regional Fishery Management Councils in this regard. It is likewise important not to cause unnecessary friction with other nations which are prepared to recognize our law and sign GIFAs. Therefore, a process must be developed which will allow, on an interim basis, fishing by foreign vessels of nations which have agreed, by signing GIFA's, to respect our jurisdiction and conserve our fisheries, but which are unable to obtain the necessary permits on time.

The legal and administrative requirements for obtaining congressional approval of GIFA's, reviewing foreign applications to fish, approving preliminary plans, complying with the National Environmental Policy Act, and collecting fees and issuing permits will require a time period of approximately 4 to 5 months subsequent to signing a GIFA. The key elements are the necessity to complete regulations for signing GIFAs as early as possible and to obtain congressional approval of GIFAs. The 60 continuous day mandatory congressional review cannot start before January 1977 and, hence, GIFA approval cannot be completed prior to March 1, 1977.

Consequently, the Department proposes requesting a "one-time waiver" of certain permit requirements of the Act, which would allow issuance of temporary permits for a five - six month period to vessels of countries having signed GIFAs. A full analysis of this issue is presented in a separate, lengthier issue paper.

Schedule

The Department of Commerce needs to secure the concurrence in seeking legislative relief of the Department of State and the Coast Guard and support from the eight Regional Councils. The Administration must request Congress to provide the specified "one-time" legislative relief as soon as possible after Congress reconvenes in January 1977.

DEEP SEABED LEGISLATION

Background

The deep seabed beyond the limits of national jurisdiction contain vast quantities of manganese nodules composed of manganese, copper, nickel and cobalt. While the technology has never been demonstrated on a commercial basis and there are still questions as to whether such technology will prove economic, two consortia led by U.S. firms and two additional U.S. firms have indicated a considerable interest in mining these nodules.

Regardless of what happens at the Law of the Sea Conference, it is conceded that these nodules lie beyond the jurisdiction of any coastal nation. They are in an international area which has been termed by U.S. Administrations (beginning with the Johnson Administration), other industrialized countries and the developing countries as the "common heritage of mankind." The developing countries (LDCs) claim that, pending agreement on an international regime, there should be a moratorium on deep seabed development. They have incorporated this view in a UN General Assembly resolution which the U.S. does not accept as binding. The U.S., and other industrialized countries, maintain that countries have the right under existing international law and as a part of traditional high seas freedoms to move forward in developing the deep seabed.

At the same time, in the Law of the Sea Conference, negotiations are still underway to establish an international deep seabed regime which would be administered by an International Seabed Authority (ISA). However, the Law of the Sea Conference completed its fourth session last September with little progress being made on any of the major unresolved issues. In particular, the seabeds discussions deteriorated into a "new international economic order" ideological debate. The next Law of the Sea session is scheduled to begin in May 1977.

There is considerable interest in the Congress in developing interim domestic legislation which would authorize U.S. companies to move forward with deep seabed mining in specific areas. The Senate Commerce and Interior Committees and the House Merchant Marine and Fisheries Committee are all involved. The companies want such legislation before they make major investments in commercial development. At the same time, from the point of view of overall U.S. national interest, there is little need for developing these minerals now as opposed to later. On the other hand, proceeding with such legislation might well provide a stimulus to the Law of the Sea negotiations, given the fact that the U.S. has a major technological lead.

Finally, there is a long standing dispute between the Commerce and Interior Departments over which agency should have the lead with respect to deep seabed development. Interior claims that deep seabed development should be an extension of their mining responsibilities on land. OMB staff tend to agree with this view. Commerce maintains that deep seabed mining is an oceans matter and not at all like mining on public lands. Commerce also points to Reorganization Act #4 of 1970 and President Nixon's transmittal statement to buttress their view. This dispute has not been resolved. (See more detailed issue paper on this jurisdictional issue).

Issue

How and in what manner should the U.S. proceed with U.S. deep seabed legislation? What should be the role of Commerce in this regard?

Analysis of Issue

Secretary Richardson has decided to proceed with legislation in the first session of the 95th Congress, but leave the opportunity to review the results of the next session of the Law of the Sea Conference prior to enactment. A more detailed paper sets out a scenario which has been recommended to the NSC Law of the Sea Task Force.

There are many unanswered questions about the kind of legislation that ought to be developed. Companies maintain that they will need investment guarantees against future treaty provisions which render their deep seabed investments and operations impossible or uneconomic. They also maintain that they need authorizations to specific sites vis-a-vis other U.S. nationals. NOAA, in conjunction with the Office of Energy and Strategic Resource Policy, is undertaking a series of detailed analyses of these provisions. They should be completed by the end of the year.

From a bureaucratic point of view, given the dispute between Interior and Commerce on policy leadership in connection with deep seabed issues, it is important for Commerce to take a leadership role in developing interim legislation.

Schedule

The Law of the Sea Task Force plans to submit a decision paper on this subject to the President in December. The Congress reconvenes January 4. Senate Commerce and Interior staff are working on draft legislation now.

ENERGY ISSUES RELATED TO
IMPLEMENTATION OF THE COASTAL ZONE MANAGEMENT ACT

Background

As described in more detail in the NOAA portion of this document, the Coastal Zone Management Act provides for a program of coastal zone planning and management, with Federal grants to assist states in this respect. Many elements of the Nation's energy "crisis", have a focus on the coastal zone. These include the development of the gas and oil resources of the outer continental shelves; the coastal siting of nuclear and conventional power plants; and the handling, storage and transportation of petroleum products including deep water ports, liquefied natural gas operations, and, in certain instances, coastal refineries and petrochemical complexes.

In most instances, successful solutions to the siting problems associated with these facilities will require a high level of intergovernmental cooperation with positive steps being taken by all three levels of government. Unfortunately, in many cases, energy-related activities clearly in the national interest are being delayed or prevented due to the lack of an adequate framework for the resolution of conflicts between levels of government and the general lack of agreement on coastal goals and objectives.

The Coastal Zone Management Act was designed to provide substantial help in facilitating a rational resolution of conflicts such as these. The Coastal Zone Management program and the related Coastal Energy Impact Program (CEIP), which was authorized by the amendments of July 1976, relate to these energy issues in two important ways. First, the basic Coastal Zone Management Act itself requires that states adequately consider the national interests involved in the siting of facilities necessary to meet requirements which are other than local in nature in their coastal management programs. To insure that this is the case, the Act requires states to fully involve appropriate Federal agencies in the development of their state programs. Second, Federal financial assistance is available through CEIP to assist coastal states and communities in energy siting planning and dealing with impacts in their coastal zones caused by coastal energy activity.

A set of issues involves assurance that States adequately take into account national interests in developing their coastal zone management plans and the implementation of the CEIP. As discussed in the NOAA section of this report, draft regulations have recently been issued on CEIP. Given the complexity of the legislation that ultimately resulted from the melding of the rather different views held by the Ford Administration and the Congress, it is not surprising that the draft regulations are somewhat complex. A number of concerns with regard to the draft CEIP regulations have been raised.

Issues

1. How do we assure adequate attention being paid to the national interest in approving coastal zone management plans?

2. What effort, if any, should be made to simplify or modify the Coastal Energy Impact Program and its draft regulations?

3. What position should be taken with regard to submission of a supplemental Fiscal 1977 appropriation request to the Congress at an early date (January 1977)?

Analysis

1. National Interest

Proposed Coastal Zone Management (CZM) Programs are coordinated extensively, in accordance with the Act, with other involved agencies prior to their approval. FEA, Interior, HUD and EPA are all consulted with as a part of the approval process, and their comments are taken into account. Nevertheless, the American Petroleum Institute (API) has written the Secretary and alleged that the Office of Coastal Zone Management does not provide fully for consideration of the national interest as regards energy facilities when approving State CZM plans. API urges that the ERC undertake a coordinated review of all future State CZM programs as they affect national energy needs prior to the approval by NOAA.

While ERC review as such of CZM Programs prior to Commerce approval would probably not be desirable or feasible other than in exceptional cases, the Office of the Secretary should review such Programs from a national interest point of view prior to approval. The current delegation of Secretarial authority with regard to such approval provides for Secretarial consultation; this is probably sufficient oversight authority.

2. Coastal Energy Impact Fund--Process

The Coastal Energy Impact Program, as developed in draft regulations, is consistent with legislative intent but admittedly is rather complex. Given the Congressional differences involved in the passage of these provisions (there were major differences between the House and Senate versions), and the desire of the Louisiana Congressional delegation to open up the bill to provide additional monies for Louisiana, it is probably undesirable to attempt to simplify the provisions legislatively. Nevertheless, the Office of the Secretary will want to insure that administrative discretion is exercised as fully as possible to make the program as simple as possible for impacted states and communities. The Office of the Secretary should maintain oversight to assure that red tape is minimized.

Concerning the discretion proposed in the regulations for NOAA in dispensing formula grants (a very controversial provision with some segments of Congress), it is difficult to see how DOC responsibilities under the National Environmental Policy Act can be met without using the procedures proposed. Nonetheless, NOAA should be encouraged to go as far as possible in providing pre-clearance and pre-assessment procedures to make the disbursement of these funds as close to automatic as possible.

3. Coastal Energy Impact Fund--Funding

(See NOAA issue paper on coastal zone management for discussion.)

BROADENED EMPLOYEE STOCK OWNERSHIP

BACKGROUND: Over the past three years Congress has passed five bills containing incentives for employee stock ownership plans (ESOPs): (1) the Regional Rail Reorganization Act of 1973 gives ConRail authority to purchase its common stock through an ESOP for distribution to employees; (2) the Employee Retirement Income Security Act of 1974 exempts ESOPs from prohibition on certain transactions between pension trustees and employees, and singles out ESOPs as the only employee benefit plan which can be used as a vehicle for corporate borrowing; (3) the Trade Act of 1974 gives preference for the Commerce Department loan guarantees to corporations that agree to place 25 percent of loans into a qualified trust under an ESOP; (4) the Tax Reduction Act of 1975 provides an additional 1 percent to the investment tax credit if the dollars saved are put into an ESOP; and (5) the Tax Reform Act of 1976 extends and liberalizes the ESOP incentives contained in the Tax Reduction Act. Most of the legislative encouragement to ESOPs has been at the insistence of Senator Russell Long, Chairman of the Senate Committee on Finance. A number of U.S. Senators, including Hubert Humphrey and Jacob Javits, have sought to expand the focus of stock ownership beyond present employee stock ownership plans. Senator Javits has announced plans to introduce legislation in this area under a program he calls "People's Capitalist". The Ford Administration favored the concept of broader stock ownership in principal, but objected to some of the features of present ESOPs. The Office of Policy Development and Coordination worked with Treasury in developing the Ford Administration's alternative, called Broadened Stock Ownership Plans (BSOPs). This alternative was not included in the final version of the Tax Reform Act voted on by Congress.

In its 1976 Annual Report, the Joint Economic Committee (JEC) recommended establishing a national policy to pursue the goal of broadened capital ownership. This policy would encourage more citizens to become owners of capital and provide an expanded source of equity financing for corporations. The goal stated by the JEC is generally accepted, but there is considerable disagreement over the means to achieve this goal. Plans proposed to date, including the ESOPs currently favored by legislation, favor specific categories of workers at the expense of others and often compromise accepted principals on diversification of risk.

Wealth in the U.S. is highly concentrated, with the richest one percent of the population owning about one-fourth of all personally-held assets. Programs that broadened stock ownership could simultaneously begin to reduce the concentration of wealth and provide a new source of badly needed equity capital. To be successful, such programs should stimulate net new saving and avoid exposing savings of middle- and low-income workers to unacceptable risk. Unfortunately, programs that are widely available and relatively simple, e.g. a tax reduction for purchases of stock, are likely to result in a shifting in savings rather than net new saving by households. Likewise, programs that encourage a worker to purchase stock in their employing company are likely to make a positive contribution to increased productivity, but also involve the greatest degree of concentration of risk. If the employing company fails, the worker may lose his job and his savings cushion. Given the complexity of the problems encountered in developing an acceptable Federal program to promote stock ownership, it is quite possible that any attempts by the Government to alter equity ownership may result in a solution less acceptable than the current market determined distribution. This conclusion, if widely accepted, would require Government to reduce and eventually withdraw its present incentives to ESOPs.

SCHEDULE: Legislation to promote stock ownership will be introduced early in the 95th Congress, and it is expected that the issue will be discussed in Congressional Hearings and in privately-sponsored meetings. The Office of Policy Development and Coordination will be in a position to comment on stock ownership legislation and can offer analyses on specific provisions of plans, as appropriate. This activity is expected to continue throughout 1977. In addition, OPDC is monitoring studies being conducted by the Economic Development Administration on ESOPs that have been assisted by Commerce Department funds.

LOCKS AND DAM 26

Background:

Locks and Dam 26 (L&D 26) is located on the Mississippi River at Alton, Illinois. The Mississippi River Inland Waterway System is a major link to the national transportation system, serving the central United States and tying together the agricultural Middle West, the industrial East, the Great Lakes, and the Gulf of Mexico over the Intracoastal Waterway System. L&D 26 is an integral part of and a vital link in the Mississippi River Waterway System. By virtue of its location just north of the confluence of the Missouri and Mississippi Rivers, its position controls commodity movements between the Upper and Lower Mississippi River.

The existing structure (nearly 40 years old) has deteriorated to the point that its replacement or rehabilitation is now necessary. In June 1976, L&D 26 was the subject of hearings held by the Subcommittee on Water Resources, Senate Public Works Committee, when the Subcommittee examined S. 3506. Authorization of funds for the replacement of L&D 26 was included in S. 3823 (the Water Resources Development Act of 1976) in the 94th Congress prior to the floor conference on the bill. The relevant sections were removed from the bill when agreement could not be reached on the sections related to user charges on inland waterways and L&D 26.

Issue:

The issue of L&D 26 concerns the Corps of Engineers (COE) proposal to replace, as opposed to rehabilitating, the existing facility. The proponents such as agricultural interests, shippers, and inland waterway operators have urged that the locks and dam be replaced with a new and larger structure while the opponents, railroad interests and some environmental groups, have argued that the present facility has sufficient capacity to meet near-term needs (through 1985), and only rehabilitation of the existing structure is economically justified.

Given the action of the 94th Congress, the issue of L&D 26 has apparently become inextricably associated with the issue of user charges on inland waterway operators.

Analysis of Issue:

The Corps of Engineers has completed its analysis on L&D 26. The General Accounting Office, at the request of the Subcommittee on Water Resources reviewed the COE analysis and found it to be acceptable. The railroad interests disagree with the COE findings in relation to costs of rehabilitation, present capacity constraints, and projected traffic flows. The Secretary of Commerce agreed with the Administration's recommendation of August 24, 1976, to authorize funds for the replacement of the existing structure and therefore believes the COE estimates to be the most reliable. The Secretary has not publicly supported the replacement of L&D 26 although such support was given in Secretarial correspondence of September 7, 1976.

Schedule:

The issue of L&D 26 should reach the 95th Congress in the first or second quarter of 1977. The Secretary should consider making a decision to support or not support (publicly) the replacement of L&D 26 during the first quarter of 1977.

USER CHARGES ON INLAND WATERWAYS

Background:

Over the past forty years administrations have forwarded proposed legislation to Congress which would place user charges on inland waterway operators in order to recoup all or part of the cost to the Federal Government for the operation, maintenance, and repair (OM&R), and new construction related to our Nation's inland waterway systems. Each time such legislation has been submitted, Congress has refused to pass favorably upon it.

The present effort to impose user charges on inland waterways, initiated and supported by the Office of Management and Budget (OMB) and the Department of Transportation (DOT), is the strongest in the past thirty years. The Senate proposed that user charges be placed on commercial craft on the inland waterways in Section 5 of S. 3823. Section 5 was removed in the floor conference prior to the passage of the Water Resources Development Act of 1976.

OMB has proposed that user charges be implemented which would recover 50 percent of construction costs and 100 percent of OM&R costs. The Administration has stated that it desired to recoup approximately $80 million of the OM&R costs of the inland waterway system.

Issue:

The fundamental issue is whether there should or should not be user charges on inland waterways. If one takes a pro position, i.e., implementation of user charges, the questions of the level (10%, 20%, 50%, 100%) and type of user charge, e.g., segment toll fee or fuel tax, come to the fore.

Analysis of Issue:

The Corps of Engineers, the Department of Commerce (MarAd), DOT,and OMB are currently examining the user charge issue. It is anticipated that the OMB staff study will be completed in early 1977 (first quarter) or very late 1976. The Commerce study can be described as a minimal effort which identifies the data and information required to analyze the user charge question. The anticipated completion date of the MarAd study is the first half of December 1976. DOT's study, through the Transportation Systems Center, Cambridge, Massachusetts, should be completed during the first quarter of 1977.

The National Transportation Policy Study Commission (NTPSC), created in the National Highway Act of 1976 and just now initiating its two-year study, will very likely examine the question of user charges. The completion date of the NTPSC report is December 31, 1978.

The official position of the Department of Commerce as stated in the Water Resources Council's Section 80(c) Study, October 24, 1975 is:

> Cost sharing, with possible implications for user charges as a means of cost recovery for the economic development objective, is sound fiscal policy and is supported by this Department. However, the economic impact of user charges and their impact on other national policies such as transportation policy must be examined before any implementation.

<u>Schedule</u>:

The issue will be discussed in the 95th Congress. Resolution of the issue will probably not come before the end of this Congress and could wait until the NTPSC reports in December of 1978. Commerce should continue to monitor all ongoing study activities and formulate a position during the last half of 1977. If there is an effort to resolve the issue earlier than that indicated above, Commerce should recommend that the decision wait until the NTPSC has an opportunity to report on its findings.

EXTENDING RIGHT OF PRIVACY LEGISLATION TO THE PRIVATE SECTOR

BACKGROUND: The concept of the right of privacy -- as a legal precept -- has a long and interesting history, beginning in 1890 with a Harvard Law Review article coauthored by Louis Brandeis. The judicial development has evolved over the years, but it was not until 1965 that the Supreme Court first agreed that there was indeed a constitutional right to privacy.

Congress has also dealt with privacy protection in statutes dealing with census data, crime control, credit reporting, and education information. And most importantly, in 1974 Congress passed the Privacy Act dealing with the information handling practices of Federal Agencies.

The Privacy Act does not include the handling of personal information in the private sector, but it did create the Privacy Protection Study Commission to assess the information handling practices of private business.

The Department has been involved in the area of privacy since the fall of 1974 when the Domestic Council Committee on the Right of Privacy extended its support to the Department in conducting a "survey and analysis of the cost, service, and possibly other effects of extending various privacy safeguards to the business sector."

The survey initially was designed to determine the nature and significance of present or potential intrusions on an individual's right of privacy in selected private industries, to determine if legislative actions are needed to correct present, and to prevent future, intrusions, and to determine the cost to private industry of implementing such actions. Subsequent findings have caused this study to be modified.

ISSUE: Should right of privacy legislation be extended to the private sector?

ANALYSIS OF ISSUE: As a concept one can hardly be opposed to the protection of individual privacy. However, when one applies that concept to the protection of personal information which exists in the information systems of American business, the sheer magnitude of the problem is staggering.

The trend is toward the gathering of more and more information, given the growth of service industries and the widespread computerization of data. Businesses need information in order to provide the goods and services the public has come to expect. The concern is whether all the information which is gathered is really needed and whether it is properly protected from unauthorized disclosure.

The major piece of legislation which was introduced in the 94th Congress, H.R. 1984, will not likely be reintroduced in the 95th Congress until the Privacy Protection Study Commission has issued its final report in June 1977. And if it is reintroduced then, it is likely to be greatly modified.

The Chamber of Commerce of the U.S. has issued a policy declaration calling for voluntary, not mandated, methods for protecting privacy. The Chamber maintains that a need for informational privacy legislation has not been demonstrated.

The Department of Commerce has not developed a policy on the extension of right of privacy legislation to private industry.

SCHEDULE: The Privacy Protection Study Commission will issue its report in June 1977.

ENSURING ADEQUATE HEALTH CARE AT REASONABLE COSTS

Background

The current debate on national health policy focuses on two major issues: how rapidly escalating medical care costs can best be contained and whether legislation should be enacted to extend coverage for basic medical services and (or) for "catastrophic" illnesses to those who are not now protected.

The discussion of these problems follows twenty-five years, especially the last decade, of dramatic growth in public sector and private sector programs aimed at meeting demands from employees, the poor, and the aged for financial protection from health risks. Today, labor and management in private industry pay approximately $20 billion per year for health insurance for workers and their families. The federal government, through the Medicaid and Medicare programs, spends nearly $25 billion annually on health care.

Issue

The purpose of a policy paper currently being completed on this subject is to examine alternative solutions to the problems of rising costs and inadequate coverage and to recommend future policy directions. Two strategies for cost containment--increased regulation and market improvement (including increased consumer price sensitivity and increased competition in the health delivery system)--will be examined. Several approaches to expanding health coverage will be explored including a federalized national health insurance program; government mandated employee minimum health benefit packages; and government financed coverage provided by a pool of private health insurers.

Analysis

All data have been collected. Policy statements, issue analyses, and analytic studies have been obtained from appropriate offices in the federal government, as well as from private associations, interest groups, private industry, labor unions, and research institutes.

Detailed recommendations will be presented in the final report; however, the general conclusions are that efforts to contain costs must include elements of both regulatory and market improvement approaches and that expanded coverage in the form of national health insurance should include a role for the public and private sectors. It may be desirable to phase in such a proposal over a period of years, focusing on cost control measures in the earliest stage.

Schedule

A final draft of the paper will be completed by January 1, 1977. This will be available to inform the debate on "national health insurance" which can be expected to reopen early in 1977.

IMPACT OF NATIONAL HEALTH INSURANCE ON BUSINESS

BACKGROUND: Competition among private insurance companies created a system that could work well for employment-based groups and for low health-risk individuals. There are, however, gaps in coverage. Limits of $10,000 to $25,000 are common, and many policies cover only 30 to 60 days of hospitalization. Physician coverage is often restricted to surgical and other inpatient services. Among 147 million nonaged persons with private insurance,

all have some hospital coverage,
98% have some inhospital physician's coverage,
62% have some outpatient physician's coverage,
69% have some outpatient drug coverage,
22% have some nursing home coverage, and
10% have some dental coverage.

Medicare and Medicaid were enacted in 1965 to provide coverage for the aged and for certain segments of the poor, and Federal involvement in the health field has been expanding. Some form of National Health Insurance seems certain to be adopted soon.

In fiscal 1975, Americans spent over $120 billion (8.3% of GNP) on health care; in fiscal 1960, we spent $26 billion (5.2% of GNP). It has been estimated that, if no National Health plan is adopted, spending on health care in fiscal 1980 will be $223 billion. Adoption of a National Health program in mid-1977 is estimated to add $10 billion to this figure in the case of the Long-Ribicoff plan, $11 billion in the case of the Health Insurance Association of America plan, $11 billion in the case of the Nixon Administration plan, $20 billion in the case of the American Medical Association plan, $25 billion in the case of the AFL-CIO backed bill, and $25 billion for the American Hospital Association plan.

ISSUE: The cost of a National Health Insurance program and the method of financing this cost can have significant impacts on business costs. Cost increases will either be passed off on labor in the form of smaller wage increases, passed off on consumers in the form of higher prices, and/or absorbed by business. Unless the costs are passed off entirely on employees the competitive disadvantage of small business is likely to increase. We assume that the proportion of businesses offering health care insurance as an employee fringe benefit increases with the size of the business. All methods of finance currently being discussed either increase small business' costs by a larger percentage than large business' costs (because large businesses already incur the cost), or decrease large business' costs by a larger percentage than small business costs (if, for example, a health program is financed using general tax revenues, large businesses have a cost eliminated that small businesses do not incur).

Minority-owned businesses tend to be small so their competitive disadvantage is likely to increase. The price of products produced by small businesses relative to the prices of products produced by large businesses will rise, leading to some redistribution of resources away from the former to the latter.

A national health program is likely to affect the already high inflation rate in the health sector and to affect the already rising proportion of GNP that is spent on health services. If the program adopted has no constraints on hospital and physician charges then these prices will increase substantially. If a fee schedule is enacted it will establish minimum fees and price inflation will be even higher. If schedule fees are made mandatory, significant inflationary impacts may be avoided. Any change in the rate of inflation in the health services industry is likely to affect the distribution of resources between this and other industries and the effects on other industries is likely to be uneven.

ANALYSIS OF ISSUE: We had appraised cost estimates of the major national health programs and judged them to be unreliable. One set of new estimates is now available and another set is being prepared. Our appraisal of the new estimates has recently begun.

We appraised the inflationary potential of a sharp increase in demand for medical and surgical equipment. With the possible exception of x-ray equipment and tubes we regard potential price increases as within acceptable bounds.

We estimated the incidence of an increase in social security taxes, one of the methods of financing a National Health program. Our finding is that when employer and employee taxes each rise by one percent,employers are able to pass about one half of their tax increase off on their employees. This finding conflicts with published estimates that employers pass the entire tax off on their employees. We will continue to try to obtain more reliable results on tax incidence.

SCHEDULE: Our appraisal of the new estimates of the costs of major health insurance programs will be available in the first quarter of 1977. In the second quarter of 1977, we will have new estimates available of the incidence of an increase of social security taxes.

THE CIVIL AIR TRANSPORT INDUSTRY:
IMPLICATIONS FOR U.S. GOVERNMENT POLICY OF
DOMESTIC AND INTERNATIONAL TRENDS

Background

U.S. manufacturers have produced approximately 80 percent of the world's (excluding the USSR's) commercial jet aircraft fleet. In 1975, U.S. exports of commercial air transports approached $3 billion. For a number of years, air transports have been our country's leading single manufactured export item. Roughly 340,000 Americans are directly or indirectly employed in the production of commercial transports and their engines.

For the first time, however, since the end of World War II the continued success and prosperity of the American air transport manufacturing industry stands in serious jeopardy. The nature of the threat is twofold. Foreign manufacturers of airframes and engines, supported by their home governments, are now mounting a major challenge to the longstanding dominance of the United States in the production of commercial transports. At the same time, in response to rising foreign competition and to rising foreign government pressure, U.S. manufacturers of airframes and engines are establishing increasing numbers of technology and production sharing arrangements with non-U.S. producers.

Three interrelated sets of events account for this state of affairs. In the first place, the financial condition of commercial air carriers, both domestic and foreign, has deteriorated steadily since the late 1960s. The upshot is that airlines, regardless of nationality, are hard pressed to finance their capital requirements. Yet, in order to replace their aging fleets, to meet noise abatement rules, and to cover fleet expansion, their capital needs in the next 10 years will be, it is estimated, $45 billion (in 1975 dollars). Under the circumstances, competition to sell to the airlines, at home and abroad, is bound to increase.

Second, the costs and risks of developing new commercial air transports are reaching prohibitive levels. Developing, from scratch, a new airliner now entails outlays of $1-$2 billion. U.S. manufacturers have not started a major new transport production program in the 1970s.

Third, for a number of reasons, foreign manufacturers may soon be able to capture a large share of the commercial transport market. Traffic growth outside the United States now exceeds that within the United States; our country is no longer the most important market. West European governments are trying to forge a European-wide transport manufacturing industry to match the economies of scale of American producers. Foreign governments (unlike the U.S. Government) are directly subsidizing their aircraft manufacturing sectors. Finally, they are insisting upon the internationalization of transport production, which means that, in exchange for purchases of U.S. aircraft, they are getting U.S. technology and jobs. In the future, if the process continues, they may well be able to outcompete U.S. producers for the world airliner market.

Issues

The purpose of this study is to answer the following questions:

(1) How will the current domestic and international trends in commercial aviation, at both the carrier and manufacturer level, affect U.S. air transport manufacturers and the U.S. economy at large?

(2) What policy options are available to the U.S. Government to respond to foreign government insistence upon co-production, offsets, technology transfer, or other international production arrangements as prerequisites for access to their home markets? What will be the cost/benefits of these alternative options and the likelihood of their success?

(3) What policies should the U.S. Government pursue in light of increasing competition from foreign air transport manufacturers?

(4) What policies, beyond existing ones, are foreign governments likely to adopt to foster their domestic aircraft manufacturing industries, and how can the U.S. Government respond to these foreign initiatives?

(5) What multilateral steps can the United States take to preserve the vitality of domestic air carriers and air transport manufacturers and, simultaneously, to maintain international harmony?

Analysis of Issues

Project just beginning.

GOVERNMENT POLICY AND INTERNATIONAL CIVIL AVIATION

Background

In June 1976, the United Kingdom denounced the Bermuda Agreement which has governed aviation relations between the United States and the United Kingdom during the past 30 years and which has been the standard for other bilateral aviation agreements. A number of other foreign countries have also indicated that they are unhappy with their existing air transportation agreements with the United States. As a consequence, the United States is presently engaged in wide-ranging aviation negotiations with the United Kingdom and Japan, and it is expected that additional bilateral talks will soon be initiated.

Under the Bermuda Agreement, countries agree on a bilateral exchange of rights to serve international air routes. The Agreement provides that passenger fares and freight charges are set by means of negotiations among the carriers and that the fares and charges are subject to review by the aviation authorities of the national governments at issue. On the other hand, the Agreement provides that the individual carriers are largely free to determine the amounts of capacity that they provide to serve their authorized international routes.

The current round of negotiations follows an extended period during which the international airlines have suffered large financial losses. These losses have occurred because of the substantial increases in air transport capacity that were made in the late 1960s and early 1970s, the recent sharp increases in fuel prices, and the recent worldwide economic recession. The losses have been of particular concern to the U.S. carriers which, unlike many of their foreign counterparts, do not receive large Government subsidies.

Issue

At issue in the bilateral negotiations is the question of whether the Bermuda Agreement should be retained or whether there should be a new agreement which would provide for strict controls on the amounts of air transport capacity provided on international routes and which would result in changes in the shares of the international air transport market which are supplied by the various countries.

Analysis of Issue

When the Bermuda Agreement was first negotiated, the United States was by far the dominant power in the area of commercial aviation. Since that time, other countries have become major aviation powers. Many of these countries have become dissatisfied with the type of aviation relations that have prevailed under the Bermuda Agreement.

The British argue that under the Bermuda Agreement there has been an incentive for airlines to provide too much capacity on international routes and that the Agreement has resulted in an unfair division among countries of the benefits from international aviation. The British argue that only one U.S. scheduled air carrier should serve any given U.S.-U.K. route. The British want to be assured that their market share will increase in the coming years and that excess air transportation capacity in the Atlantic market will be eliminated by means of strict controls on capacity.

Although a number of other countries are also dissatisfied with the Bermuda Agreement, these countries have their own points of view on what should replace it. The Japanese Government is anxious to obtain rights for its airline to provide direct air service from Japan to a number of U.S. cities for which it does not now have such rights. The Japanese also favor a reduction in the number of U.S. carriers that serve the Japanese market.

In contrast with the positions advocated by foreign governments, the United States continues to support the general principles contained in the Bermuda Agreement. The United States favors competition in the international aviation market and believes that the airlines would be less responsive to the needs of the public if strict controls on capacity were instituted. The United States does not believe that it is necessary for governments to impose strict controls on aviation capacity in order to bring capacity and demand in line with each other. Further, the United States does not accept the British argument that the U.S. and U.K. air carriers should necessarily have equal shares of the profits from air transportation between the two countries.

The Department of Commerce has an interest in the Bermuda negotiations because of its responsibilities for promoting tourism and international trade. Moreover, the negotiations are of concern to this Department because of their possible impact on the demand for aircraft manufactured in this country. The Department of Commerce has participated in the interagency work relating to the bilateral negotiations with the British. This Department has reviewed position papers and analyses prepared by the Civil Aeronautics Board and the Department of Transportation concerning the costs and benefits to the United States of the various likely alternative types of international aviation agreements.

<u>Schedule</u>

The Bermuda Agreement between the United States and the United Kingdom will expire in June 1977. Efforts are underway to reach a new agreement before that time. An exchange of analytical work relating to the negotiations is scheduled to take place in London in December 1976. It is not likely, however, that much serious bargaining will take place until early in 1977.

In the coming months, it will be necessary for the Department of Commerce to determine its position on what would be an acceptable outcome in the negotiations. In addition, it may be necessary for this Department to participate in the determination of appropriate retaliatory actions to take against the British if agreement is not reached by the spring of 1977. Further, if the negotiations have not been concluded by June 1977, a decision will have to be made on whether to extend for a temporary period the current aviation agreement with the British.

As the negotiations proceed, the Civil Aeronautics Board will be reassessing the structure of air transport routes between the United States and Europe. In the coming year, the Board will probably issue a new decision in its Transatlantic Route Proceeding to take account of the Bermuda negotiations. When the decision is issued, the Department of Commerce will be called upon to assist in the Presidential review of the decision.

SHIFTS IN THE INFLATION-UNEMPLOYMENT TRADE-OFF RELATIONSHIP

BACKGROUND: The trade-off relationship between inflation and unemployment has held the attention of economists for decades, and to many researchers that relationship is still in search of a theory. Recent investigation by OPDC of the trade-off over the course of the business cycle suggests that it has shifted. The new configuration means that a given rate of inflation is associated with a higher rate of unemployment and that a given reduction in unemployment is accompanied by a greater increase in the inflation rate than otherwise. Several hypotheses can be offered for this shift. They include modifications in the structure of productive activity, the new role of women in part-time and full-time employment, responses to previous economic policies, and changes in the quality of education and other skill-producing mechanisms.

Unemployment may be a problem which cannot be properly analyzed at the macro level, and there is some evidence to support this claim. For example, unemployment rates differ substantially by industry. The rate for construction has recently averaged 14.7% while durable manufacturing and services evidenced 8.3% and 5.7% respectively. Demographics may also have an effect. The unemployment rate for white males aged 20 years and over is 4.9%; for the nonwhite counterpart it is 9.5%. Regional variation in the unemployment rate can also be readily established. This uneven distribution of unemployment suggests that a study which treats it as homogeneous and which proposes indiscriminate fiscal and monetary actions may be wide of the mark.

The trend toward indexing reinforces the argument for a disaggregated approach. Indexing is the practice of tying a specific price or income payment to some index of the general price level, the purpose being to preserve purchasing power. Labor contracts, for example, frequently contain "escalator" clauses. Indexing, by affecting the relative prices of inputs, may alter the mix of capital and labor in the production process thereby influencing unemployment. It may also impact prices. But since the practice of indexing differs across industries, its nuances would likely be lost to a macro analysis of all industries combined.

ISSUE: The basic issue relates to the changes which have apparently occurred in the unemployment pattern by industry, by demographic group, and by geographic region. These changes should be firmly established and their causes explored. The results obtained are likely to suggest the types of policy tools which could effectively reduce unemployment without adversely affecting prices.

ANALYSIS OF ISSUE: Data have already been gathered on the inflation-unemployment relationship for all expansions and contractions since World War II. Preliminary examination of those data appears to indicate the shift described in the background section. Literature and data on regional unemployment have been reviewed, and information on the work disincentives implicit in the current welfare structure has been studied.

SCHEDULE: The issue of unemployment envisioned by this project is complex, and a comprehensive analysis of its many facets will require considerable time. Final resolution is not expected in fiscal year 1977. Nevertheless, substantial progress is anticipated within that period. Specifically, changes in the unemployment structure will have been established and tentative causal forces isolated. Policy recommendations will also have been provisionally formulated.

Unemployment is a central question to be confronted by the new Administration and the 95th Congress. Legislative proposals dealing with the problem, notably the Humphrey-Hawkins and Dole-Scott bills, are reportedly to be reintroduced in some form, and they should elicit considerable debate. A decided effort will be made to time the progress of this project to that debate.

NATIONAL ECONOMIC PLANNING:
PROCESSES, TARGETS, TECHNIQUES

BACKGROUND: The purpose of economic planning is to reduce the uncertainty of policy action. It does this by identifying targets which are attainable and by matching policy instruments to those targets. To avoid contradictory actions and to assure that important goals are not neglected, coordination among Government agencies is required.

Planning is not a free good; it comes at a price, part of which is explicit. The planning apparatus must be housed, staffed, and supplied, and these costs vary depending upon the comprehensiveness of the planning process. Part of the price is implicit. Expectations may be formed prematurely, only to be frustrated at a later date. But set against these costs are the benefits of planning: greater certainty and improved effectiveness of policy. Taken together, these costs and benefits should provide a guide for determining an optimun level of planning.

There has been a trend, especially in recent years, to sharpen and institutionalize the planning process. An early landmark piece of legislation was the Employment Act of 1946. It created the Council of Economic Advisers and a Joint Committee on the Economic Report to plan and coordinate economic policies consistent with the intentions of the Act. More recently, the Congressional Budget Act of 1974 established a structure for planning and coordinating budgetary policies while the House Concurrent Resolution 133, passed in March 1975, provided a means for improving coordination between Congress and the Federal Reserve. The most controversial legislative proposal which links planning, targets, and instruments is the Humphrey-Hawkins bill. An outgrowth of the Humphrey-Javits proposal, Humphrey-Hawkins specifies numerical targets, identifies policy instruments to be used in attaining targets, and calls for the establishment of a comprehensive economic planning apparatus. A response to Humphrey-Hawkins was offered by Senators Dole and Scott, their bill being considerably less ambitious. Both proposals reportedly will be reintroduced in the 95th Congress.

ISSUE: This project examines the economic triangle embodied in legislative proposals. Specifically, it attempts to determine if stated targets can be achieved given existing economic conditions. It looks at the policy instruments suggested for use in reaching the targets and also at the amount of planning effort involved. It endeavors to ascertain if the added cost of planning is justified by the benefits received.

A proposal contained in Humphrey-Hawkins and echoed in the Democratic Platform deserves special analysis; namely, that requiring public employment, public works projects, and direct stimulus to the private sector to be phased in automatically when unemployment rises and phased out as it declines. The use of automatic rules rather than discretionary instruments has been an issue long debated by economists. An analysis of the merits of automatics in the present case seems essential.

ANALYSIS OF ISSUE: A paper has been prepared which presents fundamentals of economic planning. It also reviews the planning features of major legislation and proposals beginning with the Employment Act of 1946. Special emphasis is given to the Humphrey-Hawkins bill. To ascertain the relative advantages of the suggested automatic stabilizers, a dynamic macro model has been created. Although the model is elementary, its structure lends itself to a straightforward accommodation of the automatic mechanism envisioned. More sophisticated models would be considered should the need arise.

SCHEDULE: Since the project entails evaluating proposed legislation, its progress is largely determined by the legislative work of Congress. It is a continuing project. Nevertheless, the model incorporating the automatic stabilizers of Humphrey-Hawkins should be operational by Summer 1977.

FIRST AMENDMENT CONSIDERATIONS RELATING TO FEDERAL FINANCIAL ASSISTANCE FOR CABLE-TV SYSTEMS

BACKGROUND: The principal forms of Federal assistance to cable-TV are: 1) guaranteed loans; 2) direct loans; 3) grants; and 4) technical and managerial assistance.

ISSUE: The lack of uniform policies and practices among Federal Agencies regarding the extension of direct loans or business loan guarantees to cable television enterprises has created growing confusion in the private sector and generated congressional concern. This situation stems mainly from differences among lending agencies in their perception of First Amendment constraints on Federal financial assistance to the telecommunications media and, also, from the absence of clear Executive Branch policy guidance in this regard.

ANALYSIS OF ISSUE: Cited below are examples of problems arising from the current lack of overall Executive Branch policy guidelines.

In August 1975, the Gary Communications Group, a minority CATV venture in Gary, Indiana, applied for an Economic Development Administration (EDA) business loan of $398,000 to help finance the second development stage of its cable-TV enterprise. The application was rejected by EDA January 22, 1975, on two grounds: 1) the applicant had failed to provide satisfactory assurances that the loan would be repaid as required by the Public Works and Economic Development Act (PWEDA); and 2) First Amendment considerations prevented EDA from making such a loan.

The First Amendment prohibits abridgement of freedom of speech, and also applies to broadcast communication by television. Consequently, EDA took the position that it is unwise for U.S. Government Agencies to finance or financially assist private enterprise active in the dissemination of opinion molding ideas or values. In effect, EDA stressed that the First Amendment requires a policy against assisting communications media companies, since possible foreclosure action by the Government against a firm might be perceived in the eyes of the public as being motivated by objectives contrary to First Amendment rights.

The aforementioned has resulted in considerable divergence of financial assistance policies between the EDA and the Office of Minority Business Enterprise (OMBE). In this example, OMBE stressed that the Gary CATV system is not a communications media company, but rather a conduit through which previously broadcast television signals or programs originated outside its control are relayed and retransmitted. Thus, OMBE asserted, the "free speech" clause of the First Amendment does not present any impediments to EDA assistance of the Gary CATV system.

Outside the Department, there is also a divergency of policy. Among Agencies engaged in assisting small cable-TV enterprises, for example, the position of the SBA most closely parallels the current policy adopted by EDA, i.e., denial of direct loans to media enterprises that engage in programming -- including cable-TV.

In this instance, however, the Small Business Administration was sharply criticized in a Report by the House Subcommittee on SBA Oversight and Minority Enterprise of the Committee on Small Business recommending that the SBA "make every appropriate effort to strike an equitable balance between its statutory duty to assist small business and constitutional obligations under the First Amendment."

On the other hand, a more flexible position appears to have been adopted by the Farmer's Home Administration. Although the FHA does not make direct loans to private entrepreneurs engaged in the business of promoting rural cable television, they do make direct loans to CATV public entities and nonprofit institutions (cooperatives). Also, the FHA Business and Industrial Loan Division makes loan guarantees to private entrepreneurs involved in developing CATV systems.

The Department of Commerce has proposed the establishment of an interagency task force to study this problem. The Office of Telecommunications Policy (OTP) presently has under consideration the recommendation that it assume a coordinating role of the task force.

In the meantime, an in-house Commerce paper on the First Amendment problem, as described above, is being prepared with possible input from the Federal Communications Commission, Department of Agriculture and the Small Business Administration.

<u>SCHEDULE</u>: Date of completion for this paper is estimated to be December 31, 1976. The First Amendment issues paper would represent an initial input to the proposed interagency task force on cable-TV.

IMPROVING MUNICIPAL AND SOCIAL SERVICES:
THE PRIVATE SECTOR'S ROLE

Background

Soaring costs and limited resources of local governments necessitate the exploration of organizational alternatives for the provision of local services. In selected circumstances "privatization," in one or another of its multiple forms, may be a way to ease the mounting burden on public authorities.

Issue

Simply stated the issue is whether, where, and how to involve the private sector more actively in meeting local service needs. On one hand, the limitations of conventional service mechanisms seem painfully apparent. As public service monopolies, measuring success in votes instead of profits, local governments frequently lack the incentive to improve productivity. Their flexibility and initiative are often impaired by rigid procedural formulae and bureaucratic aversion to risk.

"Privatization" may be a way to circumvent these obstacles. However, efforts to utilize the private sector more fully are beset by three major problems. The first of these is the paucity of comparative data on the merits of private versus public service delivery. In general, it is simply not clear which services should be "privatized" or how. A second problem is that, even where particular case studies have projected cost savings as a result of "privatization," municipal officials frequently lack the technical expertise to contract effectively. This is at least partially a result of weaknesses in service contracting technology itself, especially in regard to the specification and measurement of performance. Finally, even where evidence exists and technological obstacles can be overcome, efforts to increase the private sector's role in supplying local services may be hindered by the resistance of local bureaucracies to organizational innovation, as well as by unsupportive state and federal legal structures, and by the opposition of public employee unions.

Analysis

The initial draft of a paper on the private economy's role in supplying municipal and social services is nearing completion. Its first segment, which deals principally with the epistemological issues, contains: 1) a review and assessment of existing research; 2) a summary or organizational options for local service delivery; 3) a summary and assessment of the principal arguments for and against "privatization"; 4) an explanation of the difficulty of making valid public/private delivery cost comparisons; 5) a consideration of *a priori* indices of suitable candidates for "privatization." A second segment is devoted to a service-by-service summary and evaluation of the best available evidence bearing on the frequency and the cost advantage (or disadvantage) of "privatization," and on the opportunities for further private involvement. The services considered are: solid waste collection; public works; police; fire; ambulence; transportation; parks and recreation; education; and miscellaneous technical services; as well as social services provided under Title XX of the Social Security Act. A third segment discusses technological problems of effective purchases-of-service contracting; while a fourth reviews some of the related political obstacles. A final segment is devoted to conclusions and recommendations.

Positions tentatively advanced on the basis of research and analysis so far completed include the following:

Encouraging comparative cost studies for particular functions in individual jurisdictions, as well as encouraging efforts to develop better performance measurements;

Fostering the development of contract management capacity among local officials, including the development and dissemination of model contracts;

Recognizing that organizational patterns of service delivery tend to be very resistant to change and that, therefore, with certain exceptions (notably those cases where structual changes promise clear and substantial productivity gains, where immediate human and material costs are limited, and where political opposition is not severe), the greatest potential for "privatization" may lie outside the range of traditional municipal services, in those areas where demand for conventional services exceeds the response capacity of local governments, or where there is a market for more flexible and variegated local services, or where technological developments or federal legislation have created new service requirements.

<u>Schedule</u>

The paper mentioned above will be completed by the first of January.

There is no special deadline for Departmental action on the issue of the private sector's role in providing local services. However, it would be appropriate for the Department to consider such action soon, and to do so in the context of a general and continuing interest in realizing the fullest potential of the private economy to help solve social problems.

CORPORATE SOCIAL RESPONSIBILITY: THE GOVERNMENT'S ROLE

Background

Government has proven itself to be a limited instrument for servicing an expanding range of perceived public needs. To bring the nation's energy and resourcefulness fully to bear in responding to social problems requires exploration of new ways to utilize the flexibility, initiative, and managerial expertise of the private sector.

Issues

From the national perspective, the notion of "corporate social responsibility" poses two basic issues. First, what is the appropriate role of private business in meeting social needs, and what structure of public incentives and penalties will evoke the private sector's most productive effort in the public behalf. And second, what role can the Department of Commerce play in stimulating and supporting this effort.

Analysis

Initial steps have been taken to prepare a paper on current corporate contributions to the public interest, and a structure of incentives and penalties likely to promote greater efforts within the private economy to meet social needs.

Portions of the proposed paper have already been drafted. These include: a discussion of the scope and content of corporate social responsibility; a review of the private sector's performance of traditional production and distribution functions; a summary and assessment of the corporate record in providing employee benefits, equal opportunity employment, and charitable contributions, as well as in recognizing the full social costs of production; and a survey and analysis of the private sector's response to governmentally provided incentives (including especially, purchases, taxes, and subsidies).

Schedule

Work remains to be done in refining the material presently in draft, in conceptualizing a structure of incentives and penalties and in developing a set of recommendations for departmental action in encouraging and facilitating social responsibility in the private sector. It seems clear preliminarily, however, that the department has, and ought to have a role to play in this area.