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The following statement has been submitted to the Office of Emergency Preparedness by U.S. Senator Bob Dole (R-Kans.)

Dole asked that the statement be made part of the permanent record of the investigation OEP is conducting of recent increases in crude oil prices.

Pursuant to notification published in the Federal Register for November 17, 1970, the purpose of this statement is to set forth views with respect to the announced investigation of increased crude oil and petroleum product prices initiated by Gulf Oil Corporation on November 11.

This investigation fulfills the legal obligation of the Office of Emergency Preparedness under Section 232 of the Trade Expansion Act of 1962, which requires "surveillance" of prices for any item subjected to import controls under that section.

The purpose of the surveillance requirement is to establish whether price increases are necessary to accomplish the security objectives of Section 232. This being the primary question, my statement will be concerned first, with the vital necessity of permitting an economic climate in which adequate petroleum fuels (oil and natural gas) will be found and developed, and secondly, with the depressed conditions of the petroleum producing industry in my State of Kansas.

THE ISSUE: ECONOMIC INCENTIVE

The issue involved in this investigation is best described by a brief excerpt from testimony before the Mines and Mining Subcommittee of the House Interior and Insular Affairs Committee, by the Honorable Hollis Dole, Assistant Secretary of Interior for Minerals:

"I have (tried to) emphasize a crucial point: namely that unless we take prompt and substantial action, we shall pass from a period of energy sufficiency into a period of general energy insufficiency. There is a general recognition among knowledgeable people that at presently indicated rates of discovery, it is highly unlikely that our gas supply will be able to keep up with the demand over the next several years. But it is not only gas that is in dwindling supply: in five years out of the past nine, we have failed to replace as much oil as we withdrew from our proved reserves. We are uncomfortably close to the limits of our capacity to produce electricity.

"For the past two years, we have consumed and exported more coal than we mined, with the result that electric power plants are now operating with a 70-day supply of coal instead of the 90-day supply they customarily maintain.

"Yet the impending reductions in energy supply is an economic condition, not a physical one. The fact is that we have enormous resources of hydrocarbon fuels -- solid, liquid and gaseous -- that are available to us any time we care to undertake the cost and effort to find, extract and produce them."

The critical decline in petroleum exploration, drilling, reserves and producing capacity can be attributed -- as Secretary Dole made clear in this statement -- to insufficient economic incentive. Investment incentive in a high-cost, high-risk activity such as petroleum exploration within our economic system results from one primary consideration: reasonable expectation that successful ventures will result in an economic return that justifies the investments. It is all too apparent that incentives have not only been inadequate but have been declining since the mid-1950's. As a result, domestic exploration and drilling is now in its 14th year of decline and the United States faces the prospect of real and critical shortages in essential energy supplies. Should the nation be confronted with irreversible shortages, it clearly will be a result of the short-sighted policies of the Federal Government.

These adverse policies, I am convinced, include the unrealistic federal regulation of natural gas prices since 1954, an oil import policy characterized by almost constant uncertainty, and singling out of crude oil price increases as inflationary.

PERTINENT QUESTIONS

In assessing the security justification for improved economic conditions based upon the price function, the government should carefully weigh these very pertinent questions:

1. Are the announced price adjustments reasonable in relation to petroleum exploration and drilling costs and in relation to other wholesale raw materials prices?

2. Under federal policies that seek to depress prices with the result of further undermining domestic exploration and development, what will be the prices for alternative supplies?

3. If the national security requires reasonable self-sufficiency in essential fuels, a basic assumption of federal policies for many years, what alternative energy sources hold promise of lower cost than our conventional oil and gas resources?

Some provide an almost automatic but highly questionable answer to the first question, by asserting that any increase in domestic fuel prices is unjustified irrespective of supply and demand conditions, costs, or any other factor that normally is given weight in economic decision-making. To this school, the answer is very simple, if both impractical and dangerous: remove import controls, or outlaw state conservation practices, or both.

These apparently simple solutions, coupled with promises of great "savings," have great appeal for the consumer. Unfortunately, they ignore the basic issue of how and whether the United States is to revitalize the petroleum industry in order to insure reasonable self-sufficiency.

The question boils down, very simply, to this: do we as a nation want an adequate supply of oil and gas within our own control? If so, are we willing to pay the price that will encourage the investment of necessary capital and technology?

DOMESTIC CRUDE OIL PRICES

Dr. James McKie, the chief economist for President Nixon's Cabinet Task Force on Oil Import Controls commented in the OIL DAILY on August 7, 1970, that "If a U.S. real base price of $4 or more per barrel were necessary to guarantee minimum 'secure' coverage of U.S. (oil) needs, that result would then be consistent with the objectives of the recommended import policy."

It is clear from this assessment that Dr. McKie believes the nation's vital interest lies in maintaining "secure" petroleum supplies, even at real U.S. prices of $4 per barrel or more.

The statement by Dr. McKie was made in June, 1970, although not published until August. It was well before the publicity about $3-a-barrel-tanker rates which resulted from the rupture of the Trans-Arabian Pipeline and oil production curbs in Libya. It was also before the pressure in the world markets which led to a doubling, almost overnight, in the prices for residual fuel oil. These events nevertheless reinforced the wisdom of Dr. McKie's statement.

Cheap foreign oil, it is clear, will be cheap only until we cannot do without it. This fact now has been made abundantly clear by the overnight increase in residual fuel prices for our industrialized East Coast, which is more than 90 percent dependent for this fuel on foreign countries. The situation with respect to residual fuel which enters this country under an "open door" policy is a clear forewarning of what we can expect as to all our petroleum products if we choose deliberately to pursue policies of increased dependency on foreign supplies. One proposed means of forcing down domestic crude oil prices, removing oil import controls, would be self-defeating. It would, at this time, get no more foreign oil. It would further depress the domestic industry and we would get far less domestic oil.

The dollar received from crude oil and natural gas at the wellhead is the primary source of funds for exploration and development of both oil and gas. Since my state of Kansas contributes significantly to the nation's gas supplies, I believe it is important to recognize that government actions to control or limit prices of either oil or gas results in less supply of both. With natural gas shortages already a fact, particularly for industrial uses, the impact of inadequate crude oil prices on future gas supplies is a consideration of vital importance.

CONSUMER INTEREST

The question of the consumer's interest in sufficient gas supplies at reasonable prices, is, therefore, much involved in the question at issue here. What are the alternative costs confronting consumers as domestic gas supplies dwindle and our dependence for this vital energy source is shifted to sources other than domestic supplies?

One alternative to expanded domestic gas supplies would be liquefied natural gas, imported from North Africa. The price of this imported gas for the Northeast, it is estimated, would be $1.70 -- more than a dollar per MCF higher than delivered domestic supplies.

Both the risks and costs of foreign supplies of oil and natural gas add up to a highly questionable alternative for U.S. consumers. Domestic prices adjusted upward to assure increased domestic supplies would be in the long-range best interest of the consuming public. In fact, changes in consumer prices for petroleum have been infrequent and moderate. They have lagged far behind the rising costs of exploration, drilling and development and have reflected a stability that has been common to few other major commodities under the inflationary conditions of the past decade.

COST-PRICE SQUEEZE

In addition, crude oil prices have trailed far behind the major items of cost involved in domestic oil and gas exploration and development. In 1969, for example, the average U.S. crude price was less than four percent above the government's base years for measuring price behavior, 1957-59, while oilfield wages were up more than 40 percent and oilfield machinery almost 24 percent in the same period. In contrast to the insignificant rise in crude prices, the wholesale price for all commodities rose 13 percent from the 57-59 base years to 1969.

Because domestic exploration takes place in remote areas and drilling must be deeper than in the past, this further contributes to the cost-price squeeze.

If adequate domestic fuels are important in a security sense, then this cost-price squeeze is germane to our defense policies. But a dependable energy supply goes beyond the military requirements in a war situation, as we have learned only too well with respect to residual fuel oil.

Security against getting cold is important to the American people. Security against losing a job in a plant that is idled for want of fuel is equally important. The best and cheapest security is the domestic petroleum industry -- but we must recognize that domestic supplies of oil and gas cannot be found and developed at 1970 costs, and sold at less than 1960 prices.

My principal concern is that this government not discourage reasonable price changes for fuels that will further aggravate the drift toward "general energy insufficiency" alluded to in Assistant Secretary Dole's statement. It is clear that our great need is to reverse the decline in petroleum exploration and development, not to aggravate that decline.

KANSAS OIL AND GAS PRODUCTION

Aside from the broad question of maintaining secure supplies of essential fuels for the nation as a whole, I am deeply concerned about the impact of inadequate economic incentives on the oil and gas producing industry in Kansas. Petroleum is the second most important industry in our state, exceeded only by agriculture.

Kansas is the province of the small, independent producer. Two-thirds of our production is in the "stripper" class, producing 10 barrels or less per day. Some 35 percent of this marginal production comes from secondary recovery projects, such as waterfloods, installed at great cost.

An adequate price for crude oil not only would stimulate new exploration activity in deeper and still unexplored areas, but would assure recovery of hundreds of millions of barrels of oil obtainable only through costly secondary recovery techniques. Government actions that singled out the oil producing industry to prohibit nominal price increases that are overdue by every reasonable economic standard would have a devastating, demoralizing effect on this essential industry. Even worse, it would hasten the day of artificial, unnecessary and perhaps irreversible shortages of oil and gas. I urge that these factors be carefully weighed in the government's deliberations.