PETROLEUM INDUSTRY RESEARCH FOUNDATION, INC.
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COMMENTS ON REPORT OF SUB-COMMITTEE NO. 4, SELECT HOUSE COMMITTEE ON SMALL BUSINESS "SMALL BUSINESS PROBLEMS CREATED BY PETROLEUM IMPORTS"

I. Report Reflects only Protectionist Views.

The problem of what constitutes an adequate level of U. S. oil imports has been a subject of public debate for many years. Most government agencies and officials concerned with the problem have recognized, at least in principle, that both the free trade segments and the protectionist segments among the U. S. fuel industry have valid arguments to support their case.

Unfortunately, Sub-committee No. 4 does not appear to accept the existence of two sides to the oil import controversy. The Sub-committee's report reflects almost exclusively the views and contentions of the more extreme protectionists on oil imports. Although both sides to the controversy were given a hearing before the Sub-committee, the views and evidence of the opponents to more stringent import restrictions have been almost totally ignored in the Sub-committee's report.

II. Significance of Oil Imports to Small Marketers.

The report states that due to imports, "the economic health of the domestic fuel industry, and particularly the <u>small business segment</u> thereof, is in far more serious condition than ever before." Yet, literally thousands of small and medium size fuel oil marketers from Maine to Florida depend for their livlihood on imported residual fuel oil and the blends made from it, since the domestic production of this commodity has been steadily and irreversibly declining for a number of years. Spokesmen for these marketers appeared before the Sub-committee to explain their situation. But apparently their comments were totally ignored, as were those of several East Coast consumer groups.

III. Impact of Imports on Small Refiners.

The Sub-committee also ignored the fact that small refiners are clearly being given preferential treatment over large ones in allocating crude oil import quotas.. Thus, although small refiners - those with crude oil inputs of less than 50,000 barrels daily - accounted for only 14% of total refinery runs east of California in 1962, they were allocated 21.5% of the crude oil import quotas for the first half of

1963. This is because the existing import allocation formula is based on a progressive scale of refinery runs, weighted in favor of small volume.

Furthermore, the majority of the small refiners were never in the oil imports business until the government assigned them quotas which most of them sell at a considerable premium to historic importers who require more than their allotted quota of oil imports.

It is regrettable that the report dealing specifically with the impacts of oil imports on small business has failed to mention such impact on small oil refiners and small East Coast fuel oil marketers.

IV. No Decline in U. S. Oil Production.

. The report states on page 5 that "the production of crude oil in the U. S. is below the figure of five years ago ..."

This statement is both incorrect and misleading. It is incorrect because in 1961 total U. S. crude oil production had reached the all-time peak of 7,183,000 barrels daily; by comparison production in 1956 amounted to 7,151,000 barrels daily. (In 1962, production grew further to 7,316,000 barrels daily, according to preliminary official statistics.)

The Sub-committee's statement is misleading because it fails to point out that figures for total U. S. production are significantly affected by the fact that crude oil production in California has been declining steadily since 1953 for geological reasons and not because of imports or production controls. U.S. oil production exclusive of California shows an increase of 2.5% between 1956 and 1961.

Furthermore, during this period the U. S. production of natural gas liquids has expanded sharply - from 800,000 barrels daily to 984,000 barrels daily. Since most natural gas liquids are produced by the same firms which produce crude oil and since the two liquids are in many ways comparable and competitive, total production of oil liquids provide a more meaningful measure of the industry's performance than just crude oil production.

V. Declining Employment Unrelated to Rising Imports.

On pages 4 and 5 the Sub-committee's report seeks to tie declining employment in oil refining and in oil and gas production between 1956 and 1961 to the growing level of oil imports. Actually, the decline in employment is due entirely to technological reasons, since the level of output has been rising in refining and production.

Thus, U. S. refining operations have increased by 3.8% from 1956 to 1961. By contrast, the level of imported refined oil products - except residual fuel oil - has remained unchanged since 1959 so that imports could not have displaced additional domestic products in the last four years.

Residual fuel oil imports did, of course, rise during this period. But since domestic refiners are steadily reducing their output of this unprofitable bi-product in order to increase their output of the higher grade and more valuable oil products, residual fuel oil imports cannot be said to depress the level of domestic refinery runs.

The cited decline in employment in crude petroleum and natural gas production is also due entirely to technological reasons, since oil and gas production together have risen very sharply - by 13.7% - between 1956 and 1961, due principally to the very rapid growth of natural gas production which now supplies as much energy to the nation as domestic crude oil.

Unfortunately, the report bases its conclusions entirely on the unemployment statistics furnished by the Labor Department and ignores any of the qualifing points discussed above.

VI. Basic Element in Residual Import Problem Ignored.

The report criticizes the fact that the residual fuel oil import quotas have been steadily increasing since 1957. The Sub-committee has heard detailed and documented testimony to the effect that domestic production of residual fuel oil is in a permanent state of decline, both in absolute volume and in relation to competitive fuels. This decline reflects the technology and economics of multi-product oil refining and has occurred entirely independent of the level of imports or the prevailing domestic price of residual fuel oil.

Hence, unless residual fuel oil imports are periodically increased, the total available quantity of this product would steadily decline, with the result that marketers would be driven out of business and customers would be forced at considerable expense to install facilities to burn alternate, and often less suitable, fuels.

It is peculiar that in its findings and in its recommendations the Sub-committee chose to totally ignore all evidence of the declining domestic production of residual fuel oil, even though this fact is the key to the whole problem of residual fuel oil imports.

VII. <u>Principal Coal Market not Threatened by Residual Oil.</u>

On page 6 the report states that "more and more vital industrial plants and other installations along the East Coast are switching to residual fuel . . ."

This statement certainly does not apply to electric utilities which constitute by far coal's largest market on the East Coast and also represent a considerable market for residual fuel oil. Official statistics show that in 1958 oil accounted for 17% of total East Coast utility fuel consumption, coal for 74% and gas for 8%. By 1960 oils share had dropped to 15%, coals to 72%, while gas had risen to 11%. Preliminary figures for 1962 indicate that oil has remained at 15%, coal has risen to 75%, while gas is down to 10%.

Obviously, then, residual fuel oil has not been able to make any inroads in coal's principal East Coast market. In fact oil's share in the utility market has remained quite steady for the past decade.

VIII. <u>No "Double Depletion Allowance" on Foreign Oil Production.</u>

On page 7 the report states that "American (oil) companies operating abroad are given tax incentives in the form of a double depletion allowance". Under U. S. income tax laws U. S. oil companies producing abroad are subject to exactly the same percentage depletion as companies operating on U. S. territory. Thus, a U. S. company operating abroad will use percentage depletion to calculate its taxable U. S. income. But percentage depletion does not affect the company's foreign tax payments nor the size of its foreign tax credit against the U. S. income tax. Hence, no "double depletion allowance" is possible under U. S. tax laws, regardless of where a company conducts its operations.

Actually, most oil companies operating overseas pay higher income taxes in their host countries than they would at home because the tax laws of most major overseas oil producing countries do not contain a percentage depletion provision comparable to that of the U. S. Consequently, whatever advantages U. S. oil companies derive from operating abroad, these advantages do not lie in the area of taxation.

IX. <u>Report Inconsistent on Canadian Oil Imports</u>

On page 7 the report states that "Canada is importing cheap oil and, at the same time, exporting its' own high-price OIL to the U. S." These practices, concludes the Sub-committee, " are not conducive to the U. S. national interest ..."

It is difficult to understand the reasoning behind the Sub-committee's conclusion. The price of foreign oil imported into Canada from overseas has no effect on the U. S. domestic oil industry. The price of Canadian oil exported to the U. S. does affect U. S. oil production. But if, as the Sub-committee says, such exports consist of "high-price" oil, U. S. domestic oil producers should be able to compete with them without government protection.

The Sub-committee's comments would therefore appear to support the case against the need for restrictions on Canadian oil imports. Yet on page 10 the Sub-committee commends the administration for bringing Canadian imports into the overall level of permissable U. S. oil imports in the most recent revision of the imports control program. It would seem that the Sub-committee's advocacy of restrictions on Canadian oil imports is not consistent with its findings that such imports are "high-price".

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FOR RELEASE: Tuesday, A.M.

The Petroleum Industry Research Foundation, Inc. (PIRINC) today issued its analysis of a Congressional report entitled, "Small Business Problems Created by Petroleum Imports", recently released by a special House Small Business sub-committee under the chairmanship of Representative Tom Steed (Okla.).

PIRINC, which had testified at the Sub-committee's hearings, charged that the report is biased in that it ignores all views and arguments other than those of the extreme protectionists on oil imports. The foundation also said that the Steed Committee's report ignored the importance of oil imports to small oil products marketers on the East Coast.

Furthermore, said PIRINC, the Report has completely overlooked the most essential point in its discussion of residual fuel oil imports - namely the continuous decline in domestic residual oil production.

The Sub-committee is wrong, says PIRINC, in claiming (a) that U.S. crude oil production has declined in the past five years; (b) that imports have caused unemployment in the oil industry; and (c) that U.S. oil companies operating abroad are entitled to a "double depletion allowance."

The report also makes contradictory statements on the subject of Canadian imports, according to the foundation's analysis.

A copy of PIRINC's analysis has been sent to all members of the House Select Committe on Small Business.