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# AVAILABILITY OF GASOLINE

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HEARING

BEFORE THE

SUBCOMMITTEE ON  
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON  
INTERSTATE AND FOREIGN COMMERCE  
HOUSE OF REPRESENTATIVES

NINETY-FIFTH CONGRESS

SECOND SESSION

DECEMBER 14, 1978

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Committee on Interstate and Foreign Commerce



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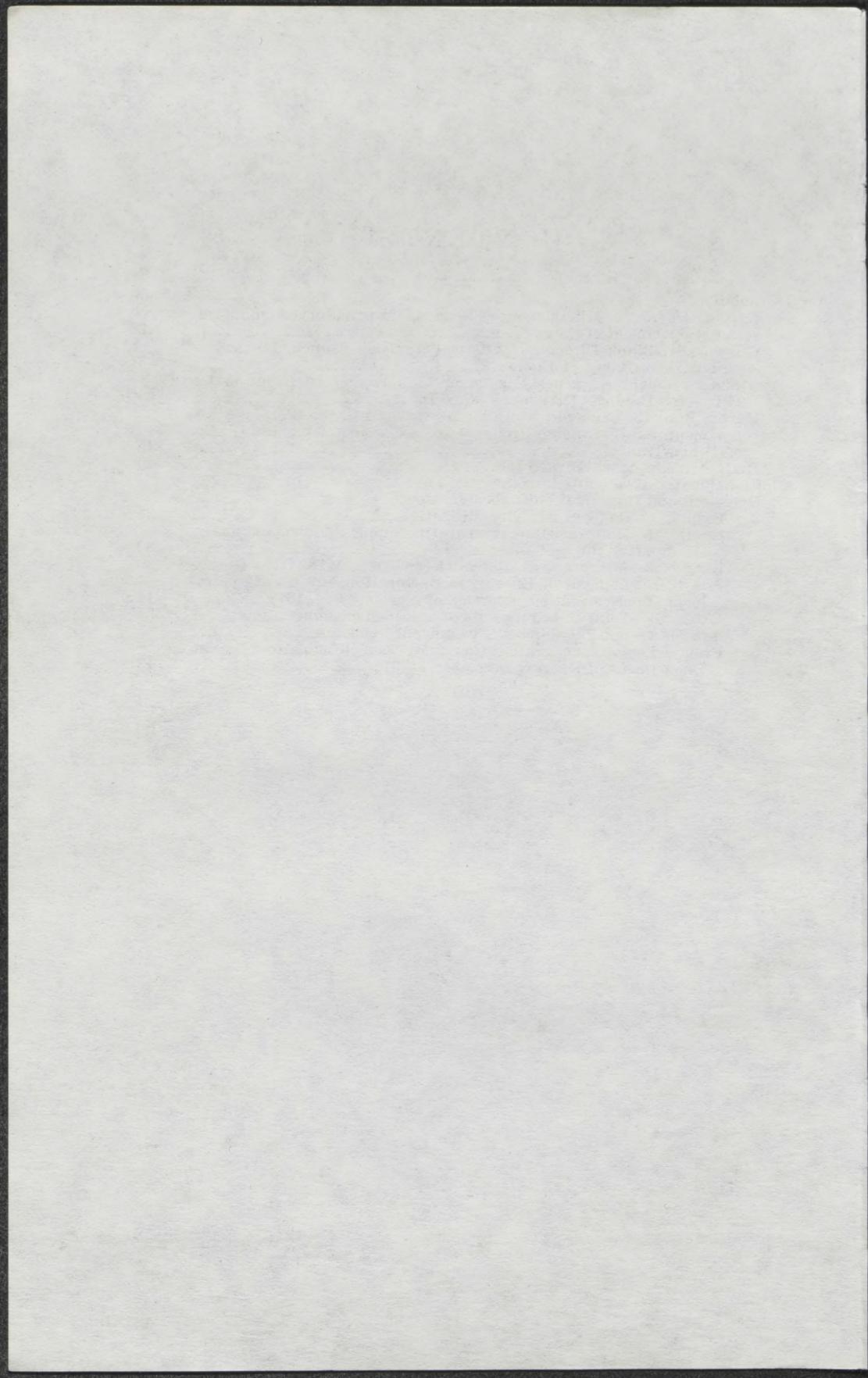
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## AVAILABILITY OF GASOLINE

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THURSDAY, DECEMBER 14, 1978

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,  
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,  
*Erie, Pa.*

The subcommittee met, pursuant to notice, at 9 a.m., in the Erie City Council Chamber, Hon. Marc L. Marks (Hon. John E. Moss, chairman), presiding.

Mr. WALGREN [presiding]. In the interest of time we will start without delay. Particularly the witnesses from the Department of Energy have a commitment later on this afternoon in Washington and have asked that they be excused no later than 10:45 a.m. So, we will proceed directly.

As the Democratic member of the Subcommittee on Oversight and Investigations, I represent the chairman of that subcommittee, a committee of the Interstate and Foreign Commerce Committee of the House of Representatives. The chairman is John E. Moss, who cannot be with us today because of other commitments in California.

Today's hearing on gasoline supplies was initiated by my Republican colleague, Marc Marks, who is to be commended for focusing the subcommittee's attention on this vital issue which affects literally every man, woman, and child in the Nation.

The witnesses this morning will be David Bardin, the Administrator of the Economic Regulatory Administration of the Department of Energy; he is accompanied by William Gillespie, who is the Director of the Statistical Analysis Branch with regard to fuels regulation.

Following Mr. Bardin will be Donald Graham, the general manager of supply and distribution for petroleum products of Texaco, and third, Mr. Paul Hertel, who is the manager of the Strategic Assessment Planning Department for Sun Petroleum Products Co.

The testimony that we will be developing today in Erie will be of direct benefit to the Congress in dealing with potential shortages of gasoline—the lifeblood of the Nation's transportation system—and in weighing the benefits of the administration's and the Department of Energy's proposal to remove price controls on gasoline, a multibillion dollar decision that may or may not result in significantly increased supplies.

Considerations that are critical to the public are in direct conflict with each other when it comes to the economics of gasoline supply. On the one hand the public is told by industry spokesmen and some voices within the administration that prices must be decontrolled to

assure continuing supplies of automotive fuel, but if prices are decontrolled, the price of gas will increase—a price increase that can only be seen as threatening to feed the fuel of inflationary attitudes and feelings within the country. Estimates are that decontrol will add up to 4 cents per gallon, with each penny representing over \$1 billion of increased cost to the American public to buy the same amount of gas.

Given the failure of other Government estimates in the past, I am afraid we can have little confidence that the actual cost may not be much more.

The present position of the Congress, as clearly stated in the law that reached out to control prices in 1973, is that when we face a shortage, that is no time to decontrol prices. The policy essentially is that taking the lid off prices during a severe shortage will predictably lead to prices being driven sharply upward in reaction to scarce supply. It is based on the public's strong commonsense belief—and that is based on experience—that when most prices go up, they never come back down.

These hearings are being held in an atmosphere of deep suspicion of the oil industry felt by the public, a suspicion that shortages have been contrived and manipulated to increase prices, only to miraculously disappear after costs go up. The public suspicion of the oil industry is heightened by the appearance of administered prices, where an industry is dominated by a few large firms who have market power, eliminating competition by their size alone because it is simply easier for everyone to follow the price leader. This is especially true in industries like the oil industry where, for all practical purposes, there is plenty of demand to go around. This atmosphere of public suspicion and distrust makes it particularly difficult to legislate wisely.

This hearing has been designed to provide a solid, factual foundation relating to present gas supplies, and the adequacy of gas supplies in the immediate future. The hearing record will be a base for future hearings by other committees and this committee in the Congress that will consider the wisdom of the administration's gasoline decontrol proposal, expected early this winter.

I am particularly pleased that Congressman Marks is pursuing this problem at the outset because in the 2 years he has served in the Congress he has developed a reputation for being most thoughtful and fairminded, and the conclusions that can be drawn from his effort will be given great weight by our other colleagues. I would like to say what a pleasure it is for me, as a "Pittsburgher," to be in Erie; and at this point would turn the chair over to Congressman Marks for his opening statement and pursuit of the witnesses.

Thank you very much.

Mr. MARKS [presiding]. Thank you very much, Doug, Congressman Walgren. I, too, am appreciative of the fact that you have taken of your time to come here and be with me in Erie, Pa., to hear testimony which, we hope, will help us here and the Nation in the serious situation that apparently now exists, and may exist in the future.

Before proceeding with the hearing I would like to have the record indicate both Congressman Walgren's and my deep appreciation to the two most professional staff people I have ever worked with, have the benefit of working with, and will continue to have the benefit of

working with in the future on this committee, and that is the gentleman on my right, Dr. John Galloway and the gentleman just to the left of Congressman Walgren, Mr. Stephen Sims. Ladies and gentlemen, these are the people who do the very, very hard work preliminarily so that those of us who chair, and who participate in these hearings, may not only know what they are looking for and talking about, but may be able to get to the heart of the problem.

I would like if I may, Doug, to take this opportunity to welcome personally a gentleman who is not only a very close friend, but who has great responsibility in Erie County, and that, of course, is our county executive, Mr. Robbie Robinson who is sitting in the back. Robbie, we welcome you and appreciate the fact that you would take a moment out of your busy day to come and be with us. I am just sorry that Denise is not here, she is Robbie's wife—and by the way, Doug, a very beautiful and talented lady.

I am sure we will have the privilege of having with us, before the morning is over, the mayor of Erie, the third largest city in New York, Mayor Louis Tullio. When Lou walks in, I might forewarn the witnesses, we will break in to introduce him to all of you; he is an extraordinary man and a close friend of mine.

I think at this time—for the sake of time, we are already 15 minutes late, and we will try to run as quickly as we can—we would now like to have the witnesses for the Department of Energy. Before that I would like, for the record, to make one other comment. That is that I am very sorry—both Doug and I are very sorry—that the chairman of this subcommittee, a most outstanding American, and a person who has served the country for so many years, John Moss, of California, could not be present with us today. Chairman Moss would have desired very much to be here in person; unfortunately his responsibilities to his family took first priority. As most of you know, he is unfortunately leaving us, this is John Moss' last term in Congress. The record should indicate forever that I am deeply indebted to that gentleman who not only served his country so very, very well, but who has made it so very comfortable for me, as a Republican freshman Congressman, to work—and work closely—with this very outstanding committee. I am most appreciative to him.

The purpose of today's hearing is to assess gasoline supplies in light of recent announced cutbacks in gasoline deliveries by major oil companies; to determine the reason for these cutbacks, and to make appropriate policy recommendations.

In the past several weeks concern has arisen over the availability of gasoline—now and for the remainder of next year. At present, and I want to emphasize this, motorists are able to obtain the gasoline they need, although not necessarily at the first station they enter. There is no need for motorists to panic and to strive to keep their tanks reasonably full, an act which in itself could conceivably upset the present delicate supply situation.

At present Shell Oil Co., the Nation's largest gasoline retailer, is reducing gasoline sales and reducing the octane level of gasoline in the Midwest. Amoco, Mobil, and Conoco are presently limiting their sales of unleaded premium gasoline, while Texaco has submitted to the Department of Energy contingency plans to sharply reduce gasoline deliveries.

If the current, unprecedented, high nonsummer demand for gasoline continues, a genuine gasoline shortage could develop by next spring. Oil company executives, while emphasizing the limited and spot nature of current gasoline shortages, have been quick to blame the Federal Government for the present state of affairs.

The oil companies tell us that gasoline price controls have discouraged investment in new equipment while at the same time environmental restrictions on the use of lead in gasoline have reduced the efficiency of their refinery operations. If the oil companies are to be believed, gasoline price controls must be eliminated and steps to reduce the lead content of gasoline must be slowed, or possibly even abandoned altogether.

There are those who suspect that industry has deliberately created a minor gasoline shortage, while pointing to the threat of more serious future shortages to pressure the Government into removing gasoline price controls and restrictions on the use of lead in gasoline.

One of the purposes of today's hearing will be to test the validity of my alternative theory which attributes the present gasoline supply situation to a fundamental miscalculation on the part of the petroleum industry last winter, that led to a dramatic reduction in petroleum product inventories and a decision to run refineries at less than full capacity. When gasoline demand was higher this summer and fall than expected, the oil companies were not fully able to compensate for their previous actions.

If my thesis is correct, gasoline price controls and restrictions on the use of lead in gasoline are not the cause of the current gasoline supply situation. If I am correct, moreover, the public is deserving of a full explanation from the petroleum industry concerning its failure to correctly forecast gasoline demand and its resulting mismanagement of gasoline inventories and production throughout the first 5 months of this year.

I welcome the opportunity to test my thesis with a leading official of the Department of Energy and representatives of two major oil companies today. I again want to thank Congressman Douglas Walgren, of Pittsburgh, for being with me for this purpose.

Now, if our friends are able to get their equipment together without disturbing us any further, we will be happy to proceed.

Our first witnesses, ladies and gentlemen, will be Mr. David J. Bardin, who is the Administrator of the Economic Regulatory Administration, Department of Energy, and who is accompanied by Mr. William Gillespie, who is the Director of the Statistical Analysis Branch, Fuels Regulation, Department of Energy.

I might say for the record, also, that Mr. Bardin is one of the bright, relatively young stars on the national scene, whose voluntary appearance here today to be interrogated is certainly appreciated by this committee. This seems appropriate. Mr. Bardin, since even the very bright and powerful star, Venus, is being interrogated these days.

May I ask you gentlemen to stand, raise your right hand, and be sworn, please?

Do you swear by Almighty God to tell the whole truth and nothing but the truth, so help you God?

Mr. BARDIN. I do.

Mr. GILLESPIE. I do.

Mr. MARKS. Please, be seated.

Mr. Bardin, in the interest of time—which is particularly pressing to you and, as I say, we appreciate your coming here—I know that you have a prepared statement. We would appreciate very much if you would enter that rather lengthy statement into the record [see p. 7], summarize for a couple of minutes; and we would like to limit your introduction, perhaps, to 4 or 5 minutes at most.

**TESTIMONY OF DAVID J. BARDIN, ADMINISTRATOR, ECONOMIC REGULATORY ADMINISTRATION, DEPARTMENT OF ENERGY; ACCOMPANIED BY WILLIAM GILLESPIE, DIRECTOR, STATISTICAL ANALYSIS BRANCH, FUELS REGULATION, DOE**

Mr. BARDIN. Thank you very much, Congressman Marks. I would appreciate your including the entire 19-page statement in the record. There are extra copies in the room. I believe the subcommittee staff is making them available.

Let me say at the outset to you and Congressman Walgren how pleased I am to be back in Pennsylvania, which is a State which is a neighbor of my home State of New Jersey, and with whose officials I have had the pleasure and privilege of working closely over my years in State government in New Jersey. I have not been in Erie for a quarter of a century—I hope I will not have to wait another quarter of a century before I have a chance to visit back here.

I want to congratulate this subcommittee and its distinguished chairman for holding field hearings. I think we just need to get out into the field where we can expose our ideas on a more general footing to the people whom we serve in Federal Government, State government, county government, or municipal government. I do appreciate the chance to meet the leaders of Erie County and municipal government here.

The topic we are discussing is basically one of demand and supply for one of the key ingredients of our energy economy. It is a complicated economy with literally tens of thousands of parts on the supply side, and tens of millions of parts on the demand side. There are over a hundred million gasoline-consuming cars in our country, which is the consumption side of the picture.

Looking at the question broadly, at the present time supplies of motor gasoline appear adequate to meet national need. There are some problems being experienced by individual refiners—which we can discuss in the course of this morning's session. However, barring a major and unexpected interruption of supply—such as an embargo—we see no possibility of a generalized gasoline shortage and long gasoline lines between now and next summer. There may be instances where an individual motorist pulls up to a filling station and finds that it has run out of a particular type or grade of gasoline that he wants; but that same product will be available at stations down the street.

We are monitoring this situation closely and will continue to do so, to identify isolated shortages as they occur, and to use short-term measures described in my statement to alleviate any problems.

One thing all of us can do—and I cannot urge that strongly enough—is in our own behavior as consumers to drive prudently; to

observe the 55 mile-per-hour speed limit, and to curtail the unnecessary, so that we conserve this valuable fuel resource and in the process save our pocketbook.

Now, we are particularly concerned about gasoline supplies for a longer term. When you make predictions, you try to make predictions about the future, there is a great element of uncertainty. Our projections through 1980 indicate supplies will be adequate, but barely so.

So, looking at the driving season, the peaks in the coming summer of 1979, and then again in the driving season that will peak again in 1980, there is that question.

Let me sketch out with the benefit of these charts which I have brought what seems to us some of the key ingredients of understanding our situation today.

Mr. MARKS. Mr. Bardin, we would appreciate your doing that, and perhaps at that point you might terminate your statement and go into questions, so that we may proceed.

Mr. BARDIN. We are engaged in the process of converting the automobile fleet of America in large measure to cars which require unleaded gasoline. Not all the new cars, but most of the new cars, require unleaded gasoline; even half of the imported cars require unleaded gasoline.

As a result, unleaded gasoline is a product whose demand is growing, at a faster rate than virtually any other commodity on the American scene. From 19 percent of the gasoline pool in 1976 unleaded, it grew to 25 percent in 1977. The EPA forecast has been that it will be 35 percent of the pool this year. We believe it is going to reach 36, certainly, by the end of the year. The forecast for next year is 42 percent. The forecast for 1980 is 50 percent; and you will have three-quarters of the gasoline unleaded by the middle 1980's.

Now, the unleaded gasoline is virtually zero-lead gasoline. Lead is an additive to gasoline. It is a cheap addition which raises the octane of the gasoline without indulging in expensive reforming in the refinery.

The remaining leaded gasoline may contain as much as 2 grams or more of lead per gallon. The average lead in the gasoline is also controlled by EPA air quality regulations in addition to that factor, and that is important to bear in mind because these air quality regulations are due to require a very substantial drop in the lead. This will create supply constraints in the months ahead.

When you look around the country you see that the proportionate use of unleaded gasoline varies from State to State and region to region—it is a function of the age of the car; the kind of car; the use of the pick-up vehicle as contrasted with the individual vehicle; farm and off-road vehicles. You see that in Pennsylvania in calendar year 1977 between 25 and 30 percent of the gasoline was unleaded. But, if you look to May of this year, Pennsylvania has risen to the 30 to 35-percent category. What you see, comparing the States, is a very steady, continued rise in the unleaded demand.

Indeed, if you look at the total demand for gasoline—and now we come to a critical point—you have a continued increase, absolute increase, in the gallons of unleaded gasoline; you have an actual decrease in the gallons of leaded gasoline, at a time when you have a slight increase in the overall gasoline use.

Much of the petroleum industry has expected the total demand to reach a peak around 1980, and decline. The view of the Department of Energy at this time is that our total demand for gasoline is likely to continue to increase slightly into the 1980's; that the decline in the demand for leaded will continue; and the increase in the demand for unleaded will continue.

Now, this is going to mean a tightness in the market unless new refining capacity is installed. There are three kinds of approaches that you can envision, Mr. Chairman.

One is constraint on the total demand by conservation. Two is increase in supply through a different management of existing resources, or investment in additional refining resources. The refining industry at this moment appears to be straining at something like 93 to 94 percent of capacity, which is a very high utilization as contrasted to where we were a year ago and what is normal. Finally, there is a possibility of an inadequacy—a failure to perform adequately in the long run, particularly beyond 1980.

The analogy I would leave you with is the difficulty you have in preparing the cost of an immediate step as against the price you pay later down the road for not taking it. We are confronted with choices in a world where gasoline prices will go up in any event because of factors involving crude oil. We are confronted with choices as to how our national Government in administering its laws arranged prices, and incentives to pricing laws, environmental laws and others, for this oil-refining industry.

If we hold the line in a way which discourages adequate production of gasoline, we may save the consumer paying today a few dollars more a year for his gasoline supplies. And yet, we may pay much more dearly in terms of our economy, our tourism industry, our farms, our homes later on.

Take the analogy of an oil change. Any time I defer buying a quart of oil for an oil change, there is no question I have saved that money. I can measure exactly how much I have saved. But, if I let it go to the point where I do damage to my engine, it can cost me much, much more dearly; and yet, it is difficult today, at the time I am trying to save the money—I can tell just how many cents a quart I pay for oil—to figure out how much more it will cost me for the kind of damage my engine might sustain.

I will be pleased to try to answer the committee's questions.

[Mr. Bardin's prepared statement follows:]

STATEMENT OF DAVID J. BARDIN, ADMINISTRATOR, ECONOMIC REGULATORY  
ADMINISTRATION, DEPARTMENT OF ENERGY

Mr. Chairman and members of the Committee, I appreciate the opportunity to appear today to discuss gasoline supplies. I intend first to provide a general summary of the situation both now and into the 1980's and the factors which we believe affect this situation. I will then provide a more detailed description of the overall situation and put into perspective some of the specific and well publicized problems that are being experienced by a few firms.

SUMMARY OF THE PRESENT AND FUTURE GASOLINE SUPPLY SITUATION

At the present time, supplies of motor gasoline appear to be adequate to meet national needs. There are some problems being experienced by individual refiners—which I will discuss in more detail later. However, barring a major and unexpected interruption of supply, such as an embargo, I see no possibility of a

generalized gasoline shortage and long gasoline lines between now and next summer. There may be instances where an individual motorist will pull into a station that has run out of a particular grade of gasoline, but the same product will be available at stations down the street. We are continuing to monitor this situation closely, and, if isolated shortages occur, we have available to us a number of short-term measures I will describe later that can help to alleviate any problem. And, over and above anything the Government can do, all of us should exercise restraint in our use of gasoline; plainly, we use too much.

We are particularly concerned about gasoline supplies for the longer term. In making predictions about the future, surprises are always possible. However, our projections through 1980 indicate that supplies will be adequate but barely so. Beyond 1980, the demand for unleaded gasoline, and therefore the need for additional refining equipment to produce it, will continue to grow.

The present price and allocation controls on gasoline have contributed to the lack of refinery investment of the last few years, and to possible supply shortages beyond 1980. These regulations discourage investment and vigorous competition to expand gasoline supplies. For this reason, the Department of Energy is considering the elimination of the present regulations. Without such action, the future holds the increasing possibility of supply shortages, long gasoline lines or ultimately higher gasoline prices and greater inconveniences for the motoring public than elimination of the current regulatory system. Let me now provide a more detailed description of how we see the present gasoline situation.

#### CURRENT GASOLINE SUPPLIES

At the present time, primary gasoline stocks (that is, the amount of gasoline in refiners' storage tanks) are lower than normal for this time of year. Although refineries have been running at near capacity, gasoline inventories have not yet been built up to normal levels. The reason is simple. Traditionally, the so-called summer driving season ends with Labor Day, and demand falls sharply thereafter. This year, however, after a summer gasoline demand that exceeded all expectations, demand remained high into the fall, reaching almost 7.5 million barrels per day during the four week period ending November 17. Compared to the same four week period during 1977, demand was up over 5 percent. Over the past three months, demand exceeded last year's levels by a total of 11 million barrels.

Demand finally tapered during the last two weeks in November, and stocks are now increasing. As an example, for the four weeks ending November 24, production exceeded demand by 400,000 barrels per day. With the onset of winter, which should reduce gasoline demand further, plus the continued operation of refineries at high gasoline production levels, we should see gasoline stocks increase to adequate levels by next spring, so that we can go through the summer without shortages.

#### PROBLEMS OF INDIVIDUAL REFINERS

I would now like to turn to some of the specific problems being experienced by individual refiners. The most widely known is that of the Shell Oil Company. In November, Shell indicated to DOE that it was having supply problems and would soon have to allocate its available supply among its wholesale and retail dealers. On November 16 Shell requested from the Department's Office of Hearings and Appeals permission to allocate gasoline on the basis of actual 1977 deliveries to its customers or 1972 base period deliveries, whichever were higher. The primary purpose for the request would be to enable Shell to make allocations to its present retailers in a manner that more closely reflects existing marketing patterns.

Shell was granted temporary relief until December 12. Following a Departmental hearing last Friday, the Office of Hearings and Appeals determined to further extend the relief until January 15, 1979.

In the meantime, on November 30 Shell announced that it would indeed have to allocate its gasoline, and said it had enough to supply its dealers with only 75 percent of their 1977 levels. On December 6 it revised its earlier estimate of the supply it would have available and raised its allocation fraction to 85 percent.

In view of Shell's prominence in the gasoline market (it has approximately 8 percent of the national gasoline market), its announcement caused substantial interest and comment, including speculation about the possibility of more widespread gasoline shortages.

Shell is one of only three refiners that offers a so-called "premium" or "super regular" unleaded gasoline—that is, with an octane substantially above the average regular unleaded gasoline. Widespread consumer dissatisfaction with unleaded regular gasoline, due to real or perceived performance effects in the high compression engines of newer cars, has resulted in higher than expected demand for high octane unleaded gasoline, which apparently has contributed to Shell's problem.

Texaco has also filed with the Office of Hearings and Appeals an application for permission to supply its wholesale and retail dealers on the basis of last year's purchases, rather than those in 1972. Texaco alleged in its application a reduction in its current gasoline stocks due to unexpected losses of production, and it says it is uncertain about its ability in the future to augment supply. Texaco's application appears to be precautionary, however, for, unlike Shell, it has not yet announced that it will have to allocate gasoline among its dealers.

Two other refiners—Conoco and Arco—have recently asked to be relieved of the obligation—under DOE's allocation regulations—to sell gasoline to certain other refiners so they can meet the needs of their own dealers. A hearing will be held on both applications this Friday. In the meantime, Conoco, whose request was based on the lost production at its refinery in Denver due to a fire, has been granted the relief it requested on a temporary basis.

Conoco is now able to meet its supply obligations to its dealers for December. Arco's situation is not so serious as to require interim relief pending a hearing on the merits.

The supply problems presented by Shell, Conoco and perhaps Texaco—while potentially serious for those firms and their wholesale and retail dealers—appear to be unique and are not in themselves an indication of a general supply shortage. This is not to say that we are sanguine about the situation in general, however. The minute we got a hint that there may be a supply problem, we called major refiners in individually to explain their supply situation. In general, these discussions indicated that refiners are concerned that gasoline supplies might be tight by next summer if the unexpectedly higher demand we have been experiencing does not diminish and gasoline stocks are not adequately replenished before next summer's driving season. In order to obtain a better picture of the current gasoline market in general and what we can expect over the next several months, DOE is conducting a public conference this Friday, December 15. Domestic refiners and marketers and interested States, members of Congress, consumer groups, and other Federal agencies have been invited to participate.

#### FUTURE GASOLINE SUPPLIES

We have also been looking beyond the short term gasoline supply situation in an effort to formulate the Government's regulatory policy for the future. Our best judgment is that if DOE regulations remain in effect and EPA adheres to its present lead phasedown schedule, gasoline supplies will be tight in 1980. However, even under pessimistic assumptions of low auto fleet efficiency and high demand we believe that domestic refiners have the capability to assure that gasoline will be available in sufficient quantities to avoid any problem of long lines forming at retail stations. There are several actions available to refiners to stretch octane and make marginal improvements in supply. For example, Shell has acknowledged that it can stretch its gasoline supplies if, in addition to high octane unleaded, it also manufactures a regular unleaded gasoline for those customers who do not need the higher octane.

If automobile efficiency standards required by the Department of Transportation are met, total demand for gasoline should stabilize and begin to decline after 1980. This phenomenon, which was widely expected following establishment of the fleet fuel efficiency standards, has in itself operated to discourage the development of added refinery capacity. However, actual vehicle fuel economy has been somewhat less than many forecasters' original expectations. Therefore, it is not prudent to assume that there will be sharply declining demand in 1981 and beyond.

Even if total gasoline demand does decline, there will be both a relative and absolute increase in the demand for unleaded gasoline, which means that additional gasoline refining equipment will be necessary. This year unleaded gasoline demand is expected to reach about 36 percent of all gasoline demands. By 1980, demand for unleaded gasoline will increase to 50 percent, and by 1985 will be 78 percent. In addition, automobile manufacturers have been meeting fuel effi-

ciency standards by increasing engine compression ratios, which require higher octane unleaded gasoline. In the additional refining process required for such gasoline, the total supply shrinks. Therefore, we are unlikely to see the kind of supply abundance that characterized 1977 until at least the mid-1980's. Thus, the need for investment in future refining capacity, and for flexibility in production, marketing, distribution, and pricing practices remains great.

#### REGULATIONS COMPOUND THE PROBLEM

The current DOE allocation and price controls on motor gasoline directly contribute to the gasoline supply problem. Seven years of price controls and general regulatory uncertainty have inhibited investment in the refinery expansions and improvements needed to make unleaded gasoline, or to make gasoline-range material out of heavy and high sulfur domestic crude oils. Refiners are allowed to depreciate new investments, but may not recover a return on all investments greater than the total amount they realized as of May 15, 1973. Refiners assert this has discouraged investment in the gasoline manufacturing capacity needed now to produce the high octane blending stocks for unleaded gasoline. This seems to be borne out by the general lack of major refinery expansions and improvements scheduled for the next two years.

Second, price controls have discouraged refinery improvements that increase efficiency, since they require that the full amount of such cost savings be reflected in the form of lower allowable prices. When we create an environment for an industry in which it does not realize a benefit from increased efficiency, we discourage improvements in production techniques that would stretch gasoline supplies.

Third, the regulations do not reflect the fact that during the period of controls cost increases relative to production of gasoline have been much greater than for other products. These cost increases reflect the increased need for unleaded gasoline production capacity.

The regulations limit refiners to passing through on gasoline only a volumetrically proportional share of their increased costs. When these regulations were put into effect there was very little unleaded gasoline. As I have indicated, the demand for unleaded gasoline will continue to increase.

Finally, the regulations take a snapshot of each refiner's prices as of May 15, 1973, and allow it to add certain costs to that price, no matter how that company's relative pricing or competitive circumstances have changed in the meantime. In 1974 this system was simple and seemed reasonably fair for a short-term price control program. Approaching 1979, it is becoming increasingly outmoded and inequitable.

DOE's allocation regulations are also antiquated. In their current form, allocation regulations do not assist refiners in achieving equitable distribution of a modest shortage of gasoline, as is demonstrated by the Shell, Texaco, and Conoco cases. The principal problem is the 1972 base period for the allocation program. In six years, the sales volumes of firms supplied by refiners have changed markedly, not only in absolute amounts but relative to each other. These changes reflect, among other things, the changes in gasoline marketing that have occurred over the past six years, such as the greatly increased marketing of unleaded gasoline and "gas and go" and other types of self-service operations.

Thus, the application of the present rules to a current shortage leaves some jobbers and dealers with considerably more supply than they need based upon recent sales experience, and others with considerably less. The resulting inequities tend to fall more heavily on the smallest independent retail dealers and marketers.

The effect of DOE regulations on supply has been compounded by the impacts of EPA regulations. We do not question the need for strong environmental controls, but we think it is important to note that they impact on energy supply and demand.

One such restriction is the recent ban on the use of MMT, a manganese compound, in unleaded gasoline. MMT has been used as an antiknock additive in combination with lead for many years. In 1974, it became the exclusive antiknock additive in unleaded gasoline. Because of concern that the additive might be harmful to antipollution equipment, however, MMT concentration in unleaded gasoline was limited by the Clean Air Act amendments of 1977 to one-sixteenth gram per gallon, and, in September of this year, its use was banned entirely by

EPA. In order to make up for the loss of this additive, unleaded gasoline must undergo more processing, during which the total volume of the product shrinks. The effect of the permanent MMT ban on unleaded gasoline production exceeds 100,000 barrels per day.

The greatest effect on supply, however, comes from the EPA lead phasedown schedule. In addition to meeting demand for unleaded gasoline, refiners are required to reduce the average lead content of all gasoline. The current limit is 0.8 gram per gallon, but many refiners have temporary waivers from the requirement so that the current average lead level is estimated to be 1.2 grams per gallon. In October 1979, the limit will be reduced to 0.5 grams per gallon for virtually all gasoline production, and EPA has indicated that no large refiners will be granted waivers to this requirement.

In order to meet the 0.5 gram per gallon requirement, refiners will not only have to produce a higher percentage of unleaded gasoline, but they also will have to reduce lead levels in their leaded gasoline from about 1.8 grams per gallon currently to about 1.2 grams per gallon. We estimate that this reduction in the lead content in leaded gasoline will alone result in a reduction in gasoline supply of about 250,000 to 350,000 barrels per day beginning in October 1979.

In short, EPA regulations will significantly reduce the amount of gasoline which can be produced from our available refining capacity. These regulations may be appropriate from an environmental standpoint. However, we should confront the energy consequences of environmental controls squarely, as well as the environmental consequences of energy controls.

#### POTENTIAL SHORT-TERM ACTIONS

Although we do not predict general gasoline shortages this winter and spring, there are a number of actions the Federal Government can take to increase supply or reduce inequities should the situation warrant. The following illustrative list should not be taken as indicating that we believe all of these measures will turn out to be viable after further examination.

1. Implementation of the so-called gasoline price tilt regulation. This is a proposed rule that would allow refiners to pass through more than a volumetrically proportional share of costs to gasoline to reflect its higher increased costs. While not adding directly to increased supplies, the tilt should provide an incentive for refiners to purchase those crude oils and other feedstocks which yield more gasoline and heating oil but which are also higher in price. This action should in the short term also provide refiners with more gasoline pricing flexibility and decrease some of the upward pressure on heating oil prices. A final decision on a tilt rule will not be made, however, until we complete an environmental impact statement on it next month.

2. Grant temporary entitlements for imported gasoline, gasoline components and middle distillates. This would have the effect of increasing gasoline and middle distillate supplies by encouraging imports. A similar action was taken in February 1977 for home heating oil when shortages threatened in that severe winter.

3. Increase product imports from Canada. There is presently unused gasoline refining capacity in Canada. As a result of discussion between Secretary Schlesinger and Canadian energy officials the last several days, we are jointly exploring with the Canadian government how some of this capacity could be made available to supplement our domestic supplies.

4. Increase West Coast, Caribbean, and other U.S. refinery utilization. West Coast refineries are operating at a capacity utilization rate that is below the national average. If this utilization can be increased, additional gasoline and middle distillates could be produced. However, in order for West Coast refiners to increase their utilization rates, they will also have to find new markets for residual fuel oil, which will also be produced as a by-product. Demand for this additional residual fuel oil does not exist on the West Coast. We are looking at means to expand the market for this product in order that more gasoline and distillate production might be possible. We are also exploring what measures might be necessary to increase gasoline capacity utilization in Puerto Rico and other domestic locations.

5. Increase gasohol production. An increase in the production of gasohol, which is a blend of 90 percent unleaded gasoline and 10 percent ethanol, could help to stretch out gasoline supply. An incentive to increase gasohol production was contained in the National Energy Act, which reduced the Federal excise tax on

gasohol by 4 cents per gallon effective January 1, 1979. DOE also recently provided the means by which gasohol manufacturers can participate in the entitlements program. While increased gasohol production cannot have a large short-term impact on gasoline supplies nationwide, it could help to avert localized shortages in some areas if entitlements for gasohol were increased.

6. Update the gasoline allocation base period for all suppliers from 1972 to a more recent period in order to achieve a more equitable allocation of available supplies.

#### STEPS FOR THE LONG TERM

For the longer term, we believe the most important step DOE can take to alleviate future supply problems is to remove the unnecessarily restrictive DOE regulations on refiners and marketers of gasoline. In the short run deregulation can have limited impact, since most major additions to refining capacity require a lead time of 2 to 3 years. But if we deregulate gasoline in the next few months, it can help to prevent the continuation of a tight supply situation beyond 1980. This will be especially critical if the hoped for decline in gasoline consumption after 1981 does not materialize.

To be sure, deregulation will have a cost. In our draft environmental impact statement on deregulation, we estimated this cost in 1980 to be 3 to 4 cents more per gallon than would occur if no action were taken. This price is reasonable, considering the fact that what it buys for the consumer is increasing supplies over the next several years of those types of gasoline that will make our cars run cleaner and more efficiently.

Our draft EIS concludes that the expected environmental impacts of deregulation are relatively insignificant, involving a delay of one month or less in meeting National Ambient Air Quality Standards for oxidants and carbon monoxide in problem cities. We are currently receiving public comments on the draft EIS and will take them into account before publishing a final statement in January.

If deregulation is approved, we will need, and intend to prepare, improvements to our current information systems to warn us of unjustified price increases and potentials for unexpected environmental impacts. These improvements will give us the ability to design and take any actions needed to correct emerging problems of supply, guarantee fair and equitable prices, and maintain a secure and safe environment.

Mr. Chairman, this concludes my formal testimony. I would be pleased to answer any questions you may have.

Mr. MARKS. Thank you very much for that statement, Mr. Bardin. It is evident from your statement that the Department of Energy apparently has the view that gasoline supplies are currently adequate, although individual refiners are presently experiencing some difficulty.

My concern, frankly, relates to gasoline supplies not only through this winter, and spring, and summer which you, as I understand it, suggest in the Department of Energy's views will be more or less adequate, but I would like your candid answer to a direct question—what about after next summer?

Mr. BARDIN. I would like to answer about next summer, as well as after, Congressman Marks, because in my judgment we have to keep a very close examination of the situation, including next summer; I am going to lump that with the period you are asking about.

Mr. MARKS. We are specific, however. My question is directed to you, sir, what happens after next summer?

Mr. BARDIN. I just did not want to leave the inference that we are resting without concern at all about next summer; we are looking at a number of measures there.

It seems to me you have to focus throughout this winter on a related situation, the weather this winter as it affects the demands for distillates.

Mr. MARKS. Excuse me. So that there is no misunderstanding, we are talking about the summer that is approaching.

Mr. BARDIN. 1979.

Mr. MARKS. 1979 and subsequent to it.

Mr. BARDIN. Let us say, summer 1979, summer 1980 and thereafter.

We generally feel that our domestic refining industry can produce something like 66 percent of the crude oil as gasoline and distillate combined; distillate is the No. 2 home heating oil, diesel fuel, and other uses in the petrochemical industry.

There is some shift capability of 3 or 4 percentage points between gasoline and distillate. If you have a relatively lower demand for distillate, that gives you more capacity for gasoline, and vice versa. So, looking at summer 1979 or any summer, you want to look carefully at what happens during the winter in the distillate market because there tends to be an increase in demand for distillate as a result of the home heating use in the wintertime, whereas there tends to be the increased demand in the summertime because of the summer driving, for the gasoline.

I think you have to look carefully—we have to look carefully—at the import potential for distillate. Two winters ago when we had that very cold winter—that 1-in-100-years winter—with all of the problems of freeze-ups, natural gas shortages, we imported a great deal of extra distillates. That is one of the tools we may have available.

Indeed, it seems to me that now that the natural gas legislation has been passed and we have unified the interstate and intrastate market, there is an opportunity for natural gas to fill back in some of the commercial and industrial uses of distillates, and back off some of the distillate. If that succeeds in happening, if it can be done safely in enough gas service areas, we will see some easing of that pressure.

Mr. MARKS. For the sake of time, could you answer my question specifically? What is your candid opinion of the situation this coming summer of 1979 and subsequent to that, the fall of 1979 into the summer of 1980, specifically?

Mr. BARDIN. In my opinion the refining industry has it within its capacity, barring extraordinary breakdowns of their own equipment or extraordinary supply disruptions—such as embargoes from abroad—given the kinds of measures we have in mind that I enumerated, to get through those two summers and meet the demand that we anticipate and that we have sketched out, and that the Energy Information Administration of the Department of Energy has recently published in its report, its December report.

But, I think it will be a close situation, and we may have to import extra gasoline in order to get by and meet the demand in those two summer driving seasons.

Mr. MARKS. Mr. Bardin, I would like for you to review, if you will, please, an exhibit which I will have the staff give you. It is marked exhibit No. 3 and was assembled by the subcommittee staff. This exhibit consists of materials prepared by the Department of Energy.

[Exhibit No. 3 referred to follows:]

## EXHIBIT 3

DEPARTMENT OF ENERGY,  
Washington, D.C. December 1, 1978.

## MEMORANDUM FOR BARTON HOUSE

From : George Hall.

Subject : Weekly petroleum supply situation report as of November 24, 1978.

*Crude Oil*

Stocks decreased by 2.5 million barrels from last week to 326.7 million barrels. Estimated production is 8.8 million barrels per day including 1.2 million barrels per day on the Alaska north slope. Imports decreased by 912,000 barrels per day from last week to 6.4 million barrels per day. Demand decreased by 395,000 barrels per day from last week to 15.6 million barrels per day. Runs increased by 346,000 barrels per day from last week to 15.4 million barrels per day. Percentage of refinery utilization increased from 90.4 percent last week to 9.0 percent, compared to 88.8 percent last year.

Comparing current four-week-running averages with those of the corresponding period of a year ago, stocks were down 4.3 percent, production was up 4.1 percent, imports were up 18.0 percent, demand was up 9.1 percent, and runs were up 5.6 percent.

As of November 24, 1978, the total volume of crude oil in the Strategic Petroleum Reserve was 54,490,000 barrels. API statistics, on which this weekly report is based, do not include such crude oil in either stocks or imports since DOE does not make a report to API. However, final DOE import and stock statistics now include the volumes imported for the SPR.

*Motor Gasoline*

Stocks increased by 5.1 million barrels from last week to 217.6 million barrels. Production increased by 350,000 barrels per day from last week to 7.7 million barrels per day. Imports decreased by 1,000 barrels per day from last week to 163,000 barrels per day. Demand decreased by 830,000 barrels per day from last week to 7.1 million barrels per day.

Comparing current four-week-running averages with those of the corresponding period of a year ago, stocks were down 12.7 percent, production was up 3.3 percent, imports were up 28.9 percent, and demand was up 5.2 percent.

This week's motor gasoline production of 7,687 MB/D is only 4 MB/D less than the record high reached during the week ending July 14, 1978.

During the past week, Shell Oil Company announced a .75 allocation fraction, Amoco Oil Company announced a restriction on the amount of unleaded premium gasoline that it will supply, and Continental Oil Company advised DOE that in view of the relief granted by OHA on interrefinery sales, it was resuming a 1.0 allocation fraction for December.

*Middle distillates*

Stocks increased by 2.2 million barrels from last week to 224.9 million barrels. Production increased by 130,000 barrels per day from last week to 3.4 million barrels per day. Imports decreased by 40,000 barrels per day from last week to 154,000 barrels per day. Demand increased by 454,000 barrels per day from last week to 3.2 million barrels per day.

Comparing current four-week-running averages with those of the corresponding period of a year ago, stocks were down 14.9 percent, production was down 0.9 percent, imports were up 32.6 percent, and demand was up 6.3 percent.

As of November 24, 1978, distillate stocks were 37.0 million barrels below 1977 levels for the same week. However, 1977 distillate stocks were unusually high. Current stocks are 7.1 million barrels higher than the average stock level for the same week over the five-year period, 1972-1976. Distillate production, at 3,376 MB/D for the week, is 79 MB/D higher than for the same week of 1977 and 442 MB/D higher than for the same week of 1977 and 442 MB/D higher than the 1972-1976 average.

*Residual fuel oil*

Stocks decreased by 154,000 barrels from last week to 84.3 million barrels this week. Production remained essentially unchanged from last week at 1.7 million barrels per day. Imports increased by 151,000 barrels per day from last week to

1.3 million barrels per day. Demand increased by 317,000 barrels per day from last week to 3.0 million barrels per day.

Comparing current four-week-running averages with those of the corresponding period of a year ago, stocks were down 11.4 percent, production was up 0.5 percent, imports were down 3.4 percent and demand was up 9.5 percent.

As of November 24, 1978, residual fuel oil stocks are 12.1 million barrels below prior year levels, but are 17.4 million barrels higher than the 1972-1976 average.

#### Jet fuel (Kerosene-base)

Stocks decreased by 463,000 barrels from last week to 27.6 million barrels this week. Production decreased by 67,000 barrels per day from last week to 825,000 barrels per day. Imports decreased by 3,000 barrels per day from last week to 55,000 barrels per day. Demand increased by 75,000 barrels per day from last week to 945,000 barrels per day.

Comparing current four-week-running averages with those of the corresponding period of a year ago, stocks were down 2.3 percent, production was up 10.7 percent, imports were up 50.0 percent, and demand was up 7.3 percent.

#### Propane

API data on propane inventories through October 1978 are compared with inventory levels for the same month in 1977:

[In thousands of barrels]

	October 1978	October 1977	Net change
East coast.....	4,453	5,541	(1,088)
Indiana, Illinois, Kentucky.....	6,103	6,201	(98)
Mid Continent.....	25,283	25,126	14
Eastern Texas, Arkansas.....	13,496	10,886	2,610
Gulf Coast.....	32,689	31,952	737
Western Texas, New Mexico.....	6,750	6,045	705
Rocky Mountains.....	351	563	(212)
West coast.....	824	1,259	(435)
Total October.....	89,949	87,716	2,233
Total September.....	90,471	86,675	3,796
Net buildup/(drawdown) during October.....	(522)	1,041	(1,563)

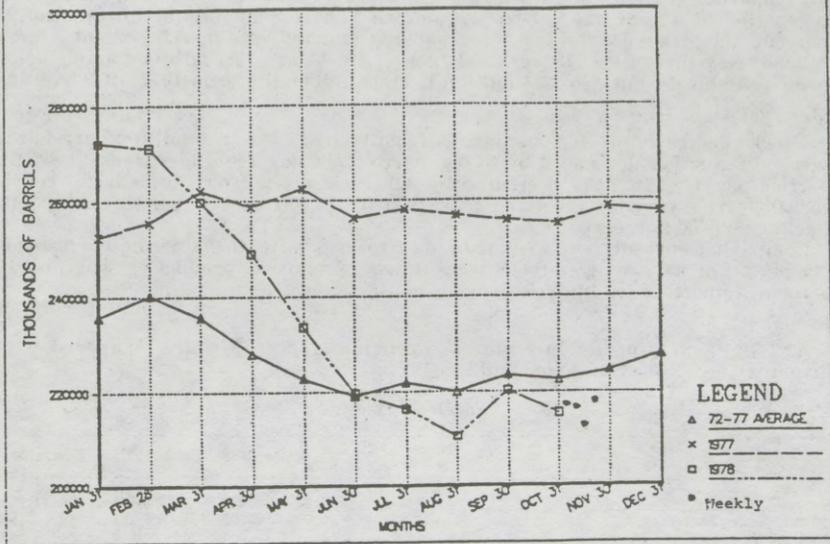
Note: The 4-week-running averages for the current and prior year used in this report are based on data as reported in the API Weekly Statistical Bulletin. The data which are published in the DOE Demand Watch compare current weekly API data with last year's monthly BOM data, interpolated to a weekly basis; thus, the comparisons with last year will vary between the 2 reports because of the differences in the basic data used for the prior year.

Attachment:

#### SCOREBOARD

Crude:	Residual:
Stocks	Stocks
Production	Production
Imports	Imports
Runs	Demand
Averages	Averages
Gasoline:	Jet Fuel:
Stocks	Stocks
Production	Production
Imports	Imports
Demand	Demand
Averages	Averages
Distillates:	
Stocks	
Production	
Imports	
Demand	
Averages	

## MOTOR GASOLINE STOCKS



## MOTOR GASOLINE STOCKS

	AVERAGE 1972-1977	1977	1978
JANUARY	235,872	252,608	272,287
FEBRUARY	240,273	255,519	271,077
MARCH	235,762	262,118	259,801
APRIL	228,161	258,831	249,079
MAY	222,628	262,498	233,612
JUNE	219,128	256,389	219,660
JULY	221,427	258,152	216,308*
AUGUST	219,957	256,904	210,355*
SEPTEMBER	224,843	255,859	220,281*
OCTOBER	224,339	255,194	215,455*
NOVEMBER	225,505	258,537	
DECEMBER	227,400	257,578	

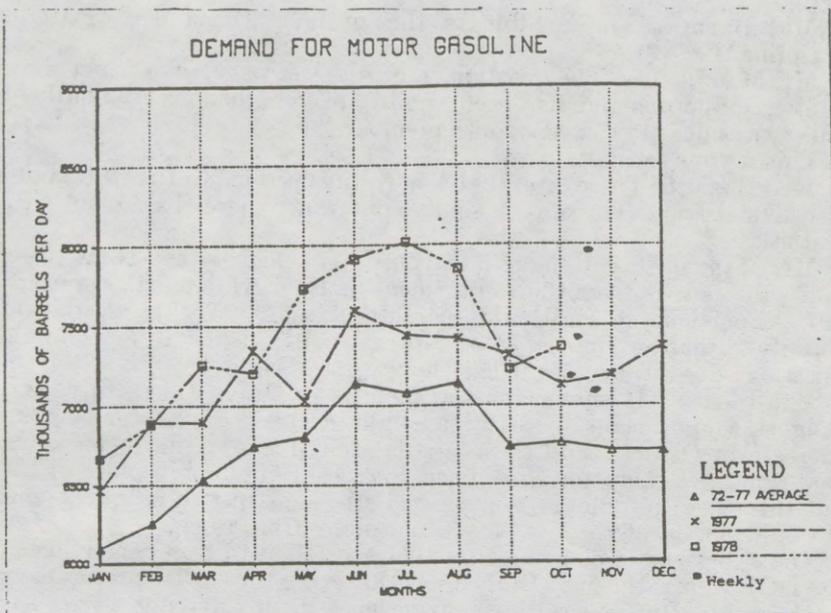
## WEEK ENDING:

NOV 3, 1978	215,888*
NOV 10, 1978	215,607*
NOV 17, 1978	212,498*
NOV 24, 1978	217,641*

SOURCE DATA: BOM/DOE

\*- BASED ON API STATISTICS. TO BE REPLACED WITH FINAL DOE DATA AS AVAILABLE.

R- REVISED FROM PREVIOUS API RELEASE.



DEMAND FOR MOTOR GASOLINE

	AVERAGE 1972-1977	1977	1978
JANUARY	6,090	6,466	6,670
FEBRUARY	6,251	6,897	6,884
MARCH	6,534	6,899	7,256
APRIL	6,751	7,348	7,206
MAY	6,809	7,034	7,731
JUNE	7,143	7,595	7,917
JULY	7,075	7,441	8,020*
AUGUST	7,142	7,419	7,853*
SEPTEMBER	6,758	7,317	7,232*
OCTOBER	6,763	7,132	7,368*
NOVEMBER	6,745	7,192	
DECEMBER	6,749	7,373	

## WEEK ENDING:

NOV 3, 1978	7,190*
NOV 10, 1978	7,442*
NOV 17, 1978	7,945*
NOV 24, 1978	7,115*

## SOURCE DATA: BOM/DOE

\*- BASED ON API STATISTICS, TO BE REPLACED WITH FINAL DOE DATA AS AVAILABLE.

R- REVISED FROM PREVIOUS API RELEASE.

Mr. MARKS. On the last page—if you would turn to it—of this exhibit it shows that gasoline demand has been significantly higher every month of this year, since May, except for September.

I would like to ask that you would look at that and answer the question of whether or not I am correct in that statement.

Mr. BARDIN. The exhibit is the graph, "Demand for Motor Gasoline"?

Mr. MARKS. Yes. The question is, on the last page, does it not show that gasoline demand has been significantly higher every month of this year, since May, except for September.

This is your exhibit.

Mr. BARDIN. These are the American Petroleum Institute published statistics. There is a source put down here, based on API statistics.

Mr. MARKS. May I suggest to you, if you look at the front page, you will see it is from the Department of Energy, dated December 1, 1978, from George Hall, and the subject says, "Weekly Petroleum Supply Situation Report as of November 24, 1978." It is a simple question; does it, or does it not show what I suggest?

Mr. BARDIN. It shows for the months of May, June, July, and August a significant increase; a slight decrease in September; an increase in October, and the four dots that I am trying to focus on, that you have there for November, the weekly figures in place of the monthly, are preliminary American Petroleum Institute figures, and I would not want to draw any conclusions from them.

The experience this summer is that there had to be a correction in the DOE figure, the final DOE figure, lowering the earlier preliminary API figures. But generally the experience in this driving season has undoubtedly been that there has been—

Mr. MARKS. Mr. Bardin, could you just answer "yes" or "no"? It is a simple question. I am just asking, does it not show that except for September, since May the demand for gasoline has been significantly higher every month?

Mr. BARDIN. Well, I am qualifying as to November, Congressman Marks.

Mr. MARKS. Fine.

Mr. BARDIN. It shows an increase in driving. One could quibble about whether the October one is significantly higher, but it is higher; the others are significantly higher, the earlier months.

Mr. MARKS. Thank you very much. Now, my next questions is, does it not show that demand in September of this year was about the same as demand for September of last year. So, that is little solace. Is that correct?

Mr. BARDIN. The demand figure for September is just a shade lower, it is very close to the one for last year.

Mr. MARKS. Now, the graph does not show November data, but if you will look on page 2 of this exhibit—will you look at page 2 of the exhibit, please?

Mr. BARDIN. Could I just correct something here?

Mr. MARKS. Sure.

Mr. BARDIN. There has been a revision on one of these numbers which you do not have the benefit of in the exhibit you are asking me about. It does appear in our publication, the November 1978 issue of the Monthly Energy Review that is put out by the Energy Information Administration. I would just like to read those numbers into the record for you.

The July number is 7,577,000 barrels.

Mr. MARKS. Why not just put it in the record?

Mr. BARDIN. You are showing me an exhibit which shows that it is 7,917,000 barrels. So, the exhibit that you are asking me about reflects the earlier number, which is considerably higher, I think about 400,000 barrels higher.

Mr. MARKS. And was used by the Department of Energy in this memo as late as December 1, 1978. Be that as it may, can we now go on? The graph does not show November data, is my question. If you will look on page 2.

Mr. BARDIN. It does not. But, Congressman, since I know you and the subcommittee want my accurate evaluation—

Mr. MARKS. We certainly do.

Mr. BARDIN [continuing]. It does require a modification as to the statement as to July.

Mr. MARKS. We just modified it, thank you.

Mr. BARDIN. It does not show a significant increase.

Mr. MARKS. Now, may we go back?? The questions is, the graph does not show November data, but if you will look on page 2, please, of this exhibit, demand for the first 4 weeks ending in November was 5.2 percent higher than in the previous year. Is that also correct?

Mr. BARDIN. That is what the graph shows. Those are the early weekly numbers put out by the American Petroleum Institute. There are much more recent numbers now available for November, and indeed for part of December. If you would like them, I can read them into the record.

The week ending December 1, the number now is 6,959,000; and the previous week, the week ending November 24, 7,115,000. I do want to suggest to you, Congressman Marks, that one has to be very cautious in using the last figures the API published, and in understanding another point, what they call "demand" is not a direct measurement of demand, but a secondarily derived measure. It is the result of several subtractions and computations. It is not photographing the real world; it is making computations.

Mr. MARKS. May I suggest to you, Mr. Bardin, that I appreciate your comments and I know that you are doing so in an effort to have the record reflect the exactness of the figures—we appreciate that. I will, however, suggest to you that if you want to meet your plane—and we want you to meet it—we would appreciate if you could answer more directly the questions if you can.

Mr. BARDIN. I can do it very easily if it is not tied to these statistics which I have some reservations about. I certainly feel that this summer's driving season has shown a significant increase over the previous summer. This is a matter that has been of interest to me since the preliminary data came in, and it is something that I have been pursuing in the refiner conference and elsewhere, and I will be happy to discuss with you.

Mr. MARKS. Now, members of your staff, Mr. Bardin, in a meeting with the subcommittee staff last week indicated that if the increased November demand continued throughout the winter, that we faced the prospect of a genuine supply shortage.

In light of the statements that you made previously, do you agree with that assessment of members of your staff?

Mr. BARDIN. I was not at the meeting, and the relevant question in light of my statement today is what my staff advises me today about

the demand today. In terms of the demand today, I am satisfied that we will not have a January supply shortage. The production has been very high. The demand has gone down. The reserves are building up, the stocks are building up again. So, it seems to me that the statement I have given you, in both my prepared statement and summary, is soundly based.

Mr. MARKS. Now, Mr. Bardin, as far, however, as the spring and summer is concerned, would you then agree that your staff's comment at that time about the possibility of a genuine shortage, might that be the fact?

Mr. BARDIN. I am sorry, I thought you said a "January" shortage. I misheard you.

Mr. MARKS. This coming spring and summer, in your opinion, sir, is there a prospect of a genuine supply shortage during that period?

Mr. BARDIN. I have not heard of any comment by my staff that there is a concern about the spring. We are, as I said several times, watching very closely the summer situation. If the stocks do not build up, then we could have a problem. For that reason we are considering a series of steps going beyond what the refineries can do, to improve the stock picture going into the 1979 summer driving season.

I do not think there is any fundamental disagreement here. There may be a question of, what is a "genuine shortage"? I think that is something the committee would do well to analyze to understand better what are the stock numbers and the reserve numbers.

Mr. MARKS. Let me discuss with you some other factors that may further aggravate the short-term supply situation, factors which, however disturbing they may be to contemplate, were not included, I do not believe, in your testimony.

Now, let us consider for a moment the current labor situation if we may, Mr. Bardin. The Oil, Chemical, and Atomic Workers Union labor contract expires January 7, 1979.

Mr. BARDIN. Right.

Mr. MARKS. The members of this union, I believe, are dissatisfied with the President's wage and price guidelines, and I do not blame them. They are threatening a strike; is that correct?

Mr. BARDIN. There is a negotiation and the threat of a strike hanging over that industry; yes.

Mr. MARKS. The union, as I understand it, has traditionally targeted a single company, but this year is reported to be considering a nationwide strike. Is that your information, also?

Mr. BARDIN. I do not have direct information, but my impression is that you have to watch for the possibility of an industrywide strike, as well as the possibility of a strike which targets one, or two, or three firms. You also have to watch, if I may just anticipate or add, the relationship to the teamster negotiation, which in many ways is perhaps a more significant one for the subject that we are talking about.

Mr. MARKS. Has the Department of Energy determined the impact of such a strike—assuming it were to come about—in attempting to calculate the amount of gasoline and other petroleum products that could be turned out by management personnel in the event of such a strike; and has it made appropriate contingency plans?

Mr. BARDIN. We are engaged in that analysis and in that planning effort, but we do not have a quantitative assessment to give you. As

your question implies, what happens in one of these petroleum strikes is, initially the managerial personnel keep the refineries going. That is probably a question that you can address in more detail to the industry witnesses that follow. I understand there comes a point in a protracted strike where you have to anticipate a certain dropping off in production.

Mr. MARKS. Well, could you be a little bit more specific with us? Has the Department of Energy made a determination of the impact of such a strike, is it attempting to do so? Is it preparing contingency plans in the event that strike comes by? In other words, what action have you taken?

Mr. BARDIN. I meant to say—perhaps I did not convey it—that we are analyzing this question, and we are doing that planning; but we do not have a quantitative figure to give you at the moment.

Mr. MARKS. When can we expect, Mr. Bardin, that this “analyza-tion” may be finished?

Mr. BARDIN. It is an ongoing process, and I am confident with each month we will have a much more detailed fix on it.

Mr. MARKS. I am afraid you are not answering my question. I am asking you specifically if you can tell us—and perhaps you cannot—but the record ought to reflect whether or not you can tell us whether that study will be finished by the end of this month, January, February, March, April, May, June 1979?

Mr. BARDIN. Congressman Marks, I have not said there is any study; I am not aware of a study underway. We are analyzing that situation. Whether it translates into a number I am not able to tell you at this moment, but I will be happy to supplement the record.

Mr. MARKS. May I suggest to you that if a study has not been made, if something very affirmative has not yet been done, may I make a respectful suggestion to the Department of Energy that it certainly make that, because it seems to me to be a very important element to be taken into consideration. I am sure you, sir, will want to have some idea of what the future portends.

Mr. BARDIN. What I want, as the officer responsible for administering a contingency and emergency program, is a feel of the exposure on the one hand, and the tools available to meet that problem. We have prepared a list of contingency tools. They are sketched out in the prepared testimony that I have given to you. We are working on a series of measures which will enhance supply—such as the Canadian import, gasoline discussion, that I mention in my prepared testimony.

Mr. MARKS. Mr. Bardin, we are going to hold the record open at this point to receive from you directly the answer to that question that I have asked you. If you can shortly give it to this committee, we would appreciate having it.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. MARKS. I would like to mention to you that I personally think the consequences—and I am sure you would agree—of a refinery workers’ strike, particularly given the current very low inventory of gasoline, could be perhaps even devastating; could it not?

Mr. BARDIN. We do not intend to allow that to happen. That is to say, we intend to take the contingency measures as the year 1979 progresses, which will avoid that kind of situation.

Now, if you are asking me, Congressman Marks, whether a situation of a progressive deterioration in production—for whatever reason, strike or equipment failures; inaction by the industry; inaction by our Government; continued high motoring by ourselves as consumers—could lead to disaster, of course, if we do not face the challenge of the moment and respond to it, it certainly could lead to very dire consequences. This administration does not intend to allow that to happen.

Mr. MARKS. I appreciate your answer, and I certainly encourage this administration, as you well know, to do all it can to prevent these things from happening. My specific question, of course, was directed to that particular incident, the fact that such a strike or strikes could be devastating. I would think you would have to agree that it would be very, very hurtful, if not devastating.

Mr. BARDIN. It is a question of supply and demand, Congressman. I am disagreeing—

Mr. MARKS. Well, I know that we are disagreeing, but we are not getting an answer from you.

Mr. BARDIN. I think of the problem that we had with the coal strike last winter. It is true that if the thing had gone on, and on, and on, with settlement after settlement rejected, we could have had very serious problems. I think of the situation in Pittsburgh and the chances that had to be taken in managing the electric load there; chances that that utility would normally never take. They had to risk power failures in order to keep the house together.

The potential for a devastating situation seemed to be very serious at that time but we pulled ourselves together. The “we” is, of course, the American people, State government, the energy industry. We showed remarkable ingenuity, and I have a great deal of confidence in the American energy industry’s and the American energy consumer’s ability to deal with that.

In the coal strike we had a conservation strategy and a supply strategy, and we pulled through rather nicely.

Mr. MARKS. Mr. Bardin, a worsening, or certainly a prolongation of the current strike in Iran could also adversely affect the impact on gasoline production, certainly, this winter; is that not correct?

Mr. BARDIN. Depending on the world oil production—you have to translate from the situation in the one country to the rest—there could be a problem on reduced runs, crude runs worldwide, and supply constraints as a result. I suspect this is not the time or the place to go further into that.

Mr. MARKS. Well, I am not sure that it is or is not. Are you suggesting that the worsening conditions there, if they were to continue, would be hurtful?

Mr. BARDIN. There has been a very substantial drop in oil production as part of the political situation there. There has been some compensation for it. The real question is not the situation in any one country, the question is, how much oil is being produced and shipped around the world.

Mr. MARKS. Mr. Bardin, the subcommittee staff was told that at least one major oil company is already experiencing supply cutbacks from Iran. Does that coincide with the information that you have, your department has?

Mr. BARDIN. Certainly, there have been supply cutbacks for individual companies on individual sources of supply. I say to you again, Congressman Marks, viewed from our governmental, national perspective, the important question is whether there is compensating crude oil available. I am not trying to minimize that question, it is a very important one; but it is a complicated one and I do not think this is the time or place to try to flush that out.

Mr. MARKS. Mr. Bardin, another disturbing element in the equation, as I view it, is the decision by Saudi Arabia to reduce its export of light crude oil. Are you aware that the Saudis have reduced the percentage of light crude oils from approximately 72 to 65 percent, and they they are contemplating, actually, a further cutback to perhaps 60 percent light oil?

Mr. BARDIN. I am not in a position to confirm any of these numbers, and I would appreciate if now, or perhaps later, the staff could furnish me the specifics on the decisions, the dates, the timetables that are implicit in that question.

Mr. MARKS. We will be very pleased to pass that on to the Department of Energy.

The significance of the Saudi cutback, obviously, in light crude oil production relates to the fact that refineries on an average produce less gasoline from very heavy oil. Is that basically correct?

Mr. BARDIN. The heavier the oil, the more difficult it is to produce gasoline.

Mr. MARKS. The answer to that is "yes;" is it not? I mean without any qualifications, can you not say "yes" or "no"?

Mr. BARDIN. As a general matter it is, "yes." I would still be interested to know whether we are talking about a decision that was discussed months ago, which I have heard of; or whether you and the staff have something new to report about a recent or contemporaneous decision.

Mr. MARKS. Mr. Bardin, may I say to you that I appreciate very much the trouble you went through in getting here. We did not provide you with our very best weather, but not our worst.

I am going to ask you the question again and ask you, please, to answer me "yes" or "no."

The significance of the Saudi cutback in light crude oil production relates to the fact that refineries on average produce less gasoline from heavy oil. Is that basically correct?

Mr. BARDIN. You are asking me a compound question, Congressman. It is basically accurate, a lighter crude oil produces more gasoline.

Mr. MARKS. Thank you very much, sir; you need say no more, sir. Thank you.

Mr. BARDIN. But I am not agreeing as to the significance of a particular Saudi action.

Mr. MARKS. Thank you very much.

Now, taking all of those factors that we have been discussing, my reading of the situation would lead me to believe that we could very well experience a significant gasoline shortage during the spring driving season because of our inability to build up winter gasoline inventories. Is that a fair reading, in your mind, of the situation?

Mr. BARDIN. The strike issue that you raised is a significant one. The question about inventory buildup is certainly significant enough that we are undergoing an exercise to find supplementary supplies.

I am not sure that I can relate all of the concerns to the specific points you make, but I do think that it is wise for both the Congress and the administration, and certainly for the refining industry, that has the responsibility to meet the demand, to consider these points as to the ability to build up inventory. We are taking that very seriously.

Mr. MARKS. Mr. Bardin, it is my understanding that the concern and confusion, perhaps even panic, in the 1973 gasoline shortage was the result of an approximate 5-percent shortage in gasoline. Is that your understanding?

Mr. BARDIN. I was not in the country at that time. My impression is that there was not a panic, at least not among the American people. But there certainly was concern, and the shortfall at that time was on the order of magnitude that you suggest.

Mr. MARKS. So that the line between adequacy of supply and a hurtful shortage, really then, is a very fine line indeed; is it not?

Mr. BARDIN. Yes. You have a complicated delivery mechanism here where you usually have a standard. If the primary stock goes below 200 million barrels it is very difficult to keep the pipeline full and moving to the various jobber terminals, and the filling stations, in a smooth and orderly way. There are tens of thousands of components in this delivery mechanism.

Mr. MARKS. Mr. Bardin, our current gasoline inventory—*noted in exhibit 3 that I showed you before*—is 217.6 million barrels; in round numbers about 200 million barrels. Now, there are about 100 million cars on the road. Were the public to panic and try to keep their gasoline tanks reasonably full, that action, that action alone today, tomorrow, or sometimes next spring—assuming a sudden call for an average of 5 gallons more per car—could, could it not, topple the entire supply situation?

May I suggest to you the situation, if that is in fact correct, is extremely grave? I am concerned, quite frankly, about the nature of the formal presentation you made before the subcommittee; and frankly, Mr. O'Leary's similar presentation before Senator Jackson's committee.

It seems clear, does it not, Mr. Bardin, from the gasoline supply numbers before you, that gasoline demand—beginning in May of this year—was much higher than it had been projected by either the Department of Energy or industry and that, if the trend continues, supplies will be extremely tight in the absence of even a labor strike, supply interruptions, perhaps, from Iran, or any of the other factors that we discussed.

That being the case, Mr. Bardin, at what point in time, this year, do you believe that a reasonable, informed person—this year, a reasonable and informed person—should have concluded that we faced a potential gasoline supply problem?

Mr. BARDIN. I am very much concerned that the subcommittee is not working with the latest numbers. I think a reasonable, informed person should make use of the latest numbers. There has been a 6-million barrel increase in those reserve figures.

I want you to know that we last summer noted the increase in demand that Congressman Marks was asking about earlier. We were

then concerned—as reasonable, informed people. The Secretary of Energy therefore, in August, asked the refinery industry to address and attack this inventory concern by increasing the gasoline output.

Mr. MARKS. May I interrupt you for a moment, please? What you are saying is that Dr. Schlesinger himself said on or about the end of August or September 1, made the projection at that time that there was a possibility of a serious shortage is that not correct?

Mr. BARDIN. At the end of August, Secretary Schlesinger asked the refining industry to take action. It was not a question of idle prediction, to take action; to keep those inventories up.

Mr. MARKS. My question, then, goes back to asking you, sir, when, in your opinion, should a reasonable person—whether in Government or in the private sector—have determined in fact that this possibility of a shortage might be forthcoming? Would that be in August, September; before that, July?

Mr. BARDIN. In August there was enough concern that a number of us in the department discussed it, and Dr. Schlesinger took the action. There was a countervailing view of a number of people—also honest, well-informed people, including a number in the industry and observers of the industry—who felt it was so clear the driving would drop off after Labor Day that we should not be concerned about that inventory situation.

Now, I am not claiming that we had any powers of prognostication as to what would happen after Labor Day, and that the demand would remain high. We were just concerned not to take a chance. Dr. Schlesinger's feeling was that we should go ahead on that initiative, the worst that could happen was that the inventory would rise a little bit.

But the important point is that driving did continue high, and so it continued to be a matter of immediacy and concern. Of course, if the other pundits had been correct, if driving had dropped down after Labor Day, there would have then perhaps ceased to be a reason for concern.

Now, you see, the concern has got to rise and fall as you track the situation. I think what you and I, and others have to do during the course of this winter is to take a very close, hard look—week by week and month by month—on the actual performance of this energy industry.

Mr. MARKS. Mr. Bardin, the latest DOE study on gasoline decontrol, which is this draft, "Environmental Impact Statement—Motor Gasoline Deregulation," November 20, 1978—this green volume I am holding in my hand—released November 20, 1978, 6 days after Shell sought allocation relief from your department, states unequivocally that the gasoline supplies would be adequate through all of 1979, and most likely through 1980.

How do you reconcile, Mr. Bardin, this study and your testimony today?

Mr. BARDIN. This draft environmental impact statement also says and emphasizes that we were about to develop, or rather the Energy Information Administration, a quasi independent group in DOE, was about to develop and publish a new supply-demand balance; and that we would reach our final environmental impact statement conclusions based on that. Indeed, we put in alternate supply-demand analyses so

that in the context of analyzing environmental impacts people who had a more pessimistic or more optimistic view of the future, could still analyze the impact.

Mr. MARKS. What about 1980?

Mr. BARDIN. The EIA report has come out, and I think you will want your record to note, Mr. Chairman, the analysis memorandum that the Energy Information Administration has put out in December, that is December 8, 1978, numbered AM/ES/79-12. That is the 1980 report.

Mr. MARKS. That is the 1980 report?

Mr. BARDIN. Yes.

Mr. MARKS. Mr. Bardin, in the time remaining I would like to state the hypothesis that I mentioned in my opening statement, namely, the present supply situation is really less a function of gasoline price controls and environmental restrictions, as claimed by the oil industry, but rather more a function of the industry's having actually misjudged demand early this year; and of its resulting decision to reduce gasoline production and inventory throughout the first quarter of this year.

At this point, if I may, Mr. Bardin, I would like the subcommittee staff to enter some additional exhibits into the record; and if they will question Mr. Bardin on those exhibits.

Mr. SIMS. Thank you, Mr. Chairman.

If the clerk would please provide the witnesses with copies of exhibits 1 through 4.

Mr. BARDIN. While they are being distributed, Mr. Chairman, if I may just say, I found this an intriguing hypothesis, and I am sorry I will not be here when the industry witnesses comment; but I will order an early transcript and want to read with interest their reactions to your hypothesis.

Mr. MARKS. Mr. Bardin, you need not order it, I will send it airmail special delivery, which means under the present status of the Post Office that you will get it sometime in February.

Mr. BARDIN. Congressman Marks, I will come back to Erie, Pa. Give me a long-distance call and I will come back and pick it up.

Mr. MARKS. Mr. Sims, do you have some questions?

Mr. SIMS. Yes. Thank you, Mr. Chairman.

Mr. Bardin, we have talked about a number of factors that may explain the shortages of gasoline experienced by several large refiners, including increased demand, less than anticipated mileage efficiency of new automobiles, and the possible impact of your department's regulations.

Now, I would like to explore another set of circumstances, described by Congressman Marks, that appears at least as important as the other factors in explaining the current tight supply situation.

If you would please look at exhibit 1, "Refinery Capacity Utilization," which is in chart form.

[Exhibit No. 1 referred to follows:]

#### EXHIBIT 1

The following monthly refinery capacity figures, derived from Department of Energy and, for the last two months in 1978 from American Petroleum Institute data, show significant underutilization of capacity in 1978 compared to both 1977 and 1976.

## TOTAL U.S. OPERABLE REFINING CAPACITY UTILIZATION

[In thousand barrels per day]

	1976	1977	1978	1978-77	1978-76
January.....	85.7	89.0	85.1	(3.9)	(0.6)
February.....	87.8	92.6	84.1	(8.5)	(3.7)
March.....	86.9	89.6	84.8	(4.8)	(2.1)
April.....	86.5	88.8	83.2	(5.6)	(3.3)
May.....	87.3	89.3	88.9	.4	1.6
June.....	92.7	91.4	87.7	(3.7)	(5.0)
July.....	93.5	90.9	88.5	(2.4)	(5.0)
August.....	90.8	89.7	192.6	2.9	2.6
September.....	89.4	91.0	191.1	.1	(2)
October.....	85.8	89.3	(2)	(2)	(2)
November.....	90.5	88.7	(2)	(2)	(2)
December.....	91.1	87.9	(2)	(2)	(2)

<sup>1</sup> API Monthly Statistical Report.<sup>2</sup> Not available.

Sources: DOE Monthly Petroleum Statement.

Given a total operable refinery capacity of 17,152,000 barrels per day and a utilization ratio of 90 percent, a 1 percent change in utilization would equal about 68,000 barrels of gasoline production per day assuming gasoline output of 44 percent.

Underutilization of capacity in 1978 to produce gasoline compared to production in 1977 and 1976, when demand was lower, can thus be estimated as:

[In barrels per day]

	1978-77	1978-76
January.....	265,200	40,800
February.....	578,000	251,600
March.....	326,400	142,800
April.....	380,800	224,400
May.....	(27,200)	(108,800)
June.....	251,600	340,000
July.....	163,200	340,000
August.....	(197,200)	(176,800)
September.....	(6,800)	(115,600)
October.....		
November.....		
December.....		

Mr. SIMS. The numbers, except where indicated by an asterisk, are as reported to and published by the Department of Energy. As you can see, monthly refinery operations are listed for 1976, 1977, and 1978. The figures indicate what percentage of available capacity was utilized.

Mr. BARDIN, the last two columns on the right compare refinery utilization in 1978 with 1977, and 1976. A number in parentheses represents a negative figure.

Assuming that I have subtracted correctly, it is obvious that through September of this year U.S. refineries on the whole were not running anywhere near the level of 1977, and were even below the 1976 level; weren't they?

Mr. BARDIN. You want my observation?

Mr. SIMS. Yes, please.

Mr. BARDIN. I presume, Mr. Chairman, that the actual exhibit will be part of the printed record.

Mr. MARKS. Certainly.

Mr. BARDIN. It seems to me there are—that is my offhand reaction—two things you want to be looking into. One is the very large stocks

we went into the year with, in January, which of course is related to the point you are trying to develop.

Mr. SIMS. We will get to that directly.

Mr. BARDIN. And two, recall the situation we had in California where we had a very low refinery utilization there because they could not find an outlet for the residual oil components. Indeed, there was a problem on gasoline, then. There were shipments of gasoline from the gulf coast to California because they cut back on the refinery utilization there as a result of the lack of market for residuals, which was a function of weather on the one hand, and the resumption of hydroelectricity and availability of natural gas.

Mr. SIMS. Mr. Bardin, you are not saying that the west coast oil glut and consequent refinery underutilization could in itself explain the differences that we have here; are you?

Mr. BARDIN. If I were doing the analysis I would want to check myself by just subtracting out PADD 5, and seeing how it looks with just the four eastern ones, and see what the trend is.

Mr. SIMS. The API has done exactly that. Although we have to agree that these API figures are preliminary, at least these preliminary numbers do not seem to explain these underutilization figures.

If you would please turn to the second page. Dr. Gillespie, assuming a 90-percent refinery utilization rate, and that refiners produce about 44 percent gasoline, a 1-percent change in utilization rate equals about 68,000 barrels of gasoline production a day. Is that a fair methodology?

Mr. GILLESPIE. I do not know, Mr. Sims, I have not made that computation myself.

Mr. SIMS. That is what you told me over the telephone last week; is that not correct?

Mr. GILLESPIE. Well, you were making the computation and asking if I agreed. I said that was in the ballpark.

Mr. SIMS. My question to you is concerning the methodology, not whether I added or subtracted correctly. Does that methodology, as I have described, appear to be reasonable to you to estimate something?

Mr. GILLESPIE. The way I understand your methodology is that you took an estimate of total refining capacity—

Mr. MARKS. Mr. Gillespie, excuse me a moment. Now, do you understand what he is saying to you? Do you understand what he is asking you? Can you answer the question—without making a speech, if you can—“yes” or “no”; can you?

Mr. GILLESPIE. Well, I am not sure of the way he computed it.

Mr. MARKS. Then ask him to explain it to you, and then get to the answer, please.

Mr. SIMS. We assumed a refinery running at a 90-percent utilization rate. We also assumed that that refinery made about 44 percent gasoline.

Now, a 1-percent change in refinery utilization comes out to about 68,000 barrels of gasoline production—increase or decrease. We discussed that over the telephone last week, did we not? In fact, I solicited your suggestion as to how to go about calculating this. As I recall from my notes, this was the methodology that we agreed to. Do you recall our telephone conversation, at least?

Mr. GILLESPIE. I agree with your number, roughly.

Mr. SIMS. This is just a rough number, I am not asking you to testify under oath that this is necessarily the best way to do it.

If you take the under-utilization figures on page 1, multiply them by the rough number, 68,000 barrels a day, it is possible to get an estimate of how much less gasoline per day was produced than the refineries apparently had the capability to do so. Do you understand that methodology?

Mr. GILLESPIE. That seems to be correct, yes.

Mr. SIMS. As we can see, the underutilization ran well into the summer of this year; did it not? You can see in June and July we have some fairly large figures.

Mr. BARDIN. Mr. Sims, are you not just defining 90 percent as one utilization, that the 90 percent is underutilization, to make that self-evident that is what the figures show?

Mr. SIMS. No; the 90-percent figure was just for that one calculation. The figures on the front of exhibit 1 are actual.

Mr. BARDIN. How do you define "underutilization"? If you define underutilization I think the answer will flow like that.

Mr. SIMS. I define underutilization the same way that the published Department of Energy figures define it. This is utilization less than what was available. These are your numbers, all I have done is subtracted them.

Mr. BARDIN. You mean less than 100 percent in that case.

Mr. SIMS. No. It is quite clear, if you look at the absolute numbers under 1976, 1977, and 1978, what the actual rate is. In January 1978, for example, the average U.S. total refining capacity utilization was 85.1. Now, do you follow the numbers on the chart?

Mr. BARDIN. In every single one of these months for every single one of these years the refinery industry is reported in these statistics as operating at less than 100 percent of operable refining capacity.

Mr. SIMS. Mr. Bardin, you are the one who raised the 100-percent figure, not the subcommittee. The subcommittee does not assume that any particular figure is optimum. I have heard that about 92 percent over a long period of time is virtually the optimum. What I am doing here is taking Department of Energy numbers, defined by the Department of Energy, and simply comparing them from year to year.

If we could move on, perhaps we could debate this in the hall.

Mr. BARDIN. Is this exhibit 1 a DOE statement, is that your point?

Mr. SIMS. My point, Mr. Bardin, is that I have taken these numbers from your publication.

Mr. BARDIN. Exhibit 1 refers to underutilization of capacity in 1978 compared to both 1977 and 1976.

Mr. SIMS. That is correct.

Mr. BARDIN. Presumably that means, you use as your standard the utilization rate for 1977 and 1976, and you note that in certain months thereafter it was less.

Mr. SIMS. This is just a year-to-year comparison.

Mr. MARKS. We could have answered that a lot earlier. Let us try to move on.

Mr. SIMS. Exhibit 2—if I could just summarize it briefly—is nothing more than an attempt to describe generally the net change in the available supplies of gasoline.

[Exhibit No. 2 referred to follows:]

## EXHIBIT No. 2

## MOTOR GASOLINE COMPARATIVE SUPPLY AND DEMAND ANALYSIS JANUARY THROUGH JUNE

[In thousands of barrels]

	1977	1978	Net change
1. Total production.....	1,257,871	1,245,355	(12,516)
a. At refineries.....	1,257,464	1,245,022	(12,442)
b. At gas processing plants.....	407	333	(74)
2. Imports.....	41,330	34,752	(6,578)
3. Exports.....	441	198	(243)
4. Net domestic supply.....	1,298,760	1,279,909	(18,851)
5. Domestic demand.....	1,273,760	1,317,829	44,069
6. Increase in domestic demand plus decrease in net supply.....			62,920

Source: DOE, Energy Information Administration, Monthly Petroleum Statement, June 1978.

Mr. SIMS. I am not even going to discuss this, I would like to go directly back to exhibit 3, which Congressman Marks put in the record in his questioning, and ask if you would turn to the first chart, labeled, "Motor Gasoline Stocks."

Do you have that before you, Mr. Bardin?

Mr. BARDIN. I certainly do.

Mr. SIMS. The chart shows that while we begin the year with unusually high stocks of gasoline—something over 272 million barrels—a rapid drawdown, which began in March and continued through June, resulted in a decrease of over 50 million barrels in only 4 months. Is that correct?

Mr. BARDIN. I will accept your numbers, and I certainly accept the rapid drawdown characterization.

Mr. SIMS. Thank you.

Mr. MARKS. Mr. Sims, would you excuse me for just a moment? Excuse me, Mr. Bardin.

Sir, the court reporter, the stenographer, is having a difficult time hearing some of the conversations because of your conversation. If you could just whisper, it would be helpful, sir. We appreciate your being here, but it would be helpful. Thank you.

Go ahead, Mr. Sims.

Mr. SIMS. I draw your attention to the month of August, when stocks were down, on this chart, to about 210 million barrels; according to the revised figures in the Department of Energy's monthly publication it is now 208 million barrels. In your previous testimony you have acknowledged—

Mr. BARDIN. I do not think the 208 million is correct, Mr. Sims.

Mr. SIMS. Well, that is what is published in your monthly "Energy Review".

Mr. BARDIN. Let us have that checked. It is higher, but we will doublecheck that.

Mr. SIMS. You have already acknowledged that it takes about 200 million barrels just to keep the distribution system—

Mr. BARDIN. I am looking at the wrong page, you are correct on the 208 million.

Mr. SIMS. Thank you. You have already acknowledged that about 200 million barrels is what is needed to keep the supply system operating.

Mr. BARDIN. I have suggested that is the conventional wisdom in this industry.

Mr. SIMS. Well, in August we almost ran out of gasoline; did we not?

Mr. BARDIN. We did not almost run out of gasoline, but we came very close to dropping below that limit and creating delivery problems. I think Chairman Marks put his finger on it when he tried to track it down to the individual fuel tank component. If you make a rough calculation—and I do not think there is time to do it now, and I do not think the chairman wants me to take the time from the questioning—but I think you can really track down what is involved in this delivery system, tanks at the refinery, pipelines, tanks at the terminals. We do not run out of gasoline, that is not literally true. What happens is, if we ever get into that situation you would have difficulty with the smooth delivery of gasoline. Put differently, this is a very efficient industry in the sense that it works from hand to mouth, it does not have great redundant stocks or great redundant capacity.

In August we were close to that conventional wisdom line, which is why Secretary Schlesinger took the actions I mentioned to you before.

Mr. SIMS. Thank you, Mr. Chairman. I would ask that exhibit 4 be placed in the record. Again, those are Department of Energy numbers, I do not think we have time to discuss them today.

This concludes my questioning.

Mr. MARKS. Thank you, Mr. Sims. Those exhibits will be placed in the record.

[Exhibit No. 4 referred to follows:]

EXHIBIT No. 4  
TOTAL U.S. SHIPMENTS OF UNLEADED GASOLINE  
[In thousands of barrels]

	1976	1977	1978	1977 compared to 1976	Percent change	1978 compared to 1977	Percent change
January.....	37,124	51,252	67,682	14,128	38.1	16,430	24.3
February.....	33,882	51,443	59,392	17,561	51.8	7,949	15.5
March.....	43,631	55,079	71,797	11,448	26.2	16,718	30.4
April.....	38,620	54,351	72,619	15,731	40.7	18,268	33.6
May.....	44,551	58,192	71,265	13,641	30.6	13,073	22.5
June.....	46,861	63,612	79,395	16,751	35.7	16,751	24.8
July.....	50,618	67,667	81,024	17,049	33.7	17,049	19.7
August.....	51,283	63,289	186,406	17,592	35.1	18,720	27.7
September.....	51,283	63,289	183,775	12,006	23.4	20,486	32.4
October.....	48,002	66,322					
November.....	46,928	64,544					
December.....	54,132	72,933					

<sup>1</sup> Decrease in growth for 6 of first 7 mo of the year.

## MOTOR GASOLINE

	Domestic demand						Exports	Stocks <sup>1</sup> (thousands of barrels)
	Total	Unleaded (thousands of barrels per day)	Unleaded percent of total (thousands of barrels per day)	Production <sup>1</sup> (thousands of barrels per day)	Imports (thousands of barrels per day)			
1972: Average.....	6,376	( <sup>3</sup> )	( <sup>3</sup> )	6,281	68	1	2 212,770	
1973: Average.....	6,674	( <sup>3</sup> )	( <sup>3</sup> )	6,527	134	4	2 209,395	
1974: Average.....	6,537	( <sup>3</sup> )	( <sup>3</sup> )	6,358	204	2	2 218,346	
1975: Average.....	6,675	( <sup>3</sup> )	( <sup>3</sup> )	6,518	184	2	2 234,925	
1976:								
January.....	6,898	( <sup>3</sup> )	( <sup>3</sup> )	6,483	92	0	240,464	
February.....	6,263	1,117	17.8	6,473	84	6	248,854	
March.....	6,890	1,456	21.1	6,455	123	6	239,049	
April.....	7,159	1,312	18.3	6,562	99	8	223,965	
May.....	6,853	1,393	20.3	6,775	112	1	225,037	
June.....	7,482	1,549	20.7	7,303	188	0	225,365	
July.....	7,315	1,594	21.8	7,174	190	1	226,922	
August.....	7,168	1,553	21.7	7,149	141	7	230,578	
September.....	7,079	1,628	23.0	6,878	171	0	229,751	
October.....	6,929	1,552	22.4	6,678	138	0	226,300	
November.....	7,038	1,604	22.8	6,938	146	1	227,742	
December.....	7,138	1,797	25.2	7,176	84	7	231,387	
Average.....	6,978	1,508	21.6	6,838	131	3		
1977:								
January.....	6,466	1,549	24.0	6,934	222	8	252,608	
February.....	6,897	1,773	25.7	6,817	184	2	255,519	
March.....	6,899	1,657	24.0	6,864	245	0	262,118	
April.....	7,348	1,863	25.4	6,968	269	1	258,831	
May.....	7,034	1,803	25.6	6,950	202	2	262,498	
June.....	7,595	2,142	28.2	7,145	246	1	256,389	
July.....	7,441	2,146	28.8	7,248	248	1	258,152	
August.....	7,419	2,096	28.3	7,191	187	1	256,904	
September.....	7,317	2,080	28.4	7,062	220	1	255,859	
October.....	7,132	2,135	29.9	6,932	179	1	255,194	
November.....	7,191	2,060	28.6	7,123	179	2	258,537	
December.....	7,373	2,400	32.6	7,146	196	1	257,578	
Average.....	7,176	1,976	27.5	7,033	215	2		
1978:								
January.....	6,670	2,097	31.4	6,932	211	1	272,287	
February.....	6,884	2,162	31.4	6,630	210	1	217,077	
March.....	7,256	2,425	33.4	6,750	142	1	259,801	
April.....	7,206	2,391	33.2	6,668	180	1	249,079	
May.....	7,732	2,343	30.3	7,059	174	2	233,612	
June.....	4 7,971	2,697	34.1	4 7,213	238	1	4 219,660	
July.....	7,577	2,629	34.7	7,268	210	( <sup>3</sup> )	216,337	
August.....	4 7,850	2,834	36.1	4 7,425	4 165	( <sup>3</sup> )	4 208,529	
September.....	7,242	( <sup>3</sup> )	( <sup>3</sup> )	7,301	276	( <sup>3</sup> )	220,281	
Average (year to date).....	7,375	2,450	33.1	7,031	200	1		

<sup>1</sup> See Definitions.

<sup>2</sup> Total as of December 31.

<sup>3</sup> Not available.

<sup>4</sup> Revised data.

Note: Bureau of Mines' stock coverage was expanded at the end of 1974 to include an additional 100 bulk terminal operators; the new coverage begins here with 1975.

Sources: Data other than unleaded—1972 through 1976: Bureau of Mines (BOM) Mineral Industry Surveys, "Petroleum Statement, Annual;" January 1977 through April 1977: Bureau of Mines Mineral Industry Surveys, "Petroleum, Statement, Monthly;" May 1977 through June 1978: Energy Information Administration (EIA) Energy Data Reports, "Petroleum Statement, Monthly;" July 1978 and August 1978: "Monthly Petroleum Statistics Report;" September 1978 data are EIA estimates based on data from the American Petroleum Institute (API) "Weekly Statistical Bulletin." Unleaded data—EIA Petroleum Reporting System.

Mr. MARKS. Mr. Bardin, I would like to summarize my impression of the data the staff has just placed into the record and see if you and Dr. Gillespie agree with my interpretations of that data.

First, it seems to me it is clear that although we went into 1978 with unusually high stocks of gasoline because of low refinery utilization and, of course, decreased imports in the first half of the year, gasoline stocks were drawn down very rapidly.

Second, just as gasoline stocks were plunging, demand increased sharply and remained high through the fall.

The combination of those trends plus some other factors such as refinery breakdowns and the glut of heavy crude oil on the west coast resulted in spot shortages in various parts of the country during the summer and the fall. After stocks fell and demand surged, the refinery industry has been trying to play catchup.

It seems clear that when Shell ran out of banked cost they had to sell gasoline at lower than market prices. This exacerbated their supply problems. However, the data presented by staff suggests that the current supply problem was less the result—less the result—of DOE regulation than a basic miscalculation of demand by the industry in the first half of this year.

Are these impressions of mine not basically factual?

Mr. BARDIN. I cannot accept them all, Congressman Marks, but I can tell you, I am very interested in some of them. There was this rapid drawdown of inventory. I think in fairness to everybody, you have to say that the annual demand forecasts were not that far off from the actual, total annual demand. I cannot tell you what Texaco, or Shell, or anybody else was using, but the published figures of the DOE were within 100,000 barrels a day of what it really turned out.

There was this higher peaking than anticipated, and then the experience of the last couple of driving seasons—the last several driving seasons—might have suggested. I think you ought to be careful in the use of the phrase in thinking about what actually happened. I am not aware of any spot shortages. There was gasoline all over the country. There was a problem of unleaded premium, or premium-type gasoline in a handful of situations; but there were not cars that went without gasoline of either the unleaded or the leaded kind.

Be that as it may, for whatever reason—plausible or unplausible, well-founded or not—you had a rate of production of gasoline, domestically, a rate of production plus imports, accretions to stocks, which drew down the inventory and was not in line with this peaking phenomenon that you pointed out in the first run of questions. I think that emphasizes for all of us the importance of looking not only at the national average consumption of gasoline, or demand for gasoline, but the relationship of peak demand to average.

We normally do that, by the way; all of the talk about the driving season of course does that. But the first half of this year we had a very low increase—in the first 6 months—a very low increase in the demand for gasoline. What first concerned me was when I saw the early summer figures, the preliminary figures, beginning to come up with a much higher increase in demand than had been experienced before. That is why I raised it at the refiners' conferences and in discussions thereafter.

I think that is something that we are now very much alert to, and that the subcommittee is quite properly alert to. I think the subcommittee has raised that question with us during the course of the year.

Mr. MARKS. Thank you very much, Mr. Bardin. At this time Congressman Walgren has some questions he would like to ask you.

Mr. WALGREN. I would just like to pursue with you a point in regard to your curiosity that was raised by the increased consumption in

the early summer of last year, and that therefore you raised this with the refinery people and perhaps within DOE.

And yet, you were in front of our subcommittee, as I understand it, in mid-July with a report that stated definitely that supplies would be more than adequate in 1978 and 1979, even under the worst case assumptions. The report states that, "Gasoline supply and demand will be in balance in 1978 and 1979, even under the worst case assumptions." Now, my problem is, when you are saying that in mid-July, how is it that we come up with an extreme shortage by September, a shortage of such dimension that the Secretary of the Department is quoted in the Wall Street Journal using words that are extremely significant, words such as, "The future gasoline availability is a very disturbing situation. We are worried about the consequences."

Now, why were you before the subcommittee in mid-July saying that everything was in balance?

Mr. BARDIN. We are talking about different time frames. The Secretary's concern reflects a continued development through the course of the summer, the concern that there was going to be a drop in production; there had not been as high a pickup as we might have hoped for. We still thought, then, in August—certainly I did—as in July, that we had a balance on an annualized basis. Frankly, we did not think then—or I certainly did not think—that we would have this continued heavy demand into the fall. There was a risk and a concern which justified pressing the point. I must say, I am surprised that it has continued as far as it has.

The questions that that experience raise go to several other areas. They go to the effectiveness of the strategy the Congress has adopted, or the assumptions as to the strategy on fuel economy in the automobile fleet, whether we are really going to get that degree of fuel economy that has been presupposed.

Mr. WALGREN. Is it not also true that about the time you were before the subcommittee in mid-July the administration was developing the decontrol proposals that would necessitate a representation that supplies were adequate, if they were to be accepted by the Congress as consistent with the 1973 act? Am I not correct in understanding that the act under which the Congress regulated the price of gasoline required that those regulations continue during any shortage, and that if we were in a situation facing a shortage, that a decontrol proposal would not lie under the policy as set out by the 1973 act.

So, was not your statement to the subcommittee in mid-July 1978 influenced by the generation and development within the Department of Energy of a proposal to decontrol the price of gasoline?

Mr. BARDIN. You are asking me about my motives, Congressman, and I hope that my motives can stand scrutiny, as I trust can the motives of the members of this committee and its staff stand scrutiny.

Let me correct a couple of points. One, a proposal had been developed—past tense—and we are still doing work on it. It was not the question whether we were going to propose, we had put forward for public discussion, as I recall, at that point a draft, or proposed environmental assessment.

The question as to the statute, there was extended discussion, but in my judgment the concern that Congress expressed in the Emer-

gency Petroleum Allocation Act was for a shortage such as Congress and the public believed had taken place during the oil embargo in 1973-1974. I must say that in my objective judgment it is irresponsible for us to think of anything that has happened this year as being a shortage, or an extreme shortage, or anything of that sort. That has not happened.

The concern, as I understand the congressional concern in EPAA, is for that kind of risk. Now, we have not begun, as a country, to take the measures which we can take to handle it. For example, next October, with the lead phasedown waivers coming into play, we are going to lose the effect of supply of 250,000 to 350,000 barrels a day, which is an awful lot more than anything that staff and I have been discussing on daily impact during the course of this hearing.

These studies we made assumed that that was going to be lost. In fact, some of the EIA studies that I referred to earlier have a higher number, 500,000 barrels a day; and that is something to be looked into.

The implementation of that program is discretionary with EPA. It could be considered. There could be an evaluation made which may, or may not take place.

Mr. WALGREN. I understand, but I feel it only proper to note that EPA is not requiring a reduction in the lead content because of its own whims. There are very substantial health reasons for pursuing the reduction of lead content in gasoline, as I understand it. It bothers me that we simply say, "well, one of the alternatives we have is to accept those risks," or "accept that harm."

Mr. BARDIN. Congressman Walgren, I am not saying "accept it." I happen to be the former environmental protection commissioner of the State of New Jersey with clean air responsibility, and I fought long and hard to back up some of the work that the full committee and the Health and the Environment Subcommittee of the full committee worked on, on the Clean Air amendments.

I am simply saying to you that in your responsibility, which happens to span the work of both agencies, there is an interrelationship between what happens on the EPA side and the DOE side.

Mr. WALGREN. I understand that.

Mr. BARDIN. There will be a shortage, or there will not be a shortage, depending on what we do. Mr. Sims has suggested to me by his statistics that the refiners could operate at a higher percentage of capacity; that is doing something. Now, your question to me seems to say, "Are we going to do nothing?" Do I sit in July advising this subcommittee thinking, one, we are going to do nothing, or move inadequately as a country and therefore have an energy shortage, and not tell the subcommittee. If that is the implication of the question I want to deny vigorously and firmly any such intention.

Quite the contrary. I have tried in my relations with this subcommittee and others, with the staffs, with the industry and in the public conferences to expose for discussion the various issues and concerns—let the chips fall where they may.

Mr. WALGREN. I think it only proper to note that there were substantial voices within the Department of Energy that were noting the rising shortage in gasoline, if not directly for the summer of 1978 and 1979, at least for 1980. So, at the time that we are saying that even

under the worst case, supplies could be in balance, there was a report within the Department of Energy which predicted a shortfall of a substantial amount in 1980.

Our problem candidly, Mr. Bardin, is that we are charged with the responsibility of understanding where the supplies of gasoline are going. We have some reports indicating substantial shortfalls by 1980; others saying supplies are going to be in balance and you do not need to worry; and then the Secretary comes out, calling the situation extremely disturbing less than 2 months later. If we are to have any confidence in our ability to regulate anything, it seems to me, we have to have a more solid, constant base of information flowing from DOE to the public.

Mr. BARDIN. We need a more penetrating investigation, a continuous penetrating investigation—let us not say “constant.” I think, Congressman, you would agree with me that we are not looking to stick by one figure, we are looking to revise it.

I am glad you asked the question you did because I do want to set the record straight on something which, frankly, maligns me unfairly and did in that last hearing, which I do not recall you had the opportunity to attend.

The hearing that took place discussed as if we were coming then forward with something brand new, saying something about supply and demand. In fact, it was based on that environmental assessment which we had put out some weeks before—a few weeks before—and there was an out-of-sequence time comparison there. I do not think that, if you took the trouble to track down the dates of each of these documents, that you would get that kind of relationship.

That does not diminish in any way from the validity of your basic point, that we are dealing with a changing target; we are dealing with a very important target, and there is a great value in the work that this subcommittee does, and the Department can do, and the industry can do and others, in trying to probe it. I am 100 percent in favor of an intensive probing and testing.

What actually happened there, there was a memo—and that was discussed at great length in the previous subcommittee hearing—a memo which was a very preliminary, anticipatory analysis of what the supply-demand balance might be. It prompted us to go into a deeper one, and we will be doing this repeatedly. Every few months we have to update these numbers and keep track of them. That is going to be true whether we deregulate motor gasoline, extend the EPAA to be a permanent statute, or come up with public utility regulations for the petroleum industry. We are just going to have to keep tabs on how this complicated system works, including our end, the 100 million motorists, as well as the other end.

Mr. WALGREN. I would like to yield to Congressman Marks for an observation.

Mr. MARKS. Thank you, Doug.

I would like to take this opportunity to break for a moment to introduce to you the mayor of the third-largest city in Pennsylvania. As I mentioned to you earlier, I anticipated him being able to break away for a few moments from his very, very heavy schedule. He has done that. He is sitting in the back of the room, and I would like to introduce to you, Congressman Walgren, Mr. Bardin, Dr. Gillespie, the

gentleman from Texaco, Mr. Donald Graham, and from Sun, Mr. Paul H. Hertel, the mayor of the city of Erie. We appreciate very much, Mayor, your coming down for the brief moment of being with us. Thank you.

May I suggest also that we appreciate very much the use of the council chamber, and I hope you will extend our thanks to the council generally for this great courtesy. Thank you, Mayor.

Mr. WALGREN. I would just like to pursue—believe me, I mean nothing personal in terms of any motive to misrepresent the facts in any way or at any time to the subcommittee in my previous questioning—the fact that we are dealing with 4 cents, and possibly a lot more. Four cents a gallon, literally billions of dollars being transferred from the American consumer to the oil companies.

We are also dealing with something that I believe has a real possibility of breaking through psychological barriers in this public to need to demand much higher wages. If the price of gasoline goes substantially higher than it is now, the demand for increased wages in our society is going to be increased substantially, perhaps much more dramatically than if other costs that were not as visible as gasoline, went up.

So, we are talking about a very, very basic point for our economy. When money like that is on the table, and when consequences like that are on the table, I would really like to understand at what levels in the Department these recommendations for decontrol are developed.

Let me ask you this, one of the basic reasons for decontrol is because, supposedly, under price control, investment is denied the attraction in the area that we are trying to increase supplies. It is my understanding that various people have made the point that there is not sufficient investment return in the unleaded refining section of the gasoline process.

Now, what consideration has the Department given to allowing a regulated return on investment, but a real return on investment that would solve that problem, before we turn to just saying, "As far as the Government is concerned, we have no interest in the price that is charged for unleaded gasoline"?

Mr. BARDIN. We have discussed that problem amongst several others of the existing regulations. The present regulations say, "Freeze the price at what it happened to be on May 15, 1973, and allow certain increases of certain costs to be passed through, over and above that."

That means implicitly, whatever return was being earned per gallon—not per dollar of investment but per gallon—in 1973 can continue; more cannot be passed through, no matter how much investment is made.

Congressman Walgren, I have been a regulator virtually all my life. I joined the Federal Power Commission staff in 1958 when I got out of the U.S. Army; stayed there 11 years under four administrations, the end of the Eisenhower, Kennedy-Johnson, the first year of the first Nixon administration; and I have been an environmental regulator.

The regulations that I inherit here from the Nixon administration are, frankly, a Frankenstein's monster. It is all very well to freeze prices in 1973 for a few months and then fiddle and tinker. But here we are at the next go-around of the the cycle of guidelines, wage-price

guidelines and all that—it takes you right back to what was it, 8 years ago, something like that. It does not make sense to continue these regulations any more.

It seems to me one of two things has to happen. Either you say, "This important commodity is like other important commodities and is to be covered by whatever anti-inflationary program we have"—and we happen to have one in place and being developed, and espoused, and argued about every day—or you decide, you want this industry to be a public utility industry. If that is what you want, I think the politically responsible way to do it is by act of Congress. But, set that aside, whether it is by act of Congress or regulations that I develop and sign, it is going to take not months, but years—in my judgment at least 2 years—to do that, and would involve a radical transformation of this industry.

I have not heard anybody on any side of this debate suggest that kind of transformation. I do not think people who are, understandably, concerned about the possibility of an increase in price which, we estimate, might be as high as 4 cents a gallon over 2 years—due to the de-regulation, standing alone. I do not think the opponents of that de-regulation have faced up to the implication of putting this refining industry on a public utility footing.

Now, I would be delighted to visit with you, or any other Member of Congress, and discuss it in detail. But, you would then have to do something like what they have in Israel; you would have to put it on a rate-base, cost-of-service method related to the particular company. Since there is such a variation in cost and you would probably want a reasonable uniformity in the price of gasoline, home heating oil, and the like, you would have to have a permanent equalization fund, in my judgment.

It is done in some parts of the world. We have tried it only once that I know of, personally, and that was with the railroads. We junked it after the experience in the 1920's, and we ought to think long, and hard, and carefully in the Commerce Committee before that kind of program is undertaken.

I am personally delighted that you are asking me these questions. Do not misunderstand me; I think they are profound and important questions. But, you know, every time these questions come up I am asked by Congress; I am asked from the Secretary's office; I am asked from people in other parts of the executive branch, "Why do you not fix that problem with an amendment to the regulations?" There is a whole host of interrelated problems which start from the basic flaw that this regulatory scheme under the Emergency Petroleum Allocation Act is a price freeze plus add on certain features. That is not a permanent system of regulation. It is not like what we do for electric utilities, gas companies, or anything else. That is not what we did—and I am one of the architects of the program to regulate natural gas at the wellhead—when we set up the area prices for it.

So, can it be done? Yes, I could amend the regulations to allow it. In fact, I have an amendment to propose, the Motor Gasoline Tilt, which indirectly would cover some of that ground; but it is not a long-term adequate solution.

Mr. WALGREN. Well, the difficulty, of course, is that we are in a position where people are being asked to accept a wage freeze. There is a great variety of opinion in this country that is very reluctant to

accept wage freezes without some kind of controls on the other side of the equation.

Your estimates are that it will be 4 cents over 2 years, which certainly would be within the 7 percent. Have the oil companies indicated to the administration that they are willing to live within the administration's pricing guidelines?

Mr. BARDIN. I am sorry, I do not know the answer to that question.

Mr. WALGREN. I appreciate your cooperation very much, and I am pleased you came to Pennsylvania for my purposes, to Erie for Mr. Marks' purpose. I shudder to think what the public must think about our abilities to actually get an estimate and pin these things down, so that we are not constantly surprised. Maybe that is the best argument against regulation that can possibly be made.

I appreciate your coming.

Mr. MARKS. Mr. Bardin, on behalf of the subcommittee, the chairman of that committee, Mr. Moss; the staff, and certainly myself; the people who have been with us, we appreciate very much both of you and Dr. Gillespie being with us today. We look forward to a continuing rapport and communication between yourselves and our committee, as we have had in the past.

Thank you very much. May I say, your cab is ready and waiting; and if necessary the chief of police will provide you the adequate protection to get out.

Mr. BARDIN. Thank you for the many courtesies you have shown today and the subcommittee has always shown.

Mr. MARKS. At this time, ladies and gentlemen, we are going to take a 5-minute recess.

[Brief recess.]

Mr. MARKS. We would like to reconvene the hearing if we may at this time, please. The hearing will come to order.

Before introducing and having the testimony of Mr. Donald Graham from Texaco, I would like to introduce to you—if I can see him here—Mr. Carl "Skip" Cannavino, who is treasurer. We appreciate very much, Skip, your coming in. This is Congressman Walgren, Mr. Graham, Mr. Galloway, Mr. Sims of our staff. We are pleased to have you join us. Thank you.

At this time, Mr. Graham, we would appreciate if you would rise and take the oath. Perhaps, before that, would you mention the name of the gentleman who is with you, and his capacity in being here?

Mr. GRAHAM. He is our counsel, Mr. Rudy, Mr. Mike Rudy.

Mr. MARKS. Mr. Rudy, welcome.

Mr. RUDY. Thank you.

Mr. MARKS. If you plan to testify, Mr. Rudy, we would like you to be sworn.

Mr. RUDY. I do not plan to testify, but I may make some remarks.

Mr. MARKS. Why not? Will you raise your right hand, please? Do you solemnly swear to tell the whole truth, so help you God?

Mr. GRAHAM. I do.

Mr. RUDY. I do.

Mr. MARKS. Mr. Donald Graham is the general manager of Supply and Distribution for Petroleum Products Division of Texaco, Inc. We welcome you, Mr. Graham and, of course, Mr. Rudy.

If you have a prepared statement, we would appreciate it if you would file that with us and perhaps take a few moments to summarize it, rather than go through it, unless it is not very lengthy.

Mr. GRAHAM. I do not think it is very lengthy; it is some 6 pages, widely typed.

Mr. MARKS. Fine. Please proceed. I might say, unless you have a transportation problem, we are willing to give you as much time as you need, in consideration, of course, of the fact that we have another witness to hear from, from Sun.

Mr. GRAHAM. I will not have a problem. So, you will cut this off, I am sure, when you are ready.

**TESTIMONY OF DONALD N. GRAHAM, GENERAL MANAGER, SUPPLY AND DISTRIBUTION FOR PETROLEUM PRODUCTS DIVISION, TEXACO INC., ACCOMPANIED BY MIKE RUDY, COUNSEL**

Mr. GRAHAM. My name is Donald N. Graham, general manager, supply and distribution of Texaco's petroleum products department, U.S.A.

The subject of these hearings is the currently tight situation in the gasoline market. Let me state at the outset that Texaco regrets that these hearings are necessary. It is neither our doing nor in our interest that Texaco and the rest of the petroleum industry face a period of uncertainty in meeting the continuing unexpectedly strong demand for gasoline just when the demand for heating oil moves towards its seasonal peak. Texaco takes seriously its responsibility to provide continuous and adequate supply at reasonable prices to its customers.

Texaco is not now allocating gasoline. There are enough uncertainties in the market, however, that we have requested the Department of Energy to allow us to update the base period against which we allocate, if we are obliged to do so by events, from 1972 to 1977-78.

There are indeed uncertainties in the market place. Gasoline sales by the industry during the first 11 months of 1978 were 3.2 percent over 1977, while most forecasts anticipated a more modest increase of about 2 percent. Normally, gasoline demand falls off rather dramatically following the Labor Day weekend, and refiners switch from a maximum gasoline production mode of operation to a maximum heating oil yield, anticipating the heating season. This year the good weather for driving continued, however, and Texaco and others have been obliged to maintain or revert to maximum gasoline production at our refineries. Heating oil production, as a result, will suffer, although we anticipate being able to cover our demand, assuming a normal winter, supplementing our own production with purchases and imports.

A number of refiners, including Texaco, have experienced unanticipated refinery or process unit shutdowns during the year. Such shutdowns are not altogether unknown in the industry, but in a tight market situation with little if any unused refining capacity in the industry, small outages are important.

There are, of course, other uncertainties in the market which may impact the availability of gasoline to the industry generally or to Texaco specifically. The political situation in Iran can deteriorate.

Forthcoming labor negotiations in the petroleum industry may result in supply disruptions. Prices are a factor creating uncertainty, since Government regulations can require price decreases just when supplies are tight and provide inadequate differentials between grades to offset costs.

The major factor contributing to the current tightness in the gasoline market, however, is the regulatory environment. Through a hideously complex web of regulations, we are, as a nation, at the same time:

Encouraging the consumption of petroleum products by constraining prices below market clearing levels, while exhorting the virtues of conservation.

Urging the construction of new refineries and the upgrading of existing facilities, while denying potential investors the ability to recover the costs of such investments in the marketplace.

Requiring the reduction of lead in gasoline while not allowing refiners to recover through price the costs of doing so.

Subsidizing the importation of foreign crude oil while urging reduced dependence on foreign supply and penalizing imports of foreign products.

With such a host of inconsistencies in our energy regulations, is it any wonder that we find ourselves in our current situation? Needed investments are discouraged, legitimate cost recovery is denied, and consumption is subsidized below replacement cost.

So much for where we are and how we got there. How do we disentangle ourselves? From the industry's standpoint, it is tempting to say simply, "Leave us alone; we'll manage." We could, too. Recognizing reality for what it is, however, let us work together, and let us do some things that will help immediately.

Let price help. Decontrol of gasoline may result in increased prices at the pump, but it will also motivate refiners to produce more, importers to import more, and consumers to use less.

If decontrol is not feasible immediately, allow gasoline related refining costs to be passed through to the market; allow refiners to recover additional legitimate costs not now recoverable; allow some of the benefits of cost reduction investment to flow to the investor; and update the base period that would be used in the event gasoline allocation is required.

Examine the present lead phasedown regulations to determine if, with some modification and postponement, additional supplies of gasoline can be made available over the next few years without sacrificing our basic environmental objectives.

These steps can be accomplished by and large through administrative action by the executive branch. Gasoline decontrol requires the consent by nonobjection of the Congress. New laws are not required, only the reasonable administration of the existing ones.

Texaco is ready to respond to the suggested steps if taken. In the absence of such action, however, with gasoline sales running in excess of our own production capacity, Texaco, in order to supply its customers, finds itself having to continue and to increase purchases on the open market at uneconomic costs. This we cannot continue to do, even if product is available. To do so would be irresponsible to our stockholders, and in the long run to the market we serve.

Mr. MARKS. Thank you, Mr. Graham.

I am particularly glad to welcome you and have you here today, as is Congressman Walgren, in view of certain perspectives that I believe Texaco is somewhat uniquely able to bring to our discussion because of Texaco's current situation in the gasoline market.

Texaco, of course, is one of the major oil companies that in recent days has submitted an allocation plan to the Department of Energy for approval in the event—and I underline that, “in the event”—that it should be forced to curtail gasoline deliveries. Is that not correct?

Mr. GRAHAM. That is correct.

Mr. MARKS. However, to date Texaco has not been forced to curtail gasoline deliveries; am I right?

Mr. GRAHAM. By allocation, that is correct.

Mr. MARKS. I would like to introduce into the record a copy of the proposed contingency allocation plan that Texaco has submitted to the Department of Energy for approval, which was given to the Department, as I understand, on December 1, 1978.

[Testimony resumes on p. 61.]

[The document referred to follows:]

TEXACO  
INC.

2000 WESTCHESTER AVENUE  
WHITE PLAINS, NEW YORK 10650

MICHAEL H. RUDY  
ATTORNEY

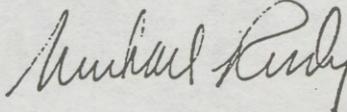
December 1, 1978

Department of Energy  
Office of Hearings & Appeals  
Washington, D. C. 20461

Gentlemen:

Enclosed for filing please find Texaco Inc.'s  
Application for Exception from 10 C.F.R. §§ 211.10  
and 211.102.

Very truly yours,



MHR:LA  
Enclosure

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Department of Energy  
Office of Hearings and Appeals  
Washington, D.C.

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OFFICE OF HEARINGS AND APPEALS  
NOV 29 1978

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In the Matter of :  
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 TEXACO INC. :  
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 Application for Exception :  
 from 10 C.F.R. §§211.10 :  
 and 211.102 :  
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Case No. DEE-2041

Michael H. Rudy  
Attorney, Texaco Inc.  
2000 Westchester Avenue  
White Plains, New York 10605  
December 1, 1978

APPLICATION FOR EXCEPTION

In accordance with the provisions of 10 C.F.R. Part 205, Subpart D, Texaco Inc. ("Texaco") hereby requests the Department of Energy to grant Texaco an exception from the provisions of 10 C.F.R. §§211.10 and 211.102 which require that a supplier, in determining an allocation fraction, shall base its supply on base period volumes during 1972, as adjusted. Texaco seeks exception relief for a period commencing December 1, 1978 through March 31, 1979 to adjust Texaco's customers' allocation entitlements to the level of such customers' purchases in the corresponding month of the preceding year. Texaco submits that the requested exception relief will permit Texaco to distribute its available supplies of gasoline, in the event it elects to allocate those supplies, in a way that more closely reflects the current demand pattern among its customers than does the 1972 base period specified in 10 C.F.R. 211.102.

To the present time, Texaco has been able to purchase on the open market sufficient gasoline to supplement supplies from its equity refining system in order to meet its contractual and base period supply obligations to its wholesalers and the requirements of its retailers. However, several foreseeable events, if they occur, could force Texaco to allocate its avails of gasoline. Such an allocation, implemented in accordance with the base period

specified in 10 C.F.R. 211.102, would certainly result in a serious hardship and gross inequity to Texaco's independent retailers. It is to protect the livelihood of these independent retailers that Texaco is submitting this Application for Exception.

At the present time, Texaco's equity refining capacity is only approximately 3 of its anticipated sales in 1978 and 1979. Therefore, Texaco is, and will be for the foreseeable future, heavily dependent on the availability of refined products on the open market. This source of supply could be adversely affected by a myriad of occurrences, such as: (1) a worsening or prolongation of the current labor unrest in Iran, a source of the United States' crude oil supplies; (2) a strike by members of OCAW (the Oil, Chemical and Atomic Workers Union) when their current contracts expire on January 7, 1979; (3) greater-than-anticipated consumption of gasoline by consumers; (4) unanticipated refinery shutdowns; (5) unusual weather conditions making deliveries of crude oil to Gulf Coast refineries difficult, and others.

In addition to difficulties which could occur in purchasing refined products on the open market, Texaco could also, of course, experience unanticipated problems within its own supply system. For example, unscheduled refinery downtime, logistical difficulties in delivery of refined products to terminals caused by bad weather or accidents,

etc. In fact, Texaco has already been experiencing some spot shortages in recent months.

As stated previously, Texaco has to date generally been able to purchase sufficient products to satisfy the needs of its customers. The cost to Texaco of continuing to do so, however, is becoming increasingly prohibitive and its ability to do so is becoming increasingly uncertain. Therefore, the occurrence of any of the events enumerated in the previous paragraph, or other unforeseen events, could make immediate allocation necessary. By this Application, Texaco is seeking to "put its house in order" so as to prevent the certain severe hardships and inequities which would result from an allocation under the current allocation regulations.

Texaco's retailers would be uniquely and more seriously affected by the necessity of an allocation than retailers served by most other major refiners, because of Texaco's fairly equal distribution of gasoline between the retail and wholesale classes of trade. In September, 1978, for example, Texaco sold % of its motor gasoline through the wholesaler class of trade and % through the retailer class. However, Texaco's distributors have purchased less than their adjusted base period allocations, while Texaco's retailers have purchased, as a class, substantially more than their adjusted base period allocations. Therefore, if Texaco declares a 1.0 allocation, Texaco's retailer class will suffer a decline in its ability to purchase gasoline, while Texaco's distributor class would suffer no decline at all.

Furthermore, the lower the allocation fraction, the more disproportionate the burden on Texaco's retailers.

The need for an updated base period was recognized by the FEA last year and enunciated in its April 20, 1977 Notice of Proposed Rulemaking as follows:

Since elimination of the "changed circumstances" provision in October of 1974 (39 FR 36854, October 25, 1974), there have been limited means available under the Mandatory Petroleum Allocation Regulations to effect adjustments in the base period uses of motor gasoline retail sales outlets, bulk purchasers, and wholesale purchaser-consumers to reflect changes in supply requirements. Upward adjustments to existing retail sales outlets' base period use have only been made through the exceptions process pursuant to FEA's regulations for its Administrative Procedures and Sanctions (10 CFR Part 205), in cases where a serious hardship or gross inequity can be established.

Information available to FEA indicates that significant changes in demand patterns have been occurring in the retail gasoline market. There is evidence of continuing growth in retail demand which has at the same time been accompanied by a general decrease in the number of retail outlets. Average volumes per station are shifting significantly from base period uses as established and adjusted during 1974. The sustained trend within the retail market toward lower-cost, higher-volume gasoline marketing methods appears to be continuing. Many firms have renovated retail outlets for the purpose of changing marketing methods and have been purchasing and retailing surplus product to meet their increased product needs.

Surplus product has been generally available to meet the normal growth requirements of retail outlets. However, not all retail outlets have experienced growth and many have

experienced actual declines in volumes throughout, which accounts in part for the surplus product available. In the event of any shortages in the supplies of motor gasoline, current regulations provide that all purchasers would receive allocations as set forth in Subparts A and F of 10 CFR Part 211, which include provisions for application of a supplier's allocation fraction to its purchasers' established base period uses. Thus, those marketers who have grown and have been relying on surplus product would be severely disadvantaged by a shortage, while those which have experienced declines in throughput would be entitled during shortage periods to purchase supplies in excess of their current actual sales volumes.

If FEA's view of the current market situation is correct, severe market distortions and inequities as between retailers could occur if outlets which are retailing significantly increased volumes of motor gasoline were restricted by 1972 base period use levels in the event of any shortage of product supplies. In particular, competitive inequities could result in cases where an outlet currently relying on surplus product would be forced to operate at or below base period levels and compete with a new high volume outlet that under current regulations has been assigned a base period use reflective of high volume operations. Furthermore, consumers in high growth areas which are served by outlets relying heavily on surplus product might not have access to an equitable share of product in a shortage.

FEA recognizes that its regulations should to the maximum extent practicable, be consistent with the objectives set forth in Section 4(b) (1) of the Emergency Petroleum Allocation Act of 1973, Pub. L. 93-159, as amended ("EPAA"). FEA believes that the amendments being proposed today, reflecting an attempt to update the regulations to account for current market conditions, would render the regulations more in conformity with the objectives of EPAA.

The DOE has recently reaffirmed the inequities of the present regulations in granting a stay to Shell Oil Company to permit Shell to allocate motor gasoline on the basis of their customers' actual purchases during the corresponding month of 1977 or the 1972 base period, whichever is greater. In its Decision and Order dated November 22, 1978 (Case Number DST-2014) the DOE stated:

"Having reviewed Shell's submission, we have concluded that the firm's request for temporary stay relief should be granted. Under the DOE allocation regulations, 20 C.F.R. Par 211, Shell would be required to impose an allocation fraction of less than 1.0 if its motor gasoline supply is insufficient to fully meet its supply obligation. If Shell does impose an allocation fraction, those dealers who are supplied directly by the firm would be subject to significantly greater problems than the dealers who are supplied by Shell-branded jobbers. This results from the fact that under the regulations, dealers who are directly supplied have generally not obtained adjustments to their base period allocations to reflect expanding business activities. On the other hand, jobbers that have been assigned new or increased supply obligations subsequent to the 1972 base period have generally increased their allocations automatically under the "upward certification" provisions of 10 C.F.R. 211.13(c). In addition, the jobbers may retain the allocations of dealers who have gone out of business since 1972. Consequently, the allocation levels of dealers supplied by jobbers more closely reflect current market conditions, whereas the allocations of directly supplied dealers have generally remained at 1972 base period levels.

In the present situation, it appears that the combined effect of changes in the industry since 1972, and the general operation of the DOE allocation and price regulations, will cause the class of dealers supplied directly by Shell to bear a

significantly greater burden than the class of dealers supplied by Shell jobbers. Accordingly, we have determined that Shell should be granted a temporary stay, as an emergency measure, in order to prevent such an unfair distribution of burdens. The relief will be implemented by permitting the firm to temporarily allocate motor gasoline on the basis of a customer's actual purchases of motor gasoline during the corresponding month of 1977, or the 1972 base period, whichever is greater. This relief will more fairly distribute the burdens associated with Shell's supply shortage in accordance with the current state of Shell's marketing and distribution system."

The potential crisis Texaco and its dealers face is essentially the same as that faced by Shell and its dealers.

In 1972 approximately \_\_\_\_\_ gallons or \_\_\_\_\_ % of Texaco's total motor gasoline sales were made through distributors and \_\_\_\_\_ gallons, or \_\_\_\_\_ % were made through Texaco's resale class of trade (open retailers investment retailers, etc.). In 1978 that ratio has changed completely: \_\_\_\_\_ gallons, or \_\_\_\_\_ %, will be sold through distributors and \_\_\_\_\_ gallons, or \_\_\_\_\_ %, will be sold through the resale class of trade. In other words, both the total volume and percent of sales has gone up for distributors and down for resale customers. (Texaco had some company operated stations in 1972 and has \_\_\_\_\_ today, but the average sales at these stations is only slightly higher than their average adjusted base period allocations, and therefore the overall impact of current regulations upon these stations does not impose a special hardship on Texaco).

The resale class of trade, as just mentioned, includes small independent retailers, comprised of "investment retailers" (retailers who occupy stations leased to them by Texaco) and open and first party retailers who own their own stations or lease them from third parties. In 1972, there were investment retailers selling an average of . gallons per month. Today there are only investment retailers, but these remaining retailers sell an average of gallons per month. The statistics for Texaco's other retailers are even more dramatic. In 1972, there were approximately open retailers selling an average of gallons per month. Today there are . open retailers selling an average of . gallons per month, over twice the average sales of such stations in 1972.

A sampling of investment retailers in Texaco's Los Angeles, Atlanta, and Houston divisions (which Texaco believes are representative of investment retailers nationwide) shows that % of such retailers are currently purchasing more than their base period allocations, and half of those are buying more than 150% of their base period allocations. A sampling of open retailers shows that almost % of them are purchasing more than their base period allocations.

This shift in demand patterns is the result of normal market forces such as:

1. Traffic patterns have shifted with population changes and road construction;

2. Uneconomic stations throughout the industry have been closed at record rates;
3. The self-serve mode of gasoline marketing has grown from virtually nothing in 1972 to the point that a significant percentage of stations now offer total self-serve or "split-island" self-service (for example, approximately half of Texaco's investment stations now offer either full self-serve or split-island self-serve);  
and
4. Gasoline-only operation has become economically viable.

These shifts in demand patterns have been accommodated by application of the "redistribution" provisions of the DOE regulations, whereby product made available by underliftings from some units can be made available to satisfy growth at other locations. However, should Texaco be required to declare an allocation fraction based upon adjusted 1972 volumes, redistribution to direct served retailers would become impossible and Texaco predicts the following consequences:

1. At a 1.0 allocation fraction, many Texaco retailers would be able to purchase only a fraction of their current requirements of gasoline. Furthermore, if Texaco declared an 80% allocation fraction, most of Texaco's retailers would

suffer severe shortages and over 25% of Texaco's investment retailers, for example, could purchase only 53% or less of their current requirements.

2. Since gasoline sales represent approximately 84% of the revenue received by the average retailer and about 59% of his gross profits, a decrease in gasoline sales of 47% would represent a decrease in his profits of about 28% (Source: 1977 NPH Factbook )

3. If half of Texaco's investment station retailers and 20% of its other retailers cannot purchase their requirements of gasoline, and cannot get surplus gasoline elsewhere, the DOE will be deluged with thousands of requests for change of supplier, for increases in base period allocations, and for other types of exception relief. It is questionable whether the DOE has the manpower to handle these requests expeditiously enough to afford these retailers any meaningful relief.

Granting Texaco and its customers the exception relief requested herein will further the goals enunciated in Section 4(b)(1) of the EPAA in that it will provide for (1) the preservation of Texaco retailers as an integral and competitive element in the petroleum industry and (2) the equitable distribution of refined petroleum products among all sectors of the petroleum industry, including branded independent marketers.

While a change in the base period from the corresponding month in 1972 to the corresponding month in the

previous year will certainly do nothing to increase Texaco's avails of gasoline, it will permit Texaco's directly served retailers to obtain a more equitable share of those avails. Without such a change, the disparity between the allocations available to Texaco's distributors and their retailers on the one hand and Texaco's directly served retailers on the other will further increase.

More importantly, a failure to permit Texaco to distribute its available supplies of gasoline in accordance with a more current base period, in the event of a shortage of gasoline avails, will certainly cause substantial numbers of small businessmen to go out of business.

#### RELIEF REQUESTED

Texaco requests an exception from 10 C.F.R. 211.10 and 211.102 so that in the event it elects to allocate its allocable supply of gasoline to its wholesale purchasers and end-users, it may do so during the period from December 1, 1978 to and including March 31, 1979 based upon each purchaser's purchases during the corresponding calendar month of the preceding year.

Texaco has limited the time for which it seeks exception relief to the period from December 1, 1978 to March 31, 1979 for the following reasons:

(1) Secretary Schlesinger has recently stated at a press conference that a proposal to decontrol gasoline will

soon be sent to Congress. It is anticipated that if Congress ratifies this proposal, decontrol would be achieved prior to March 31, 1978.

(2) On November 14, 1978 Texaco submitted to Mr. David Bardin, Administrator of the Economic Regulatory Administration, a Petition for Rulemaking to Amend the definition of "base period" in 10 C.F.R. Section 211.102. It is hoped that if gasoline has not been decontrolled by March 31, 1978, Texaco's Petition for Rulemaking will have been acted on by that time, and that the relief requested herein will have been codified in the allocation regulations.

(3) Implementing the changes requested herein will have minimal impact upon consumers, particularly since the period involved is a period of historically reduced gasoline demand. (While Texaco may be required to seek additional exception relief for the period subsequent to March 31, 1979 if gasoline is not decontrolled and the "base period" is not changed by rule change by that time, the changed base periods will have been computed and operational. Thus, continuing the procedures then in effect at that time would have no disruptive effect on consumers).

#### Procedural Certifications

(1) I hereby certify that I am a duly authorized agent and representative of Texaco Inc. for purposes of filing this Application for Exception.

(2) To the best of Texaco's knowledge, other than as herein described, the same or related issues, acts or transactions have not been nor are they presently being considered or investigated by any other federal agency, department or instrumentality; or by a state office, a state or municipal agency or court or any law enforcement agency. On November 9, 1978 Messrs. Card, Seamans, Tell, Goldman and Slye, employees of Texaco Inc. met with Mr. David C. Bardin and several members of his staff at Mr. Bardin's office. At this meeting the matters raised in this submission were discussed. On November 14, 1978 Texaco submitted a Petition for Rulemaking to amend the definition of "base period" in 10 C.F.R. §211.102. On November 16, 1978, Shell Oil Company filed an Application for Exception with the Office of Hearings and Appeals. Shell's Application raises similar issues and requests similar relief to the issues raised and relief requested herein.

(3) Texaco hereby requests that confidential treatment be granted for certain sales and supply data contained in this Application. This treatment is requested on the grounds that this material is exempt from the mandatory public disclosure requirements of the Freedom of Information Act (5 U.S.C. §552). This information comes within the exception in 5 U.S.C. §552(b)(4) for trade secrets and commercial or financial information. Texaco is supplying two additional copies of this Application from which confidential information has been deleted.

(4) To the best knowledge of the undersigned, most of Texaco's retailers and wholesalers would be affected by the granting of this Application. Texaco had determined that compliance with Section 205.53(a) of the DOE's regulations is impracticable since Texaco has approximately 15,000 dealers and wholesalers. Therefore, Texaco has determined that it is reasonable and practicable to notify the following persons who may be aggrieved by the denial of this Application for Exception:

The National Congress of  
Petroleum Retailers  
Attn: Mr. Charles Binsted  
N.W. 2021 K Street, N.W.  
Washington, D.C. 20006

National Oil Jobbers Council  
Attn: Mr. Robert Bassman  
1715 New York Avenue,  
Washington, D.C. 20006

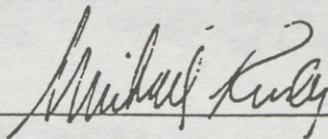
The National Association of  
Texaco Wholesalers, Inc.  
Attn: Jack E. Meintzer, Jr.  
President  
P.O. Box 95265  
Atlanta, Georgia 30347

Mr. Tom R. Jackson  
Anderson Oil Co., Inc.  
Box 8  
Williston, S. C. 29853

On November 16, 1978 Shell Oil Company filed an Application for Exception with the Office of Hearings and Appeals in which Shell requested relief similar to that requested herein. Shell represented in that petition that service of its Application upon its approximately 8,300 dealers and jobbers would be impracticable, and, in lieu of service on each of them, notified the National Congress of Petroleum Retailers, the National Oil Jobbers Council, and thirteen members of the "Shell Jobber Council". It is Texaco's understanding that this mode of service was satis-

factory to the Office of Hearings and Appeals and therefore Texaco has given similar notification pursuant to 10 C.F.R. 205.53(b). Inasmuch as there is no organization of Texaco's wholesalers exactly like the Shell Jobber Council, Texaco has given notification to The National Association of Texaco Wholesalers, Inc. and to Mr. Tom R. Jackson, who is the Texaco Brand Chairman of the National Oil Jobbers Council.

(5) Texaco does not request a conference or public hearing regarding this Application. Texaco does, however, intend to participate in the Public Hearing to be convened by the Office of Hearings and Appeals on December 8, 1978 on Shell Oil Company's Application for Exception, which Application involves similar issues.

A handwritten signature in cursive script, reading "Michael H. Rudy", is written over a horizontal line.

MICHAEL H. RUDY

Dated: December 1, 1978

CERTIFICATE OF SERVICE

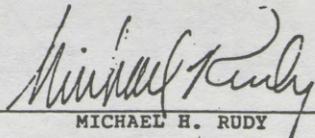
The undersigned hereby certifies that the foregoing Application for Exception has been sent by United States mail to the following persons and each person has been notified that such person may submit comments regarding this Application for Exception to the Office of Hearings and Appeals within ten days.

The National Congress of  
Petroleum Retailers  
Attn: Mr. Charles Binsted  
N.W. 2021 K Street, N.W.  
Washington, D.C. 20006

National Oil Jobbers Council  
Attn: Mr. Robert Bassman  
1715 New York Avenue,  
Washington, D.C. 20006

The National Association of  
Texaco Wholesalers, Inc.  
Attn: Jack E. Meinstzer, Jr.  
President  
P.O. Box 95265  
Atlanta, Georgia 30347

Mr. Tom R. Jackson  
Anderson Oil Co., Inc.  
Box 8  
Williston, S. C. 29853



MICHAEL H. RUDY

Mr. MARKS. Having that in front of you—as I assume you do now—would you turn to page 2 of that petition, please? Mr. Graham, I note that Texaco is unable—and I understand that this has been the case traditionally with Texaco—to refine all the gasoline that it sells; and that accordingly Texaco is forced to purchase gasoline on the spot, or what we call the open market. Is that correct, sir?

Mr. GRAHAM. The first part of your question, I think, I missed.

Mr. MARKS. The first part of my question is this, as I understand it, Mr. Graham, Texaco is unable—and I understand that this has been the case, actually, traditionally with Texaco—to refine all the gasoline that it sells.

Mr. GRAHAM. That is correct, yes.

Mr. MARKS. That accordingly, Texaco is forced to purchase gasoline on the open or spot market.

Mr. GRAHAM. That is right.

Mr. MARKS. Texaco's reliance on the open market renders it particularly vulnerable, does it not, to declines in gasoline supply?

Mr. GRAHAM. That would be right, yes.

Mr. MARKS. And that, of course, in turn leads to Texaco's petition to the DOE; is that correct?

Mr. GRAHAM. That is part of it, yes. Excuse me, were you going to continue with your question?

Mr. MARKS. If you want to answer that more fully, we will be pleased to have it on the record.

Mr. GRAHAM. All right. Historically, the policy of Texaco has been to sell more than it refines, and the difference has been made up by processing with other refineries purchases and imports. This policy in the past has served Texaco well.

Very recently we have lost one of the processing agreements that we had, and that has caused us one of the concerns here—the contingency plan, if you want to put it that way.

Mr. MARKS. Mr. Graham, Texaco's concern over the short-term future of the open market is spelled out on page 2 of the petition that you have in front of you.

Mr. RUDY. Excuse me, Congressman, we were having our table rearranged while you started that question.

Mr. MARKS. Certainly, I would be glad to ask the question again. Texaco's concern over the short-term future of the open market is spelled out, I believe, on page 2 of the petition that you have there, and which Texaco filed, where Texaco lists five factors that could adversely affect gasoline supplies.

Now, some of those are the same factors that I reviewed with the DOE witnesses previously. We, of course, do not know if any of those unfortunate developments will come to pass in the next 6 months. But I would assume, based on Texaco's petition, that a combination, or even one of those developments, could in fact lead to a fairly widespread supply shortage. Would that be correct?

Mr. GRAHAM. Well, "widespread" in areas since the requirement if we allocate, that it would be nationwide; that is the regulation.

Now, widespread from a volume standpoint would not be that significant.

Mr. MARKS. One of the items on your list of lurking problems is No. 3, "Greater than anticipated consumption of gasoline by con-

sumers." I wonder if you could explain that for us. What does Texaco anticipate the average monthly increase in demand for gasoline to be for the next 6 months?

I might say that the 5.2-percent increase in demand that was experienced this past November over last November, or the 2.5 increase in demand that was generally forecast by the industry at the beginning of this year.

Mr. GRAHAM. Our forecast for the industry for next year is somewhere between 2 and 3 percent, the increase. For Texaco we do not anticipate to have that kind of an increase.

As you know, we are withdrawing from certain areas, withdrawing from the market in the upper Midwest and the upper Rocky Mountain area. Hopefully, these shortfalls will offset any other increases that we make.

Mr. MARKS. You are using a figure of 2.5, was that what you were using?

Mr. GRAHAM. It would be in the range somewhere between 2 and 3, 2.5 percent.

Mr. MARKS. The 5.2 figure, I take it by your answer, obviously, you do not agree with, that it might be as high as 5.2.

Mr. GRAHAM. No, we do not.

Mr. MARKS. The reason we find that interesting is, that happens to be the current demand.

Mr. GRAHAM. That is right.

Mr. MARKS. I am curious, if in fact the 5.2 is the current demand, your projection about the 2.5. How did you get to that figure?

Mr. GRAHAM. I am a little out of my field, excuse me, I am supply and demand. You are talking about forecasts, finance and economics, looking forward. You have gotten me a little out of my area. So, what I am quoting for you is what we hear from them now. You are asking me, how did they arrive at those numbers and why did they not continue the 5.2—I do not know. I would be happy to find that out for you.

Mr. MARKS. I was going to suggest that this would be very important to this committee and the Nation. We would appreciate it, and we will hold the record open at this point for you to get us that answer.

[The information requested was not available at the time of printing.]

Mr. MARKS. It is a fact, however, that if your projection of 2.5 is not correct, if you have miscalculated and it is, say, 5 percent, then we really have ourselves a serious problem; do we not?

Mr. GRAHAM. The industry is going to be tight next year. We think it is going to be tight next year.

Mr. MARKS. So, what you are saying is, yes.

Mr. GRAHAM. Yes, by whatever that difference in percent would be, if it does go to 5.2.

Mr. MARKS. A continuation, obviously, of that trend, that demand trend, if it is coupled with one or more of the other factors cited in your brief, raises the specter, I would assume, of at least a potentially serious shortage

Mr. GRAHAM. Again, tight. How serious depends on how tight.

Mr. MARKS. I am sure that you are trying to answer the question as candidly as you can.

Mr. GRAHAM. Right.

Mr. MARKS. I think it is important that I say to you that the comments I received from the ladies and gentlemen who were here earlier when the Department of Energy witnesses testified, as I went out during our brief recess—and which was obvious to Congressman Walgren and myself, and the staff—was that they were not really as direct and candid in their answers as we thought they could be, in some areas. I appreciate the fact that you are trying. May I suggest to you that when you get to the point—as we may be now—that you be as candid as you can be with us because, what you are now saying, of course, is not only of great interest to this subcommittee and the Congress of the United States, but to the people of this country.

When I say, "A potentially serious shortage", if you can agree with that, I think it will be better that we know that now. I think what you are trying to say is, "Yes, in fact it could be."

Mr. GRAHAM. If we were going to restrict the question to Texaco and its supply, I would say, yes, if any of these were to happen.

Mr. MARKS. Mr. Graham, there is talk within the industry that, if the Department of Energy approves Texaco's allocation plans, Texaco might declare then an 80-percent allocation fraction. Admittedly, the regulations are very complex on that point. That required Texaco deliveries of gasoline to customers would be cut 20 percent.

Indeed, page 9 of Texaco's petition sets forth the possibility of an 80-percent supply fraction. Is that a realistic possibility in your mind?

Mr. GRAHAM. Well, 80 percent is not, against what we are selling today. Eighty percent is an adjusted base which is well above what we have been marketing, and well above what we plan to market. The 80 percent goes against the factor that the distributors and other people in the marketplace have gone back to 1972, gotten an adjusted base. That adjusts a high number, so we have to take a high number to start with.

Mr. MARKS. So, what you are saying, it is really more than 20 percent; is it not?

Mr. GRAHAM. No, no, from what we sell it is much less than 20 percent.

Mr. MARKS. This point is exceedingly complex, and I would hope that we do not have to get bogged down in needless details. I would like to appreciate what a supply shortage of that magnitude would mean, were the Department of Energy not to approve Texaco's approved curtailment plan; and assuming that Texaco is unable to provide an amount of gasoline equivalent to an 80-percent allocation fraction. The resulting cutback in deliveries to Texaco retailers would result, would it not, in a severe shortage at Texaco stations? Indeed, as noted on page 10 of your petition, over 25 percent of Texaco dealers would receive only 53 percent—53 percent—of their current requirements. Is that correct?

Mr. GRAHAM. You are talking of Texaco investment retailers.

Mr. MARKS. Dealers.

Mr. GRAHAM. There are basically two or three classes of trade. Now, we are talking about, one, a distributor, who is a wholesaler. The distributors have, by regulation, greater opportunity to get their

bases adjusted, and have. In many cases they have gotten new bases that they have never sold and probably could not sell; but they have a high number.

The retailers are of two classes, one is our investment stations, and then there are other retail outlets.

Mr. MARKS. What you mean by that, you own some of the stations yourselves?

Mr. GRAHAM. We own and lease out to independent business people.

Mr. MARKS. Right.

Mr. GRAHAM. Then, there are other retail outlets which are outright owned by the service operator. The latter two are retail outlets. In other words, the Texaco retail dealer, lease-owned stations, and those owned by other retail outlets, have not had the opportunity, the regulations have encumbered them from getting adjusted bases. Some, during the period, they have gotten some.

So, what we have to do is add up all the 1972, 1973 bases, and then we add up the adjusted bases of the distributors; then we come up with a new total. With that total, and placing supplies against that, then we end up with a fraction.

Well, obviously, the retailers, the Mom & Pops, the smaller ones that you see around here, are going to take a bigger penalty if we have to allocate. It would not be fair to have the local ones suffer. Do I make myself clear?

Mr. MARKS. I think you do because I think what you are saying is—and certainly, that is backed up by your petition which may or may not be a bit qualified by which you are now saying—that 25 percent of what we call the “Mom & Pop” stations are going to take a 53 percent decrease.

Mr. GRAHAM. Yes.

Mr. RUDY. Excuse me—

Mr. MARKS. Excuse me, sir. Do you want to testify on that point, is that the idea, Mr. Rudy?

Mr. RUDY. I will confer with Mr. Graham.

Mr. MARKS. We would be delighted to hear your comments on it, if that is what you want.

What we are saying is, really, they are going to get 53 percent of what they have gotten previously.

Mr. RUDY. Fifty-three percent of investment retailers, which are not generally the Mom & Pop stations. The Mom & Pop stations are what we characterize as open retailers.

Mr. MARKS. Let us go back again because I think what Mr. Graham said and what you are saying now, Mr. Rudy, is conflicting. So, let us get it straight.

Mr. RUDY. Now, bear in mind that Mr. Graham is qualified to speak as to supply problems.

FROM THE FLOOR. Speak up.

Mr. MARKS. Yes, would you speak into the microphone, please? May I say to you that I am aware of Mr. Graham's qualifications, and I would remind you that you do not have to remind this committee, Mr. Rudy because when notification was given to Texaco we made it very clear that we wanted to have somebody here at this hearing who could answer questions of this type.

Now, I appreciate the fact that Mr. Graham cannot know everything, but since he has been with Texaco over a quarter of a century, we are pleased to have him here. If in fact there is some detail that he is not as aware of as some other people, we are happy to have you advise him of that fact. But since the record is now conflicting, let us try to straighten it out. Either one of you may do that.

Mr. RUDY. I think I have.

Mr. MARKS. Would you do it again because I am not now clear.

Mr. RUDY. Our petition states that in the event of an 80-percent allocation fraction—which is a number that we just chose as an example, and not necessarily based on predictions—that 25 percent of our investment retailers would suffer a shortage of gasoline in the event we had to allocate.

Investment retailers are generally not what you characterized as Mom and Pop stations, which are open retailers.

Mr. MARKS. All right, what is an open retailer if it is not a Mom and Pop operation?

Mr. RUDY. It is a retailer that operates a station in which Texaco has no real estate interest.

Mr. MARKS. I see. All right, those are the people—however many there will be—that will suffer the 53-percent decrease.

Mr. RUDY. They would suffer a shortfall. I am not sure that the 53 percent is an accurate number.

Mr. MARKS. Well, we are using the figures based on your own petition.

Mr. RUDY. We have submitted that figure on investment retailers.

Mr. MARKS. Be that as it may. How many of those dealers will be involved?

Mr. RUDY. I do not know.

Mr. MARKS. If you do not know, perhaps Mr. Graham knows. Do you know, Mr. Graham, can you answer that question?

Mr. GRAHAM. There are in the range of about 30,000 Texaco service stations; about 15,000 of those are operated by distributors, they are in the wholesale network; about 6,000 are company owned and leased out to independents. The 9,000 are the other, or open retailers.

Mr. MARKS. So, we are talking about 9,000?

Mr. GRAHAM. Yes.

Mr. MARKS. 9,000 dealers all over the country.

Mr. GRAHAM. All over the country.

Mr. MARKS. Can you be any more precise? I am interested and I know Mr. Walgren would be as well—about how many of those dealerships are in this 24th Congressional District, which is Erie, Mercer, and Crawford Counties; and/or in Mr. Walgren's district?

Mr. GRAHAM. No. I have some numbers here of those in Pennsylvania; I do not have that.

Mr. MARKS. Well, how many in Pennsylvania, then? We will start there, and I am sure you will get us the other information.

Mr. GRAHAM. Do you want that now, do you want me to get into this?

Mr. MARKS. Yes, if it will not take you too long.

Mr. GRAHAM. The number of service stations in Pennsylvania is 1,316.

Mr. MARKS. 1,316 Texaco service stations in Pennsylvania.

Mr. GRAHAM. Yes.

Mr. MARKS. And how many of them are of the type that will suffer?

Mr. GRAHAM. Could we submit this to you later?

Mr. MARKS. Yes. Could you give us a ballpark figure, if you could, just because it is of great interest, I believe.

Mr. GRAHAM. I would say close to 400.

Mr. MARKS. 400 stations in Pennsylvania.

Mr. GRAHAM. No, of those that would suffer the unusual penalty, of the total.

Mr. MARKS. Yes, of the 1,316 Pennsylvania Texaco dealerships approximately 400 will suffer as a result of this.

Mr. GRAHAM. Yes.

Mr. MARKS. You will provide, may I suggest, I would appreciate if you would provide to the committee the exact number; we will hold the record open for that. Also, we would like to know the exact number of dealerships in the 24th Congressional District—my own—as well as Mr. Walgren's district.

Mr. GRAHAM. All right.

Let me qualify one statement there.

Mr. MARKS. Sure.

Mr. GRAHAM. We are talking about the open dealers and investment stations. I think your question stated, "would suffer." I am not saying that all these would suffer. They would fall in the category of these stations that "may suffer." They may have had an opportunity to get an adjusted base themselves that I would not be aware of here; they would not suffer from that. So, let me qualify that.

Mr. MARKS. Fine. For the record, I would ask you to provide the subcommittee with specific figures, and I am sure that you will be able to get those to us as quickly as possible.

Mr. GRAHAM. Yes.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. MARKS. I note, also, that your petition seeks approval of a curtailment plan to March 31, 1979, in the expectation that gasoline controls will be lifted by then; is that correct?

Mr. GRAHAM. That is the application date, sir.

Mr. MARKS. The point here, however, is not that the gasoline deregulation would result in a sudden increase in gasoline supply, but rather that decontrol would free Texaco of its current delivery obligations, leaving it free to apportion gasoline in any way that it chooses. Is that correct?

Will you pull the microphone closer to you, Mr. Rudy, please, and speak up?

Mr. RUDY. Mr. Graham has not read our application for exception.

Mr. MARKS. Well, we will give you a page number that you can go by. You are telling us that Mr. Graham has not read the application; is that correct?

Mr. RUDY. That is correct.

Mr. MARKS. Have you, sir?

Mr. RUDY. Yes, I have.

Mr. MARKS. Would you be prepared to answer the question, then, the question that I am now asking; would you be prepared to answer that?

Mr. RUDY. Would you repeat the question?

Mr. MARKS. Certainly. My statement and question was that the point is not that gasoline deregulation would result in a sudden increase in gasoline supply, but rather that decontrol would free Texaco of its current delivery obligations, leaving it free to apportion gasoline in any way that it chooses. Is that not correct?

Mr. RUDY. Our petition does not address the issue of decontrol at all, other than the fact that we hope the situation will change by March 31. Our petition is merely seeking a change of rule as to Texaco as to a base period.

Mr. MARKS. May I read from your petition at page 11; would you care to look at the bottom of page 11, please?

Under a paragraph entitled "Relief Requested," it says:

Texaco has limited the time for which it seeks exception relief from the period from December 1, 1978, to March 31, 1979, for the following reasons:

One: Secretary Schlesinger has recently stated at a press conference that a proposal to decontrol gasoline will soon be sent to Congress. It is anticipated that if Congress ratifies this proposal, decontrol would be achieved prior to March 31, 1978.

Is that correct?

Mr. RUDY. Yes.

Mr. MARKS. Is that what you stated?

Mr. RUDY. That is right.

Mr. MARKS. Is that what you meant?

Mr. RUDY. Yes, sir.

Mr. MARKS. Fine. That being the case, Mr. Rudy, is the point that we are now making a correct one, that the deregulation would not result, in fact, in a sudden increase in gasoline supply, but really, rather, that decontrol would free Texaco from its current delivery obligations, leaving it free to apportion gasoline wherever it wanted?

Mr. RUDY. I cannot predict what would happen in the event of decontrol.

Mr. MARKS. Well, does it not give you a right to stop selling gasoline to anybody, if you want to?

Mr. RUDY. Sure, it does.

Mr. MARKS. So, obviously, then, if it gives you the total right, it gives you a partial right; is that correct?

Mr. RUDY. Of course.

Mr. MARKS. Fine. Then the answer to that question has to be, "yes."

Mr. RUDY. Well, aside from our contractual commitments, of course.

Mr. MARKS. Mr. Graham, I would like now to review with you the extent to which the current gasoline supply crunch relates to the industry having dramatically reduced gasoline inventories and limited gasoline production earlier this year. Texaco, I assume, is among those major oil companies that attributes the current gasoline supply situation to Government price and environmental regulations; is that correct?

Mr. GRAHAM. That is correct.

Mr. MARKS. Is it not the fact, Mr. Graham, that those restrictions notwithstanding, Texaco fully expected the industry to be able to satisfy gasoline demand through 1978 and 1979, and that the industry would have done so, had it not misjudged demand?

Mr. GRAHAM. That is right.

Mr. MARKS. We appreciate your candor in that answer.

Mr. RUDY. Congressman, I am sorry, I am having a difficult time because of the length of the questions, understanding exactly what you are requiring, a yes or no answer.

Mr. MARKS. Well, I understand that you may be, Mr. Rudy, but apparently Mr. Graham understands them. If he does not, I would appreciate very much, Mr. Graham, if you would so notify me before you answer.

We have a yes answer to that question. Would you like to change it?

Mr. GRAHAM. Repeat the question.

Mr. MARKS. I will be glad to. Is it not a fact that those restrictions that we were talking about notwithstanding, Texaco fully expected the industry to be able to satisfy gasoline demand throughout 1978 and 1979, and that the industry would have done so had it, the industry, not misjudged demand. Your answer to that was "yes."

Mr. GRAHAM. Was yes in the time the demand for gasoline in 1978 was going to be 2 percent. So, specifically to your answer the question is yes, in meeting the industry demand of 2 percent. The industry feeling was that it was going to meet the demand—and we are.

The industry also had felt that there was going to be a decline soon, something like in 1980, 1981. There is now a question. We have revised our estimates now up to the 2½ to 3 percent.

Now, if you are asking, do I think at this time that we can meet the demand, that is one question. I related your question back to, say, the first of the year, in which case my answer is, yes.

Mr. MARKS. I assume that you are familiar with the gentleman whose name is Mr. R. J. Fisher of your company.

Mr. GRAHAM. Yes.

Mr. MARKS. Mr. Fisher is the assistant general manager, resale for marketing; is that correct?

Mr. GRAHAM. Yes.

Mr. MARKS. I call to your attention, just to make the record clear, on November 30, 1977, Mr. R. J. Fisher, assistant general manager, resale for marketing of Texaco stated, "Industry supplies are currently adequate, and they are forecast to remain so for the foreseeable future." Is that correct, sir?

Mr. GRAHAM. That was dated November 30, 1977?

Mr. MARKS. Yes. That is on page 374, sir.

Mr. GRAHAM. Yes, I see it.

Mr. MARKS. That is correct; is that right?

Mr. GRAHAM. That was the feeling at the time, yes.

Mr. MARKS. Now, clearly, Mr. Graham, this previous testimony would indicate that Texaco viewed the industry as being able to satisfy 1979 gasoline demand; and the fact that Texaco has suddenly become concerned over gasoline supplies seems to be suggestive of but two possibilities: Either the industry misjudged demand; or Texaco in its 1977 presentation before the Federal Energy Regulatory Commission deliberately misstated the facts in projecting adequate gasoline supplies for the foreseeable future to lull the Government into believing that it could proceed with gasoline decontrol in the face of an adequate supply situation.

Mr. GRAHAM. The situation on November 30 was one taking the requirements as forecast, that there was enough supply. There have been other factors since then, and it has been, I think, a rather unusual year in the industry of unscheduled downtime in 1978. We have been subject to unscheduled downtime ourselves.

Mr. MARKS. Mr. Graham, I must just repeat to you—and then I will turn the questioning over to Congressman Walgren—the fact that your answer to my question certainly indicates that it was not the controls that did it; that it was either a misjudgment, a serious misjudgment on the part of the industry, or in fact at that time Texaco made a deliberate attempt to lull the Government into an area, which it should not have done.

Mr. GRAHAM. Taking off controls basically is to allow investments to be made. One big reason is to make investments that will be required, that can now not be passed through. The controls discourage and have discouraged—and will continue to discourage—any new investment either in new refining capacity, or equipment for upgrading.

Mr. MARKS. Mr. Graham, that would not happen in 1 year. It takes 5 years to build a refinery; is that not correct?

Mr. GRAHAM. That is correct. The controls have been on all of that.

Mr. MARKS. Thank you, Mr. Graham. I have no further questions at this time. Mr. Walgren?

Mr. WALGREN. Mr. Graham, does Texaco have specific plans to increase its refining capacity in the event of decontrol?

Mr. GRAHAM. We have bottleneck removal projects. We do not have, say, a grassroots refinery plant on the board right now. We have several old units that are rather inefficient. We do have in mind replacing some of the older equipment with, say, a new crude still, which would shut down part of our old equipment, and at the same time add an incremental refining capacity to our total capacity.

Mr. WALGREN. What do you estimate the incremental refining capacity that would be added by other than a grassroots facility; what do you estimate the increase in supply—in percentage terms—to be which that kind of incremental capacity would give Texaco?

I gather there is not a specific answer within the company at this point.

Mr. GRAHAM. No, you placed it in a different set of numbers than I am used to looking at, you are asking about percent. I would say we are probably looking at maybe 1 or 2 percent.

Mr. WALGREN. So, essentially bottleneck removal and some incremental adaptations you make to present facilities would add 1 or 2 percent. But you have no plans at present for any—I gather grassroots is “green acre”, or whatever they call it, “brandnew” facilities in the refining area.

Texaco is essentially asking for a decontrol, in your statement, without any specific plans to provide other than 1 or 2 percent in increased refining capacity. Is that not correct?

Mr. GRAHAM. That is correct.

Mr. WALGREN. You indicate that you would like to see under the current regulations, if you cannot have decontrol, you would like to see a passthrough of increased refining costs apparently, so that the price received can reflect increased costs. Has there been a reduction in the profit margin on unleaded gasoline for Texaco?

Mr. GRAHAM. I cannot answer that because you specifically asked unleaded. I have not seen the books on gasoline, the supply manuals.

Mr. WALGREN. If we might mark the record at this point in hopes of receiving an answer from someone in the company who could give us a direct response to that because it seems to me that on the one hand we are saying that there is a direct need to pass through increased costs. Now, that must mean that profit margins are not there for you.

Mr. GRAHAM. Right.

Mr. WALGREN. I would like to know what the measure of those costs are.

[The information was not available to the subcommittee at the time of printing.]

Mr. WALGREN. How has that profit margin in that line of unleaded gasoline fallen, so that we might be able to make some judgment about the necessity of considering a passthrough of those costs.

It troubles me a little that we always come up against the argument, well, with any kind of regulated or controlled price no investment flows to that area and therefore the only answer is to stop controlling the price in any way. And yet, we have no specific plans for exactly what Texaco is prepared to do in the event of decontrol. It is my understanding that we are contemplating decontrol in the very near future, within the space of 1 year—one of the timeframes was even less than 1 year. I would think that, given the long lead time of these facilities, that we would have specific plans that would be returned to the public, or stated and certainly developed, so that the public knows what it gets in return for a totally uncontrolled situation of prices in gasoline.

Mr. GRAHAM. Probably where you and I are differing here is on the definition of "plan." I took your definition as, what is on the books and we immediately start doing in regard to designs, even. We have other plans to increase gasoline manufacture, but it is going to take a major investment; we do have that in mind, planned.

Mr. WALGREN. How much would that increase that you have planned increase your production by a ballpark percentage figure?

Mr. GRAHAM. May I give that to you confidentially, also?

Mr. MARKS. Mr. Walgren, would you yield for a moment?

Mr. WALGREN. Certainly.

Mr. MARKS. I am a little bit concerned about the statement you made, if I understand it correctly. That is, you are proposing that there be decontrol, hoping that there will be, and I am sure working very hard to see that there will be decontrol as of March 31. If that is the case, are you telling us that you do not have any plans for what will happen at that particular point?

Mr. GRAHAM. No. As any organization, you are always planning. It is contingency planing. You have to plan "what if" constantly. If there is no decontrol this rather large investment cannot be made; there is no way of recovery.

Mr. MARKS. Mr. Graham—if you will again, Mr. Walgren—I read from your petition, Texaco's petition, again at the top of page 12, I believe, where it says, "It is anticipated that if Congress ratifies this proposal, decontrol will be achieved prior"—prior—"to March 31, 1978," obviously meaning just exactly what it says, I assume.

Now, if that were the case, if you anticipated that as of March 31, I must tell you, to use the word "shock" may be an understatement, to hear you say that you had no plans as of that time; maybe you do not have any now.

May I suggest to you, sir, that if in fact that is the case—and I am sure you are trying to be as candid as possible—that is not your responsibility. But, would you please pass the word back that this committee is very concerned about that statement and that situation, and that we will expect to hear immediately from Texaco as to what if any plans they do have that you may not be aware of.

Thank you, Mr. Walgren.

MR. WALGREN. I am certainly concerned that Texaco and other oil companies may have an interest in a shortage because in a shortage situation, if it is decontrolled, there is no question that scarcity would just drive the price upward in a commodity like gasoline, which is very much in demand. Our lifestyle in this country is such that it probably will continue to be in demand, where we are consuming about everything that is brought on. I would like that in return for asking for decontrol and asking the Congress to contemplate decontrol, certainly, we ought to have more firm representations of what increased capacity is going to come, other than just the laissez faire economics that by definition decontrol will draw investment into that sector.

What bothers me most is that I think now we are really faced with psychological dangers to prices. If, let us say, gasoline, for example, goes over a dollar a gallon, then it will be just, "Damn the torpedoes" as far as any other price that exists in this economy because it may not be just that incremental penny. What is the attitude of somebody who has to pay \$1 a gallon—or even a less price—what is their attitude when they price what they may be selling in Woolworth, or what they may be asking for at the bargaining table?

So, I think at this time we really have some very unusual considerations. I would be very reluctant to see any kind of decontrol of prices without some very direct, concrete plans that would increase capacity in such a way that we would know we would not face that kind of a shortage.

MR. MARKS. May I interrupt one more time?

MR. WALGREN. Certainly.

MR. MARKS. Mr. Graham, last night between the hours of 7:10 p.m. and about 9:30 I sat in this city with 12 responsible, concerned labor leaders. Although the major part of that meeting was to give to me their views—therefore the views of their people—about the President's wage and price control, their bitterness over what he is doing to the people, the people they represent, they dramatically portrayed for me what is happening to their people—the same people you must sell gasoline to, who must buy from you. They cannot afford—they cannot afford, with inflation being what it is today—to pay 1 penny, or 2 pennies, or 3 pennies, or 4 pennies more per gallon of gas because over the course of a year, whether it is \$20, or \$30, or \$40, or \$50, sir, they have told me that those people just cannot take it any more. God knows what is happening—because you know—to the people on a fixed income, the elderly.

Now, I suggest to you that they went beyond that and suggested to me that there is going to be an uprising, a social uprising, unless some-

thing is done about it. I suggest that one of the messages, if you will, sir—and I do not mean to be presumptuous in suggesting this to you—that you take back to your company that they must have some great concern for those people that I am now talking about.

Mr. WALGREN?

Mr. WALGREN. Does Texaco have a position on the President's wage-price guidelines?

Mr. GRAHAM. Let me go back just one step. When you talk about plans and your feeling, apparently, that I have given you that we do not have anything, we do have a lot of plans continuously. However, at each time, at the point when we decide to go again, we must look at the crude available, what crude is available to us; what the sulfur is; what yields it will make from it. Following that, what kinds of operating conditions go into that unit. These things change almost as fast as the gasoline requirements.

Iran, for instance, will cause us to make big changes in what we would design in this particular equipment.

Mr. WALGREN. Suppose that the crude availability was very uncertain. Would you not then withdraw any recommendation of decontrol of prices because your real reason for decontrolling prices is to attract investment to that need, supplies in that area? If there were no raw material to put into a plant, even if you built it, then you certainly would not argue for decontrolled prices.

Mr. GRAHAM. Well, you are talking here of crude and the possibility of the world crude supply peaking out. I think the experts have stated they look at some time between 1985 and 1990 as the time world crude supplies peak out, or world crude production will peak out.

What we are talking about is converting some of the lower quality product into gasoline, possibly not increasing the crude running capability itself.

Mr. WALGREN. Does Texaco have a policy to limit their investment to the oil industry? Texaco does not hold stock in Disney Land, or any entertainment companies, "Six Flags over America"?

Mr. GRAHAM. We are, as you might expect, in the petrochemical business likewise. Our field is an energy field.

Mr. RUDY. Let me say, we may have isolated investments that we are not familiar with. But basically our investment thrust is in the petroleum field.

Mr. WALGREN. I understand. If we were to add \$4 billion to the oil companies' revenues per year, how much of that money do you believe would go into investment in refining capacity for unleaded gasoline?

Mr. GRAHAM. You are talking about the industry. I could not answer for the industry. If we were to pursue ours, a large part of it, very large numbers in investment.

Mr. WALGREN. I see. Perhaps large numbers, but how about large percentages of the \$4 billion. Would it be over 50 percent that went into unleaded gasoline capacity?

My point is, the industry is not willing to make a commitment that the benefit from decontrol, in order to solve the problem of shortage in unleaded gasoline, will go to solve the shortage in unleaded gasoline; are they?

Mr. GRAHAM. I do not think I can answer that.

Mr. WALGREN. Perhaps we will hold the record at this point. You might read it later on, and if there is anybody in Texaco that would like to address that problem, we would be very happy to have it.

Mr. MARKS. We will hold the record open for that purpose.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. WALGREN. Just very quickly, has Texaco made any representations to the administration that they will live within the administration's price guidelines, to your knowledge?

Mr. MARKS. His voluntary plan.

Mr. WALGREN. Yes, voluntary wage-price guidelines. Has Texaco taken a position that it will hold any increases in price within the guidelines that have been presently put forward by the administration?

Mr. RUDY. I can answer that question. I do not know whether we have made any specific representations to the administration, but we are complying with them, and we intend to comply with them. In 1972, when voluntary wage and price guidelines were implemented, we complied with them at that time. So, I am certain that we would live within them.

Mr. WALGREN. I see. One of the problems in the oil industry is that when you have both company owned and independently owned gas stations, a shortage has even greater leverage because to the degree you have the power to supply your own outlets and deny supply to independently owned outlets, you can wipe them right off the map. Then, in a later period of increased supply, you are the only party in town.

Would decontrol as you envision it give Texaco the power to allocate shortages, or greater amounts of the burden of shortages, to the independently owned, as opposed to the Texaco owned?

Mr. GRAHAM. Well, from a supply and distribution standpoint we would not. Now, you are getting into the marketing areas and marketing strategies, and I am not familiar with the strategy. I would say as a principle, though, Texaco would abide by all our contracts. We have been good citizens in this area and we will continue to be.

Mr. WALGREN. As counsel to the company's operations in this area, does necessity in terms of an imposed shortage on the company as a whole, does that release you from contractual obligations? That would be a defense to a claim of nonperformance under basic contract law; would it not?

Mr. RUDY. No, I do not think so, just without specific contractual provisions. If you want my opinion as a lawyer, I do not think that a shortage would necessarily release us of a contract.

Mr. WALGREN. Do you know whether Texaco in their approaches to the political side of the Government made any suggestions as to how we might protect the independent suppliers in hopes of maintaining competition, and not winding up just with Texaco-owned outlets?

Mr. RUDY. Maybe we should try to define what you mean by "independent" and "company" operated. We only have less than 100 company-operated stations nationwide. I do not think those stations would have any dramatic impact.

Mr. WALGREN. How about company owned, where the investment is owned by the company?

Mr. RUDY. There are more.

Mr. WALGREN. There are more.

Mr. RUDY. There are substantially more than that.

Mr. WALGREN. What is the balance in the total number of outlets where somebody secures a contract with Texaco and gets the right to use the insignia and a contract for you to supply him just with the gasoline, but he owns the pumps and he owns the station; versus a station where you are the owners and you lease it to somebody who is essentially supplying labor alone. What is the balance, 50-50, 25-75?

Mr. RUDY. I am a little concerned that that may be getting into some proprietary information that we may not want to disclose in a public hearing, but we would be glad to provide you in writing after the hearing.

Mr. WALGREN. I would appreciate that. Also, perhaps, you might address yourself to the question of, if we have decontrol, what assurances do we as people interested in maintaining competition, literally, have? When you talk about decontrol, you are asking the public to take a real flyer, the flyer being, perhaps a good flyer, that competition will in fact deliver goods at the lowest possible price. In this balance between independent and company-owned supplies is the essence of what you are asking the country to rely on, the competitive forces within the market structure.

I would like to see the company address itself to, in the event of decontrol, what assurances is the company prepared to make to the people they are asking to vote for decontrol, that those competitive factors will not be substantially undercut by a future shortage.

Thank you very much, I appreciate the opportunity.

Mr. MARKS. Thank you, Mr. Walgren.

Mr. GRAHAM, before you leave, I think it is important that I mention something to you. That is, if the people in my district—the 24th Congressional District—are any indication about what our people think across this country, they not only think, but they believe that the reason that Texaco and the other big oil companies want deregulation is to make more money.

May I suggest to you that if Texaco has not already—and I assume it has, as the other members of the industry—not thought about it, they had better get an awfully good public relations group together to try to lay the facts, the real facts before the American people because basically the American people do not believe—if the people in my district are any indication of their thoughts—that you have anything in mind—anything in mind and when I say you, of course I mean the big oil companies, but to make more dollars. I heard your comment which I am sure you believe, sir—I am very impressed with you personally.

Mr. RUDY. I am impressed with you, sir.

Mr. MARKS. I believe that you believe it when you said, "We are good citizens", I remember those remarks, "good citizens. We have been good citizens and will continue to be." Let us hope that is the case.

We thank you very much for your candor, your willingness to come today—both you and Mr. Rudy. We are certain to have our paths cross again some time. Thank you for being with us.

Mr. RUDY. Let me say, Mr. Marks, that we appreciate the opportunity of being here and providing you with information that you have asked for today. Let me express, on behalf of the company, our willingness to continue to work with you; to continue to provide you with all the information that you might need on this very important topic.

Mr. MARKS. We appreciate those comments, Mr. Rudy. Mr. Graham, thank you again, sir, very, very much for being with us.

If the reporter is now ready, may I go on the record—in case I forget later—to say how much we appreciate the fact that you are with us today, and what a wonderful job you are doing, in spite of the fact that we talk awfully fast sometimes. We appreciate it very much.

We would like, then, to call our next witness, who is Mr. Paul H. Hertel, Strategic Assessment Planning Department, Sun Petroleum Products Co.

Mr. HERTEL, we appreciate very much your being here. If you would rise, please, and be sworn, we will proceed.

Do you swear that the testimony you will give will be the truth, the whole truth and nothing but the truth, so help you God?

Mr. HERTEL. I do.

Mr. MARKS. Thank you. Please, be seated. Mr. Hertel, as we have with our previous witnesses, if you have a prepared statement that is not very long, we would like to hear it; otherwise we would like you to summarize it—for the sake of time. I might ask before you are going on, do you have any transportation deadlines to meet?

Mr. HERTEL. We have a 2:28 flight.

Mr. MARKS. Fine. We will see, sir, if you are brief and succinct in your answers, we will be the same in our questions, we will get you out.

**TESTIMONY OF PAUL H. HERTEL, MANAGER, STRATEGIC ASSESSMENT GROUP, PLANNING DEPARTMENT, SUN PETROLEUM PRODUCTS CO., A DIVISION OF THE SUN OIL CO., OF PENNSYLVANIA**

Mr. HERTEL. First of all I would like to say, my name is Paul H. Hertel, and I am manager of the Strategic Assessment Group in the Planning Department of Sun Petroleum Products Co., a division of the Sun Oil Co., of Pennsylvania.

The Sun Petroleum Products Co. operates five refineries in the continental United States, and one refinery in Puerto Rico. We are primarily a domestic oil company, and not an international major.

The duties of my position include advising management as to the inventories and availability of petroleum products on a national and an international basis. Since Sun Petroleum Products Co. markets only east of the Rockies, my main international interest is in the Caribbean region and in Europe.

I have prepared no formal testimony but am here at the request of the subcommittee staff with whom I met this past Monday, to answer questions of the subcommittee to the best of my ability.

Mr. MARKS. Mr. Hertel, would you do us a favor, please, and give the clerk a copy of that when you have finished. We seem to have lost the copy. Thank you very much.

Mr. HERTEL. The subcommittee seems to have been directing their attention—

Mr. MARKS. Excuse me again, Mr. Hertel. I understood you to say that you do not have a prepared statement. Are you making one now?

Mr. HERTEL. No; just an opening statement.

Mr. MARKS. Oh, fine.

Mr. HERTEL. The subcommittee has directed its attention toward the differences in the industry operations between 1978 and 1977. I would like to clarify at least Sun's operations during that same time period.

Mr. MARKS. Excuse me just one moment, please. As counsel advises me, that is really the purpose of our questioning, and if we may, we would like to ask you the questions, if we can.

Mr. HERTEL. Sure.

Mr. MARKS. Thank you.

I want to state that I personally—and I know I speak for Congressman Walgren as well, and the staff—appreciate your being here today in view of the relatively short notice that was provided to you, and for the cooperation which you extended to the subcommittee in your meeting with the staff earlier this week.

I take it, based on the meeting that you held with the staff, that Sun Oil Co.—which is one of the Nation's largest refiners—is fairly pessimistic concerning gasoline supplies this spring, assuming a continuation of current gasoline demand. Is that correct?

Mr. HERTEL. That is correct. For the record, we are not one of the larger suppliers, we represent less than 5 percent of the total domestic refining capacity.

Mr. MARKS. One of the top 15.

Mr. HERTEL. Yes.

Mr. MARKS. Your company, I believe, at the beginning of this year projected a 2.5-percent increase in gasoline demand, as opposed to the 5.2-percent increase experienced in November 1978. Am I correct?

Mr. HERTEL. We did project a 2.5-percent increase in demand. I would caution the subcommittee in looking at only a given month. I would think, looking at year-to-date figures would be more appropriate because weather does change from one November to another November. Weather conditions change from one year to the next.

The year-to-date figures are of the order of a 3- to 3½-percent increase.

Mr. MARKS. What factors, in your view, are contributing to the increase in demand?

Mr. HERTEL. Well, the increase in demand is attributed to the driving habits, as was previously mentioned, of over 150 million people. There are approximately 120 million cars. This alone is highly unpredictable.

Another factor, we believe, is that the actual experienced efficiency of the automobiles which have been sold in the past few years has not met the EPA measured efficiency.

Mr. MARKS. Would you repeat that again? If not for the record, at least for emphasis.

Mr. HERTEL. The actual miles per gallon experienced by the average driver is not very close to the EPA mileage ratings, as they perform their tests.

Mr. MARKS. Go right ahead, sir. Any other reasons?

Mr. HERTEL. Those would be the prime reasons.

Mr. MARKS. Would the increased sale of light trucks and vans also have something to do with it?

Mr. HERTEL. Yes, it would; it certainly would. There has been a run on light trucks and vans this year.

Mr. MARKS. So, it is then your view, sir, that the unexpectedly high demand for gasoline, beginning in May of this year and continuing for—no one really knows how long—is responsible for the current gasoline supply situation?

Mr. HERTEL. Yes, it is.

Mr. MARKS. And it is your view also, is it not, that if the current high demand for gasoline continues, we could conceivably face a situation this spring in which motorists will experience difficulty in obtaining gasoline; is that correct?

Mr. HERTEL. If we continue at rates of increase of 4 to 5 percent, yes, that is correct.

Mr. MARKS. It would appear to me that by July of this year the figures on gasoline demand were such as to cause a reasonable person to suspect a potential gasoline shortfall; is that not true?

Mr. HERTEL. Yes, that is true.

Mr. MARKS. I want to be perfectly frank with you, Mr. Hertel, in my next question; and yet, at the same time I do not intend any disrespect to you personally, especially in view of the extent to which Sun Oil has cooperated with the subcommittee during its inquiry. But in a relatively short time that I have had the honor of representing my district in Washington I have developed certain suspicions regarding the credibility of the oil industry—a view which, as you know, is shared by many of my colleagues.

Mr. HERTEL. Yes.

Mr. MARKS. My question to you, sir, is this: Why in view of the fact that a reasonable man could only have concluded by July of this year that the Nation faced a somewhat precarious gasoline supply situation did Sun Oil Co. in testimony before the Department of Energy on July 14, 1978, go along with the Department of Energy's optimistic forecast regarding 1979 gasoline supplies?

I refer here to testimony of a Mr. Kenneth L. Moore, which you are now being handed, vice president of SunMark Industries, the marketing arm of Sun Oil Co. who stated on July 14, 1978, "Department of Energy estimates call for adequate supply, at least through 1979. In the case of Sun this condition is also true, and we concur," I repeat, "And we concur with the Department's estimates. This conclusion takes into consideration the fact that phasedown of lead content will result in lowered average yields of gasoline. These two factors, adequate supplies and market-determined prices lead Sun to the conclusion that decontrol will not affect prices or demand."

Mr. HERTEL. In July 1979 the only information that was available on gasoline consumption—

Mr. MARKS. Excuse me just a moment. Counsel called to my attention that you said July 1979.

Mr. HERTEL. July 1978, I am sorry.

In July 1978 the only official DOE information on gasoline consumption represented the first quarter of the year—January, Febru-

ary, and March. There is a considerable delay in official reporting of information.

The increase in the first quarter of 1978 over the first quarter of 1977 was 2.6 percent. At that time it was very reasonable to assume that the forecast of 2.5 percent would be within the ballpark for the remainder of the year.

Mr. MARKS. I assume that is your answer for what was said on July 14, 1978, when Sun not only went along, but was out front on saying, "Don't worry, everything is going to be OK."

Mr. HERTEL. Pardon me?

Mr. MARKS. That is your answer?

Mr. HERTEL. Yes, we based our answer on Government information.

Mr. MARKS. I see. I have to ask you this question, was Sun's presentation—the Sun Oil Co.'s presentation before the Department of Energy in July—colored to promote the gasoline deregulation proposal that the Department of Energy was planning at that time to submit to Congress in the fall?

Mr. HERTEL. I believe not.

Mr. MARKS. But you do agree, do you not, that the supply situation as it was known to Sun and the major oil companies in July of this year was such as to preclude one's dismissing any consideration of a potential gasoline shortage in a period of rapidly increasing demand.

Mr. HERTEL. Demand was not increasing rapidly, sir. I am trying to tell you, it was increasing at the rate that was expected, 2.5 percent in the first quarter of 1978. In fact, the demand increase over previous years had declined in six of seven quarters since 1976, up to the first quarter of 1978.

Mr. MARKS. Mr. Hertel, another factor that Sun's July assurance concerning gasoline supplies through 1979 suggests to me is that the current supply situation is a function, really, not of Government price and environmental regulations, but rather that it almost relates wholly to the industry's failure to project short-term gasoline demand. Do you agree?

Mr. HERTEL. No, I do not think that the industry failed up to April, or May, or June, up to that time period. Again, our forecast was right on the money for the first quarter of 1978.

Mr. MARKS. That is exactly the point counsel has suggested, but after that you were way the hell off.

Mr. HERTEL. Well, the second quarter increase over 1978 was 2.8 percent, which again is not too far from the 2.5 percent. From the first to the second quarter of this year, the industry increased capacity utilization by approximately 3 percentage points; they went from 84 to 87. So, there was a recognition, at that point, by the industry that demand seemed to be a little higher than expected. So, the refineries operated—

Mr. MARKS. A "little higher than expected"?

Mr. HERTEL. Well, at 2.6.

Mr. MARKS. Excuse me, sir, did you see the chart that was presented?

Mr. HERTEL. Yes, I did.

Mr. MARKS. Did you see that curve of demand from May on?

Mr. HERTEL. That difference is 2.6 percent, sir.

Mr. MARKS. I would like to review with you, finally, if I may, Mr. Hertel, the decision on the part of the oil industry to reduce gasoline

inventories through the first quarter of this year. Now, one reason for an oil companies' efforts to project short-term gasoline demand is of course a desire to keep inventory no higher than necessary to eliminate the cost of maintaining a higher than necessary inventory; is that true?

Mr. HERTEL. That is correct.

Mr. MARKS. One of the costs of maintaining inventory is the interest charge made on the money borrowed by the company prior to sale; is that correct?

Mr. HERTEL. That is correct.

Mr. MARKS. So that in interest charges alone the cost of maintaining 1 barrel of gasoline in inventory for 1 year is approximately \$1.80; am I correct?

Mr. HERTEL. That is approximately correct, yes, sir. May I make a comment at this point?

Mr. MARKS. Certainly.

Mr. HERTEL. Sun, during this same time period, was in a slightly different position than the industry in general. Our inventories were below what they were the previous year; and our refinery operations were much higher than the industry average during that same time period. We were striving to make as much gasoline and provide as much gasoline as possible to the general public.

Mr. MARKS. My final question is this, is it not really the case that our current gasoline supply situation would be markedly better today if the industry had maintained the record high gasoline inventory that it had going into January 1978?

Mr. HERTEL. There would be more barrels in inventory, yes; we would be in better shape.

Mr. MARKS. We would be in better shape.

Mr. HERTEL. Pardon me?

Mr. MARKS. As you say, we would be in better shape.

Mr. HERTEL. Yes. Well, we are not really in bad shape.

Mr. MARKS. Thank you, Mr. Hertel. Mr. Walgren?

Mr. WALGREN. I understand that some of the data that Sun bases its position on is that supplied by Government information.

Mr. HERTEL. Yes, sir.

Mr. WALGREN. The reason we brought you here this morning because we wanted you to see the basis of the Government information, and I hope that you will evaluate the presentation made by DOE and perhaps send the word back that we cannot rely too heavily on the accuracy of some of the projections.

Mr. HERTEL. Congressman, it is our only source of information for the industry. I would recommend, and we have recommended as a corporation that the Government improve their reporting requirements so that we do have an early warning system.

Mr. WALGREN. I recognize Mr. Sims at this point.

Mr. SIMS. Thank you, Mr. Walgren.

I just want to explore one other source of data with you, if I could.

Mr. HERTEL. Sure.

Mr. SIMS. That is the weekly report by the American Petroleum Institute, which is an industry trade association, which gives a preliminary estimate of demand with a timelag of about 2 weeks; is that correct?

Mr. HERTEL. Yes, that is correct.

Mr. SIMS. They do this every week.

Mr. HERTEL. They do it every week, and they revise previous figures almost every week.

Mr. SIMS. That is correct. But, is it not true that this source is used by the industry, as it is by the Government and by the Congress, as a sort of initial testing of the water?

Mr. HERTEL. It is a barometer of the situation.

Mr. SIMS. While there is clearly a time delay in the Bureau of Mines/Department of Energy official actual demand figures, is it not also true that this barometer that API was putting out on a weekly basis clearly showed in July that things were heating up?

Mr. HERTEL. That is correct, but the data also reports that beginning in April or May the refineries were increasing their throughput; so that the refining industry had recognized the potential situation that we were headed for. They have increased their throughput, capacity utilization, as I mentioned, from the first-quarter figure of 83 percent up to a third-quarter figure of 92 percent. So, the refining industry did recognize that inventories were declining, and reacted accordingly and responsibly.

Mr. SIMS. Well, if we are to believe the Department of Energy figures depicted here in exhibit 1, refinery utilization in 1978, even through June and July, was clearly less than for the corresponding months in both 1977 and 1976.

Mr. HERTEL. That is why I caution you in using monthly data. I think quarterly data is a much better indication. There is no doubt that refinery utilization was lower in 1978 than it was in 1977. But, if you look at the absolute refining capacity you will find that it is probably much higher in 1978 than it was in 1977. So, the number of barrels going into the refinery, although the utilization was less, was probably more.

Mr. SIMS. Texaco, and I think the Department of Energy, told us that Government regulations were a clear constraint on the expansion of refinery capacity. Has refinery capacity in fact increased enough during a period of Government regulation to more than negate the constraint on the industry?

Mr. HERTEL. The capacity of the domestic industry increased 2 million barrels in the 2 years of 1976 and 1977.

Mr. SIMS. In the face of Government regulations?

Mr. HERTEL. These investment decisions were made in 1974, when investing 1974 dollars, the margins that we were controlled at, returns seemed adequate for those who wanted to increase investment in facilities. Since then the margins have remained the same and the costs have escalated probably no less than 30 or 35 percent. Currently the margins are inadequate for increasing the capacity of the industry.

Mr. SIMS. So, just to kind of oversimplify a point that we have been discussing here all day, these regulations do not prevent refiners, generally, from running their existing refineries. But, what the refiners are saying is that they prevent the industry from building new refineries.

Mr. HERTEL. They prevent the industry from economically building new refineries. As far as new refineries are concerned, sir, I might

also point out that there have been a number of grassroots refineries proposed for construction throughout the United States over the last 5 years, and there have been many turned down, based on siting regulations.

The DOE itself has published a list of those independent refiners, people not currently in the business, who have indicated that they would be willing to invest in facilities if they could find a place to put their facilities. The EPA has actually, by their regulations, reduced the competition within the industry.

Mr. SIMS. Mr. Chairman, I do not want to take all of Congressman Walgren's time, and am happy to yield back to him in hope that after Congressman Walgren has had a chance to complete his questioning, that I could be recognized for one or two additional questions.

Mr. MARKS. Congressman Walgren?

Mr. WALGREN. How does the trade-off between heating oil and automobile gasoline occur in the industry? It was said earlier that we expected demand for gasoline to fall off after Labor Day, and then we can switch our capacity to producing the heating oil needed. But, what happens if the demand for gasoline does not fall off, are we walking right into a heating oil problem?

Mr. HERTEL. It depends on the availability of heating oil outside the United States. We, as an industry, in times of shortages have gone outside the United States for imports of distillate fuel oil. The most recent time that was done in large quantities was the first quarter of 1977, 2 years ago; a very cold winter with natural gas curtailments. Home heating oil was actually imported from the Caribbean area and from as far away as Europe.

Mr. WALGREN. Are there supplies there so that if we do not go through this shift from gasoline to heating oil, that there will not be a shortage of heating oil?

Mr. HERTEL. To my knowledge, there is no timely reporting of inventories in Europe or in the Caribbean. The only thing that one can look at is the pricing structure in these various areas. The pricing structure that currently exists would indicate that there are not large surpluses.

Mr. WALGREN. What is the danger if we decontrol the price of the refined gasoline for automobile purposes, would that not provide a much greater incentive for the refineries to stick with the production of unleaded gasoline to the detriment of producing heating oil, and therefore bring on a shortage of heating oil?

Mr. HERTEL. I think the industry would continue to maximize gasoline production, as they are currently attempting to.

Mr. WALGREN. So, there would be a spill-over effect which would then increase the price of home heating oil to the degree the gasoline prices rose to meet the shortage there, heating oil would come right up with it.

Mr. HERTEL. There could be, and I would recommend to the subcommittee that they consider both distillate and gasoline in their deliberations because they are related. The industry has a fixed capacity to produce the sum of the two and has some flexibility between gasoline and distillate.

Mr. WALGREN. Is presently the decision to produce one or the other based on price?

Mr. HERTEL. I would say in general, yes. The refining industry in the United States, although you speak in terms of billions of dollars, has a very small profit. The profitability of our particular refining company—although it was \$100 million last year—amounted to about 1¼ cents per gallon on every product that we sold. We are working on a very small margin. The rate of return on our capital employed was well under 10 percent.

So, the average investor would not invest in the domestic refining industry as it currently exists.

Mr. WALGREN. I see. As I understand it, some suggestions that you have to stretch gasoline and perhaps get us through some tight spots involve the use of the additive MMT.

Mr. HERTEL. Yes.

Mr. WALGREN. The reservation about MMT being apparently that although it gives you more "bang" for the gallon and gets you farther, and therefore the same amount of gasoline would go farther, it does have an impact on the catalytic converters that have been required by EPA, and which are now on many, many automobiles. Is that correct?

Mr. HERTEL. There have been studies on the effect of MMT on catalytic converters, and in my opinion the evidence is not conclusive.

Mr. WALGREN. Are there any short opinions to that effect that we might incorporate in this record, to indicate your scientific reservations about this?

Mr. HERTEL. I think a review of the EPA hearings and the court cases, they might be the best source of technical information.

Mr. WALGREN. Do you have an estimate as to about how much using MMT might stretch our capacity?

Mr. HERTEL. I would estimate for our system—and that is all I can speak for—that the increase would be in the order of one-half to 1 percent. You see, what we are dealing here with is small differences as between two very extremely large numbers, each of which is subject to a lot of error.

Mr. WALGREN. So, it would be helpful, in your view, to allow MMT.

Mr. HERTEL. It would be in the proper direction.

Mr. WALGREN. That, coupled with a delaying of the reduction in lead that is scheduled, apparently, for next fall, is that right?

Mr. HERTEL. Yes.

Mr. WALGREN. That is requiring the refiners to anticipate to make some changes in advance of that, so that they are meeting those levels.

Mr. HERTEL. That is right. We are currently investing in each one of our refineries in order to meet and comply with EPA regulations. If we could use those investments to produce gasoline in a leaded environment, we could produce more.

Mr. WALGREN. Do you know how much more you might be able to produce, just looking at Sun Oil?

Mr. HERTEL. We have made an estimate of 2 percent.

Mr. WALGREN. That is all I have, Mr. Chairman; thank you.

Mr. MARKS. Thank you, Mr. Walgren. Mr. Sims, you wanted to ask a question, I believe.

Mr. SIMS. Yes, thank you.

Mr. Hertel, did I understand your earlier testimony correctly, that while the DOE numbers apparently showed significantly less utiliza-

tion of existing capacity in the first half of the year, Sun because of lesser stocks than average was actually running its refineries more than the industry average?

Mr. HERTEL. That is correct.

Mr. SIMS. You wish to correct this?

Mr. HERTEL. Well, I want the record to show that Sun was in a different position than the industry. Our inventories were below prior years, and our operations were at higher capacity utilizations.

Mr. SIMS. Would the clerk please provide the witness with a copy of exhibit 5 which, Mr. Chairman, I would like to introduce into the record at this point.

Mr. MARKS. It is so introduced.

[Exhibit No. 5 follows:]

EXHIBIT No. 5

SUN OIL SHIPMENTS OF UNLEADED GASOLINE

[Thousand barrels]

	1976-78	Percent change, 1977 over 1976	Percent change, 1978 over 1977
January .....	( )	65.5	44.7
February .....	( )	35.8	24.3
March .....	( )	117.9	(7.9)
April .....	( )	46.2	3.3
May .....	( )	(11.0)	16.4
June .....	( )	28.1	4.6
July .....	( )	70.6	(16.0)
August .....	( )	6.8	32.5
September .....	( )	8.8	26.1
October .....	( )	-----	-----
November .....	( )	-----	-----
December .....	( )	-----	-----

<sup>1</sup> Proprietary data, actual numbers omitted.

Mr. SIMS. Mr. Hertel, please take a moment to study this, and let me explain to you what this exhibit represents. This exhibit is derived from data which your company reported to the Department of Energy regarding unleaded gasoline shipments from your refineries.

Since the actual data is proprietary, we have omitted the numbers. Rather, the staff has calculated the percentage change in unleaded gasoline shipments from year to year. In other words, the first column shows the percentage of increased production in 1977 of unleaded gasoline, compared to 1976; the second column shows the same comparison, 1978 to 1977.

Now, Sun's increased production through July 1978 is clearly at a much slower rate than it was in 1977; is that correct?

Mr. HERTEL. A sight average would indicate that.

Mr. MARKS. Assuming the figures are correct.

Mr. HERTEL. It appears that an average of the increase in 1978 over 1977 is less than the average increase from 1977 over 1976.

Mr. SIMS. And it would also appear, would it not, that in July 1978 you actually produced less than you did in the same month for 1977.

Mr. HERTEL. It says that the shipments from our refineries were less, yes. It does not say we produced less.

Mr. SIMS. Let me strike the word "production" because it is kind of a misnomer when applied to unleaded gasoline. This reports shipments from the refineries.

Mr. HERTEL. Shipments from the refineries—it says nothing about what be produced in those refineries; it says what we shipped out of the refineries.

Mr. SIMS. Right. Now, Sun has approximately five refineries now, and those existed, I presume, in 1977.

Mr. HERTEL. Yes, sir.

Mr. SIMS. Was there a significant expansion in the refinery capacity from 1977 to 1978 that could possibly explain the decline in shipments?

Mr. HERTEL. No, there was not a significant change. Do you want an explanation for the decline, is that what you are driving at?

Mr. SIMS. Yes, please, could you explain to us—

Mr. HERTEL. Our marketing—

Mr. MARKS. Just one moment, if you will finish the question and then answer.

Mr. HERTEL. I am sorry.

Mr. SIMS. No, please, I was just trying to ask you that basic question.

Mr. HERTEL. The data seem to indicate that our increases in shipments from 1977 to 1978 are less than they were from 1976 to 1977. This relates to the type of market that we are in. Sun does not market an unleaded premium grade of gasoline. During 1978 a larger portion of the cars that were produced in Detroit required unleaded premium for satisfactory operation. So, our unleaded regular could not satisfy these cars; whereas the cars that were shipped out of Detroit during 1977 operated very well on unleaded regular. So, our increased shipments and increased production in 1977 over 1976 related very well to the type of car that was being sold. In 1978, which are the 1978 models, a higher percentage of those required a premium gasoline which we did not supply to our dealers. This is the reason why it would appear that our shipments of unleaded grade declined.

Mr. SIMS. I am glad you mentioned the Detroit problem because I know the subcommittee has been focusing more on the refinery aspect of the problem. That should not by implication mean that we are not fully aware of the ever-increasing octane demands from Detroit.

Mr. HERTEL. The Detroit problem can be roughly summarized as follows, they are striving to meet mileage standards, and in doing so they are operating on a very ragged edge of car performance. Each model year seems to require a higher octane unleaded gasoline to satisfy the average motorist. The regulations, or the understanding that was arrived at between the industries was that all tests would be performed on a particular grade of gasoline, which is currently what we call "unleaded regular," and that all cars would perform satisfactorily with that particular gasoline. The facts are that the cars are not performing satisfactorily on unleaded regular gasoline.

Mr. SIMS. My final question, Mr. Hertel. Could this same problem be visited upon you next year by Detroit; could this happen again?

Mr. HERTEL. Yes.

Mr. SIMS. Thank you very much, Mr. Chairman.

Mr. HERTEL. I think, again, you would be in a better position, or EPA would be in a better position—

Mr. WALGREN. I just found under the seat here a Civil Defense helmet, and I wanted to apologize for not providing these kinds of things to the witnesses that come before the committee.

I am pleased to see that Erie is far ahead of the President's program at this point by providing these protections to your public officials.

Mr. MARKS. Thank you, Congressman Walgren.

Mr. HERTEL. I might point out that Sun is pleased to participate in these types of hearings, and in the future would hope to have more time to prepare and answer specific questions.

Mr. MARKS. Mr. Hertel, in behalf of the committee, certainly particularly Mr. Walgren and myself, Mr. Sims, and Mr. Galloway, our staff, we appreciate very much—as I have said at the opening, after you were sworn—the fact that your coming before this committee was not only in a cooperative manner, but at such short notice; we appreciate it very much. We appreciate your company's making it possible for you to come.

I hope, however, and I am sure you were in the room when I suggested to the gentlemen from Texaco the very, very serious concern that the people in my district—who I think are representative of people all over the country—have, as concerns the problem that will be before, and is before, the Congress of the United States, who represent those people as far as decontrol of gasoline is concerned.

I suggest to you again very, very strongly, sir, that the people just do not believe it.

Mr. HERTEL. I would like to add to that, sir, that the Sun Co. employs 28,000 people who are in the same position as many of your constituents.

Mr. MARKS. I am sure that is true.

Mr. HERTEL. We are deeply concerned about inflation and other matters too.

Mr. MARKS. I am sure that is true, sir.

At this particular point I very much would like to say publicly, as I will many times privately to Congressman Douglas Walgren, thank you very much for joining we here.

I do not think that some of you in this room understand the significance of what Mr. Walgren did today. It is the rule of the subcommittee that we have at least two members to conduct the hearing, and our chairman, Mr. Moss, abides by the rules—in fact, helped to make them. Therefore, when I asked Mr. Walgren to join me here in Erie today when he could very well have been in his own district, working as hard as he works—just as hard as I, if not harder—I am particularly appreciative of the fact that he came up.

But beyond that, the fact that he is a Democrat, that committees are made up of the majority party, a vast number of the committees; we divide them up almost 2 to 1, Democrats and Republicans. They have the right to chair the subcommittees and committee. His gentlemanliness and his courtesy in turning over the chairmanship to me today was an extraordinary bit of good will, and it takes a person like Douglas Walgren to have done that. We appreciate the fact that the chairman himself would understand that particular situation.

I think it foretells a great future for this country because we have, with the mostly new people coming into the Congress, less of a partnership in these procedural matters than we used to have, and it seems to work—and hopefully will work—for the benefit of the country.

So, I am most appreciative, Doug, of this gesture of yours.

Mr. WALGREN. I appreciate that. You know, sometimes us Congressmen have to say nice things about each other because not very many other people say them.

I think, thinking of Congressman Mark's being here, one of the guides you should use is that the rest of the Members of Congress are presently out of the country. I know that those opportunities are given to every Congressman. There are a group of, I think, newer and perhaps more well-motivated Congressmen that are not traveling, that are staying home and trying to convince the public that we have their best interests at heart, and they are going to stay and see those problems through with them. So, you are to be commended for not being in Japan, let alone doing what you are doing here in Erie.

Mr. MARKS. Thank you very much, Doug.

In addition to thanking Doug Walgren, who is a close personal friend and a Member of the Congress whom I admire very, very much, I want to thank again the staff, John Galloway, Steve Sims; and repeat to you again that you have no idea what a professional group of gentlemen they are. They are just superb; they have done their homework; therefore, it makes us look good and helps us do ours. I want to personally again thank you both for just a marvelous job.

I also want to thank Sue Brookhouser from my staff here who helped us so very much, and Joe Shafran from our staff; and of course our court reporter, who did a marvelous job. We thank you very much, ma'am.

I would also like to thank those of you who have stuck out these many hours of this lengthy hearing. I am particularly appreciative of the coverage we received from the media. This is a very vital and important area that we are in, and it is up to you to be able to transfer now to the people not only in this district, but we hope nationally, that which we have been able to do here today, and which we will continue to do in the future.

In spite of the fact, however, that this has been a lengthy hearing, and a technical one at times, I do believe, personally, that it has been a very worthwhile one. We have established today evidence to strongly suggest, in my opinion, that the current tight gasoline supply situation is in large measure the result of three fairly simple facts. One, that the oil industry operated its refineries during the first part of this year at less than full capacity; two, that the oil industry sharply reduced its gasoline inventory during the first quarter of this year; and three, that the oil industry seriously underestimated gasoline demand earlier this year.

Those factors, taken together, provide in my view a significant piece of information for consideration by the Congress of the United States.

I might add one other thing, Mr. Hertel; your comment about the problem that has resulted from Detroit is one that we will not let go unnoticed. I thank you again, sir, for your cooperation.

This meeting is now adjourned.

[Whereupon, at 1:05 p.m. the subcommittee adjourned.]

